PIZZA PIZZA Limited

Consolidated Annual Financial Statements

For the 52-week period ended December 31, 2017 and the 52-week period ended January 1, 2017

Pizza Pizza Limited

Consolidated Statements of Financial Position
As at December 31, 2017 and January 1, 2017
(Expressed in thousands of Canadian dollars)

	December 31, 2017 $	January 1, 2017 $
Assets		
Current assets		
Cash and cash equivalents	12,758	13,024
Short-term investment	6,000	7,000
Trade, other receivables and prepayments (note 3)	14,959	17,907
Inventories	5,718	6,161
Income taxes recoverable	1,473	5,017
Receivables from jointly-controlled companies (note 22)	3,275	2,702
Recoverable franchisee expenses (note 4)	727	3,876
Total current assets	**44,910**	**55,687**
Non-current assets		
Property, plant and equipment (note 5)	13,160	11,860
Notes receivable (note 6)	13,256	14,841
Renovation funds (note 7)	7,834	6,075
Deferred tax asset (note 15)	49,191	45,471
Investment in Pizza Pizza Royalty Limited Partnership (note 8)	23,877	23,648
Investment in jointly-controlled companies (note 9)	18,929	19,235
Intangible assets (note 10)	3,891	130
Total non-current assets	**130,138**	**121,260**
Total assets	**175,048**	**176,947**
Liabilities and shareholders' deficiency		
Current liabilities		
Trade and other payables (note 11)	52,696	43,558
Deposits from franchisees	415	2,486
Borrowings (note 12)	474	570
Provisions (note 13)	1,328	489
Total current liabilities	**54,913**	**47,103**
Non-current liabilities		
Borrowings (note 12)	560	747
Unearned vendor allowances	-	1,096
Advances from related party (note 22)	16,261	17,452
Leasehold inducements	7	8
Renovation funds (note 7)	4,586	3,227
Deferred gain (note 14)	201,549	203,879
Total non-current liabilities	**222,963**	**226,409**
Shareholders' deficiency		
Common shares and special voting shares (note 17)	-	-
Accumulated other comprehensive loss	(170)	(102)
Deficit	(102,658)	(96,463)
Total shareholders' deficiency attributable to the shareholders	**(102,828)**	**(96,565)**
Total liabilities and shareholders' deficiency	**175,048**	**176,947**

Commitments and contingencies (note 16)

The accompanying notes are an integral part of these consolidated financial statements.
Approved by the Directors on February 28, 2018

Pizza Pizza Limited
Consolidated Statements of Income (Loss)
For the 52-week period ended December 31, 2017 and the 52-week period ended January 1, 2017
(Expressed in thousands of Canadian dollars)

	December 31, 2017 $	January 1, 2017 $
Revenue		
Food sales (note 19)	188,014	189,222
Royalties, franchise fees and other revenue (note 20)	30,817	30,104
Total revenue	**218,831**	**219,326**
Cost of food sales	(150,998)	(152,200)
General and administrative expenses (note 21)	(58,982)	(48,790)
Royalty payments	(35,614)	(35,333)
Equity income from Pizza Pizza Royalty Limited Partnership (note 8)	6,952	6,531
Equity income from jointly-controlled companies (note 9)	4,871	5,382
Gain on sale of Company-owned restaurants	77	331
Operating loss	**(14,863)**	**(4,753)**
Interest and other income	1,186	1,426
Amortization of deferred gain (note 14)	2,330	2,330
Interest on borrowings	(35)	(56)
Loss for the period before income taxes	**(11,382)**	**(1,053)**
Current income tax recovery (note 15)	1,524	5,290
Deferred tax recovery (expense) (note 15)	3,663	(981)
Income (loss) for the period attributable to the shareholders of Pizza Pizza Limited	**(6,195)**	**3,256**

Pizza Pizza Limited
Consolidated Statements of Comprehensive Income (Loss)
For the 52-week period ended December 31, 2017 and the 52-week period ended January 1, 2017
(Expressed in thousands of Canadian dollars)

	December 31, 2017 **$**	January 1, 2017 **$**
Income (loss) for the period	**(6,195)**	**3,256**
Other comprehensive income (loss)		
Items that may be reclassified subsequently to net income:		
Share of other comprehensive income of the Pizza Pizza Royalty Limited Partnership (note 8)	240	140
Deferred tax impact of share of other comprehensive income of Pizza Pizza Royalty Limited Partnership	(47)	(44)
Items that will not be reclassified subsequently to net income:		
Employee benefits	(364)	-
Deferred tax impact of employee benefits	103	-
Total comprehensive income (loss) attributable to shareholders	**(6,263)**	**3,352**

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

Pizza Pizza Limited
Consolidated Statements of Changes in Shareholders' Deficiency
For the 52-week period ended December 31, 2017 and the 52-week period ended January 1, 2017
(Expressed in thousands of Canadian dollars)

	Common shares and special voting shares (note 17) $	Accumulated other comprehensive income (loss) $	Deficit $	Total $
As at January 1, 2017		**(102)**	**(96,463)**	**(96,565)**
Comprehensive loss				
Loss for the 52-week period ended December 31, 2017	-	-	(6,195)	(6,195)
Employee benefits	-	(364)	-	(364)
Tax effect of employee benefits	-	103	-	103
Share of other comprehensive income on Pizza Pizza Royalty Limited Partnership's cash flow hedge	-	240	-	240
Tax effect of cash flow hedge	-	(47)	-	(47)
Total comprehensive loss	-	**(68)**	**(6,195)**	**(6,263)**
As at December 31, 2017	**-**	**(170)**	**(102,658)**	**(102,828)**
As at January 3, 2016	**-**	**(198)**	**(99,719)**	**(99,917)**
Comprehensive income (loss)				
Income for the 52-week period ended January 1, 2017	-	-	3,256	3,256
Employee benefits	-	-	-	-
Tax effect of employee benefits	-	-	-	-
Share of other comprehensive income on Pizza Pizza Royalty Limited Partnership's cash flow hedge	-	140	-	140
Tax effect of cash flow hedge	-	(44)	-	(44)
Total comprehensive income	-	**96**	**3,256**	**3,352**
As at January 1, 2017	**-**	**(102)**	**(96,463)**	**(96,565)**

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

Pizza Pizza Limited
Consolidated Statements of Cash Flows
For the 52-week period ended December 31, 2017 and the 52-week period ended January 1, 2017
(Expressed in thousands of Canadian dollars)

	December 31, 2017 $	January 1, 2017 $
Operating activities		
Income (loss) for the period	(6,195)	3,256
Depreciation of property, plant and equipment (note 5)	3,867	2,852
Amortization of intangible assets (note 10)	130	323
Amortization of leasehold inducements	(3)	(2)
Amortization of unearned vendor allowances	(1,096)	(648)
Amortization of deferred gain (note 14)	(2,330)	(2,330)
Net provision for notes receivable (note 6)	(151)	(143)
Net provisions during the period (note 13)	839	(445)
Gain on sale of Company-owned restaurants	(77)	(331)
Equity income from Pizza Pizza Royalty Limited Partnership (note 8)	(6,952)	(6,531)
Equity income from jointly-controlled companies (note 9)	(4,871)	(5,382)
Deferred income tax expense (recovery) (note 15)	(3,663)	981
	(20,502)	**(8,400)**
Changes in non-cash operating elements of working capital (note 24)	16,214	(13,557)
Cash used in operating activities	**(4,288)**	**(21,957)**
Investing activities		
Additions to property, plant and equipment (note 5)	(5,477)	(7,331)
Additions to intangible assets (note 10)	(3,891)	-
Proceeds from sale of Company-owned restaurants	390	1,417
Distributions from Pizza Pizza Royalty Limited Partnership (note 8)	6,963	6,585
Dividends from jointly-controlled companies (note 9)	5,177	5,084
Repayment of notes receivable	6,532	8,024
Issuance of notes receivable	(4,796)	(10,418)
Contributions to renovation funds	13,712	13,500
Disbursement from renovation funds	(14,113)	(11,710)
Withdrawals from (additions to) short-term investments	1,000	16,000
Cash provided by investing activities	**5,497**	**21,151**
Financing activities		
Proceeds from borrowings	434	1,025
Repayments of borrowings	(718)	(129)
Repayment of advances from related party (note 22)	(3,360)	(3,193)
Advances from related party (note 22)	2,169	1,767
Cash used in financing activities	**(1,475)**	**(530)**
Decrease in cash and cash equivalents	**(266)**	**(1,336)**
Cash and cash equivalents, beginning of period	13,024	14,360
Cash and cash equivalents, end of period	**12,758**	**13,024**

See supplementary cash flow information (note 24)
The accompanying notes are an integral part of these consolidated financial statements.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

1. Nature of Business

Pizza Pizza Limited ("PPL" or the "Company"), a privately-held corporation incorporated by Articles of Incorporation under the *Business Corporations Act* (Canada) on December 27, 1989, operates in the food service industry primarily throughout Ontario and Alberta and primarily franchises and operates quick-service restaurant ("QSR") businesses under the brand names of Pizza Pizza and Pizza 73. PPL derives revenue from franchises through the sale of franchise restaurants, food and beverages and royalties. PPL also derives revenue from Company-owned and managed restaurants through the sale of food products to retail customers.

PPL is incorporated and domiciled in Canada and the address of its registered office is 500 Kipling Avenue, Toronto, Ontario, Canada. The parent of PPL is 1373153 Ontario Limited, a private Corporation that does not prepare and make available financial statements for public use.

During the 52-week period ended December 31, 2017, PPL acquired 6 traditional franchises (52-week period ended January 1, 2017 – 17) and franchised 11 traditional restaurants (52-week period ended January 1, 2017 – 30). Below are the number of traditional and non-traditional franchisees and licensees as at:

	December 31, 2017	January 1, 2017
Franchisees and licensees	674	667
Jointly-controlled restaurants	79	75
Company-owned restaurants	7	10

2. Significant Accounting Policies

The significant accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all periods presented unless otherwise stated.

a) Fiscal year-end and interim period

PPL has a floating year-end on the Sunday closest to December 31; accordingly, interim periods consist of four 13-week periods with an additional week added to the last interim period every 5 to 6 years.

b) Basis of presentation

PPL prepares its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

The policies applied in these consolidated financial statements are based on IFRS standards, which have been applied consistently to all periods presented. These consolidated financial statements were issued and effective as of February 28, 2018, the date the Directors approved the consolidated financial statements.

These consolidated financial statements have been prepared using the historical cost convention and on a going concern basis.

c) Changes in accounting policies and disclosure

Standards, amendments and interpretations to existing standards that are not yet effective and have not yet been early adopted by PPL:

IFRS 9, Financial Instruments ("IFRS 9")
IFRS 9, as issued in 2014, introduces new requirements for the classification and measurement of financial instruments, a new expected-loss impairment model that will require more timely recognition of expected credit losses and a substantially reformed model for hedge accounting, with enhanced disclosures about risk management activity. IFRS 9 also removes the volatility in profit or loss that was caused by changes in an entity's own credit risk for liabilities elected to be measured at fair value. IFRS 9 is effective for annual periods beginning on or after January 1, 2018. Earlier application is permitted. PPL has formed a project team and has begun the

process of evaluating the impact of this standard on its consolidated financial statements, specifically the trade and other receivables and notes receivable.

IFRS 15, Revenue from Contracts with Customers ("IFRS 15")
In May 2014, the IASB issued IFRS 15, which covers principles for reporting about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The standard contains a single model that applies to contracts with customers and two approaches to recognizing revenue: at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized. IFRS 15 becomes effective for annual periods beginning on or after January 1, 2018. The new revenue standards may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. PPL is in the final phase of completing its review of the standard to determine the impact on the consolidated financial statements. PPL does not expect the recognition of food sales and royalties to change; however, PPL does expect the recognition of franchise fees to change from point in time to over time with the implementation of the new standard. Additionally, PPL expects to recognize the contributions from franchisees and corresponding costs related to advertising and order processing services on a gross basis in the consolidated statements of income. Under the current standard, franchisee contributions and related costs have been recognized under recoverable franchisee expenses in the consolidated statements of financial position.

IFRS 16, Leases ("IFRS 16")
In January 2016, the IASB has issued IFRS 16, Leases, its new leases standard that requires lessees to recognize assets and liabilities for most leases on their balance sheets. Lessees applying IFRS 16 will have a single accounting model for all leases, with certain exemptions. Lessor accounting is substantially unchanged. The new standard will be effective from January 1, 2019 with limited early application permitted. PPL has formed a project team and has begun the process of evaluating the impact of this standard on its consolidated financial statements.

d) Basis of consolidation

These consolidated financial statements incorporate the assets and liabilities of PPL and its subsidiaries as at December 31, 2017 and January 1, 2017 and the results of these entities for the 52-week periods ended.

PPL consolidates the results of its investments over which it exercises control. Specifically, an investor controls an investee when it has power over the investee, it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is transferred to PPL and deconsolidated from the date that control ceases. Inter-entity transactions, balances and unrealized gains/losses on transactions between entities are eliminated.

Investment in associate

An associate is an entity over which the Company has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

PPL accounts for its 21.1% (January 1, 2017 – 21.1%) share interest in the Pizza Pizza Royalty Limited Partnership (the "Partnership") as an investment in an associate and applies equity accounting whereby PPL's investment is increased by its 21.1% share of income for the period of the Partnership and reduced for distributions received during the Partnership's fiscal period. The Partnership's financial and fiscal periods differ from PPL's, as the Partnership operates on a calendar year-end.

PPL assesses at each period-end whether there is any objective evidence that its interest in the Partnership is impaired. If impaired, the carrying value of PPL's share of the underlying assets of the Partnership is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and the write-down is charged to the consolidated statements of income.

Investments in joint ventures

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

PPL accounts for its 50% (January 1, 2017 – 50%) share interest in the 79 jointly-controlled companies as an investment in a joint venture and applies equity accounting whereby PPL's investment is increased by its 50% share of income for the period of the joint ventures and reduced for distributions received during the joint ventures' fiscal period. The jointly-controlled companies' financial and fiscal periods differ from PPL's, as the joint ventures have a floating year-end of the Saturday immediately preceding July 31.

PPL assesses at each period-end whether there is any objective evidence that its interest in the joint ventures is impaired. If impaired, the carrying value of PPL's share of the underlying assets of the joint ventures is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and the write-down is charged to the consolidated statements of income.

e) Functional and presentation currency

Items included in the consolidated financial statements are measured using the currency of the primary economic environment in which PPL operates (the functional currency). These consolidated financial statements are presented in Canadian dollars, which is PPL's functional and presentation currency.

f) Financial assets and liabilities

A financial asset or liability is recognized if PPL becomes a party to the contractual provisions of the asset or liability. A financial asset or liability is recognized initially (at the trade date) at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the instrument. Financial assets and liabilities carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the consolidated statements of income.

After initial recognition, financial assets are measured at their fair values, except for loans and receivables and held to maturity financial assets, which are measured at amortized cost. After initial recognition, financial liabilities are measured at amortized cost except for financial liabilities at fair value through profit or loss, which are measured at fair value.

PPL classifies its financial assets and liabilities according to their characteristics and management's intentions related thereto for the purposes of ongoing measurement.

Classification choices for financial assets include:

i. Fair value through profit or loss - measured at fair value with changes in fair value recorded in the consolidated statements of income;

ii. Held to maturity - recorded at amortized cost with gains and losses recognized in the consolidated statements of income in the period in which the financial asset is no longer recognized or impaired;

iii. Available for sale - measured at fair value with changes in fair value recognized in other comprehensive Income (loss) for the current period until realized through disposal or impairment; and

iv. Loans and receivables - recorded at amortized cost with gains and losses recognized in profit in the period in which the financial asset is no longer recognized or impaired.

Classification choices for financial liabilities include:

i. Fair value through profit or loss - measured at fair value with changes in fair value recorded in the consolidated statements of income; and

ii. Other financial liabilities - measured at amortized cost with gains and losses recognized in the consolidated statements of income in the period in which the financial liability is no longer recognized.

PPL's financial assets and liabilities are classified and measured as follows:

Assets/liabilities	Category	Measurement
Cash and cash equivalents	Loans and receivables	Amortized cost
Short-term-investment	Loans and receivables	Amortized cost
Trade, other receivables and prepayments	Loans and receivables	Amortized cost
Receivables from jointly-controlled companies	Loans and receivables	Amortized cost
Recoverable franchisee expenses	Loans and receivables	Amortized cost
Notes receivable	Loans and receivables	Amortized cost
Renovation funds	Loans and receivables	Amortized cost
Trade and other payables	Other financial liabilities	Amortized cost
Deposits from franchisees	Other financial liabilities	Amortized cost
Borrowings	Other financial liabilities	Amortized cost
Advances from related party	Other financial liabilities	Amortized cost

Financial assets are derecognized if PPL's contractual rights to the cash flows from the financial assets expire or if PPL transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Financial liabilities are derecognized if PPL's obligations specified in the contract expire or are discharged or cancelled.

g) Impairment of financial assets

PPL assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event) and that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

In the case of financial assets measured at amortized cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The asset's carrying amount is reduced and the amount of the loss is recognized in the consolidated statements of income. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the reversal of the previously recognized impairment is recognized in the consolidated statements of income.

h) Cash and cash equivalents

Cash and cash equivalents consist of cash and short-term deposits with a maturity at acquisition of less than 90 days.

i) Short-term investment

The short-term investment includes amounts invested in a Guaranteed Investment Certificate with a maturity at acquisition between 90 and 365 days.

j) Trade, other receivables and prepayments

Trade and other receivables are amounts due for the sale of goods to franchises and jointly-controlled entities, prepayments, and customer rebate from non-franchisees. If collection is expected in one year or less, they are classified as current assets. If not, they are presented as non-current assets. Trade and other receivables are initially recognized at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment.

k) Inventories

Inventories consist of food, supplies, and construction materials available to be sold to restaurants. Inventories are valued at the lower of cost and net realizable value. Cost is determined on the first-in, first-out basis.

l) Notes receivable

Notes receivable are amounts due from franchisees bearing interest at agreed interest rates. Notes are classified as non-current taking into consideration their nature and management's intention with respect to timing of recovery of these balances.

Notes receivable are initially recognized at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment.

m) Recoverable franchisee expenses

PPL provides advertising and order processing services to Pizza Pizza and Pizza 73 restaurants. Expenses related to the provision of these services are paid by PPL. PPL recovers advertising expenses based on a percentage of individual restaurant sales and order processing service expenses based on the number of orders directed to the restaurant. Recoveries from franchisees are recorded as a reduction of the related expenses. To the extent that expenses recovered exceed or are less than expenses paid by PPL, the difference is recorded as a payable or a receivable, net of any provision for impairment.

In addition to providing advertising and order processing services to Pizza 73 restaurants, PPL also operates two Pizza 73 commissaries. A consulting agreement controls the markup on food sales, which is designed to cover the expenses of the commissary operations. Recoveries are recorded as a reduction of the related expenses. To the extent that expenses recovered exceed or are less than expenses paid by PPL, the difference can be allocated annually to individual restaurants based on a percentage of individual restaurant sales.

n) Property, plant and equipment

Owned assets

Property, plant and equipment are stated at historical cost less accumulated depreciation and impairment losses, if any. Historical cost includes expenditures that are directly attributable to the acquisition or construction of items. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the asset will flow to PPL and the cost can be measured reliably. The carrying amount of any replaced part is derecognized. All other repairs and maintenance are charged to the consolidated statements of income during the period in which they are incurred.

Leased assets

Operating lease payments are recognized as an expense on a straight-line basis over the period of the lease.

Depreciation

Depreciation is calculated on a straight-line or declining balance basis to allocate the cost of the asset, less any residual value, over its estimated useful life. The depreciation method and range of estimated useful lives for each class of property, plant and equipment are as follows:

On the declining balance method -	
Equipment	20%
Furniture and fixtures	20%
Vehicles	30%
On the straight-line method -	
Leasehold improvements	5 years
Computer - software	3 years
- hardware	4 years
Company-owned restaurant assets	5 years

PPL allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant components and depreciates separately each such component. Residual values, method of depreciation and useful lives of items of property, plant and equipment are reviewed annually and adjusted if appropriate.

Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included as part of general and administrative expenses in the consolidated statements of income.

o) Intangible assets

Intangible assets are assets acquired that lack physical substance and that meet the specified criteria for recognition. Intangible assets with a finite life are recorded at cost and are amortized over the period of expected future benefit on the straight-line method:

Lease agreements	10 years
Computer software	3 years

p) Impairment of non-financial assets

The Company assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Company estimates the asset’s recoverable amount. The recoverable amount is the higher of an asset’s fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows. Specifically, assets are grouped at the cash-generating unit (“CGU”) level, namely Pizza Pizza restaurants and Pizza 73 restaurants. In determining fair value less costs to sell, recent market transactions are taken into account, if available. In assessing value in use, the estimated further cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is recognized for the amount by which the asset’s carrying amount exceeds its recoverable amount. Impairment losses are recognized in the consolidated statements of income.

The Company bases its impairment calculation on detailed budgets that are prepared for each of the CGUs and generally cover a period of one year. For longer periods, a long-term growth rate is calculated and applied to project future cash flows after the one-year period.

An assessment is made at each reporting date whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the Company estimates the asset’s recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset’s recoverable amount since the last impairment loss was recognized. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the consolidated statements of income.

q) Renovation funds

PPL maintains a long-term renovation program whereby franchisees contribute towards future restaurant renovations and upgrades. The franchise owner acknowledges that the renovation fund contribution may be used by PPL, without interest or other compensation to the franchise owner, to fund the renovation, expansion or relocation of other Pizza Pizza outlets until such time as the funds are required by the franchise owner for renovation, expansion or relocation of the franchised outlet.

r) Deferred franchise costs

Certain costs related to the construction of new franchised locations are deferred and amortized over the term of the franchise agreement, generally being five years.

s) Income taxes

Income tax expense for the period is comprised of current and deferred tax. Income taxes are recognized in the consolidated statements of income except to the extent it relates to items recognized directly in equity.

Current income taxes

Current income tax expense is based on the income for the period as adjusted for items that are not taxable or not deductible. Current income taxes are calculated using tax rates and tax laws that were substantively enacted at the end of the reporting periods. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. Provisions are established, where appropriate, on the basis of amounts expected to be paid to the tax authorities.

Deferred taxes

Deferred taxes are recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred taxes are determined using tax rates (and tax laws) that have been enacted or substantively enacted by the consolidated statement of financial position dates and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled. The measurement of deferred tax assets and liabilities reflect the tax consequences that would follow from the manner in which PPL expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets are recognized only to the extent that it is probable that future taxable income will be available against which the temporary differences can be utilized.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current taxes and when the deferred tax assets and liabilities relate to income taxes levied by the same taxation authority where there is an intention to settle the balances on a net basis.

t) Trade and other payables

Trade and other payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade and other payables are classified as current liabilities if payment is due within one year or less.

u) Borrowings

Borrowings are initially recognized at fair value net of any financing fees. Borrowings are classified as current liabilities unless PPL has an unconditional right to defer settlement of the liability for more than 12 months. After initial recognition, borrowings are carried at amortized cost with any difference between the proceeds (net of financing fees) and the redemption value recognized in the consolidated statements of income over the period of the borrowing using the effective interest method.

v) Provisions

Provisions represent liabilities to PPL for which the amount or timing is uncertain. Provisions are recognized when PPL has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognized in the consolidated statements of income.

w) Unearned vendor allowances

Unearned vendor allowances relate to an allowance received from a supplier in consideration of the achievement of certain volume commitments. The unearned vendor allowances are being amortized based on the proportion of volume commitments met during each period.

x) Common shares and special voting shares

Common shares and special voting shares are classified as equity. Incremental costs directly attributable to the issuance of new shares are shown in equity as a deduction, net of income taxes, from the proceeds.

y) Revenue recognition

PPL recognizes revenue on the following basis:

- Food sales are recognized when the products are delivered to the franchised and jointly-controlled restaurants. Pizza Pizza franchisees and joint ventures are required to purchase from Pizza Pizza, at an agreed markup on cost, all of the raw materials and supplies used and sold in their Pizza Pizza restaurants. Payment for materials and supplies are due within seven days.
- Company-owned and managed restaurant retail sales are recognized when the services are rendered and the products are sold to the public. Payment by the public is immediate.
- Franchise royalties and administration and accounting fees are recognized as earned and are based on a percentage of the franchisees' sales as provided for in individual franchise agreements. Royalties are due within seven days.
- Initial and renewal franchise fees are recognized at the commencement of the initial term of the franchise agreement and upon the renewal of such an agreement. The initial franchise fee is payable, in full, at the commencement of the agreement and is non-refundable. The renewal fee is charged to franchisees upon renewal of their franchise agreement, which is typically five years from the initial agreement.
- Construction fees are recognized when the costs are incurred. Fees are generated by PPL acting as general contractor as per the franchise agreement.
- Interest and other income is recognized and accrued when earned. Interest income is derived from notes receivable with franchisees and investments in cash equivalents that have maturity dates less than 90 days.

z) Critical accounting estimates and assumptions

PPL makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial period are addressed below:

Impairment of investment in Pizza Pizza Royalty Limited Partnership

PPL, at each period-end, identifies impairment indicators and assesses whether there is any objective evidence that its interest in the Partnership is impaired. If impaired, the carrying value of PPL's share of the underlying assets of the Partnership is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and the write-down is charged to the consolidated statements of income.

The value-in-use calculation requires the Company to estimate the future cash flows expected to arise from the Partnership and a suitable discount rate in order to calculate present value. In measuring future cash flows, PPL makes assumptions about future sales and terminal growth rates that are based on historical experience and expected future performance. Determining the applicable discount rate also involves estimating appropriate adjustments to market risk and PPL specific risk factors. The two most sensitive assumptions are pre-tax discount rates and terminal growth rates.

Impairment of investment in jointly-controlled companies

PPL, at each period-end, identifies impairment indicators and assesses whether there is any objective evidence that its interest in the joint ventures is impaired. If impaired, the carrying value of PPL's share of the underlying assets of the joint ventures is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and charged to the consolidated statements of income.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The value-in-use calculation requires the Company to estimate the future cash flows expected to arise from the CGU and a suitable discount rate in order to calculate present value. In measuring future cash flows, PPL makes assumptions about future sales, tax rates, and terminal growth rates that were based on historical experience and expected future performance. Determining the applicable discount rate also involves estimating appropriate adjustments to market risk and PPL specific risk factors. The two most sensitive assumptions used are pre-tax discount rates and terminal growth rates.

Impairment of non-trade assets

PPL, at each period-end, identifies impairment indicators and assesses whether there is any objective evidence that its non-trade assets are impaired. If impaired, the carrying value of these assets is written down to its estimated recoverable amount, and charged to the consolidated statements of income.

aa) Critical judgments

Consolidation

Determining which entities are to be consolidated by PPL requires judgment on the definition of control. The definition of control under IFRS 10, *Consolidated Financial Statements* ("IFRS 10"), states that an investor controls an investee when it has power over the investee, is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Based on an assessment of the activities of the Partnership and the franchisees, it was concluded that PPL does not control these entities, and therefore shall not consolidate their operations. The Partnership is consolidated by Pizza Pizza Royalty Corp ("PPRC"), formerly Pizza Pizza Royalty Income Fund (the "Fund").

Identification of CGUs

For the purposes of identifying CGUs, assets are grouped at the lowest levels for which there are separately identifiable cash flows. PPL concludes there are interdependencies of cash flows between Pizza 73 restaurants and PPL and therefore, the investment in jointly-controlled Pizza 73 restaurants is considered a single CGU. PPL's assets pertaining to Pizza Pizza operations are classified as a separate CGU.

Sale of Rights and Marks and annual vend-ins

PPL has applied judgment in assessing the application of the revenue recognition accounting policy for the initial sale of Rights and Marks, described in note 14, and the annual vend-ins of restaurants in the Royalty Pool (note 8). In making its assessment, management considered the substance of these transactions and whether the risks and rewards of ownership have been transferred. Based on this assessment, management has determined that revenue relating to the sale will be deferred and amortized as earned and that the subsequent vend-ins will have no impact on PPL. Cash in lieu of vend-ins is considered as proceeds of disposition of the contractual right to an increase in the Exchange Multiplier and is taken to income when due.

3. Trade, Other Receivables and Prepayments

	As at December 31, 2017	As at January 1, 2017
Trade receivables	12,181	12,709
Less: provision for impairment of trade receivables	(715)	(427)
Trade receivables less provision for impairment	11,466	12,282
Prepayments and other receivables	3,493	5,625
Total trade and other receivables	**14,959**	**17,907**

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Movements in the provision for impairment of trade receivables		
Opening balance	427	1,136
Provisions made during the period	454	-
Utilization of the impairment provision	(166)	(709)
Closing balance	**715**	**427**

The establishment and release of the provision for impaired trade receivables have been included within general and administrative expenses in the consolidated statements of income. Amounts charged to the provision are generally written off when there is no expectation of recovering additional cash. The other classes within trade and other receivables do not contain impaired assets and accordingly, no amounts were written off during the period.

4. Recoverable Franchisee Expenses

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Movements in recoverable franchisee expenses		
Opening balance	3,876	9,662
Receipts and contributions	(83,833)	(84,115)
Provision for impairment of recoverable franchisee expenses	(14,606)	(9,850)
Disbursements	95,290	88,179
Closing balance	**727**	**3,876**

5. Property, Plant and Equipment

	Equipment	Furniture and fixtures	Vehicles	Leasehold improvements	Computer hardware and software	Company-owned restaurant assets	Total
52-week period ended December 31, 2017							
Opening net book value	1,642	44	16	679	943	8,536	11,860
Additions	671	18	-	492	198	4,098	5,477
Disposals	(22)	-	(2)	-	-	(286)	(310)
Depreciation charge	(450)	(9)	(3)	(293)	(389)	(2,723)	(3,867)
Closing net book value	**1,841**	**53**	**11**	**878**	**752**	**9,625**	**13,160**
Cost	15,628	1,142	489	10,353	14,761	26,577	68,950
Accumulated depreciation	(13,787)	(1,089)	(478)	(9,475)	(14,009)	(16,952)	(55,790)
Net book value	**1,841**	**53**	**11**	**878**	**752**	**9,625**	**13,160**

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

	Equipment	Furniture and fixtures	Vehicles	Leasehold improvements	Computer hardware and software	Company-owned restaurant assets	Total
52-week period ended January 1, 2017							
Opening net book value	1,742	55	28	754	511	5,384	8,474
Additions	270	-	-	213	792	6,056	7,331
Disposals	(10)	-	(5)	-	-	(1,078)	(1,093)
Depreciation charge	(360)	(11)	(7)	(288)	(360)	(1,826)	(2,852)
Closing net book value	**1,642**	**44**	**16**	**679**	**943**	**8,536**	**11,860**
Cost	14,979	1,124	491	9,862	14,562	22,841	63,859
Accumulated depreciation	(13,337)	(1,080)	(475)	(9,183)	(13,619)	(14,305)	(51,999)
Net book value	**1,642**	**44**	**16**	**679**	**943**	**8,536**	**11,860**

Depreciation in the amount of $572 (52-week period ended January 1, 2017 - $388) for the 52-week period ended December 31, 2017 has been recovered from franchisees. Accumulated depreciation of $76 on disposals (January 1, 2017 - $704) has been removed from accumulated depreciation on property plant and equipment as at January 1, 2017.

6. Notes Receivable

	As at December 31, 2017	As at January 1, 2017
From franchisees, bearing interest from 5% to 9% (January 1, 2017 – 5% to 9%)	9,365	8,859
From franchisees, non-interest bearing	4,753	6,995
Less: provision for impairment of notes receivable	(862)	(1,013)
Total notes receivable	**13,256**	**14,841**

The notes receivable from franchisees are unsecured and are repayable in varying monthly principal amounts. The effective interest rate on the notes receivable as at December 31, 2017 is 6.6% (January 1, 2017 – 6.4%).

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Movements in the provision for impairment of notes receivable		
Opening balance	1,013	1,156
Provisions made during the period	-	431
Utilization of the impairment provision	(151)	(574)
Closing balance	**862**	**1,013**

7. Renovation Funds

The renovation funds are non-interest bearing and are collected from franchisees on a monthly basis at amounts based on a percentage of sales.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

8. Investment in Pizza Pizza Royalty Limited Partnership

a) PPL owns Class B and Class D Partnership Units that are exchangeable for PPRC shares based on the Exchange Multiplier applicable at the exchange date and represent an effective 21.1% interest in the Partnership as at December 31, 2017 (January 1, 2017 – 21.1%).

The table below reconciles the balance of PPL's investment in the Partnership, which is accounted for using equity accounting.

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Balance – beginning of period	23,648	23,562
Equity income of the Partnership	6,952	6,531
Distributions received from Partnership	(6,963)	(6,585)
Share of Partnership other comprehensive income	240	140
Balance – end of period	**23,877**	**23,648**

The business of the Partnership is the ownership and licensing of the Pizza Pizza and Pizza 73 Rights and Marks through two separate Licence and Royalty Agreements with PPL. Additionally, the Partnership will collect the royalty payable under each Licence and Royalty Agreement as well as perform the administration of PPRC pursuant to the Administration Agreement.

A breakdown of the Partnership's aggregated assets, liabilities, revenue and profit is as follows:

	As at December 31, 2017	As at December 31, 2016
Total assets	348,597	345,045
Total liabilities	77,295	80,133

	For the 52-week period ended December 31, 2017	For the 52-week period ended December 31, 2016
Revenue	35,614	35,333
Profit for the period	34,037	33,790

b) 2016 Royalty Pool Adjustment – Class B Exchange Multiplier

In early January 2017, adjustments to royalty payments and PPL's Class B Exchange Multiplier were made based on the actual performance of the 24 new restaurants added to the Royalty Pool on January 1, 2016. As a result of the adjustments, the new Class B Exchange Multiplier is 1.819988 and Class B Units can be exchanged for 4,564,964 shares, which is an increase of 5,422 shares, effective January 1, 2016.

c) 2016 Royalty Pool Adjustment – Class D Exchange Multiplier

In early January 2017, adjustments to royalty payments and PPL's Class D Exchange Multiplier were made based on the actual performance of the two Pizza 73 restaurants added to the Royalty Pool on January 1, 2016. As a result of the adjustments, the new Class D Exchange Multiplier is 17.52620 and Class D Units can be exchanged for 1,752,620 shares, which is an increase of 9,313 shares, effective January 1, 2016.

d) 2017 Royalty Pool Adjustment – Class B Exchange Multiplier

On January 1, 2017, 15 net Pizza Pizza restaurants were added to the Royalty Pool as a result of 23 new restaurants opening and eight closing from January 1, 2016 to December 31, 2016. The additional system sales from the 23 new restaurants are estimated at $7,674 annually less sales of $873 from eight permanently closed Pizza Pizza restaurants resulting in net estimated Pizza Pizza sales of $6,801 added to the Royalty Pool. The total number of Pizza Pizza restaurants in the Royalty Pool has increased to 651. The yield of the shares was determined to be 5.16% calculated using $16.43 as a weighted average share price. Weighted average share price is calculated based on the market price of the shares traded on the Toronto Stock Exchange during the period of twenty consecutive days ending on the fifth trading day before January 1, 2017. As a result of the contribution of the additional net sales to the Royalty Pool, the Class B Exchange Multiplier increased fractionally by 80% of the total adjustment or 0.110643; the new Class B Exchange Multiplier is 1.930631. This adjustment will also increase the entitlement of the holders of the Class B Units to distributions of cash and allocations of income from the Partnership. The second adjustment to the Class B Exchange Multiplier will be adjusted to be effective January 1, 2017, once the actual performance of the new restaurants is determined in early 2018. Please refer to note 27 for further details.

e) 2017 Royalty Pool Adjustment – Class D Exchange Multiplier

On January 1, 2017, the Pizza 73 Royalty Pool remained unchanged as a result of four new restaurants opening between September 2, 2015 and September 1, 2016 and four restaurants closing between January 1, 2016 and December 31, 2016. The forecasted additional system sales from the four new restaurants are estimated at $1,226 annually less $179 in system sales attributable to the four closed Pizza 73 restaurants resulting in net estimated Pizza 73 sales of $1,047 added to the Royalty Pool. The net estimated sales were further reduced by $2,086 in system sales attributable to certain restaurants previously added to the Royalty Pool whose territory adjusted a previously existing restaurant, resulting in a negative Pizza 73 Estimated Determined Amount. As per the Pizza Pizza Royalty Limited Partnership agreement, whenever the Estimated Determined Amount is negative it shall be deemed to be zero. Accordingly, the Class D Exchange Multiplier remained unchanged at 17.52620. Once the actual performance of the new restaurants is determined in early 2018, the Class D Exchange Multiplier may be adjusted to be effective January 1, 2017. Please refer to note 27 for further details. The total number of Pizza 73 restaurants in the Royalty Pool remains at 100 for 2017.

f) PPRC Outstanding Shares

In exchange for adding the forecasted Pizza Pizza system sales to the Royalty Pool, PPL has received 277,519 additional equivalent shares (through the change to the Class B Exchange Multiplier). These represent 80% of the forecasted equivalent shares entitlement to be received (346,899 equivalent shares represent 100%), with the final equivalent shares entitlement to be determined when the new restaurants' 2017 actual sales performance is known with certainty in early 2018.

PPL's Class D equivalent share entitlement is unchanged for 2017. In any year that the forecasted system sales (less closed restaurants sales and other adjustments) is negative, as was the case with the Class D equivalent share entitlement calculation for 2017, no increase or decrease in the Exchange Multiplier is made. PPL will only have a Class D equivalent share entitlement for 2017 if the actual sales performance of the four new Pizza 73 restaurants, less the sales of adjustment restaurants, significantly exceeds forecasted system sales and yields net, positive sales when the actual sales performance is known with certainty in early 2018.

After giving effect to PPL's entitlement to additional equivalent shares as at January 1, 2017, PPL owns equivalent shares representing 21.1% of the Partnership's fully diluted shares.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The chart below shows the Shares that would be outstanding if all of PPL's Class B and D Units of the Partnership were converted to Shares after accounting for their respective multipliers.

Shares outstanding and issuable on December 31, 2017		
Shares outstanding		24,618,392
Class B equivalent Shares held by PPL as at December 31, 2016	4,559,542	
PPL additional Class B equivalent shares - True-up Holdback as at December 31, 2016	5,422	
Additional PPL Class B equivalent shares as at January 1, 2017	277,519	4,842,483
Class D equivalent Shares held by PPL as at December 31, 2016	1,743,307	
PPL additional Class D equivalent shares - True-up Holdback as at December 31, 2016	9,313	
Additional PPL Class D equivalent shares as at January 1, 2017	-	1,752,620
Number of fully diluted shares		31,213,495
PPL's proportion of all shares outstanding and available for exchange		21.1%

9. Investment in Jointly-controlled Companies

Jointly-controlled companies are joint ventures, consisting of PPL's 50% interest in 79 Pizza 73 restaurants (January 1, 2017 – 75 Pizza 73 restaurants). Jointly-controlled restaurants are companies, owned and operated as an independent business, equally owned by PPL and an Owner/Operator. Licensing, consulting and other agreements govern the relationship of PPL and the Owner/Operator as shareholders of these jointly-controlled restaurants, and establish a framework under which each restaurant is operated.
The financial statements of all jointly-controlled companies have a floating year-end of the Saturday immediately preceding July 31 and all operations are continuing.

The table below reconciles the balance of PPL's investment in the jointly-controlled companies, which is accounted for using equity accounting.

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Balance – beginning of period	19,235	18,937
Equity income from jointly-controlled companies	4,871	5,382
Dividends received from jointly-controlled companies	(5,177)	(5,084)
Balance – end of period	**18,929**	**19,235**

A breakdown of PPL's share in jointly-controlled companies' comprehensive income is as follows:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Revenue	40,684	41,103
Expenses	(35,813)	(35,721)
Income for the period after income taxes	**4,871**	**5,382**

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

10. Intangible Assets

	Lease agreements	Computer software	Total
52-week period ended December 31, 2017			
Opening net book value	89	41	130
Additions	-	3,891	3,891
Amortization charge	(89)	(41)	(130)
Closing net book value	**-**	**3,891**	**3,891**
As at December 31, 2017			
Cost	1,600	5,873	7,473
Accumulated amortization	(1,600)	(1,982)	(3,582)
Net book value	**-**	**3,891**	**3,891**
52-week period ended January 1, 2017			
Opening net book value	248	205	453
Additions	-	-	-
Amortization charge	(159)	(164)	(323)
Closing net book value	**89**	**41**	**130**
As at January 1, 2017			
Cost	1,600	1,982	3,582
Accumulated amortization	(1,511)	(1,941)	(3,452)
Net book value	**89**	**41**	**130**

Amortization in the amount of $40 (52-week period ended January 1, 2017 - $164) for the 52-week period ended December 31, 2017 has been recovered from franchisees.

11. Trade and Other Payables

	As at December 31, 2017	As at January 1, 2017
Trade payables	27,798	24,542
Accruals	12,152	6,206
Sales tax payable	7,409	8,790
Other payables	5,337	4,020
Total trade and other payables	**52,696**	**43,558**

Sales Tax Payable

PPL collects provincial sales tax and federal goods and services tax on behalf of certain franchised restaurants in addition to the collection of tax on its own account. These accounts are included in trade and other payables above as follows:

	As at December 31, 2017	As at January 1, 2017
Sales tax disbursed in PPL’s operations	205	237
Sales tax collected on behalf of certain franchised restaurants	7,204	8,553
Total sales tax payable	**7,409**	**8,790**

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

12. Borrowings

	As at December 31, 2017	As at January 1, 2017
Notes payable, bearing interest from 5.2% to 7.4%, repayable in varying monthly principal amounts, maturing between 2018 and 2021. These notes were secured by specific company-owned restaurant assets. The effective interest rate as at December 31, 2017 was 5.87% (January 1, 2017 – 6.5%).	1,034	1,317
	1,034	**1,317**
Less: current portion	(474)	(570)
Total non-current borrowings	**560**	**747**

13. Provisions

The provision for onerous leases represents the liability for the leased premises that are either vacant or subleased at a lower rate. The provision is made for the losses to be incurred over the remaining term period of the lease.

Future outflows may differ if the Company is able to franchise, sublease or terminate the lease before the expiry of the agreement.

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Movements in the provision for onerous leases		
Opening balance	489	934
Arising during the period	1,270	118
Reversals	(52)	(97)
Utilized during the period	(466)	(541)
Imputed interest	88	75
Closing balance	**1,328**	**489**

Reversals in the period relate to leases that were franchised, subleased or terminated during the period.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

14. Deferred Gain

The deferred gain arose following the sale of the Pizza Pizza Rights and Marks to the Partnership following the initial public offering of the Fund. Concurrent with the sale, PPL entered into a 99-year License and Royalty Agreement with the Partnership, whereby PPL has the right to use the Rights and Marks and pays a royalty equal to 6% of the total system sales of restaurants in the Royalty Pool. The deferred gain is being amortized on a straight-line basis over the term of the License and Royalty Agreement.

The movement in the deferred gain balance during each period is as follows:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Balance – beginning of period	203,879	206,209
Amortization for the period	(2,330)	(2,330)
Balance – end of period	**201,549**	**203,879**

A summary of the deferred gain and accumulated amortization at the end of each period is as follows:

	As at December 31, 2017	As at January 1, 2017
Deferred gain	230,675	230,675
Accumulated amortization	(29,126)	(26,796)
Balance – end of period	**201,549**	**203,879**

15. Income Taxes

The components of the income tax (expense) recovery are as follows:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Current income tax recovery (expense)	1,524	5,290
Deferred tax recovery (expense)	3,663	(981)
Income tax recovery (expense)	**5,187**	**4,309**

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The reconciliation to the statutory tax rate is as follows:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Income (loss) for the period before income taxes	(11,382)	(1,053)
Combined Canadian federal and provincial rates	26.59%	26.59%
Computed expected income tax recovery (expense)	**3,026**	**280**
Non-taxable portion of capital gain	-	20
Effect of income taxable at lower rates	-	200
Equity income from jointly-controlled companies	1,295	1,431
Prior year dividend refund booked in current year	-	333
Rate differential	813	2,090
Permanent adjustments	(52)	(44)
Other	105	(1)
Income tax recovery (expense)	**5,187**	**4,309**

The deferred tax asset arises as a result of the temporary difference between the accounting and tax basis on the Rights and Marks, deferred financing fees and cash flow hedge as shown below.

	As at December 31, 2017	As at January 1, 2017
Property, plant and equipment	(1,136)	(933)
Intangible assets	12	(21)
Pizza Pizza Royalty Limited Partnership	(8,528)	(8,266)
Deferred gain	53,572	54,191
Donations	34	31
Provisions and other	353	130
Non-capital losses carried forward	4,021	-
Ontario Corporate Minimum Tax	491	-
Share of cash flow hedge of Partnership	(9)	47
Employee benefits	381	292
Deferred tax asset	**49,191**	**45,471**

16. Commitments and contingencies

Commitments

Future minimum lease payments for premises, sponsorships and vehicles to related parties, which are companies under common control, and non-related entities, are as follows:

	Third parties	Related parties
Not later than 1 year	37,849	2,747
Later than 1 year and no later than 5 years	98,218	4,582
Later than 5 years	26,299	1,114

During the 52-week period ended December 31, 2017, lease payments of approximately $30,322 (52-week period ended January 1, 2017 - $24,882) were recovered under sublease agreements with various franchised restaurants. These recoveries are offset against rent expense.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The amounts receivable under future committed subleases are as follows:

	Third parties	Related parties
Not later than 1 year	32,297	-
Later than 1 year and no later than 5 years	89,322	-
Later than 5 years	26,287	-

Contingencies

PPL is a party to various legal proceedings, mainly related to claims brought against it by former franchisees. It is not possible at this time to determine the outcome of these proceedings and, accordingly, no provisions have been made in these consolidated financial statements.

PPL has entered into an agreement with certain lenders to establish a line of credit of $33,730 (January 1, 2017 – $33,730) for the purpose of providing certain equipment and leasehold improvement loans to its franchisees. As security under these lines of credit facilities, PPL has provided certain guarantees as described in the agreement including a letter of credit in the amount of $3,373 (January 1, 2017 – $3,373). PPL has the right to increase the limit under these credit facilities by providing additional letters of credit.

As security for repayment of a borrowing facility held by the Partnership to the amount of $47,000, PPL has granted a continuing, general security interest, subject to certain exceptions, in all present and acquired property of PPL, which may not be assigned without the prior consent of PPL. With respect to the Partnership's borrowing facility, PPL must comply with certain financial covenants. As at December 31, 2017, PPL was in compliance with these financial covenants.

17. Common Shares and Special Voting Shares

	As at December 31, 2017	As at January 1, 2017
Authorized without limit as to number -		
Common shares (with no par value)		
Special voting shares, non-participating, entitling the holder to one vote per share (with no par value)		
Issued and paid -		
100 common shares	100	100
100,000 special voting shares	100	100
Total common shares and special voting shares	**200**	**200**

18. Capital Disclosures

PPL's objectives when managing capital are to safeguard PPL's ability to continue as a going concern so that it can continue to provide returns for the shareholder and benefits for other stakeholders and to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk.

PPL evaluates its capital as all components of shareholders' deficiency, other than amounts in accumulated other comprehensive loss related to PPL's share of the Partnership's cash flow hedge.

PPL sets the amount of capital in proportion to risk. PPL manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, PPL may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, or sell assets to reduce debt.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

19. Food Sales

Food sales include the following:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Food sales	172,803	173,343
Company-owned restaurant sales	15,211	15,879
Total food sales	**188,014**	**189,222**

20. Royalties, Franchise Fees and Other Revenue

Royalties, franchise fees and other revenue include the following:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Royalties	25,205	24,475
Initial and renewal franchise fees	1,764	1,661
Construction fees	1,109	1,204
Administration and accounting fees	2,739	2,764
Total royalties, franchise fees and other revenue	**30,817**	**30,104**

21. Expenses by Nature

The following table summarizes significant general and administrative expenses:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Depreciation of property, plant and equipment	3,305	2,464
Amortization of intangible assets	89	159
Operating lease payments	3,302	3,015
Provision for recoverable franchisee expenses	14,606	9,850
Employee benefit expense	17,976	16,996

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

22. Related Party Transactions

The following table summarizes PPL's transactions with related parties in the normal course of business:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Rent expense(i)	2,589	2,601
Food purchases(i)	11,817	12,526
Recovery of expenses(i)	600	600
Administration and accounting fee revenue(ii)	2,739	2,764

(i) Transactions with commonly controlled companies
(ii) Transactions with jointly-controlled companies

As at December 31, 2017, PPL has trade payables of $935 (as at January 1, 2017 - $930) payable to a company under common management control. As at December 31, 2017, trade and other payables includes amounts payable of $2,519 (as at January 1, 2017 - $3,498) to the Partnership, which were paid subsequent to the end of the period.

In addition, PPL has the following advances to and from related parties:

	As at December 31, 2017	As at January 1, 2017
Receivables from jointly-controlled companies	3,275	2,702
Advances from related party	(16,261)	(17,452)

Advances from related party are due to the parent company. Advances from related party and receivables from jointly-controlled companies are non-interest bearing, have no specified terms of repayment and are unsecured. The related party has waived the right to demand repayment prior to January 1, 2019. Accordingly, the advances from related party have been classified as long-term.

Key management compensation

The compensation expense or amounts payable to management, including officers and directors, is shown below:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Salaries and other short-term employee benefits	3,343	3,716
Other long-term benefits	226	188
Total key management compensation	**3,569**	**3,904**

23. Segmented Information

Operating segments are defined as components of an enterprise about which discrete separate financial information is available and which is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The chief operating decision maker is the Chief Executive Officer and Director. The operations of Pizza Pizza consist of two reportable segments; Pizza Pizza and Pizza 73. While they both operate in the pizza QSR segment, they are in predominantly different geographic markets in Canada. Pizza Pizza operates mainly in the Ontario and Quebec (Eastern Canada) pizza QSR segment, whereas Pizza 73 operates mainly in the Alberta (Western Canada) pizza QSR segment. In addition, the return on Pizza Pizza's investment in the Partnership is included in the Pizza Pizza segment. The eliminations column represents adjustments required to reconcile PPL's segmented reporting, to the reporting on the consolidated statements of financial position and the consolidated statements of income. This column represents adjustments required to account for joint ventures under IFRS 11.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

For the 52-week period ended December 31, 2017	Eastern	Western	Eliminations	Total
Food sales	188,014	40,647	(40,647)	188,014
Royalties, franchise fees and other revenue	27,503	3,314	-	30,817
Interest and other income	1,186	37	(37)	1,186
Cost of food sales	150,998	16,374	(16,374)	150,998
General and administrative expenses	56,925	20,793	(18,736)	58,982
Equity income from jointly-controlled companies	-	-	4,871	4,871
Interest on borrowings	35	7	(7)	35
Income (loss) for the period before income taxes	(9,858)	4,043	(5,567)	(11,382)
Segment income (loss) for the period	(4,671)	3,347	(4,871)	(6,195)
Additions to property, plant and equipment	5,307	1,541	(1,371)	5,477

As at December 31, 2017	Eastern	Western	Eliminations	Total
Total assets	141,270	37,111	(3,333)	175,048
Intangible assets	3,891	-	-	3,891

For the 52-week period ended January 1, 2017	Eastern	Western	Eliminations	Total
Food sales	189,063	41,153	(40,994)	189,222
Royalties, franchise fees and other revenue	27,287	2,817	-	30,104
Interest and other income	1,120	367	(61)	1,426
Cost of food sales	152,134	15,039	(14,973)	152,200
General and administrative expenses	46,800	19,689	(17,699)	48,790
Equity income from jointly-controlled companies	-	-	5,382	5,382
Interest on borrowings	56	8	(8)	56
Income (loss) for the period before income taxes	259	4,890	(6,202)	(1,053)
Segment income (loss) for the period	4,567	4,071	(5,382)	3,256
Additions to property, plant and equipment	7,302	428	(399)	7,331

As at January 1, 2017	Eastern	Western	Eliminations	Total
Total assets	149,524	30,531	(3,108)	176,947
Intangible assets	41	89	-	130

24. Statements of Cash Flows Information

Changes in non-cash working capital are as follows:

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Trade and other receivables	2,948	(5,219)
Inventories	443	(120)
Income taxes recoverable	3,544	(5,017)
Receivables from jointly-controlled companies	(573)	(1,520)
Recoverable franchisee expenses	3,149	5,786
Trade and other payables	8,774	68
Income taxes payable	-	(7,651)
Deposits from franchisees	(2,071)	116
	16,214	(13,557)

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

	For the 52-week period ended December 31, 2017	For the 52-week period ended January 1, 2017
Interest paid	35	57
Income taxes paid	-	7,843

25. Financial Risk Management

PPL's objective is to minimize risk with respect to financial instruments by monitoring the performance of its franchisees and jointly-controlled companies, maintaining restaurants in different geographic regions and having the ability to assume the operations of franchisees for inadequate financial performance and/or default under the franchise agreement.

Fair Values

The carrying amounts of cash and cash equivalents, trade, other receivables and prepayments and trade and other payables approximate fair values given the short-term maturity of these instruments and are Level 3 instruments.

A reasonable estimate of fair value could not be made for receivables from jointly-controlled companies, advances from related party, recoverable franchisee expenses, renovation funds and deposits from franchisees as there are no fixed terms of repayment.

The fair value of the non-current notes receivable is based on the estimated future discounted cash flows using a comparable market rate of interest as at December 31, 2017 of 6.58% (January 1, 2017 – 6.4%).

The fair value of the borrowings is based on the estimated future discounted cash flows using a comparable market rate of interest as at December 31, 2017 of prime plus a spread varying by loan (January 1, 2017 - prime plus a spread varying by loan). The Company has no plans to prepay these instruments prior to maturity. The fair value of the borrowings was determined using Level 2 inputs, which are observable inputs or inputs that can be corroborated by observable market data for substantially the full term of the asset or liability.

The carrying value and fair value of PPL's financial instruments are as follows:

		As at December 31, 2017		As at January 1, 2017	
	Category	**Carrying value**	**Fair value**	**Carrying value**	**Fair value**
Cash and cash equivalents	L&R	12,758	12,758	13,024	13,024
Trade and other receivables	L&R	14,959	14,959	17,907	17,907
Notes receivable	L&R	13,256	12,379	14,841	13,891
Trade and other payables	OFL	52,696	52,696	43,558	43,558
Borrowings	OFL	1,034	930	1,317	1,167

Financial instruments category guide:

L&R Loans and receivables
OFL Other financial liabilities

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The different fair value hierarchy levels are as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical financial assets or financial liabilities;
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the financial asset or financial liability, either directly or indirectly; and
- Level 3: Inputs for the financial asset or financial liability that are not based on observable market data.

Credit Risk

PPL is exposed to credit risk as all of the franchisees and jointly-controlled companies operate within the same segment: commercial food service. PPL is also exposed to credit risk in the event of non-payment by its franchisees and jointly-controlled companies of its trade receivables, recoverable franchisee expenses, notes receivable, receivables from jointly-controlled companies and renovation funds receivable. PPL's credit risk is mitigated by the large number of franchisees and jointly-controlled companies operating in different geographical markets and by PPL's ultimate ability to assume operations of the franchisees if there is inadequate financial performance and/or default under the franchisee agreement.

PPL writes off receivable accounts, including trade receivables, notes receivable and renovation funds, to expected realizable value as soon as the account is determined not to be fully collectible, with such write-offs charged to income (loss), unless the loss has been provided for in prior periods, in which case the write-off is applied to reduce the provision for impairment of those receivables. PPL updates its estimate of the provision for impairment of receivables, based on a customer-by-customer evaluation of the collectability of receivable balances as at each consolidated statements of financial position reporting date, taking into account amounts that are past due, and any available information indicating that a customer could be experiencing liquidity or going concern problems. A reconciliation of the provision for impairment of trade, other receivables and prepayments is shown in note 3 and a reconciliation of the provision for notes receivable is shown in note 6.

The aging of trade receivable balances that are past due, but not impaired are as follows:

	As at December 31, 2017	As at January 1, 2017
Past due 0-30 days	880	1,069
Past due 31-120 days	837	719
Total trade receivables past due, but not impaired	**1,717**	**1,788**

Liquidity Risk

PPL is subject to liquidity risk with respect to the items outlined in the table below. The risk is mitigated as the majority of PPL's revenue is earned from franchisees and jointly-controlled companies, which have agreements with PPL and whose activities are closely monitored by PPL. In the case of franchisees, the majority of PPL's business, PPL is able to assume operations of the franchises if there is inadequate financial performance and/or default under the franchise agreement. Liquidity requirements are monitored by PPL's head office functions in order to guarantee effective access to financial resources.

Management believes that currently available funds and credit facilities, apart from those that will be generated by operating and financing activities, will allow PPL to satisfy its requirements for investment, working capital management, and borrowing repayment at maturity.

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The following are the contractual undiscounted cash flows of financial liabilities as at December 31, 2017:

	Carrying amount	0 to 12 months	1 to 2 years	2 to 5 years	More than 5 years
Trade and other payables	52,696	52,696	-	-	-
Deposits from franchisees	415	415	-	-	-
Borrowings	1,034	474	327	67	166
Advances from related party	16,261	-	16,261	-	-

Interest Rate Risk

PPL is exposed to interest rate risk from its borrowings. All borrowings are based on floating interest rates.

26. Seasonality

Historically, PPL's system sales experience a decrease in the first calendar quarter when compared to the fourth quarter, which has historically been the strongest quarter.

27. Subsequent Events

The chart below shows PPRC shares that would be outstanding if all of the Class B and Class D Units held by PPL were converted to PPRC shares after accounting for their respective multipliers and adjustments as described below.

Shares outstanding & issuable on January 1, 2018		
Shares outstanding		24,618,392
Class B equivalent Shares held by PPL at December 31, 2017	4,842,483	
PPL additional Class B equivalent Shares - True-up Holdback as at December 31, 2017	175,727	
Additional PPL Class B equivalent Shares as of January 1, 2018	-	5,018,210
Class D equivalent Shares held by PPL at December 31, 2017	1,752,620	
PPL additional Class D equivalent Shares - True-up Holdback as at December 31, 2017	-	
Additional PPL Class D equivalent Shares as of January 1, 2018	276,781	2,029,401
Number of fully diluted shares		31,666,003
PPL's proportion of all shares outstanding and available for exchange		22.3%

a. 2017 Royalty Pool Adjustment

In early January 2018, adjustments to royalty payments and PPL's Class B Exchange Multiplier were made based on the actual performance of the 23 new restaurants added to the Royalty Pool on January 1, 2017. As a result of the adjustments, the new Class B Exchange Multiplier is 2.000691 and Class B Units can be exchanged for 5,018,210 shares, which is an increase of 175,727 shares, effective January 1, 2017.

In early January 2018, adjustments to royalty payments and PPL's Class D Exchange Multiplier were made based on the actual performance of the four Pizza 73 restaurants added to the Royalty Pool on January 1, 2017. As a result of the adjustments, the new Class D Exchange Multiplier remains unchanged at 17.52620 and Class D Units can be exchanged for 1,752,620 shares effective January 1, 2017.

b. 2018 Royalty Pool Adjustment – Class B Exchange Multiplier

On January 1, 2018, one net Pizza Pizza restaurant was added to the Royalty Pool as a result of 17 new restaurants opening and 16 closing from January 1, 2017 to December 31, 2017. The total number of Pizza Pizza restaurants in the Royalty Pool has increased to 652. The additional system sales from the 17 new restaurants are estimated at $3,860 annually, less sales of $3,861 from 16 permanently closed Pizza Pizza restaurants, resulting in the Estimated Determined Amount being ($1). As per the Pizza Pizza Royalty Limited Partnership agreement, whenever the Estimated Determined Amount is negative it shall be deemed to be zero. Accordingly, the Class B Exchange Multiplier remained unchanged at 2.000691. The second adjustment to the Class B Exchange Multiplier will be adjusted to be effective January 1, 2018, once the actual performance of the new restaurants is determined in early 2019.

c. 2018 Royalty Pool Adjustment – Class D Exchange Multiplier

On January 1, 2018, six, net Pizza 73 restaurants were added to the Royalty Pool as a result of eight new restaurants opening between September 2, 2016 and September 1, 2017 and two restaurants closing between January 1, 2017 and December 31, 2017. The forecasted additional system sales from the eight new restaurants are estimated at $4,836 annually, less $260 in system sales attributable to the two closed Pizza 73 restaurants, resulting in net estimated Pizza 73 sales of $4,576 added to the Royalty Pool. The total number of Pizza 73 restaurants in the Royalty Pool has increased to 106. The yield of the shares was determined to be 5.39% calculated using $15.88 as a weighted average share price. Weighted average share price is calculated based on the market price of the shares traded on the Toronto Stock Exchange during the period of twenty consecutive days ending on the fifth trading day before January 1, 2018. As a result of the contribution of the additional net sales to the Royalty Pool, the Class D Exchange Multiplier increased fractionally by 80% of the total adjustment or 2.76781; the new Class D Multiplier is 20.29401. This adjustment will also increase the entitlement of the holders of the Class D units to distributions of cash and allocations of income from the Partnership. The second adjustment to the Class D Exchange Multiplier will be adjusted to be effective January 1, 2018, once the actual performance of the new restaurants is determined in early 2019.

d. Pizza Pizza Royalty Corp. Outstanding Shares

PPL's Class B equivalent Share entitlement is unchanged for 2018, due to the fact that, in any year that the forecasted system sales (less closed restaurants sales and other adjustments) is negative, as was the case with the Class B equivalent Share entitlement calculation for 2018, no increase or decrease in the Exchange Multiplier is made. PPL will only have a Class B equivalent Share entitlement for 2018 if the actual sales performance of the 17 new Pizza Pizza restaurants, significantly exceeds forecasted system sales and yields net, positive sales which will be determined in early 2019.

In exchange for adding the forecasted Pizza 73 system sales to the Royalty Pool, PPL has received 276,781 additional equivalent Shares (through the change to the Class D Exchange Multiplier). These represent 80% of the forecasted equivalent Shares entitlement to be received (345,977 equivalent Shares represent 100%), with the final equivalent Shares entitlement to be determined when the new restaurants' 2018 actual sales performance is known with certainty in early 2019.

After giving effect to PPL's entitlement to additional equivalent Shares at January 1, 2018, PPL owns equivalent Shares representing 22.3% of PPRC's fully diluted shares.