Texas Roadhouse, Inc.
Form 10-Q
November 03, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 26, 2017

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 000-50972

Texas Roadhouse, Inc.

(Exact name of registrant specified in its charter)

Delaware	20-1083890
(State or other jurisdiction of	(IRS Employer

incorporation or organization) Identification Number)

6040 Dutchmans Lane, Suite 200

Louisville, Kentucky 40205

(Address of principal executive offices) (Zip Code)

(502) 426-9984

(Registrant's telephone number, including area code)

Indicate by check mark whether 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 Regulations S-T 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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	Accelerated filer	Non-accelerated filer	Smaller reporting company
(Do not check if a smaller reporting company)			Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The number of shares of common stock outstanding were 71,106,215 on October 25, 2017.

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PART I — FINANCIAL INFORMATION

ITEM 1 — FINANCIAL STATEMENTS

Texas Roadhouse, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(in thousands, except share and per share data)

(unaudited)

	September 26, 2017	December 27, 2016
Assets		
Current assets:		
Cash and cash equivalents	$ 114,436	$ 112,944
Receivables, net of allowance for doubtful accounts of $52 at September 26, 2017 and $33 at December 27, 2016	24,979	56,127
Inventories, net	15,453	16,088
Prepaid income taxes	—	954
Prepaid expenses	10,461	12,150
Deferred tax assets, net	—	1,996
Total current assets	165,329	200,259
Property and equipment, net of accumulated depreciation of $512,061 at September 26, 2017 and $457,102 at December 27, 2016	886,972	830,054
Goodwill	121,040	116,571
Intangible assets, net of accumulated amortization of $12,445 at September 26, 2017 and $11,753 at December 27, 2016	2,930	3,622
Other assets	36,448	29,465
Total assets	$ 1,212,719	$ 1,179,971
Liabilities and Stockholders’ Equity		
Current liabilities:		
Current maturities of long-term debt and obligation under capital lease	$ 9	$ 167
Accounts payable	48,979	50,789
Deferred revenue-gift cards	70,648	129,558
Accrued wages	29,580	26,039
Income taxes payable	8,581	—
Accrued taxes and licenses	23,483	19,698
Dividends payable	14,931	13,418
Other accrued liabilities	42,058	39,858
Total current liabilities	238,269	279,527

Long-term debt and obligation under capital lease, excluding current maturities	51,984	52,381
Stock option and other deposits	7,549	7,491
Deferred rent	40,261	36,103
Deferred tax liabilities, net	4,707	12,268
Other liabilities	39,157	33,959
Total liabilities	381,927	421,729
Texas Roadhouse, Inc. and subsidiaries stockholders' equity:		
Preferred stock ($0.001 par value, 1,000,000 shares authorized; no shares issued or outstanding)	—	—
Common stock ($0.001 par value, 100,000,000 shares authorized, 71,101,654 and 70,619,737 shares issued and outstanding at September 26, 2017 and December 27, 2016, respectively)	71	71
Additional paid-in-capital	229,909	219,626
Retained earnings	588,826	530,723
Accumulated other comprehensive loss	(63)	(194)
Total Texas Roadhouse, Inc. and subsidiaries stockholders' equity	818,743	750,226
Noncontrolling interests	12,049	8,016
Total equity	830,792	758,242
Total liabilities and equity	$ 1,212,719	$ 1,179,971

See accompanying notes to condensed consolidated financial statements.

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Texas Roadhouse, Inc. and Subsidiaries

Condensed Consolidated Statements of Income and Comprehensive Income

(in thousands, except per share data)

(unaudited)

	13 Weeks Ended		39 Weeks Ended	
	September 26, 2017	September 27, 2016	September 26, 2017	September 27, 2016
Revenue:				
Restaurant sales	$ 536,341	$ 477,617	$ 1,661,821	$ 1,493,531
Franchise royalties and fees	4,166	4,020	12,634	12,473
Total revenue	540,507	481,637	1,674,455	1,506,004
Costs and expenses:				
Restaurant operating costs (excluding depreciation and amortization shown separately below):				
Cost of sales	176,498	161,886	545,862	506,565
Labor	169,355	145,301	514,287	442,861
Rent	11,257	10,266	33,238	30,477
Other operating	83,679	73,583	254,176	227,082
Pre-opening	4,548	5,017	14,302	14,253
Depreciation and amortization	23,534	20,941	69,236	60,718
Impairment and closure	2	13	13	54
General and administrative	26,123	26,162	94,594	82,933
Total costs and expenses	494,996	443,169	1,525,708	1,364,943
Income from operations	45,511	38,468	148,747	141,061
Interest expense, net	500	288	1,211	902
Equity income from investments in unconsolidated affiliates	(359)	(4)	(1,149)	(831)
Income before taxes	45,370	38,184	$ 148,685	$ 140,990
Provision for income taxes	13,046	11,381	41,159	42,325
Net income including noncontrolling interests	32,324	26,803	$ 107,526	$ 98,665
Less: Net income attributable to noncontrolling interests	1,310	1,128	4,618	3,792
Net income attributable to Texas Roadhouse, Inc. and subsidiaries	$ 31,014	$ 25,675	$ 102,908	$ 94,873
Other comprehensive income (loss), net of tax:				
Unrealized gain on derivatives, net of tax of ($-), ($-), ($-) and ($18), respectively	—	—	—	27
Foreign currency translation adjustment, net of tax of ($55), ($18), ($82) and $7, respectively	88	29	131	(11)
Total other comprehensive income, net of tax	88	29	131	16
Total comprehensive income	$ 31,102	$ 25,704	$ 103,039	$ 94,889

Net income per common share attributable to Texas Roadhouse, Inc. and subsidiaries:				
Basic	$ 0.44	$ 0.36	$ 1.45	$ 1.35
Diluted	$ 0.43	$ 0.36	$ 1.44	$ 1.34
Weighted average shares outstanding:				
Basic	71,067	70,477	70,939	70,338
Diluted	71,532	70,981	71,449	70,898
Cash dividends declared per share	$ 0.21	$ 0.19	$ 0.63	$ 0.57

See accompanying notes to condensed consolidated financial statements.

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Texas Roadhouse, Inc. and Subsidiaries

Condensed Consolidated Statement of Stockholders' Equity

(in thousands, except share and per share data)

(unaudited)

	Shares	Par Value	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Texas Roadhouse, Inc. and Subsidiaries	Noncontrolling Interests	Total
Balance, December 27, 2016	70,619,737	$ 71	$ 219,626	$ 530,723	$ (194)	$ 750,226	$ 8,016	$ 758,242
Net income	—	—	—	102,908	—	102,908	4,618	107,526
Other comprehensive income, net	—	—	—	—	131	131	—	131
Noncontrolling interests contribution	—	—	—	—	—	—	3,457	3,457
Distributions to noncontrolling interest holders	—	—	—	—	—	—	(4,042)	(4,042)
Dividends declared and paid ($0.42 per share)	—	—	—	(29,805)	—	(29,805)	—	(29,805)
Dividends declared ($0.21 per share)	—	—	—	(14,931)	—	(14,931)	—	(14,931)
Shares issued under share-based compensation plans	701,827	1	1,484	—	—	1,485	—	1,485
Indirect repurchase of shares for minimum tax withholdings	(219,910)	(1)	(10,096)	—	—	(10,097)	—	(10,097)
Cumulative effect of change in accounting	—	—	69	(69)	—	—	—	—

principle								
Share-based compensation	—	—	18,826	—	—	18,826	—	18,826
Balance, September 26, 2017	71,101,654	$ 71	$ 229,909	$ 588,826	$ (63)	$ 818,743	$ 12,049	$ 830,792

See accompanying notes to condensed consolidated financial statements.

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Texas Roadhouse, Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	39 Weeks Ended September 26, 2017	September 27, 2016
Cash flows from operating activities:		
Net income including noncontrolling interests	$ 107,526	$ 98,665
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	69,236	60,718
Deferred income taxes	(5,647)	(3,270)
Loss on disposition of assets	3,490	3,509
Impairment and closure costs	—	139
Equity income from investments in unconsolidated affiliates	(1,149)	(831)
Distributions of income received from investments in unconsolidated affiliates	585	1,765
Provision for doubtful accounts	19	9
Share-based compensation expense	18,826	18,347
Changes in operating working capital:		
Receivables	31,129	23,373
Inventories	805	1,276
Prepaid expenses	1,689	1,985
Other assets	(5,729)	(3,003)
Accounts payable	(3,162)	(9,352)
Deferred revenue—gift cards	(59,302)	(46,146)
Accrued wages	3,541	(8,471)
Excess tax benefits from share-based compensation	—	(2,698)
Prepaid income taxes and income taxes payable	9,535	9,760
Accrued taxes and licenses	3,785	1,698
Other accrued liabilities	3,536	5,594
Deferred rent	4,158	3,412
Other liabilities	5,199	3,303
Net cash provided by operating activities	188,070	159,782
Cash flows from investing activities:		
Capital expenditures—property and equipment	(117,037)	(113,219)
Acquisition of franchise restaurants, net of cash acquired	(16,528)	—
Net cash used in investing activities	(133,565)	(113,219)
Cash flows from financing activities:		
Proceeds from revolving credit facility, net	—	25,000
Debt issuance costs	(476)	—
Proceeds from noncontrolling interest contribution	3,457	—
Repurchase of shares of common stock	—	(4,110)

Distributions to noncontrolling interest holders	(4,042)	(3,538)
Excess tax benefits from share-based compensation	—	2,698
Proceeds from stock option and other deposits, net	438	283
Indirect repurchase of shares for minimum tax withholdings	(10,097)	(7,927)
Principal payments on long-term debt and capital lease obligation	(555)	(106)
Proceeds from exercise of stock options	1,485	2,172
Dividends paid to shareholders	(43,223)	(38,656)
Net cash used in financing activities	(53,013)	(24,184)
Net increase in cash and cash equivalents	1,492	22,379
Cash and cash equivalents—beginning of period	112,944	59,334
Cash and cash equivalents—end of period	$ 114,436	$ 81,713
Supplemental disclosures of cash flow information:		
Interest paid, net of amounts capitalized	$ 948	$ 201
Income taxes paid	$ 37,271	$ 35,849
Capital expenditures included in current liabilities	$ 5,470	$ 3,189

See accompanying notes to condensed consolidated financial statements.

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Texas Roadhouse, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements

(tabular amounts in thousands, except share and per share data)

(unaudited)

(1) Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Texas Roadhouse, Inc. ("TRI"), our wholly-owned subsidiaries and subsidiaries in which we have a controlling interest (collectively the "Company," "we," "our" and/or "us") as of September 26, 2017 and December 27, 2016 and for the 13 and 39 weeks ended September 26, 2017 and September 27, 2016.

As of September 26, 2017, we owned and operated 455 restaurants and franchised an additional 85 restaurants in 49 states and six foreign countries. Of the 455 company-owned restaurants that were operating at September 26, 2017, 437 were wholly-owned and 18 were majority-owned.

As of September 27, 2016, we owned and operated 422 restaurants and franchised an additional 85 restaurants in 49 states and five foreign countries. Of the 422 company-owned restaurants that were operating at September 27, 2016, 406 were wholly-owned and 16 were majority-owned.

As of September 26, 2017 and September 27, 2016, we owned 5.0% to 10.0% equity interest in 24 franchise restaurants. Additionally, as of September 26, 2017 and September 27, 2016, we owned a 40% equity interest in four non-Texas Roadhouse restaurants as part of a joint venture agreement with a casual dining restaurant operator in China. The unconsolidated restaurants are accounted for using the equity method. Our investments in these unconsolidated affiliates are included in Other assets in our unaudited condensed consolidated balance sheets, and we record our percentage share of net income earned by these unconsolidated affiliates in our unaudited condensed consolidated statements of income and comprehensive income under Equity income from investments in unconsolidated affiliates. All significant intercompany balances and transactions for these unconsolidated restaurants as well as the entities whose accounts have been consolidated have been eliminated.

We have made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the unaudited condensed consolidated financial statements and the reporting of revenue and expenses during the periods to prepare these unaudited condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles ("GAAP"). Significant items subject to such estimates and assumptions include the carrying amounts of property and equipment and goodwill, obligations related to insurance reserves, leases and leasehold improvements, legal reserves, gift card discounts and breakage and income taxes. Actual results could differ from those estimates.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, necessary to present fairly our consolidated financial position, results of operations and cash flows for the periods presented. The unaudited condensed consolidated financial statements have been prepared in accordance with GAAP, except that certain information and footnotes have been condensed or omitted pursuant to rules and regulations of the Securities and Exchange Commission ("SEC"). Operating results for the 13 and 39 weeks ended September 26, 2017 are not necessarily indicative of the results that may be expected for the year ending December 26, 2017. The unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 27, 2016.

Our significant interim accounting policies include the recognition of income taxes using an estimated annual effective tax rate.

(2) Share-based Compensation

On May 16, 2013, our stockholders approved the Texas Roadhouse, Inc. 2013 Long-Term Incentive Plan (the "Plan"). The Plan provides for the granting of incentive and non-qualified stock options to purchase shares of common

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stock, stock appreciation rights, and full value awards, including restricted stock, restricted stock units ("RSUs"), deferred stock units, performance stock and performance stock units ("PSUs"). This Plan replaced the Texas Roadhouse, Inc. 2004 Equity Incentive Plan.

The following table summarizes the share-based compensation expense recorded in the accompanying unaudited condensed consolidated statements of income and comprehensive income:

	13 Weeks Ended		39 Weeks Ended	
	September 26, 2017	September 27, 2016	September 26, 2017	September 27, 2016
Labor expense	$ 1,822	$ 1,570	$ 5,255	$ 4,475
General and administrative expense	4,639	5,074	13,571	13,872
Total share-based compensation expense	$ 6,461	$ 6,644	$ 18,826	$ 18,347

Effective December 28, 2016, we adopted Accounting Standards Update No. 2016-09, Compensation – Stock Compensation ("ASU 2016-09") which amends and simplifies the accounting for stock compensation. As a result of the adoption of ASU 2016-09, we made a change in our accounting for forfeitures to record as they occur and, as a result, we recorded a $0.1 million cumulative-effect reduction to retained earnings under the modified retrospective approach. We elected prospective transition for the requirement to classify excess tax benefits as an operating activity in the consolidated statement of cash flows. No prior periods have been adjusted. Additionally, as a result of the new guidance requirements, on a prospective basis, all excess tax benefits and tax deficiencies are recognized within the income tax provision in the consolidated statements of income and comprehensive income in the period in which the restricted shares vest or options are exercised. See note 4 for further discussion.

Beginning in 2008, we changed the method by which we provide share-based compensation to our employees by granting RSUs as a form of share-based compensation. Prior to 2008, we issued stock options as share-based compensation to our employees. Beginning in 2015, we began granting PSUs to two of our executives. An RSU is the conditional right to receive one share of common stock upon satisfaction of the vesting requirement. A PSU is the conditional right to receive one share of common stock upon meeting defined performance obligations along with the satisfaction of the vesting requirement. Share-based compensation activity by type of grant as of September 26, 2017 and changes during the 39 weeks then ended are presented below.

Summary Details for RSUs

	Shares	Weighted-Average Grant Date Fair Value	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Outstanding at December 27, 2016	919,463	$ 37.06		
Granted	349,049	46.70		
Forfeited	(35,041)	37.40		
Vested	(404,505)	38.14		
Outstanding at September 26, 2017	828,966	$ 40.57	1.2	$ 39,991

As of September 26, 2017, with respect to unvested RSUs, there was $17.4 million of unrecognized compensation cost that is expected to be recognized over a weighted-average period of 1.2 years. The vesting terms of the RSUs range from 1.0 to 5.0 years. The total intrinsic value of RSUs vested during the 39 weeks ended September 26, 2017 and September 27, 2016 was $18.8 million and $17.4 million, respectively. The excess tax benefit, which was recognized within the income tax provision, associated with vested RSUs was $1.2 million for the 39 weeks ended September 26, 2017. The excess tax benefit associated with vested RSUs for the 39 weeks ended September 27, 2016 was $1.2 million which was recorded in additional paid-in-capital in the unaudited condensed consolidated balance sheets.

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Summary Details for PSUs

In 2015 and 2016, we granted PSUs to two of our executives subject to an approximate one-year vesting term and the achievement of certain earnings targets, which determine the number of units to vest at the end of the vesting period. Share-based compensation is recognized for the number of units expected to vest at the end of the period and is expensed beginning on the grant date and through the performance period. For each grant, PSUs vest after meeting the performance and service conditions.

On November 19, 2015, we granted PSUs with a grant date fair value of approximately $3.9 million based on a grant date price per share of $34.11. On January 8, 2017, 188,237 shares vested related to this PSU grant and were distributed during the 13 weeks ended March 28, 2017. On November 9, 2016, we granted PSUs with a grant date fair value of approximately $4.6 million based on a grant date price per share of $39.88. As of September 26, 2017, with respect to unvested PSUs, there was $1.1 million of unrecognized compensation cost that is expected to be recognized over a weighted-average period of three months. Any distribution of vested PSUs as common stock related to the November 9, 2016 grants will occur in the first quarter of 2018. For the 39 weeks ended September 26, 2017, the excess tax benefit, recognized within the income tax provision, associated with vested PSUs was $0.8 million.

Summary Details for Stock Options

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Outstanding at December 27, 2016	118,073	$ 13.57		
Granted	—	—		
Cancelled/Expired	(2,836)	15.47		
Exercised	(109,085)	13.61		
Outstanding at September 26, 2017	6,152	$ 11.93	0.1	$ 223
Exercisable at September 26, 2017	6,152	$ 11.93	0.1	$ 223

No stock options vested during the 39 weeks ended September 26, 2017 or September 27, 2016. For the 39 weeks ended September 26, 2017 and September 27, 2016, the total intrinsic value of options exercised was $3.7 million and $5.3 million, respectively.

For the 39 weeks ended September 26, 2017 and September 27, 2016, cash received before tax withholdings from options exercised was $1.5 million and $2.2 million, respectively. The excess tax benefit, recognized within the income tax provision, associated with options exercised was $1.0 million for the 39 weeks ended September 26, 2017. The excess tax benefit for the 39 weeks ended September 27, 2016 was $1.5 million which was recorded in additional paid-in-capital in the unaudited condensed consolidated balance sheets.

(3) Long-term Debt and Obligation Under Capital Lease

Long-term debt consisted of the following:

	September 26, 2017	December 27, 2016
Installment loan	$ —	$ 550
Obligation under capital lease	1,993	1,998
Revolver	50,000	50,000
	51,993	52,548
Less current maturities	9	167
	$ 51,984	$ 52,381

The interest rate for our installment loan outstanding at December 27, 2016 was 10.46%. The installment loan was repaid during the 13 weeks ended September 26, 2017.

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During the 52 weeks ended December 27, 2016, we amended an existing lease at one restaurant location to acquire additional square footage. As a result of this amendment, the lease qualified as a capital lease.

On August 7, 2017, we entered into the Amended and Restated Credit Agreement (the "Amended Credit Agreement") with respect to our revolving credit facility with a syndicate of commercial lenders led by JPMorgan Chase Bank, N.A., PNC Bank, N.A., and Wells Fargo Bank, N.A. The revolving credit facility remains an unsecured, revolving credit agreement under which we may borrow up to $200.0 million with the option to increase the revolving credit facility by an additional $200.0 million subject to certain limitations. The Amended Credit Agreement extends the maturity date of our revolving credit facility until August 5, 2022.

The terms of the Amended Credit Agreement require us to pay interest on outstanding borrowings at the London Interbank Offered Rate ("LIBOR") plus a margin of 0.875% to 1.875% and to pay a commitment fee of 0.125% to 0.30% per year on any unused portion of the revolving credit facility, in each case depending on our leverage ratio, or the Alternate Base Rate, which is the highest of the issuing banks' prime lending rate, the Federal Funds rate plus 0.50% or the Adjusted Eurodollar Rate for a one month interest period on such day plus 1.0%. The weighted-average interest rate for the revolving credit facility as of September 26, 2017 and December 27, 2016 was 2.11% and 1.57%, respectively. As of September 26, 2017, we had $50.0 million outstanding under the revolving credit facility and $142.9 million of availability, net of $7.1 million of outstanding letters of credit.

The lenders' obligation to extend credit pursuant to the Amended Credit Agreement depends on us maintaining certain financial covenants, including a minimum consolidated fixed charge coverage ratio of 2.00 to 1.00 and a maximum consolidated leverage ratio of 3.00 to 1.00. The Amended Credit Agreement permits us to incur additional secured or unsecured indebtedness outside the revolving credit facility, except for the incurrence of secured indebtedness that in the aggregate is equal to or greater than $125.0 million and 20% of our consolidated tangible net worth. We were in compliance with all financial covenants as of September 26, 2017.

(4) Income Taxes

A reconciliation of the statutory federal income tax rate to our effective tax rate for the 13 and 39 weeks ended September 26, 2017 and September 27, 2016 is as follows:

	13 Weeks Ended				39 Weeks Ended			
	September 26, 2017		September 27, 2016		September 26, 2017		September 27, 2016	
Tax at statutory federal rate	35.0	%	35.0	%	35.0	%	35.0	%
State and local tax, net of federal benefit	3.4		3.5		3.4		3.5	
FICA tip tax credit	(7.1)		(7.1)		(7.1)		(6.9)	
Work opportunity tax credit	(0.9)		(0.9)		(0.8)		(0.8)	
Stock compensation	(0.9)		—		(2.0)		—	
Net income attributable to noncontrolling interests	(1.1)		(1.1)		(1.1)		(0.9)	
Other	0.4		0.4		0.3		0.1	
Total	28.8	%	29.8	%	27.7	%	30.0	%

As a result of the adoption of ASU 2016-09, excess tax benefits and tax deficiencies from share-based compensation are recognized within the income tax provision in the period in which the restricted shares vest or options are exercised. During the 13 weeks ended September 26, 2017, we recognized \$0.4 million as an income tax benefit, which resulted in a 0.9% impact on the tax rate. During the 39 weeks ended September 26, 2017, we recognized \$3.0 million as an income tax benefit, which resulted in a 2.0% impact on the tax rate. Prior to the adoption of ASU 2016-09, excess tax benefits and deficiencies were recognized in additional paid-in capital in the unaudited condensed consolidated balance sheets.

During the first quarter of 2017, we adopted ASU 2015-17, Balance Sheet Classification of Deferred Taxes, which required deferred tax assets and liabilities to be classified as noncurrent on our condensed consolidated balance sheets. We adopted ASU 2015-17 on a prospective basis.

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(5)Commitments and Contingencies

The estimated cost of completing capital project commitments at September 26, 2017 and December 27, 2016 was approximately $150.6 million and $157.5 million, respectively.

As of September 26, 2017 and December 27, 2016, we were contingently liable for $15.8 million and $16.4 million, respectively, for seven lease guarantees, listed in the table below. These amounts represent the maximum potential liability of future payments under the guarantees. In the event of default, the indemnity and default clauses in our assignment agreements govern our ability to pursue and recover damages incurred. No material liabilities have been recorded as of September 26, 2017 and December 27, 2016 as the likelihood of default was deemed to be less than probable and the fair value of the guarantees is not considered significant.

	Lease Assignment Date	Current Lease Term Expiration
Everett, Massachusetts (1)(2)	September 2002	February 2023
Longmont, Colorado (1)	October 2003	May 2019
Montgomeryville, Pennsylvania (1)	October 2004	March 2021
Fargo, North Dakota (1)(2)	February 2006	July 2021
Logan, Utah (1)	January 2009	August 2019
Irving, Texas (3)	December 2013	December 2019
Louisville, Kentucky (3)(4)	December 2013	November 2023

(1) Real estate lease agreements for restaurant locations which we entered into before granting franchise rights to those restaurants. We have subsequently assigned the leases to the franchisees, but remain contingently liable under the terms of the lease if the franchisee defaults.
(2) As discussed in note 7, these restaurants are owned, in whole or part, by certain officers, directors and 5% shareholders of the Company.
(3) Leases associated with non-Texas Roadhouse restaurants which were sold. The leases were assigned to the acquirer, but we remain contingently liable under the terms of the lease if the acquirer defaults.
(4) We may be released from liability after the initial contractual lease term expiration contingent upon certain conditions being met by the acquirer.

During the 13 and 39 weeks ended September 26, 2017, we bought most of our beef from three suppliers. Although there are a limited number of beef suppliers, we believe that other suppliers could provide a similar product on comparable terms. A change in suppliers, however, could cause supply shortages and/or higher costs to secure adequate supplies and a possible loss of sales, which would affect operating results adversely. We have no material minimum purchase commitments with our vendors that extend beyond a year.

We and the U.S. Equal Employment Opportunity Commission entered into a consent decree dated March 31, 2017 (the "Consent Decree") to settle the lawsuit styled Equal Employment Opportunity Commission v. Texas Roadhouse, Inc., Texas Roadhouse Holdings LLC and Texas Roadhouse Management Corp. in the United States District Court, District of Massachusetts, Civil Action Number 1:11-cv-11732 (the "Lawsuit"). The Consent Decree resolves the issues litigated in the Lawsuit. Under the Consent Decree, among other terms, we have established a fund of $12.0 million, from which awards of monetary relief, allocated as wages for tax purposes, may be made to eligible claimants in accordance with procedures set forth in the Consent Decree. We recorded a pre-tax charge of $14.9 million ($9.2 million after-tax) related to the Lawsuit and Consent Decree. The pre-tax charge includes $12.6 million of costs associated with the legal settlement and $2.3 million of legal fees associated with the defense of the case during the 13 weeks ended March 28, 2017. The pre-tax charge was recorded in general and administrative expense in our unaudited condensed consolidated statements of income and comprehensive income.

Occasionally, we are a defendant in litigation arising in the ordinary course of our business, including "slip and fall" accidents, employment related claims, claims related to our service of alcohol, and claims from guests or employees alleging illness, injury or food quality, health or operational concerns. None of these types of litigation, most of which are covered by insurance, has had a material effect on us and, as of the date of this report, we are not party to any litigation that we believe could have a material adverse effect on our business.

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(6) Acquisitions

On December 28, 2016, we acquired four franchise restaurants in Florida and Georgia. Pursuant to the terms of the acquisition agreements, we paid a total purchase price of $16.5 million, net of cash acquired. Two of the acquired restaurants are wholly-owned and the remaining two restaurants are majority-owned. These acquisitions are consistent with our long-term strategy to increase net income and earnings per share.

These transactions were accounted for using the purchase method as defined in ASC 805, Business Combinations ("ASC 805"). Based on a purchase price of $16.5 million, $4.5 million of goodwill was generated by the acquisition, which is not amortizable for book purposes, but is deductible for tax purposes.

The purchase price has been allocated as follows:

Current assets	$ 170
Property and equipment	12,281
Goodwill	4,469
Current liabilities	(392)
	$ 16,528

Pro forma results of operations and revenue and earnings for the 39 weeks ended September 26, 2017 have not been presented because the effect of the acquisitions was not material to our consolidated financial position, results of operations or cash flows.

(7) Related Party Transactions

As of September 26, 2017 and September 27, 2016, we had 10 franchise restaurants owned in whole or part, by certain officers, directors and 5% stockholders of the Company. For both 13 week periods ended September 26, 2017 and September 27, 2016, these entities paid us fees of approximately $0.5 million. For the 39 week periods ended September 26, 2017 and September 27, 2016, these entities paid us fees of approximately $1.6 million and $1.5 million, respectively. As disclosed in note 5, we are contingently liable on leases which are related to two of these restaurants.

(8) Earnings Per Share

The share and net income per share data for all periods presented are based on the historical weighted-average shares outstanding. The diluted earnings per share calculations show the effect of the weighted-average stock options and RSUs outstanding from our equity incentive plans as discussed in note 2.

For both 13 week periods ended September 26, 2017 and September 27, 2016, there were no shares of nonvested stock that were outstanding, but not included in the computation of diluted earnings per share because their inclusion would have had an anti-dilutive effect. For the 39 week periods ended September 26, 2017 and September 27, 2016, there were 7,960 and six shares of nonvested stock, respectively, that had an anti-dilutive effect. For all periods presented, there were no outstanding options that had an anti-dilutive effect.

PSUs are not included in the diluted earnings per share calculation until the performance-based criteria have been met. See note 2 for further discussion of PSUs.

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The following table sets forth the calculation of earnings per share and weighted-average shares outstanding (in thousands) as presented in the accompanying unaudited condensed consolidated statements of income and comprehensive income:

	13 Weeks Ended		39 Weeks Ended	
	September 26, 2017	September 27, 2016	September 26, 2017	September 27, 2016
Net income attributable to Texas Roadhouse, Inc. and subsidiaries	$ 31,014	$ 25,675	$ 102,908	$ 94,873
Basic EPS:				
Weighted-average common shares outstanding	71,067	70,477	70,939	70,338
Basic EPS	$ 0.44	$ 0.36	$ 1.45	$ 1.35
Diluted EPS:				
Weighted-average common shares outstanding	71,067	70,477	70,939	70,338
Dilutive effect of stock options and nonvested stock	465	504	510	560
Shares-diluted	71,532	70,981	71,449	70,898
Diluted EPS	$ 0.43	$ 0.36	$ 1.44	$ 1.34

(9) Fair Value Measurements

ASC 820, Fair Value Measurements and Disclosures ("ASC 820"), establishes a framework for measuring fair value and expands disclosures about fair value measurements. ASC 820 establishes a three-level hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs in measuring fair value. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability on the measurement date.

Level 1Inputs based on quoted prices in active markets for identical assets.

Level 2Inputs other than quoted prices included within Level 1 that are observable for the assets, either directly or indirectly.

Level 3Inputs that are unobservable for the asset.

There were no transfers among levels within the fair value hierarchy during the 13 and 39 weeks ended September 26, 2017.

The following table presents the fair values for our financial assets and liabilities measured on a recurring basis:

	Fair Value Measurements		
	Level	September 26, 2017	December 27, 2016
Deferred compensation plan—assets	1	$ 26,966	$ 21,951
Deferred compensation plan—liabilities	1	(26,980)	(22,128)

The Second Amended and Restated Deferred Compensation Plan of Texas Roadhouse Management Corp., as amended, (the "Deferred Compensation Plan") is a nonqualified deferred compensation plan which allows highly compensated employees to defer receipt of a portion of their compensation and contribute such amounts to one or more investment funds held in a rabbi trust. We report the amounts of the rabbi trust in other assets and the corresponding liability in other liabilities in our unaudited condensed consolidated financial statements. These investments are considered trading securities and are reported at fair value based on quoted market prices. The realized and unrealized holding gains and losses related to these investments, as well as the offsetting compensation expense, are recorded in general and administrative expense in the unaudited condensed consolidated statements of income and comprehensive income.

At September 26, 2017 and December 27, 2016, the fair values of cash and cash equivalents, accounts receivable and accounts payable approximated their carrying values based on the short-term nature of these instruments. The fair value of our revolving credit facility at September 26, 2017 and December 27, 2016 approximated its carrying value since it is a variable rate credit facility (Level 2).

(10) Stock Repurchase Program

On May 22, 2014, our Board of Directors approved a stock repurchase program under which we may repurchase up to $100.0 million of our common stock. This stock repurchase program has no expiration date and replaced a previous stock repurchase program which was approved on February 16, 2012. All repurchases to date under our stock repurchase program have been made through open market transactions. The timing and the amount of any repurchases will be determined by management under parameters established by our Board of Directors, based on an evaluation of our stock price, market conditions and other corporate considerations.

We did not repurchase any shares of common stock during the 13 and 39 week periods ended September 26, 2017. As of September 26, 2017, we had approximately $69.9 million remaining under our authorized stock repurchase program. For the 13 week period ended September 27, 2016, we did not repurchase any shares of common stock. For the 39 week period ended September 27, 2016, we paid approximately $4.1 million to repurchase 114,700 shares of our common stock.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CAUTIONARY STATEMENT

This report contains forward-looking statements based on our current expectations, estimates and projections about our industry and certain assumptions made by us. Words such as "anticipates," "expects," "intends," "plans," "believes," "seeks," "estimates," "may," "will" and variations of these words or similar expressions are intended to identify forward-looking statements. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances, including any underlying assumptions, are forward-looking statements. Such statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to predict. Therefore, our actual results could differ materially and adversely from those expressed in any forward-looking statements as a result of various factors. The section entitled "Risk Factors" in our Annual Report on Form 10-K for the year ended December 27, 2016, in Part II, Item 1A in this Form 10-Q and disclosures in our other Securities and Exchange Commission ("SEC") filings discuss some of the important risk factors that may affect our business, results of operations, or financial condition. You should carefully consider those risks, in addition to the other information in this report, and in our other filings with the SEC, before deciding to invest in our Company or to maintain or increase your investment. We undertake no obligation to revise or update publicly any forward-looking statements for any reason. The information contained in this Form 10-Q is not a complete description of our business or the risks associated with an investment in our common stock. We urge you to carefully review and consider the various disclosures made by us in this report and in our other reports filed with the SEC that discuss our business in greater detail and advise interested parties of certain risks, uncertainties and other factors that may affect our business, results of operations or financial condition.

OVERVIEW

Texas Roadhouse, Inc. is a growing restaurant company operating predominately in the casual dining segment. Our founder, chairman and chief executive officer ("CEO"), W. Kent Taylor, started the business in 1993 with the opening of the first Texas Roadhouse restaurant in Clarksville, Indiana. Since then, we have grown to 540 company and franchise restaurants in 49 states and six foreign countries. Our mission statement is "Legendary Food, Legendary Service®." Our operating strategy is designed to position each of our restaurants as the local hometown favorite for a broad segment of consumers seeking high quality, affordable meals served with friendly, attentive service. As of September 26, 2017, our 540 restaurants included:

- 455 "company restaurants," of which 437 were wholly-owned and 18 were majority-owned. The results of operations of company restaurants are included in our unaudited condensed consolidated statements of income and comprehensive income. The portion of income attributable to noncontrolling interests in company restaurants that are not wholly-owned is reflected in the line item entitled "Net income attributable to noncontrolling interests" in our unaudited condensed consolidated statements of income and comprehensive income. Of the 455 restaurants we owned and operated as of September 26, 2017, we operated 433 as Texas Roadhouse restaurants and operated 20 as Bubba's 33 restaurants. In addition, we operated two restaurants outside of the casual dining segment.

· 85 "franchise restaurants," 24 of which we have a 5.0% to 10.0% ownership interest. The income derived from our minority interests in these 24 franchise restaurants is reported in the line item entitled "Equity income from investments in unconsolidated affiliates" in our unaudited condensed consolidated statements of income and comprehensive income. Additionally, we provide various management services to these franchise restaurants, as well as six additional franchise restaurants in which we have no ownership interest. All of the franchise restaurants operated as Texas Roadhouse restaurants.

We have contractual arrangements which grant us the right to acquire at pre-determined formulas the remaining equity interests in 16 of the 18 majority-owned company restaurants and 66 of the franchise restaurants.

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Throughout this report, we use the term "restaurants" to include Texas Roadhouse and Bubba's 33, unless otherwise noted.

Presentation of Financial and Operating Data

Throughout this report, the 13 weeks ended September 26, 2017 and September 27, 2016 are referred to as Q3 2017 and Q3 2016, respectively. The 39 weeks ended September 26, 2017 and September 27, 2016 are referred to as 2017 YTD and 2016 YTD, respectively.

Long-term Strategies to Grow Earnings Per Share and Create Shareholder Value

Our long-term strategies with respect to increasing net income and earnings per share, along with creating shareholder value, include the following:

Expanding Our Restaurant Base. We will continue to evaluate opportunities to develop restaurants in existing markets and in new domestic and international markets. Domestically, we will remain focused primarily on markets where we believe a significant demand for our restaurants exists because of population size, income levels and the presence of shopping and entertainment centers and a significant employment base. Our ability to expand our restaurant base is influenced by many factors beyond our control and, therefore, we may not be able to achieve our anticipated growth.

In 2017 YTD, we opened 20 company restaurants while our franchise partners opened three restaurants. We currently plan to open 26 or 27 company restaurants in 2017 including four Bubba's 33 restaurants. In addition, we anticipate that our existing franchise partners will open as many as five, primarily international, Texas Roadhouse restaurants during 2017.

Our average capital investment for the 21 Texas Roadhouse restaurants opened during 2016, including pre opening expenses and a capitalized rent factor, was $5.0 million. We expect our average capital investment for Texas Roadhouse restaurants opening in 2017 to be approximately $5.2 million. For 2016, the average capital investment, including pre-opening expenses and a capitalized rent factor, for the nine Bubba's 33 restaurants opened during the year was $6.6 million. We expect our average capital investment for Bubba's 33 restaurants opened in 2017 to be approximately $6.1 million.

We remain focused on driving sales and managing restaurant investment costs to maintain our restaurant development in the future. Our capital investment (including cash and non-cash costs) for new restaurants varies significantly depending on a number of factors including, but not limited to: the square footage, layout, scope of required site work, type of construction labor (union or non-union), local permitting requirements, our ability to negotiate with landlords, cost of liquor and other licenses and hook-up fees and geographical location.

We may, at our discretion, add franchise restaurants, domestically and/or internationally, primarily with franchisees who have demonstrated prior success with Texas Roadhouse or other restaurant concepts and in markets in which the franchisee demonstrates superior knowledge of the demographics and restaurant operating conditions. In conjunction with this strategy, we signed our first international franchise development agreement in 2010 for the development of Texas Roadhouse restaurants in eight countries in the Middle East over a 10-year period. In 2015, we amended our agreement in the Middle East to add one country to the territory. In addition to the Middle East, we currently have signed franchise development agreements for the development of Texas Roadhouse restaurants in Taiwan, the Philippines, Mexico and China. We currently have 10 restaurants open in four countries in the Middle East, three restaurants open in Taiwan and two in the Philippines for a total of 15 restaurants in six foreign countries. Additionally, in 2010, we entered into a joint venture agreement with a casual dining restaurant operator in China for a minority ownership in four non Texas Roadhouse restaurants, all of which are currently open. We continue to explore opportunities in other countries for international expansion. We may also look to acquire domestic franchise restaurants under terms favorable to us and our stockholders. In Q1 2017, we acquired four franchise restaurants located in Florida and Georgia for an aggregate purchase price of $16.5 million. Additionally, from time to time, we will evaluate potential mergers, acquisitions, joint ventures or other strategic initiatives to acquire or develop additional concepts domestically and/or internationally.

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Maintaining and/or Improving Restaurant Level Profitability. We plan to maintain, or possibly increase, restaurant-level profitability (restaurant margin) through a combination of increased comparable restaurant sales and operating cost management. In general, we continue to balance the impacts of inflationary pressures with our value positioning as we remain focused on our long-term success. This may create a challenge in terms of maintaining and/or increasing restaurant margin, as a percentage of restaurant sales, in any given year, depending on the level of inflation we experience. In addition to restaurant margin, as a percentage of restaurant sales, we also focus on the growth of restaurant margin dollars per store week as a measure of restaurant-level profitability. In terms of driving higher guest traffic counts, we remain focused on encouraging repeat visits by our guests and attracting new guests through our continued commitment to operational standards relating to food and service quality. To attract new guests and increase the frequency of visits of our existing guests, we also continue to drive various localized marketing programs, focus on speed of service and increase throughput by adding seats in certain restaurants.

Leveraging Our Scalable Infrastructure. To support our growth, we continue to make investments in our infrastructure. Over the past several years, we have made significant investments in our infrastructure, including information and accounting systems, real estate, human resources, legal, marketing, international and restaurant operations, including the development of new concepts. Our goal is for general and administrative costs to increase at a slower growth rate than our revenue. Whether we can leverage our infrastructure in future years will depend, in part, on our new restaurant openings, our comparable restaurant sales growth rate going forward and the level of investment we continue to make in our infrastructure.

Returning Capital to Shareholders. We continue to pay dividends and evaluate opportunities to return capital to our shareholders through repurchases of common stock. In 2011, our Board of Directors declared our first quarterly dividend of $0.08 per share of common stock. We have consistently grown our per share dividend each year since that time and our long-term strategy includes increasing our regular quarterly dividend amount over time. On August 31, 2017, our Board of Directors declared a quarterly dividend of $0.21 per share of common stock. The declaration and payment of cash dividends on our common stock is at the discretion of our Board of Directors, and any decision to declare a dividend will be based on many factors, including, but not limited to, earnings, financial condition, applicable covenants under our revolving credit facility, other contractual restrictions and other factors deemed relevant.

In 2008, our Board of Directors approved our first stock repurchase program. From inception through September 26, 2017, we have paid $216.6 million through our authorized stock repurchase programs to repurchase 14,844,851 shares of our common stock at an average price per share of $14.59. On May 22, 2014, our Board of Directors approved a stock repurchase program under which we may repurchase up to $100.0 million of our common stock. This stock repurchase program has no expiration date and replaced a previous stock repurchase program which was approved on February 16, 2012. All repurchases to date have been made through open market transactions. As of September 26, 2017, $69.9 million remains authorized for stock repurchases.

Key Measures We Use to Evaluate Our Company

Key measures we use to evaluate and assess our business include the following:

Number of Restaurant Openings. Number of restaurant openings reflects the number of restaurants opened during a particular fiscal period. For company restaurant openings, we incur pre opening costs, which are defined below, before the restaurant opens. Typically, new Texas Roadhouse restaurants open with an initial start up period of higher than normalized sales volumes, which decrease to a steady level approximately three to six months after opening. However, although sales volumes are generally higher, so are initial costs, resulting in restaurant margins that are generally lower during the start up period of operation and increase to a steady level approximately three to six months after opening.

Comparable Restaurant Sales Growth. Comparable restaurant sales growth reflects the change in sales for company-owned restaurants over the same period in prior years for the comparable restaurant base. We define the comparable restaurant base to include those restaurants open for a full 18 months before the beginning of the period measured excluding restaurants closed during the period. Comparable restaurant sales growth can be impacted by

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changes in guest traffic counts or by changes in the per person average check amount. Menu price changes and the mix of menu items sold can affect the per person average check amount.

Average Unit Volume. Average unit volume represents the average quarterly or annual restaurant sales for company-owned restaurants open for a full six months before the beginning of the period measured excluding restaurants closed during the period. Historically, average unit volume growth is less than comparable restaurant sales growth which indicates that newer restaurants are operating with sales levels lower than the company average. At times, average unit volume growth may be more than comparable restaurant sales growth which indicates that newer restaurants are operating with sales levels higher than the company average.

Store Weeks. Store weeks represent the number of weeks that our company-owned restaurants were open during the period measured.

Restaurant Margin. Restaurant margin (in dollars and as a percentage of restaurant sales) represents restaurant sales less operating costs, including cost of sales, labor, rent and other operating costs. Depreciation and amortization expense, substantially all of which relates to restaurant-level assets, is excluded from restaurant operating costs and is shown separately as it represents a non-cash charge for the investment in our restaurants. Restaurant margin is widely regarded as a useful metric by which to evaluate restaurant-level operating efficiency and performance. Restaurant margin is not a measurement determined in accordance with U.S. generally accepted accounting principles ("GAAP") and should not be considered in isolation, or as an alternative, to income from operations or other similarly titled measures of other companies. Restaurant margin, as a percentage of restaurant sales, may fluctuate based on many factors, including, but not limited to, inflationary pressures, commodity costs and wage rates. As such, we also focus on the growth of restaurant margin dollars per store week as a measure of restaurant-level profitability as it provides additional insight on operating performance.

Other Key Definitions

Restaurant Sales. Restaurant sales include gross food and beverage sales, net of promotions and discounts, for all company-owned restaurants. Sales taxes collected from customers and remitted to governmental authorities are accounted for on a net basis and therefore are excluded from restaurant sales in the unaudited condensed consolidated statements of income and comprehensive income.

Franchise Royalties and Fees. Franchise royalties consist of royalties, as defined in our franchise agreements, paid to us by domestic and international franchisees. Domestic and/or international franchisees also typically pay an initial franchise fee and/or development fee for each new restaurant or territory. The terms of the international agreements may vary significantly from our domestic agreements.

Restaurant Cost of Sales.   Restaurant cost of sales consists of food and beverage costs of which approximately 50% relates to beef costs.

Restaurant Labor Expenses.   Restaurant labor expenses include all direct and indirect labor costs incurred in operations except for profit-sharing incentive compensation expenses earned by our restaurant managing partners and market partners. These profit-sharing expenses are reflected in restaurant other operating expenses. Restaurant labor expenses also include share-based compensation expense related to restaurant-level employees.

Restaurant Rent Expense.   Restaurant rent expense includes all rent, except pre-opening rent, associated with the leasing of real estate and includes base, percentage and straight-line rent expense.

Restaurant Other Operating Expenses.   Restaurant other operating expenses consist of all other restaurant-level operating costs, the major components of which are utilities, supplies, local store advertising, repairs and maintenance, equipment rent, property taxes, credit card and gift card fees and general liability insurance offset by gift card breakage income. Profit-sharing incentive compensation expenses earned by our restaurant managing partners and market partners are also included in restaurant other operating expenses.

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Pre-opening Expenses. Pre-opening expenses, which are charged to operations as incurred, consist of expenses incurred before the opening of a new restaurant and are comprised principally of opening team and training team compensation and benefits, travel expenses, rent, food, beverage and other initial supplies and expenses. On average, over 70% of total pre-opening costs incurred per restaurant opening relate to the hiring and training of employees. Pre-opening costs vary by location depending on many factors, including the size and physical layout of each location; the number of management and hourly employees required to operate each restaurant; the availability of qualified restaurant staff members; the cost of travel and lodging for different geographic areas; the timing of the restaurant opening; and the extent of unexpected delays, if any, in obtaining final licenses and permits to open the restaurants.

Depreciation and Amortization Expenses. Depreciation and amortization expenses ("D&A") include the depreciation of fixed assets and amortization of intangibles with definite lives, substantially all of which relates to restaurant-level assets.

Impairment and Closure Costs. Impairment and closure costs include any impairment of long-lived assets, including goodwill, and expenses associated with the closure of a restaurant. Closure costs also include any gains or losses associated with a relocated restaurant or the sale of a closed restaurant and/or assets held for sale as well as lease costs associated with closed or relocated restaurants.

General and Administrative Expenses. General and administrative expenses ("G&A") are comprised of expenses associated with corporate and administrative functions that support development and restaurant operations and provide an infrastructure to support future growth including certain advertising costs incurred less amounts remitted by franchise restaurants. Supervision and accounting fees received from certain franchise restaurants are offset against G&A. G&A also includes legal fees, settlement charges and share-based compensation expense related to executive officers, support center employees and area managers, including market partners. The realized and unrealized holding gains and losses related to the investments in our deferred compensation plan, as well as offsetting compensation expense, are also recorded in G&A.

Interest Expense, Net. Interest expense includes the cost of our debt or financing obligations including the amortization of loan fees, reduced by interest income and capitalized interest. Interest income includes earnings on cash and cash equivalents.

Equity Income from Unconsolidated Affiliates. As of September 26, 2017 and September 27, 2016, we owned a 5.0% to 10.0% equity interest in 24 franchise restaurants. Additionally, as of September 26, 2017 and September 27, 2016, we owned a 40% equity interest in four non-Texas Roadhouse restaurants as part of a joint venture agreement with a casual dining restaurant operator in China. Equity income from unconsolidated affiliates represents our percentage share of net income earned by these unconsolidated affiliates.

Net Income Attributable to Noncontrolling Interests. Net income attributable to noncontrolling interests represents the portion of income attributable to the other owners of the majority-owned restaurants. Our consolidated subsidiaries at September 26, 2017 and September 27, 2016 included 18 and 16 majority-owned restaurants, respectively, all of which were open.

Q3 2017 Financial Highlights

Total revenue increased $58.9 million, or 12.2%, to $540.5 million in Q3 2017 compared to $481.6 million in Q3 2016 primarily due to the opening of new restaurants combined with an increase in average unit volume driven by comparable restaurant sales growth. Store weeks and comparable restaurant sales increased 8.1% and 4.5%, respectively, at company restaurants in Q3 2017.

Restaurant margin increased $9.0 million to $95.6 million in Q3 2017 compared to $86.6 million in Q3 2016 while restaurant margin, as a percentage of restaurant sales, decreased to 17.8% in Q3 2017 compared to 18.1% in Q3 2016. The decrease in restaurant margin, as a percentage of restaurant sales, was primarily due to higher labor costs as a result of higher average wage rates, current staffing initiatives, and a change in our compensation structure. Higher labor costs were partially offset by commodity deflation of approximately 2.0% driven by lower food costs, primarily beef.

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Net income increased $5.3 million, or 20.8%, to $31.0 million in Q3 2017 compared to $25.7 million in Q3 2016 primarily due to an increase in restaurant margin dollars, partially offset by higher depreciation costs. Diluted earnings per share increased in Q3 2017 by 19.9% to $0.43 from $0.36 in Q3 2016.

Results of Operations

	13 Weeks Ended September 26, 2017		September 27, 2016		39 Weeks Ended September 26, 2017		September 27, 2016	
	$	%	$	%	$	%	$	%
	(In thousands)				(In thousands)			
Consolidated Statements of Income:								
Revenue:								
Restaurant sales	536,341	99.2	477,617	99.2	1,661,821	99.2	1,493,531	99.2
Franchise royalties and fees	4,166	0.8	4,020	0.8	12,634	0.8	12,473	0.8
Total revenue	540,507	100.0	481,637	100.0	1,674,455	100.0	1,506,004	100.0
Costs and expenses:								
(As a percentage of restaurant sales)								
Restaurant operating costs (excluding depreciation and amortization shown separately below):								
Cost of sales	176,498	32.9	161,886	33.9	545,862	32.8	506,565	33.9
Labor	169,355	31.6	145,301	30.4	514,287	30.9	442,861	29.7
Rent	11,257	2.1	10,266	2.1	33,238	2.0	30,477	2.0
Other operating	83,679	15.6	73,583	15.4	254,176	15.3	227,082	15.2
(As a percentage of total revenue)								
Pre-opening	4,548	0.8	5,017	1.0	14,302	0.9	14,253	0.9
Depreciation and amortization	23,534	4.4	20,941	4.3	69,236	4.1	60,718	4.0
Impairment and closure	2	NM	13	NM	13	NM	54	NM
General and administrative	26,123	4.8	26,162	5.4	94,594	5.6	82,933	5.5
Total costs and expenses	494,996	91.6	443,169	92.0	1,525,708	91.1	1,364,943	90.6
Income from operations	45,511	8.4	38,468	8.0	148,747	8.9	141,061	9.4
Interest expense, net	500	0.1	288	0.1				