Wendy's Co
Form 10-Q
November 06, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 28, 2014

OR

( ) TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______________ to _______________

Commission file number: 1-2207
THE WENDY'S COMPANY
(Exact name of registrants as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	38-0471180 (I.R.S. Employer Identification No.)
One Dave Thomas Blvd., Dublin, Ohio (Address of principal executive offices)	43017 (Zip Code)

(614) 764-3100
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer [x]   Accelerated filer [ ]   Non-accelerated filer [ ]   Smaller reporting company [ ]

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

There were 365,267,004 shares of The Wendy’s Company common stock outstanding as of October 31, 2014.

THE WENDY'S COMPANY AND SUBSIDIARIES
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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

THE WENDY’S COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In Thousands)

	September 28, 2014 (Unaudited)	December 29, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$342,446	$580,152
Accounts and notes receivable	69,084	62,885
Inventories	8,305	10,226
Prepaid expenses and other current assets	81,887	81,759
Deferred income tax benefit	100,497	120,206
Advertising funds restricted assets	68,014	67,183
Total current assets	670,233	922,411
Properties	1,234,992	1,165,487
Goodwill	815,990	842,544
Other intangible assets	1,338,483	1,305,780
Investments	77,768	83,197
Deferred costs and other assets	41,989	43,621
Total assets	$4,179,455	$4,363,040
LIABILITIES AND STOCKHOLDERS’ EQUITY		
Current liabilities:		
Current portion of long-term debt	$37,485	$38,543
Accounts payable	96,812	83,700
Accrued expenses and other current liabilities	136,833	160,100
Advertising funds restricted liabilities	68,014	67,183
Total current liabilities	339,144	349,526
Long-term debt	1,409,066	1,425,285
Deferred income taxes	509,494	482,499
Other liabilities	193,036	176,244
Commitments and contingencies		
Stockholders’ equity:		
Common stock, $0.10 par value; 1,500,000 shares authorized; 470,424 shares issued	47,042	47,042
Additional paid-in capital	2,827,965	2,794,445
Accumulated deficit	(449,103)	(492,215)
Common stock held in treasury, at cost; 104,483 and 77,637 shares	(676,419)	(409,449)
Accumulated other comprehensive loss	(20,770)	(10,337)
Total stockholders’ equity	1,728,715	1,929,486
Total liabilities and stockholders’ equity	$4,179,455	$4,363,040

See accompanying notes to condensed consolidated financial statements.

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THE WENDY’S COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In Thousands Except Per Share Amounts)

	Three Months Ended		Nine Months Ended	
	September 28, 2014	September 29, 2013	September 28, 2014	September 29, 2013
	(Unaudited)			
Revenues:				
Sales	$409,059	$558,029	$1,266,493	$1,659,900
Franchise revenues	103,430	82,750	292,619	235,105
	512,489	640,779	1,559,112	1,895,005
Costs and expenses:				
Cost of sales	343,807	469,177	1,065,777	1,403,303
General and administrative	65,774	76,518	203,122	216,623
Depreciation and amortization	36,274	44,325	117,790	134,841
Facilities action charges (income), net	7,520	22,275	(35,630)	31,690
Impairment of long-lived assets	3,408	5,327	3,740	5,327
Other operating expense (income), net	8,783	(3,653)	4,522	(3,043)
	465,566	613,969	1,359,321	1,788,741
Operating profit	46,923	26,810	199,791	106,264
Interest expense	(13,204)	(15,620)	(39,328)	(55,548)
Loss on early extinguishment of debt	—	—	—	(21,019)
Other income, net	373	2,273	1,753	50
Income before income taxes and noncontrolling interests	34,092	13,463	162,216	29,747
Provision for income taxes	(11,262)	(15,625)	(64,076)	(17,774)
Net income (loss)	22,830	(2,162)	98,140	11,973
Net loss attributable to noncontrolling interests	—	223	—	445
Net income (loss) attributable to The Wendy’s Company	$22,830	$(1,939)	$98,140	$12,418
Basic and diluted net income (loss) per share attributable to The Wendy’s Company	$.06	$—	$.26	$.03
Dividends per share	$.05	$.05	$.15	$.13

See accompanying notes to condensed consolidated financial statements.

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THE WENDY’S COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In Thousands)

	Three Months Ended		Nine Months Ended	
	September 28, 2014	September 29, 2013	September 28, 2014	September 29, 2013
	(Unaudited)			
Net income (loss)	$22,830	$(2,162)	$98,140	$11,973
Other comprehensive (loss) income, net:				
Foreign currency translation adjustment	(10,213)	4,851	(9,238)	(7,029)
Change in unrecognized pension loss, net of income tax (provision) benefit of $(213) and $37, respectively	—	—	338	(62)
Change in unrealized loss on cash flow hedges, net of income tax (provision) benefit of $(549) and $972, respectively	885	—	(1,533)	—
Other comprehensive (loss) income, net	(9,328)	4,851	(10,433)	(7,091)
Comprehensive income	13,502	2,689	87,707	4,882
Comprehensive loss (income) attributable to noncontrolling interests	—	301	—	(103)
Comprehensive income attributable to The Wendy’s Company	$13,502	$2,990	$87,707	$4,779

See accompanying notes to condensed consolidated financial statements.

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THE WENDY’S COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands)

	Nine Months Ended September 28, 2014 (Unaudited)	Nine Months Ended September 29, 2013
Cash flows from operating activities:		
Net income	$98,140	$11,973
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	118,265	138,924
Share-based compensation	25,208	11,564
Impairment (see below)	11,224	23,686
Deferred income tax	59,597	19,292
Excess tax benefits from share-based compensation	(11,979)	—
Non-cash rent expense	6,239	6,506
Net receipt of deferred vendor incentives	9,160	14,731
Gain on dispositions, net (see below)	(74,092)	(7,712)
(Gain) loss on sale of investments, net	(690)	799
Distributions received from TimWen joint venture	10,028	10,148
Equity in earnings in joint ventures, net	(7,659)	(6,980)
Non-cash financing activities, net (see below)	2,708	28,193
Other, net	(5,553)	(795)
Changes in operating assets and liabilities:		
Accounts and notes receivable	(6,074)	(1,643)
Inventories	925	2,237
Prepaid expenses and other current assets	(8,889)	(5,962)
Accounts payable	(3,347)	(2,715)
Accrued expenses and other current liabilities	(40,615)	10,445
Net cash provided by operating activities	182,596	252,691
Cash flows from investing activities:		
Capital expenditures	(197,886)	(130,802)
Acquisitions	(5,949)	(1,812)
Dispositions	119,892	44,055
Change in restricted cash	1,750	(22,593)
Proceeds from sales of investments	1,789	2,680
Other, net	434	2,757
Net cash used in investing activities	(79,970)	(105,715)
Cash flows from financing activities:		
Proceeds from long-term debt	—	350,000
Repayments of long-term debt	(28,983)	(358,364)
Deferred financing costs	—	(5,827)
Repurchases of common stock	(291,240)	(41,469)
Dividends	(55,012)	(51,065)
Proceeds from stock option exercises	25,254	20,950
Excess tax benefits from share-based compensation	11,979	—
Other, net	—	438
Net cash used in financing activities	(338,002)	(85,337)
	(235,376)	61,639

Net cash (used in) provided by operations before effect of exchange rate changes on cash				
Effect of exchange rate changes on cash	(2,330	)	(1,569	)
Net (decrease) increase in cash and cash equivalents	(237,706	)	60,070	
Cash and cash equivalents at beginning of period	580,152		453,361	
Cash and cash equivalents at end of period	$342,446		$513,431	

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THE WENDY’S COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS—CONTINUED
(In Thousands)

	Nine Months Ended	
	September 28, 2014	September 29, 2013
	(Unaudited)	
Detail of cash flows from operating activities:		
Impairment:		
System Optimization Remeasurement	$7,484	$18,359
Impairment of long-lived assets	3,740	5,327
	$11,224	$23,686
Gain on dispositions, net:		
Gain on sales of restaurants, net	$(60,490)	$(2,941)
Gain on disposal of assets, net	(13,602)	(4,771)
	$(74,092)	$(7,712)
Non-cash financing activities, net:		
Accretion of long-term debt	$890	$5,281
Amortization of deferred financing costs	1,818	1,893
Loss on early extinguishment of debt	—	21,019
	$2,708	$28,193
Supplemental cash flow information:		
Cash paid for:		
Interest	$37,507	$46,931
Income taxes, net of refunds	$11,231	$1,484
Supplemental non-cash investing and financing activities:		
Capital expenditures included in accounts payable	$58,629	$45,566
Capitalized lease obligations	$11,223	$5,891

See accompanying notes to condensed consolidated financial statements.

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THE WENDY’S COMPANY AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(In Thousands Except Per Share Amounts)

(1) Basis of Presentation

The accompanying unaudited condensed consolidated financial statements (the “Financial Statements”) of The Wendy’s Company (“The Wendy’s Company” and, together with its subsidiaries, the “Company,” “we,” “us” or “our”) have been prepa in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and, therefore, do not include all information and footnotes required by GAAP for complete financial statements. In our opinion, the Financial Statements contain all adjustments necessary to present fairly our financial position as of September 28, 2014 and the results of our operations for the three and nine months ended September 28, 2014 and September 29, 2013 and cash flows for the nine months ended September 28, 2014 and September 29, 2013. The results of operations for the three and nine months ended September 28, 2014 are not necessarily indicative of the results to be expected for the full 2014 fiscal year. These Financial Statements should be read in conjunction with the audited consolidated financial statements for The Wendy’s Company and notes thereto, included in our Annual Report on Form 10-K for the fiscal year ended December 29, 2013 (the “Form 10-K”).

The principal subsidiary of the Company is Wendy’s International, LLC (“Wendy’s”) and its subsidiaries (formerly known as Wendy’s International, Inc.). The Company manages and internally reports its business geographically. The operation and franchising of Wendy’s® restaurants in North America (defined as the United States of America (“U.S.”) and Canada) comprises virtually all of our current operations and represents a single reportable segment. See Note 2 for information on our Canadian operations. The revenues and operating results of Wendy’s restaurants outside of North America are not material.

We report on a fiscal year consisting of 52 or 53 weeks ending on the Sunday closest to December 31. All three and nine month periods presented herein contain 13 and 39 weeks, respectively. All references to years and quarters relate to fiscal periods rather than calendar periods.

Certain reclassifications have been made to the prior year presentation to conform to the current year presentation.

In connection with the reimaging of restaurants as part of our Image Activation program, we have recorded $1,180 and $16,199 of accelerated depreciation and amortization during the three and nine months ended September 28, 2014, respectively, and $5,755 and $24,509 during the three and nine months ended September 29, 2013, respectively, on certain long-lived assets to reflect their use over shortened estimated useful lives. We describe the circumstances under which we record accelerated depreciation and amortization for properties in our Form 10-K.

Our condensed consolidated statements of operations for the three and nine months ended September 28, 2014 include a correction to increase rental income by $3,436 and lease expense by $3,436 to properly reflect Wendy’s subleasing of restaurant facilities to franchisees for the operation of Wendy’s/Tim Hortons combo units in Canada during the six months ended June 29, 2014. We recorded $1,949 and $1,949 of rental income and lease expense, respectively, for such subleasing activity during the three months ended September 28, 2014. The Company’s previously reported rental income and lease expense for the nine months ended September 29, 2013 were both understated by $5,667. The effect of the offsetting understatements on the condensed consolidated statement of operations for the nine months ended September 29, 2013 was not material. The correction did not result in any changes to the reported consolidated balance sheets, statements of cash flows and operating profit, net income or basic and diluted net income per share attributable to The Wendy’s Company included in our condensed consolidated statements of operations.

(2) Facilities Action Charges (Income), Net

	Three Months Ended		Nine Months Ended	
	September 28, 2014	September 29, 2013	September 28, 2014	September 29, 2013
System optimization initiative	$7,520	$21,557	$(35,630)	$26,356
Facilities relocation and other transition costs	—	632	—	3,956
Breakfast discontinuation	—	86	—	1,115
Arby’s transaction related costs	—	—	—	263
	$7,520	$22,275	$(35,630)	$31,690

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System Optimization Initiative

In August 2014, the Company announced a plan to sell all of its company-owned restaurants in Canada to franchisees by the end of the first quarter of 2015 as part of its ongoing system optimization initiative. During the third quarter of 2014, the Company completed the sale of two Canadian restaurants and classified its remaining Canadian restaurants’ assets as held for sale.
During the first quarter of 2014, the Company completed the sale of 174 company-owned restaurants in the U.S. to franchisees, bringing the aggregate total to 418 during 2013 and 2014 under its system optimization initiative announced in July 2013. This initiative also included the consolidation of regional and divisional territories which was substantially completed by the end of the second quarter of 2014.
As a result of the system optimization initiative, the Company has recorded losses on remeasuring long-lived assets to fair value upon determination that the assets will be leased and/or subleased to franchisees in connection with the sale of restaurants (“System Optimization Remeasurement”). In addition, the Company has recognized costs related to the system optimization initiative which are illustrated in the table below. These costs have been substantially offset by net gains recognized on sales of restaurants, all of which are recorded to “Facilities action charges (income), net” in our condensed consolidated statements of operations.
The Company anticipates recognizing additional system optimization related costs through the first quarter of 2015 of between $2,000 and $4,000 which include severance and related employee costs and professional fees. The Company is unable to estimate any gains or losses resulting from future sales of its Canadian restaurants. The Company plans to retain its ownership in a Canadian restaurant real estate joint venture with Tim Hortons Inc. For additional information on the joint venture see Note 4.

The following is a summary of the activity recorded under our system optimization initiative:

	Three Months Ended		Nine Months Ended		Total Incurred Since Inception
	September 28, 2014	September 29, 2013	September 28, 2014	September 29, 2013	
Loss (gain) on sales of restaurants, net	$921	$(1,665)	$(60,490)	$(2,941)	$(107,157)
System Optimization Remeasurement (a)	5,210	12,421	7,484	18,359	27,990
Accelerated amortization (b)	—	3,130	475	3,130	17,382
Severance and related employee costs	715	6,131	6,641	6,131	16,291
Professional fees	38	704	3,227	829	5,616
Share-based compensation (c)	125	755	3,760	755	5,013
Other	511	81	3,273	93	4,136
Total system optimization initiative	$7,520	$21,557	$(35,630)	$26,356	$(30,729)

(a) Includes remeasurement of land, buildings, leasehold improvements and favorable lease assets at company-owned restaurants included in our system optimization initiative. See Note 5 for more information on non-recurring fair value measurements.

(b) Includes accelerated amortization of previously acquired franchise rights related to company-owned restaurants in territories that were sold in connection with our system optimization initiative.

(c)

Represents incremental share-based compensation resulting from the modification of stock options and performance-based awards in connection with the termination of employees under our system optimization initiative.

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(Loss) Gain on Sales of Restaurants, Net

	Three Months Ended		Nine Months Ended	
	September 28, 2014	September 29, 2013	September 28, 2014	September 29, 2013
Number of restaurants sold to franchisees	2	53	176	61
Proceeds from sales of restaurants	$62	$22,871	$95,053	$25,671
Net assets sold (a)	(132)	(13,646)	(41,351)	(14,489)
Goodwill related to sales of restaurants	(10)	(5,621)	(12,653)	(6,302)
Net (unfavorable) favorable lease (liabilities)/assets (b)	(420)	(1,884)	20,501	(1,884)
Other	—	(22)	478	(22)
	(500)	1,698	62,028	2,974
Post-closing adjustments on sales of restaurants	(421)	(33)	(1,538)	(33)
(Loss) gain on sales of restaurants, net	$(921)	$1,665	$60,490	$2,941

(a) Net assets sold consisted primarily of cash, inventory and equipment.

(b) During the three and nine months ended September 28, 2014, the Company recorded favorable lease assets of $164 and $43,496, respectively, and unfavorable lease liabilities of $584 and $22,995, respectively, as a result of leasing and/or subleasing land, buildings, and/or leasehold improvements to franchisees, in connection with sales of restaurants. During the three and nine months ended September 29, 2013, the Company recorded favorable lease assets of $8,789 and unfavorable lease liabilities of $10,673.

The table below presents a rollforward of our accrual for the system optimization initiative, which is included in "Accrued expenses and other current liabilities."

	Balance December 29, 2013	Charges	Payments	Balance September 28, 2014
Severance and related employee costs	$7,051	$6,641	$(10,898)	$2,794
Professional fees	137	3,227	(3,226)	138
Other	260	3,273	(2,382)	1,151
	$7,448	$13,141	$(16,506)	$4,083

Assets Held for Sale

	September 28, 2014	December 29, 2013
Number of restaurants classified as held for sale	134	181
Net assets held for sale	$28,317	$29,630

In August 2014, the Company determined that all of its company-owned restaurants in Canada, which are part of the system optimization initiative, met the criteria to be classified as held for sale. Net assets held for sale consist primarily of cash, inventory, equipment and an estimate of allocable goodwill and are included in "Prepaid expenses and other current assets."

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Facilities Relocation and Other Transition Costs

As announced in December 2011, we commenced the relocation of the Company’s Atlanta restaurant support center to Ohio, which was substantially completed during 2012. The Company incurred $632 and $3,956 of expense during the three and nine months ended September 29, 2013, respectively, and $39,091 since inception. The Company did not incur any expenses during the nine months ended September 28, 2014 and does not expect to incur additional costs related to the relocation.

(3) Acquisitions and Dispositions

Acquisitions

During the nine months ended September 28, 2014, Wendy’s acquired six franchised restaurants for total net cash consideration of $5,949. The total consideration was allocated to net tangible and identifiable intangible assets acquired, primarily properties and franchise rights, based on their estimated fair values. Three of the franchised restaurants were acquired during the second quarter of 2014 and the fair value of the assets acquired exceeded the total consideration, resulting in income of $349 after post-closing adjustments which is included in “Other operating expense (income), net” for the nine months ended September 28, 2014. The remaining franchised restaurants acquired in the third quarter of 2014, resulted in an excess of consideration over the estimated fair value of assets acquired of $720 which was recognized as goodwill.

During the nine months ended September 29, 2013, Wendy’s acquired one franchised restaurant; such transaction was not material.

Dispositions

During the nine months ended September 28, 2014, Wendy’s received cash proceeds of $24,839 from dispositions, which were not part of the system optimization initiative, consisting of (1) $9,196 from the sale of 14 company-owned restaurants to franchisees, (2) $7,027 primarily from the sale of surplus properties and (3) $8,616 from the sale of company-owned aircraft. These sales resulted in a net gain of $13,602 which is included in “Other operating expense (income), net,” and a reduction to goodwill of $1,483 related to the sale of company-owned restaurants.

During the nine months ended September 29, 2013, Wendy’s received cash proceeds of $18,384 from dispositions, consisting of (1) $9,731 primarily from the sale of surplus properties and (2) $8,653 resulting from franchisees exercising options to purchase previously leased properties. These sales resulted in a net gain of $4,771, which was included in “Other operating expense (income), net.” See Note 2 for discussion of restaurant dispositions in connection with our system optimization initiative.

(4) Investments

Investment in Joint Venture with Tim Hortons Inc.

Wendy’s is a partner in a Canadian restaurant real estate joint venture (“TimWen”) with Tim Hortons Inc. Wendy’s 50% share of the joint venture is accounted for using the equity method of accounting. Our equity in earnings from TimWen is included in “Other operating expense (income), net.”

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THE WENDY’S COMPANY AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(In Thousands Except Per Share Amounts)

Presented below is an unaudited summary of activity related to our investment in TimWen included in “Investments” in our unaudited condensed consolidated financial statements:

	Nine Months Ended	
	September 28, 2014	September 29, 2013
Balance at beginning of period	$79,810	$89,370
Equity in earnings for the period	9,651	10,357
Amortization of purchase price adjustments (a)	(1,992)	(2,288)
	7,659	8,069
Distributions received	(10,028)	(10,148)
Foreign currency translation adjustment included in “Other comprehensive (loss) income, net”	(3,187)	(3,052)
Balance at end of period	$74,254	$84,239

(a) Based upon an average original aggregate life of 21 years.

Presented below is a summary of certain unaudited interim income statement information of TimWen:

	Nine Months Ended	
	September 28, 2014	September 29, 2013
Revenues	$27,622	$29,113
Income before income taxes and net income	19,302	20,714

Joint Venture in Japan

A wholly-owned subsidiary of Wendy’s entered into a joint venture for the operation of Wendy’s restaurants in Japan (the “Japan JV”) with Ernest M. Higa and Higa Industries, Ltd., a corporation organized under the laws of Japan (collectively, the “Higa Partners”) during the second quarter of 2011. Through the first quarter of 2013, our 49% share of the Japan JV was accounted for as an equity method investment.

As a result of changes in the ownership rights and obligations of the partners in April 2013, Wendy’s consolidated the Japan JV beginning in the second quarter of 2013 and reported the Japan JV’s results of operations in the appropriate line items in our condensed consolidated statements of operations and the net loss attributable to the Higa Partners’ ownership percentage in “Net loss attributable to noncontrolling interests.” The consolidation of the Japan JV’s three restaurants did not have a material impact on our condensed consolidated financial statements. In August 2013, additional contributions of $1,000 and $219 were made by Wendy’s and the Higa Partners, respectively. We have reflected our capital contributions of $2,000, net of cash acquired of $188, in “Acquisitions” in our condensed consolidated statements of cash flows for the nine months ended September 29, 2013.

Subsequently, the joint venture was terminated on December 27, 2013 and as a result, Wendy’s has no remaining funding requirements for, or exposure under guarantees to lenders to, the Japan JV.

(5) Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Valuation techniques under the accounting guidance related to fair value measurements are based on observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect our market assumptions. These inputs are classified into the following hierarchy:

Level 1 Inputs - Quoted prices for identical assets or liabilities in active markets.

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(In Thousands Except Per Share Amounts)

Level 2 Inputs - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs - Pricing inputs are unobservable for the assets or liabilities and include situations where there is little, if any, market activity for the assets or liabilities. The inputs into the determination of fair value require significant management judgment or estimation.

Financial Instruments

The following table presents the carrying amounts and estimated fair values of the Company’s financial instruments at September 28, 2014 and December 29, 2013:

	September 28, 2014		December 29, 2013		
	Carrying Amount	Fair Value	Carrying Amount	Fair Value	Fair Value Measurements
Financial assets					
Cash equivalents	$145,777	$145,777	$405,874	$405,874	Level 1
Non-current cost method investments (a)	3,514	142,563	3,387	130,433	Level 3
Cash flow hedges (b)	—	—	1,212	1,212	Level 2
Financial liabilities					
Cash flow hedges (b)	1,293	1,293	—	—	Level 2
Term A Loans, due in 2018 (c)	548,955	547,926	570,625	569,555	Level 2
Term B Loans, due in 2019 (c)	761,682	756,921	767,452	767,452	Level 2
7% debentures, due in 2025 (c)	85,555	106,000	84,666	98,250	Level 2
Capital lease obligations (d)	50,359	52,789	40,732	38,716	Level 3
Guarantees of franchisee loan obligations (e)	1,000	1,000	884	884	Level 3

(a) The fair value of our indirect investment in Arby’s Restaurant Group, Inc. (“Arby’s”) is based on applying a multiple to Arby’s earnings before income taxes, depreciation and amortization per its current unaudited financial information. The carrying value of our indirect investment in Arby’s was reduced to zero during 2013 in connection with the receipt of a dividend. The fair values of our remaining investments are not significant and are based on our review of information provided by the investment managers or investees which was based on (1) valuations performed by the investment managers or investees, (2) quoted market or broker/dealer prices for similar investments and (3) quoted market or broker/dealer prices adjusted by the investment managers for legal or contractual restrictions, risk of nonperformance or lack of marketability, depending upon the underlying investments.

(b) The fair values were developed using market observable data for all significant inputs.

(c) The fair values were based on quoted market prices in markets that are not considered active markets.

(d) The fair values were determined by discounting the future scheduled principal payments using an interest rate assuming the same original issuance spread over a current U.S. Treasury bond yield for securities with similar durations.

(e) Wendy’s has provided loan guarantees to various lenders on behalf of franchisees entering into debt arrangements for new restaurant development and equipment financing. In addition during 2012, Wendy’s provided a guarantee to a lender for a franchisee in connection with the refinancing of the franchisee’s debt. We have accrued a liability for the fair value of these guarantees, the calculation of which was based upon a weighted average risk percentage established at inception adjusted for a history of defaults.

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The carrying amounts of cash, accounts payable and accrued expenses approximated fair value due to the short-term nature of those items. The carrying amounts of accounts and notes receivable (both current and non-current) approximated fair value due to the effect of the related allowance for doubtful accounts. Our derivative instruments, cash and cash equivalents and guarantees are the only financial assets and liabilities measured and recorded at fair value on a recurring basis.

Derivative Instruments

The Company’s primary objective for entering into interest rate swap agreements is to manage its exposure to changes in interest rates, as well as to maintain an appropriate mix of fixed and variable rate debt.

Our derivative instruments as of September 28, 2014 and December 29, 2013 consist of seven forward starting interest rate swap agreements to change the floating rate interest payments associated with $350,000 and $100,000 in borrowings expected to be outstanding under our Term A Loans and Term B Loans, respectively, to fixed interest rate obligations beginning on June 30, 2015 and maturing on December 31, 2017. At inception, the forward starting swap agreements were designated as cash flow hedges and are evaluated for effectiveness quarterly.