

NORTH STATE GROCERY, INC.

FINANCIAL STATEMENTS
December 31, 2016 and December 26, 2015

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INDEPENDENT AUDITOR'S REPORT

To The Board of Directors
North State Grocery, Inc.
Cottonwood, California

Report on the Financial Statements

We have audited the accompanying financial statements of North State Grocery, Inc., (a California S-Corporation), which comprise the balance sheets as of December 31, 2016 and December 26, 2015, and the related statements of income, changes in stockholders' equity, and cash flows for the periods then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain evidence about amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of North State Grocery, Inc. as of December 31, 2016 and December 26, 2015, and the results of its operations and its cash flows for the periods then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary schedules on pages 17-18 are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Neal & Leidholdt

Redding, California
July 5, 2017

NORTH STATE GROCERY, INC.
BALANCE SHEETS
December 31, 2016 and December 26, 2015

ASSETS

	<u>2016</u>	<u>2015</u>
CURRENT ASSETS:		
Cash	\$ 7,117,432	\$ 3,994,859
Trade receivables (net of allowances for doubtful accounts of \$233 and \$506, respectively)	66,138	60,828
Other receivables (net of allowances for doubtful accounts of \$11,395 and \$72,967, respectively)	1,032,925	1,058,419
Merchandise inventory	10,310,770	9,894,199
Prepaid expenses	<u>625,432</u>	<u>616,700</u>
TOTAL CURRENT ASSETS	<u>19,152,697</u>	<u>15,625,005</u>
 PROPERTY AND EQUIPMENT (Note 2):	 31,376,617	 29,047,529
Less accumulated depreciation	(<u>16,156,868</u>)	(<u>15,543,694</u>)
PROPERTY AND EQUIPMENT, NET	<u>15,219,749</u>	<u>13,503,835</u>
 OTHER ASSETS:		
Off-sale liquor licenses	581,014	581,014
Investment in real estate (Note 3)	2,184,759	1,390,651
Goodwill – net (Note 1)	1,054,006	1,054,006
Loan fees - net of accumulated amortization (Note 4)	141,452	118,487
Deposits	239,948	10,054
Cash surrender value of officers' life insurance	<u>245,313</u>	<u>190,636</u>
TOTAL OTHER ASSETS	<u>4,446,492</u>	<u>3,344,848</u>
 TOTAL ASSETS	 \$ <u>38,818,938</u>	 \$ <u>32,473,688</u>

LIABILITIES AND STOCKHOLDERS' EQUITY

	<u>2016</u>	<u>2015</u>
CURRENT LIABILITIES:		
Current maturities of notes payable (Note 5 and 13)	\$ 6,813,934	\$ 1,654,948
Obligations under capital leases, current portion (Note 7)	44,691	58,318
Trade accounts payable and disbursements outstanding	6,688,994	6,779,543
Accrued wages, payroll taxes, and employee benefits withheld	1,598,097	2,159,499
Accrued liabilities (Note 13)	2,003,820	1,906,483
Deferred income taxes (Note 10)	<u>299</u>	<u>1,779</u>
TOTAL CURRENT LIABILITIES	<u>17,149,835</u>	<u>12,560,570</u>
 LONG-TERM LIABILITIES:		
Notes payable, net of current maturities (Note 5 and 13)	34,920,615	8,818,343
Obligations under capital leases, net of current portion (Note 7)	19,714	64,405
Deferred income taxes (Note 10)	<u>15,184</u>	<u>15,227</u>
TOTAL LONG-TERM LIABILITIES	<u>34,955,513</u>	<u>8,897,975</u>
TOTAL LIABILITIES	<u>52,105,348</u>	<u>21,458,545</u>
 STOCKHOLDERS' EQUITY:		
Common stock, no par value, 1,000,000 shares authorized, 222,800 shares issued and 102,800 outstanding	5,140	11,140
Additional paid in capital (Note 12)	3,261,071	4,606,134
Unearned ESOP shares (Note 9)	(582,735)	(699,282)
Retained (deficit) earnings	<u>(15,969,886)</u>	<u>7,097,151</u>
TOTAL STOCKHOLDERS' EQUITY	<u>(13,286,410)</u>	<u>11,015,143</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 38,818,938</u>	<u>\$ 32,473,688</u>

See accompanying notes and accountant's report.

NORTH STATE GROCERY, INC.
STATEMENTS OF INCOME
For The Year Ended December 31, 2016 and December 26, 2015

	2016		2015	
	Amount	%	Amount	%
SALES	\$ 204,034,615	100.0	\$ 196,508,727	100.0
COST OF SALES	<u>147,333,687</u>	<u>72.2</u>	<u>142,703,024</u>	<u>72.6</u>
GROSS PROFIT	56,700,928	27.8	53,805,703	27.4
Lottery income	77,377	.0	73,921	.0
Money order fees	9,905	.0	14,999	.0
Miscellaneous income	<u>165,259</u>	<u>.1</u>	<u>104,182</u>	<u>.1</u>
TOTAL OPERATING REVENUES	56,953,469	27.9	53,998,805	27.5
OPERATING EXPENSES	<u>49,571,214</u>	<u>24.3</u>	<u>46,947,910</u>	<u>23.9</u>
INCOME FROM OPERATIONS (Note 14)	<u>7,382,255</u>	<u>3.6</u>	<u>7,050,895</u>	<u>3.6</u>
OTHER INCOME (EXPENSES):				
Interest income	2,610	.0	6,954	.0
Interest expense	(1,408,880)	(.7)	(512,694)	(.3)
Gain (loss) on disposal of assets	(<u>186,842</u>)	(<u>.1</u>)	(<u>63,367</u>)	(<u>.0</u>)
OTHER EXPENSES, NET	(<u>1,593,112</u>)	(<u>.8</u>)	(<u>569,107</u>)	(<u>.3</u>)
INCOME (LOSS) BEFORE TAXES	5,789,143	2.8	6,481,788	3.3
Income tax (expense) benefit (Note 10)	(<u>106,477</u>)	(<u>.0</u>)	(<u>122,801</u>)	(<u>.1</u>)
NET INCOME (LOSS)	\$ <u>5,682,666</u>	<u>2.8</u>	\$ <u>6,358,987</u>	<u>3.2</u>

See accompanying notes and accountant's report.

NORTH STATE GROCERY, INC.
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
For The Year Ended December 31, 2016 and December 26, 2015

2016

		Common Stock	Paid In Capital	Unearned ESOP Share	Retained Earnings (Deficit)	Total
Beginning Balance	\$	11,140	\$ 4,606,134	\$ (699,282)	\$ 7,097,151	\$ 11,015,143
Current Period Income		0	0	0	5,682,666	5,682,666
Shareholder Distributions		0	0	0	(1,422,161)	(1,422,161)
Corporate Stock Redemption (Note 12)	(6,000)	(2,487,312)	0	(27,506,688)	(30,000,000)
ESOP Funding		0	1,142,249	116,547	179,146	1,437,942
Ending Balance	\$	<u>5,140</u>	\$ <u>3,261,071</u>	\$ (<u>582,735</u>)	\$ (<u>15,969,886</u>)	\$ (<u>13,286,410</u>)

2015

		Common Stock	Paid In Capital	Unearned ESOP Share	Retained Earnings	Total
Beginning Balance	\$	11,140	\$ 3,610,768	\$ (811,258)	\$ 5,032,066	\$ 7,842,716
Current Period Inc(Loss)		0	0	0	6,358,987	6,358,987
Shareholder Distributions		0	0	0	(5,053,519)	(5,053,519)
ESOP Funding		0	995,366	111,976	759,617	1,866,959
Ending Balance	\$	<u>11,140</u>	\$ <u>4,606,134</u>	\$ (<u>699,282</u>)	\$ <u>7,097,151</u>	\$ <u>11,015,143</u>

See accompanying notes and accountant's report.

NORTH STATE GROCERY, INC.
STATEMENTS OF CASH FLOWS
For The Year Ended December 31, 2016 and December 26, 2015

	<u>2016</u>	<u>2015</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ 5,682,666	\$ 6,358,987
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,881,225	1,524,680
Loss on disposition of fixed assets	186,842	63,367
(Increase) Decrease in cash surrender value of life insurance	(54,677)	(53,730)
(Decrease) Increase in deferred income tax liability	(1,523)	2,129
Changes in current assets and liabilities:		
Trade accounts receivable	(5,310)	(5,638)
Other accounts receivable	25,494	(218,568)
Merchandise inventory	(416,571)	1,216
Prepaid expenses	(8,732)	(11,245)
Deposits	(229,894)	25,581
Trade accounts payable	(90,550)	1,361,975
Accrued salaries and wages, payroll taxes and employee benefits	(561,402)	136,145
Accrued liabilities	97,337	(10,146)
NET CASH PROVIDED BY OPERATIONS	<u>6,504,905</u>	<u>9,174,753</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of assets	20,183	56,907
Purchase of land	(808,504)	0
Purchase of property and equipment	(3,773,733)	(4,162,018)
NET CASH (USED) BY INVESTING ACTIVITIES	(4,562,054)	(4,105,111)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings on notes payable	34,025,742	329,396
Principal payments on notes payable	(2,764,483)	(1,690,943)
ESOP funding	1,437,942	1,866,959
Proceeds from borrowings on capital leases	0	18,417
Shareholder distributions	(1,422,161)	(5,053,519)
Common stock repurchase	(30,000,000)	0
Payment of loan fees	(39,000)	0
Payments on capital leases	(58,318)	(78,876)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	<u>1,179,722</u>	(4,608,566)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	<u>3,122,573</u>	<u>461,076</u>
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>3,994,859</u>	<u>3,533,783</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 7,117,432</u>	<u>\$ 3,994,859</u>

See accompanying notes and accountant's report.

NORTH STATE GROCERY, INC.
NOTES TO THE FINANCIAL STATEMENTS
December 31, 2016 and December 26, 2015

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BUSINESS ACTIVITY OR NATURE OF BUSINESS - The Company engages in the business of retail grocery and fuel sales. As of the balance sheet date, operations consisted of stores in nineteen locations, two with fuel stations, throughout Northern California.

ACCOUNTING PERIOD - The Company has adopted a 52-53 week fiscal year and has elected to end its accounting period on the last Saturday in December.

ACCOUNTING METHOD - The financial statements are presented on the accrual basis of accounting in accordance with generally accepted accounting principles, whereby revenues are recognized when earned, and expenses are recognized when incurred.

CASH AND CASH EQUIVALENTS - For purposes of the accompanying statement of cash flows, cash equivalents include time deposits, certificates of deposit, and all highly liquid debt instruments purchased with an original maturity of three months or less.

CONCENTRATION OF CREDIT RISK - The Company's financial instruments that are potentially exposed to concentration of credit risk consist primarily of cash and cash equivalents. The Company places its cash and temporary cash investments with high credit quality institutions. At times, such investments may be in excess of the FDIC insurance limit; however, the Company believes that the credit risk is nominal and in the normal course of business. As of December 31, 2016 and December 26, 2015, the Company had cash and cash equivalents in excess of the FDIC insured limit of \$3,752,024 and \$337,822, respectively.

ACCOUNTS RECEIVABLE - Allowances and reserves for doubtful accounts have been recorded at December 31, 2016 and December 26, 2015. The Company's policy is not to accrue interest on accounts receivable. Accounts are written off as uncollectable at the time management determines that collection is unlikely.

INVENTORIES - Merchandise inventory is valued at the lower of cost or market, with cost determined using the first-in, first-out method, on an average cost method.

PROPERTY AND EQUIPMENT - Additions to property and equipment are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets; except for leasehold improvements, which are generally amortized over the lesser of the lease term or the estimated useful lives of the improvements.

Estimated useful lives are as follows:

<u>Description</u>	<u>Lives Years</u>
Store fixtures and equipment	3-15
Leasehold improvements	6-40

INTANGIBLE ASSETS - Intangible assets, including liquor licenses, are stated at cost less accumulated amortization. Amortization has been provided for on a straight-line basis for covenants not to compete and leasehold acquisition costs. Covenants not to compete and leasehold acquisition costs are amortized over the lives of the underlying agreements, on the straight-line method. Covenants not to compete have been fully amortized.

RECLASSIFICATIONS - Certain accounts in the prior-year financial statements have been reclassified for comparative purposes to conform to the presentation in the current-year financial statements. There was no effect on previously reported stockholders' equity or net income.

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

GOODWILL - The Company has classified as goodwill the cost in excess of the carrying value of net assets related to the acquisition of several businesses from their former owners. The company tests goodwill annually for impairment. If goodwill is determined to be impaired, it will be adjusted to its fair value. The value of the goodwill at December 31, 2016 and December 26, 2015 is \$1,054,006 and \$1,054,006, respectively.

EMPLOYEE STOCK OWNERSHIP PLAN (ESOP) - The Company accounts for its ESOP in accordance with FASB Accounting Standards Codification (ASC) 718-40, *Employee Stock Ownership Plans*. Accordingly, shares pledged as collateral are reported as "Unearned ESOP Shares" in the Balance Sheet. As shares are released from collateral, the Company reports compensation expense equal to the current market price of the shares. The compensation expense resulting from the ESOP at December 31, 2016 and December 26, 2015 is \$1,321,394 and \$1,754,983, respectively.

Dividends on unallocated shares are recorded as compensation expense. Dividends on allocated shares are recorded as a reduction in retained earnings.

USE OF ESTIMATES - The preparation of financial statements in conformity with generally accepted accounting principals requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

INCOME TAXES - The Company has elected to be taxed under the provisions of Subchapter S of the Internal Revenue Code and the California Income Tax Code. Under those tax provisions the Company generally does not pay federal corporate income taxes on its taxable income. Instead, the stockholder's are liable for individual income taxes on their share of the Company's taxable income for both federal and California tax purposes. As of July 1, 2016, the Company is fully owned by the Employee Stock Ownership Plan which will result in the tax liability being shifted to the employees when they redeem their ownership shares.

The Company, however, is required to pay a 1.5% California corporate tax in addition to the taxes paid to California by its stockholders. Accordingly, the Company accounts for income taxes in accordance with Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) 740. Deferred taxes are provided for accumulated temporary differences due to basis differences for assets and liabilities for financial reporting and income tax purposes.

It is the Company's policy to include interest and penalties assessed by income taxing authorities as a component of income tax expense. No such penalties and interest were incurred during the years ended December 31, 2016 and December 26, 2015. The Company's federal and state income tax returns for 2013 through 2016 are subject to examination (generally for the three years after they are filed and four years for California) by the Internal Revenue Service and the State of California.

FASB ASC 740 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements. FASB ASC 740 details how companies should recognize, measure, present, and disclose uncertain tax positions that have been or are expected to be taken. As such, financial statements will reflect expected future tax consequences of uncertain tax positions presuming the taxing authorities' full knowledge of the position and all relevant facts.

The Company did not have unrecognized tax benefits as of December 31, 2016 and December 26, 2015, and does not expect this to change significantly over the next 12 months.

PRESENTATION OF SALES TAX - The State of California and counties within the State impose a sales tax on certain products the Company sells to customers. The Company collects that sales tax from customers and remits the entire amount to the State. The Company's accounting policy is to exclude the tax collected and remitted to the State from revenue and cost of sales.

ADVERTISING - Advertising costs are expensed as incurred. Advertising expenses for the years ended December 31, 2016 and December 26, 2015 were \$204,983 and \$183,712, respectively.

Note 2 PROPERTY AND EQUIPMENT

The following is a summary of property and equipment as of December 31, 2016 and December 26, 2015:

	<u>2016</u>	<u>2015</u>
Fixtures and equipment	\$ 20,348,958	\$ 19,808,974
Leasehold improvements	8,768,240	7,239,743
Vehicles	514,108	527,270
Office equipment	<u>1,745,311</u>	<u>1,471,542</u>
 TOTAL	 \$ <u>31,376,617</u>	 \$ <u>29,047,529</u>

Note 3 INVESTMENT IN REAL ESTATE

In a prior year the Company foreclosed on the note receivable from Violet Plaza, LLC. As a result of the foreclosure, the Company received a piece of real estate valued at \$1,390,651 and had to assume a note payable of \$500,000 payable to various individuals and a profit sharing plan. In the year ended December 27, 2014, the \$500,000 note payable was paid in full.

During the year ending December 31, 2016 the Company purchased a lot in Corning, California that they intend to build a new store to replace the current Corning location. The Company paid \$757,015 for the Corning lot.

Also, during the year ending December 31, 2016, the Company purchased five lots in Chester, California on which they intend to build a gas station. The Company sold two of the excess lots resulting in a net basis of \$37,093 for the Chester lots.

Note 4 INTANGIBLE ASSETS

Costs incurred in connection with obtaining financing through the bank have been capitalized and are being amortized using the straight-line method over the life of the related financing arrangement. Amortization expense for the year ended December 31, 2016 and December 26, 2015 were \$16,035 and \$18,652, respectively.

The Company's intangible assets consisted of the following at December 31, 2016 and December 26, 2015:

	<u>2016</u>	<u>2015</u>
LOAN FEES		
Costs	186,028	147,028
Accumulated amortization	(<u>44,576</u>)	(<u>28,541</u>)
	<u>141,452</u>	<u>118,487</u>
TOTALS		
Costs	186,028	147,028
Accumulated amortization	(<u>44,576</u>)	(<u>28,541</u>)
 TOTAL NET	 \$ <u>141,452</u>	 \$ <u>118,487</u>

Note 4 INTANGIBLE ASSETS (continued)

Future amortization expenses as of December 31, 2016 are as follows:

Year Ending:

December 30, 2017	\$	31,274
December 29, 2018		17,275
December 28, 2019		17,274
December 26, 2020		17,275
December 25, 2021		17,274
Thereafter		<u>41,080</u>
TOTAL	\$	<u>141,452</u>

Note 5 NOTES PAYABLE

Notes payable consist of the following at December 31, 2016 and December 26, 2015:

	<u>2016</u>	<u>2015</u>
Note payable to National Cooperative Bank, Revolving Credit Line in the amount of \$2,800,000, currently matures on November 30, 2018, interest at 3.25% which is based on the lenders prime rate minus 25 basis points, secured by inventory, property and equipment.	0	0
Note payable to PG&E, payable in monthly installments of \$2,564, including interest at 0%, original note \$100,000, due January 2016, unsecured.	0	2,564
Note payable to PG&E, payable in monthly installments of \$2,403, including interest at 0%, original note \$67,273, due June 2016, unsecured.	0	14,416
Note payable to PG&E, payable in monthly installments of \$2,192, including interest at 0%, original note \$61,368, due October 2016, unsecured.	0	21,917
Note payable to PG&E, payable in monthly installments of \$2,041, including interest at 0%, original note \$100,000, due December 2016, unsecured.	0	24,490
Note payable to PG&E, payable in monthly installments of \$2,041, including interest at 0%, original note \$100,000, due December 2016, unsecured.	0	24,490
Note payable to Ford Motor Credit, payable in monthly installments of \$598, including interest at 4.24%, original note \$26,355, due December 2016, secured by vehicle.	0	7,013
Note payable to Ford Motor Credit, payable in monthly installments of \$598, including interest at 4.24%, original note \$26,355, due December 2016, secured by vehicle.	0	7,013
Note payable to PG&E, payable in monthly installments of \$1,907, including interest at 0%, original note \$99,183, due January 2017, unsecured.	1,907	24,796

Note 5 NOTES PAYABLE – (Continued)

Note payable to PG&E, payable in monthly installments of \$1,923, including interest at 0%, original note \$100,000, due March 2017, unsecured	28,846	51,923
Note payable to PG&E, payable in monthly installments of \$2,703, including interest at 0%, original note \$72,970, due April 2017, unsecured.	10,810	43,241
Note payable to PG&E, payable in monthly installments of \$1,818, including interest at 0%, original note \$100,000, due May 2017, unsecured.	9,091	30,909
Note payable to Richard Morgan, Jr., related party, payable in monthly installments of interest only \$9,963, interest at 3.50%, principal of \$589,000 was paid September 2016, and principal balance due June 2017, original note \$4,000,000, unsecured. Paid in full January 2017.	3,415,986	0
Note payable to PG&E, payable in monthly installments of \$1,534, including interest at 0%, original note \$73,615, due September 2017, unsecured.	13,803	32,206
Note payable to PG&E, payable in monthly installments of \$2,174, including interest at 0%, original note \$100,000, due September 2017, unsecured.	19,565	45,652
Note payable to Ally Bank, payable in monthly installments of \$647, including interest at 4.99%, original note \$34,301, due October 2017, secured by vehicle.	6,327	13,580
Note payable to Ford Motor Credit, payable in monthly installments of \$513, including interest at 0%, original note \$30,783, due November 2017, secured by vehicle.	5,644	11,800
Note payable to Ford Motor Credit, payable in monthly installments of \$649, including interest at 4.99%, original note \$34,313, due January 2018, secured by vehicle.	8,188	15,359
Note payable to Toyota Financial, payable in monthly installments of \$462, including interest at 3.55%, original note \$25,349, due August 2018, secured by vehicle.	8,953	14,076
Note payable to PG&E, payable in monthly installments of \$1,169, including interest at 0%, original note \$70,131, due November 2018, unsecured.	26,883	40,910
Note payable to PG&E, payable in monthly installments of \$2,083, including interest at 0%, original note \$100,000, due February 2019, unsecured.	52,083	79,167
Note payable to Toyota Financial Services, payable in monthly installments of \$488, including interest at 3.49%, original note \$26,240, due March 2019, secured by vehicle.	12,384	17,579

Note 5 NOTES PAYABLE – (Continued)

Note payable to Toyota Financial Services, payable in monthly installments of \$488, including interest at 3.49%, original note \$26,240, due March 2019, secured by vehicle.	12,384	17,579
Note payable to Chrysler Corporation, payable in monthly installments of \$463, including interest at 3.69%, original note \$25,288, due April 2019, secured by vehicle.	12,391	17,379
Note payable to Toyota Financial Services, payable in monthly installments of \$508, including interest at 0%, original note \$30,461, due August 2019, secured by vehicle.	16,246	22,338
Note payable to Toyota Financial Services, payable in monthly installments of \$584, including interest at 1.90%, original note \$33,353, due August 2019, secured by vehicle.	18,188	25,314
Note payable to Toyota Financial Services, payable in monthly installments of \$492, including interest at 1.90%, original note \$28,100, due January 2020, secured by vehicle.	17,647	23,149
Note payable to PG&E, payable in monthly installments of \$1,267, including interest at 0%, original note \$75,996, due February 2020, unsecured.	48,131	63,330
Note payable to Toyota Financial Services, payable in monthly installments of \$480, including interest at .91%, original note \$28,115, due April 2020, secured by vehicle.	18,886	24,901
Note payable to Toyota Financial Services, payable in monthly installments of \$472, including interest at 2.99%, original note \$26,300, due August 2020, secured by vehicle.	19,665	25,076
Note payable to Toyota Financial Services, payable in monthly installments of \$472, including interest at 3.39%, original note \$26,016, due January 2021, secured by vehicle.	21,570	26,016
Note payable to C & S Wholesale Grocers, Inc., payable in seven annual installments of \$277,814, interest at 0%, payments to be deducted from the earned annual rebates based on purchase volume, original note \$1,944,695, due May 2021, secured by a second position to National Cooperative Bank in inventory, property and equipment.	1,389,068	1,666,881
Note payable to Toyota Financial Services, payable in monthly installments of \$474, including interest at 4.00%, original note \$25,742, due April 2021, secured by vehicle.	22,997	0
Note payable to Lavonne Morgan, related party, payable in monthly installments of \$15,094, including interest at 7%, with an additional annual principle payment of \$100,000, original note \$2,633,156, due February 2022, unsecured (See Note 12 & 13).	1,037,739	1,238,227

Note 5 NOTES PAYABLE – (Continued)

Note Payable to National Cooperative Bank, FSB, payable in eighty-four monthly installments of \$67,199, including interest of 3.50% which shall be adjusted on the first day of January, 2017, and the first day of every month thereafter based on the Lender's Prime Rate minus twenty-five basis points, original note \$5,000,000, due January 2024, secured by inventory, property and equipment.

5,000,000 0

Note payable to National Cooperative Bank, FSB, payable in sixty monthly installments of \$66,667, plus interest at 5.16% through June 1, 2019, after which 60 payments of principal plus interest at the greater of 5% or the then prevailing Five Year Treasury Rate plus 350 basis points, original note \$8,000,000, secured by inventory, property and equipment.

6,000,000 6,800,000

Note payable to Richard Morgan, Jr., related party, payable in eighty-four monthly installments of \$104,167, plus interest at 7.00% through June 2023, original note, \$25,000,000, unsecured.

24,479,167 0

Total Notes Payable

41,734,549 10,473,291

Less Current Portion

(6,813,934) (1,654,948)

LONG-TERM PORTION

\$ 34,920,615 \$ 8,818,343

Maturities for notes payable for each of the next five years and thereafter are as follows:

Year Ending

December 30, 2017	\$ 6,813,934
December 29, 2018	3,341,604
December 28, 2019	3,320,972
December 26, 2020	3,324,586
December 25, 2021	3,140,775
Thereafter	21,792,678
TOTAL NOTES PAYABLE	\$ 41,734,549

The note agreement with National Cooperative Bank, FSB contains two restrictive covenants, debt service coverage ratio and EBITDA to funded debt. The Company is in compliance with all loan covenants at December 31, 2016 and December 26, 2015.

Note 6 OPERATING LEASE COMMITMENTS

The Company occupies all of its store facilities under operating lease agreements, which expire at various dates. Rent expenses under these leases for the year ended December 31, 2016 and December 26, 2015 were \$4,823,996 and \$4,552,853, respectively. Future minimum payments under these leases are as follows:

<u>Year Ending</u>	
December 30, 2017	\$ 4,025,129
December 29, 2018	3,913,013
December 28, 2019	3,784,686
December 26, 2020	3,285,618
December 25, 2021	2,847,377
Thereafter	<u>14,793,352</u>
TOTAL FUTURE MINIMUM LEASE PAYMENTS	\$ <u>32,649,175</u>

Many of these leases have renewal options and require payment of property taxes and insurance. At December 31, 2016, some store leases provide for additional rentals based on a percentage of sales, (ranging from 1% to 2%) if sales exceed a specified amount.

Note 7 CAPITALIZED LEASES

Leased property under capital leases at December 31, 2016 and December 26, 2015 consists of:

	<u>2016</u>	<u>2015</u>
Fixtures and equipment	\$ 611,944	\$ 625,680
Less accumulated depreciation	(478,043)	(406,963)
LEASED PROPERTY, NET	\$ <u>133,901</u>	\$ <u>218,717</u>

The following is a schedule by years of future minimum lease payments for all capital leases, together with the present value of the net lease payments at December 31, 2016:

<u>Year Ending</u>	
December 30, 2017	\$ 47,011
December 29, 2018	15,126
December 28, 2019	4,588
December 26, 2020	659
December 25, 2021	0
Thereafter	<u>0</u>
Total Minimum Lease Payments	67,384
Less amount representing interest and executors costs	(2,979)
Present Value of Net Minimum Lease Payments	64,405
Less Current Portion	(44,691)
LONG-TERM PORTION	\$ <u>19,714</u>

Note 8 PROFIT-SHARING PLAN

The Company has a profit-sharing plan for its eligible employees. The Company maintains a deferred-salary arrangement under Internal Revenue Service code section 401(k). The Company's matching contribution is up to 4% of annual employee compensation based on the employees' elective deferral; additional contributions may be made at the discretion of the Board of Directors. The expense for the profit sharing plan for the years ended December 31, 2016 and December 26, 2015 were \$433,422 and \$0, respectfully.

Note 9 ESOP

On January 1, 2006 the company adopted an Employee Stock Ownership Plan for its employees. Employees are eligible to participate after attaining the age of 21, completing one year of service and are credited with at least 1,000 hours of service during the year. All contributions to the plan are made by the employer and are at the employer's discretion. Company stock that was in the company's 401K plan was transferred to the ESOP in 2006. The expense for the company as a result of additions to the ESOP during the years ended December 31, 2016 and December 26, 2015, were \$1,321,394 and \$1,754,983, respectfully.

Note 10 INCOME TAX EXPENSE

Income tax expense consists of the following for the year ending December 31, 2016 and December 26, 2015:

	2016	2015
Federal income tax	\$ 0	\$ 0
Federal income tax – deferred	0	0
State income tax	108,000	119,931
State income tax – deferred	(1,523)	2,870
INCOME TAX EXPENSE (BENEFIT)	\$ 106,477	\$ 122,801

Deferred income tax expense arises from timing differences between financial and tax reporting and relates principally to depreciation, amortization and vacation accruals. On July 30, 2006, the Company converted to an S-Corp and is no longer subject to Federal taxes.

The net deferred tax assets/(liabilities) in the accompanying balance sheets includes the following amounts of deferred tax assets/(liabilities):

	2016		2015	
	State	Total	State	Total
Deferred tax current	\$ (299)	\$ (299)	\$ (1,779)	\$ (1,779)
Deferred tax non-current	(15,184)	(15,184)	(15,227)	(15,227)
NET DEFERRED TAX ASSETS (LIABILITIES)	\$ (15,483)	\$ (15,483)	\$ (17,006)	\$ (17,006)

The deferred tax liability results from the use of accelerated methods of depreciation of property and equipment and the difference in amortization methods, and the items that can be amortized, between tax and GAAP. The deferred tax asset results from a difference in inventory basis due to overhead costs capitalized in accordance with tax law and vacation accruals.

Note 11 STATEMENT OF CASH FLOWS

Cash paid for interest and income taxes for the year ended December 31, 2016 and December 26, 2015:

	2016	2015
Interest Paid	\$ 1,252,406	\$ 518,161
Income Taxes Paid	\$ 10,000	\$ 144,057

Note 12 STOCK TRANSACTIONS

During the year, the company redeemed 120,000 shares of its common stock from Richard E. Morgan Jr. After the transaction, the company is 100% owned by the North State Grocery Inc., Employee Stock Ownership Plan. The purchase price was \$250 per share (\$30,000,000) with \$5,000,000 down and a \$25,000,000 note payable over a seven year period at 7% interest. There will be a balloon payment due on June 2023 of \$16,556,181. The note carries a monthly principle payment of \$104,167 plus interest. Also, as part of the transaction a warrant representing up to 23,000 shares was issued and can be exercised at a price of \$250 a share after June 30, 2021 until the later of July 1, 2023 or payment in full of the \$25,000,000 note.

During the fiscal year ending July 29, 2006 North State Grocery, Inc., had a 200 for 1 stock split. After the stock split the company agreed to redeem 80,000 shares of stock from its 36% shareholder, effectively buying them out, for a purchase price of \$2,633,156. A note for \$2,633,156 was issued to pay for the purchase with monthly payments of \$15,094 at a 7% interest rate. An annual principal payment of \$100,000 will be paid in addition to the above monthly payment. The transaction resulted in an adjustment of \$2,629,156, which was recorded in the retained earnings account.

Immediately after the purchase of the 80,000 shares of stock they were sold to the ESOP plan for \$2,128,000. The transaction resulted in an increase of \$2,124,000 to additional paid in capital and created a new account, Unearned ESOP Shares, to account for the shares that have not yet been allocated in the ESOP.

Note 13 COMMON STOCK

As of July 1, 2016, all of the Company's stock is owned by the Employee Stock Ownership Plan.

Note 14 RELATED PARTY TRANSACTIONS

The Company leases stores and office facilities from a related party. Rent expense for these facilities for the year ended December 31, 2016 and December 26, 2015 were \$757,301 and \$626,268, respectively.

The Company has an outstanding loan with a related party, related to the purchase of company stock for the ESOP. The balance as of December 31, 2016 and December 26, 2015 is \$1,037,739 and \$1,238,227, respectively.

The Company has an outstanding loan with a related party, as a result of the redemption of company stock. The balance as of December 31, 2016 and December 26, 2015 is \$3,415,986 and \$0. This note was paid off in January of 2017.

The Company has an outstanding loan with a related party, as a result of the redemption of company stock. The balance as of December 31, 2016 and December 26, 2015 is \$24,479,167 and \$0.

Note 15 SUBSEQUENT EVENTS

Management has evaluated subsequent events through July 5, 2017, the date on which the financial statements were available to be issued.

SUPPLEMENTAL SCHEDULES

NORTH STATE GROCERY, INC.
SCHEDULES OF GROSS PROFIT
For The Year Ended December 31, 2016 and December 26, 2015

	2016		2015	
	AMOUNT	%	AMOUNT	%
SALES:				
Grocery	\$ 62,133,934	30.4	\$ 59,708,947	30.4
Grocery DSD	28,778,595	14.1	28,559,178	14.5
Liquor	20,820,260	10.2	18,960,571	9.7
Produce random weight	17,214,299	8.4	16,473,131	8.4
Meat	16,524,393	8.1	16,157,035	8.2
Meat/Deli	15,747,462	7.7	15,180,228	7.7
Bakery	15,062,040	7.4	13,648,376	7.0
Fuel	9,084,451	4.5	10,447,907	5.3
Produce set weight	7,558,313	3.7	6,989,541	3.5
General merchandise	7,139,814	3.5	6,693,347	3.4
Bakery/Deli	4,648,762	2.3	4,374,923	2.2
Discounts	(677,708)	(.3)	(684,457)	(.3)
TOTAL SALES	204,034,615	100.0	196,508,727	100.0
COST OF SALES:				
Grocery	45,612,597	22.4	43,815,199	22.3
Grocery DSD	20,691,869	10.1	20,478,657	10.4
Liquor	16,120,727	7.9	14,687,831	7.5
Produce random weight	12,227,230	6.0	11,811,544	6.0
Meat	11,504,022	5.6	11,729,723	6.0
Meat/Deli	10,829,586	5.3	10,562,389	5.4
Bakery	8,971,645	4.4	8,113,073	4.1
Fuel	8,270,246	4.1	9,438,535	4.8
Produce set weight	5,155,190	2.5	4,754,159	2.4
General merchandise	4,918,566	2.4	4,506,775	2.3
Bakery/Deli	3,032,009	1.5	2,805,139	1.4
TOTAL COST OF SALES	147,333,687	72.2	142,703,024	72.6
GROSS PROFIT:				
Grocery	16,521,337	26.6	15,893,748	26.6
Grocery DSD	8,086,726	28.1	8,080,521	28.3
Liquor	4,699,533	22.6	4,272,740	22.5
Produce random weight	4,987,069	29.0	4,661,587	28.3
Meat	5,020,371	30.4	4,427,312	27.4
Meat/Deli	4,917,876	31.2	4,617,839	30.4
Bakery	6,090,395	40.4	5,535,303	40.6
Fuel	814,205	9.0	1,009,372	9.7
Produce set weight	2,403,123	31.8	2,235,382	32.0
General Merchandise	2,221,248	31.1	2,186,572	32.7
Bakery/Deli	1,616,753	34.8	1,569,784	35.9
Discounts	(677,708)	(100.0)	(684,457)	(100.0)
TOTAL GROSS PROFIT	\$ 56,700,928	27.8	\$ 53,805,703	27.4

See accountant's report.

NORTH STATE GROCERY, INC.
SCHEDULES OF OPERATING EXPENSES
For The Year Ended December 31, 2016 and December 26, 2015

	2016		2015	
	AMOUNT	%	AMOUNT	%
OPERATING EXPENSE:				
Wages	\$ 20,815,668	10.2	\$ 19,241,363	9.8
Occupancy costs	5,168,260	2.5	4,802,302	2.4
Employee benefits	4,804,813	2.4	5,519,777	2.8
Utilities	3,316,099	1.7	3,278,817	1.7
Bank charges	2,101,801	1.0	1,915,637	1.0
Payroll taxes	2,077,498	1.0	1,896,041	1.0
Depreciation and amortization	1,881,225	.9	1,524,680	.8
Operating supplies	1,695,075	.8	1,740,609	.9
Repairs and maintenance	1,279,711	.6	1,255,870	.6
Worker's compensation	1,122,409	.6	1,326,114	.7
Legal and accounting	1,116,086	.6	769,800	.4
Promotions	779,707	.4	682,651	.3
Training	610,120	.3	562,922	.3
Dues and subscriptions	609,587	.3	583,682	.3
Insurance	463,327	.2	412,021	.2
Janitorial and laundry	278,583	.1	271,535	.1
Telephone	249,903	.1	252,190	.1
Advertising	204,983	.1	183,712	.1
Travel	196,776	.1	71,604	.0
Other contract services	181,929	.1	167,956	.1
Taxes and licenses	180,083	.1	177,977	.1
Office supplies	163,937	.1	119,374	.1
Auto expense	108,917	.1	100,947	.1
Settlements	62,671	.0	0	.0
Bad debts	41,049	.0	5,223	.0
Equipment rent	32,287	.0	29,028	.0
Cash shortage	13,337	.0	27,543	.0
Penalties	10,750	.0	0	.0
Security	4,623	.0	28,535	.0
TOTAL OPERATING EXPENSES	\$ <u>49,571,214</u>	<u>24.3</u>	\$ <u>46,947,910</u>	<u>23.9</u>

See accountant's report.