

NORTH STATE GROCERY, INC.

FINANCIAL STATEMENTS
December 26, 2015 and December 27, 2014

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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 26, 2015 and December 27, 2014, and the related statements of income, retained earnings, and cash flows for the years 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. 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 26, 2015 and December 27, 2014, and the results of its operations and its cash flows for the years 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 16-17 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 & Reidholdt

Redding, California
August 25, 2016

NORTH STATE GROCERY, INC.
BALANCE SHEETS
December 26, 2015 and December 27, 2014

ASSETS

	<u>2015</u>	<u>2014</u>
CURRENT ASSETS:		
Cash	\$ 3,994,859	\$ 3,533,783
Trade receivables (net of allowances for doubtful accounts of \$506 and \$389, respectively)	60,828	55,190
Other receivables (net of allowances for doubtful accounts of \$72,967 and \$84,259, respectively)	1,058,419	839,851
Merchandise inventory	9,894,199	9,895,415
Prepaid expenses	<u>616,700</u>	<u>605,455</u>
TOTAL CURRENT ASSETS	<u>15,625,005</u>	<u>14,929,694</u>
PROPERTY AND EQUIPMENT (Note 2):	29,047,529	25,997,885
Less accumulated depreciation	(<u>15,543,694</u>)	(<u>15,029,766</u>)
PROPERTY AND EQUIPMENT, NET	<u>13,503,835</u>	<u>10,968,119</u>
OTHER ASSETS:		
Off-sale liquor licenses	581,014	581,014
Investment in real estate (Note 3)	1,390,651	1,390,651
Goodwill – net (Note 1)	1,054,006	1,054,006
Loan fees - net of accumulated amortization (Note 4)	118,487	137,139
Deposits	10,054	35,635
Cash surrender value of officers' life insurance	<u>190,636</u>	<u>136,906</u>
TOTAL OTHER ASSETS	<u>3,344,848</u>	<u>3,335,351</u>
TOTAL ASSETS	\$ <u><u>32,473,688</u></u>	\$ <u><u>29,233,164</u></u>

LIABILITIES AND STOCKHOLDERS' EQUITY

	2015	2014
CURRENT LIABILITIES:		
Current maturities of notes payable (Note 5 and 13)	\$ 1,654,948	\$ 1,625,365
Obligations under capital leases, current portion (Note 7)	58,318	76,084
Trade accounts payable and disbursements outstanding	6,779,543	5,417,568
Accrued wages, payroll taxes, and employee benefits withheld	2,159,499	2,023,354
Accrued liabilities (Note 13)	1,906,483	1,916,629
Deferred income taxes (Note 10)	1,779	2,829
TOTAL CURRENT LIABILITIES	12,560,570	11,061,829
 LONG-TERM LIABILITIES:		
Notes payable, net of current maturities (Note 5 and 13)	8,818,343	10,209,473
Obligations under capital leases, net of current portion (Note 7)	64,405	107,098
Deferred income taxes (Note 10)	15,227	12,048
TOTAL LONG-TERM LIABILITIES	8,897,975	10,328,619
TOTAL LIABILITIES	21,458,545	21,390,448
 STOCKHOLDERS' EQUITY:		
Common stock, no par value, 1,000,000 shares authorized, 222,800 shares issued and outstanding	11,140	11,140
Additional paid in capital (Note 12)	4,606,134	3,610,768
Unearned ESOP shares (Note 9)	(699,282)	(811,258)
Retained earnings	7,097,151	5,032,066
TOTAL STOCKHOLDERS' EQUITY	11,015,143	7,842,716
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 32,473,688	\$ 29,233,164

See accompanying notes and accountant's report.

NORTH STATE GROCERY, INC.
STATEMENTS OF INCOME
For The Year Ended December 26, 2015 and December 27, 2014

	2015		2014	
	Amount	%	Amount	%
SALES	\$ 196,508,727	100.0	\$ 191,462,454	100.0
COST OF SALES	<u>142,703,024</u>	<u>72.6</u>	<u>140,483,363</u>	<u>73.4</u>
GROSS PROFIT	53,805,703	27.4	50,979,091	26.6
Lottery income	73,921	.0	70,947	.0
Money order fees	14,999	.0	16,596	.0
Miscellaneous income	<u>104,182</u>	<u>.1</u>	<u>170,568</u>	<u>.1</u>
TOTAL OPERATING REVENUES	53,998,805	27.5	51,237,202	26.7
OPERATING EXPENSES	<u>46,947,910</u>	<u>23.9</u>	<u>44,261,232</u>	<u>23.1</u>
INCOME FROM OPERATIONS (Note 14)	<u>7,050,895</u>	<u>3.6</u>	<u>6,975,970</u>	<u>3.6</u>
OTHER INCOME (EXPENSES):				
Interest income	6,954	.0	0	.0
Interest expense	(512,694)	(.3)	(638,502)	(.3)
Gain (loss) on disposal of assets	(63,367)	(.0)	(129,833)	(.1)
OTHER EXPENSES, NET	(<u>569,107</u>)	(<u>.3</u>)	(<u>768,335</u>)	(<u>.4</u>)
INCOME (LOSS) BEFORE TAXES	6,481,788	3.3	6,207,635	3.2
Income tax (expense) benefit (Note 10)	(<u>122,801</u>)	(<u>.1</u>)	(<u>99,169</u>)	(<u>.0</u>)
NET INCOME (LOSS)	\$ <u><u>6,358,987</u></u>	<u>3.2</u>	\$ <u><u>6,108,466</u></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 26, 2015 and December 27, 2014

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 Income	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>

2014					
	Common Stock	Paid In Capital	Unearned ESOP Share	Retained Earnings	Total
Beginning Balance	\$ 11,140	\$ 3,271,537	\$ (927,153)	\$ 440,137	\$ 2,795,661)
Current Period Inc(Loss)	0	0	0	6,108,467	6,108,467
Shareholder Distributions	0	0	0	(1,896,667)	(1,896,667)
ESOP Funding	0	339,231	115,895	380,129	835,255
Ending Balance	<u>\$ 11,140</u>	<u>\$ 3,610,768</u>	<u>\$ (811,258)</u>	<u>\$ 5,032,066</u>	<u>\$ 7,842,716</u>

See accompanying notes and accountant's report.

NORTH STATE GROCERY, INC.
STATEMENTS OF CASH FLOWS
For The Year Ended December 26, 2015 and December 27, 2014

	<u>2015</u>	<u>2014</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ 6,358,987	\$ 6,108,467
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,524,680	1,296,753
Loss on disposition of fixed assets	63,367	129,833
(Increase) Decrease in cash surrender value of life insurance	(53,730)	(50,417)
Increase (Decrease) in deferred income tax liability	2,129	741
Changes in current assets and liabilities:		
Trade accounts receivable	(5,638)	4,442
Other accounts receivable	(218,568)	(130,090)
Merchandise inventory	1,216	(123,276)
Prepaid expenses	(11,245)	(150,972)
Deposits	25,581	21,295
Trade accounts payable	1,361,975	(2,308,533)
Accrued salaries and wages, payroll taxes and employee benefits	136,145	22,411
Accrued liabilities	(10,146)	240,746
Accrued interest	<u>0</u>	<u>(166,750)</u>
NET CASH PROVIDED BY OPERATIONS	<u>9,174,753</u>	<u>4,894,650</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of assets	56,907	46,907
Purchase of property and equipment	(<u>4,162,018</u>)	(<u>3,113,800</u>)
NET CASH (USED) BY INVESTING ACTIVITIES	(<u>4,105,111</u>)	(<u>3,066,893</u>)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings on notes payable	329,396	10,243,018
Principal payments on notes payable	(1,690,943)	(8,830,458)
ESOP Funding	1,866,959	455,126
Proceeds from borrowings on capital leases	18,417	143,621
Shareholder distributions	(5,053,519)	(1,516,538)
Payment of loan fees	0	(42,028)
Payments on capital leases	(<u>78,876</u>)	(<u>110,415</u>)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	(<u>4,608,566</u>)	<u>342,326</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	461,076	2,170,083
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>3,533,783</u>	<u>1,363,700</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ <u><u>3,994,859</u></u>	\$ <u><u>3,533,783</u></u>

See accompanying notes and accountant's report.

NORTH STATE GROCERY, INC.
NOTES TO THE FINANCIAL STATEMENTS
December 26, 2015 and December 27, 2014

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. As of December 26, 2015 and December 27, 2014, the Company had cash and cash equivalents in excess of the FDIC insured limit of \$337,822 and \$697,899, respectively.

ACCOUNTS RECEIVABLE - Allowances and reserves for doubtful accounts have been recorded at December 26, 2015 and December 27, 2014. 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, or 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.

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 26, 2015 and December 27, 2014 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 26, 2015 and December 27, 2014 is \$1,754,983 and \$719,360, 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 his share of the Company's taxable income for both federal and California tax purposes.

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 26, 2015 and December 27, 2014. The Company's federal and state income tax returns for 2012 through 2015 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 26, 2015 and December 27, 2014, 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 26, 2015 and December 27, 2014 were \$183,712 and \$178,789, respectively.

Note 2 PROPERTY AND EQUIPMENT

The following is a summary of property and equipment as of December 26, 2015 and December 27, 2014:

	<u>2015</u>	<u>2014</u>
Fixtures and equipment	\$ 19,808,974	\$ 17,296,852
Leasehold improvements	7,239,743	6,566,044
Vehicles	527,270	655,645
Office equipment	<u>1,471,542</u>	<u>1,479,344</u>
TOTAL	\$ <u>29,047,529</u>	\$ <u>25,997,885</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. Also, as a result of the transaction the Company booked an interest expense accrual of \$166,750 related to the note payable the Company assumed. In the year ended December 27, 2014, the \$500,000 note payable and the accrued interest associated with the transaction were paid in full.

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 26, 2015 and December 27, 2014 were \$18,652 and \$66,554, respectively.

The Company's intangible assets consisted of the following at December 26, 2015 and December 27, 2014:

	<u>2015</u>	<u>2014</u>
LOAN FEES		
Costs	147,028	147,028
Accumulated amortization	(<u>28,541</u>)	(<u>9,889</u>)
	<u>118,487</u>	<u>137,139</u>
TOTALS		
Costs	147,028	147,028
Accumulated amortization	(<u>28,541</u>)	(<u>9,889</u>)
TOTAL NET	\$ <u>118,487</u>	\$ <u>137,139</u>

Future amortization expenses as of December 26, 2015 are as follows:

Year Ending:

December 31, 2016	\$ 16,072
December 30, 2017	13,703
December 29, 2018	13,703
December 28, 2019	13,703
December 26, 2020	13,703
Thereafter	<u>47,603</u>
TOTAL	\$ <u>118,487</u>

Note 5 NOTES PAYABLE

Notes payable consist of the following at December 26, 2015 and December 27, 2014:

	<u>2015</u>	<u>2014</u>
Note payable to National Cooperative Bank, Revolving Credit Line in the amount of \$2,000,000, currently matures on June 1, 2016, interest at 4.25% which is based on the lenders base rate plus 100 basis points, secured by inventory, property and equipment.	0	0
Note payable to Ford Motor Credit Company, payable in monthly installments of \$657, including interest at 7.49%, original note \$27,174 due January 2015, secured by vehicle.	0	653
Note payable to R & K Market, payable in monthly installments of \$2,769, including interest at 10%, original note \$60,000, due January 2015.	0	2,746
Note payable to PG&E, payable in monthly installments of \$2,651, including interest at 0%, original note \$98,078, due September 2015, unsecured.	0	23,857
Note payable to PG&E, payable in monthly installments of \$2,564, including interest at 0%, original note \$100,000, due January 2016, unsecured.	2,564	33,333
Note payable to PG&E, payable in monthly installments of \$2,403, including interest at 0%, original note \$67,273, due June 2016, unsecured.	14,416	43,247
Note payable to PG&E, payable in monthly installments of \$2,192, including interest at 0%, original note \$61,368, due October 2016, unsecured.	21,917	48,218
Note payable to PG&E, payable in monthly installments of \$2,041, including interest at 0%, original note \$100,000, due December 2016, unsecured.	24,490	48,980
Note payable to PG&E, payable in monthly installments of \$2,041, including interest at 0%, original note \$100,000, due December 2016, unsecured.	24,490	48,980
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.	7,013	13,735
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.	7,013	13,735
Note payable to PG&E, payable in monthly installments of \$1,907, including interest at 0%, original note \$99,183, due January 2017, unsecured.	24,796	47,684
Note payable to PG&E, payable in monthly installments of \$1,923, including interest at 0%, original note \$100,000, due March 2017, unsecured.	51,923	75,000

Note 5 NOTES PAYABLE – (Continued)

Note payable to PG&E, payable in monthly installments of \$2,703, including interest at 0%, original note \$72,970, due April 2017, unsecured.	43,241	0
Note payable to PG&E, payable in monthly installments of \$1,818, including interest at 0%, original note \$100,000, due May 2017, unsecured.	30,909	52,727
Note payable to PG&E, payable in monthly installments of \$1,534, including interest at 0%, original note \$73,615, due September 2017, unsecured.	32,206	50,610
Note payable to PG&E, payable in monthly installments of \$2,174, including interest at 0%, original note \$100,000, due September 2017, unsecured.	45,652	71,739
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.	13,580	20,480
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.	11,800	17,957
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.	15,359	22,175
Note payable to Toyota Financial, payable in monthly installments of \$462, including interest at 3.49%, original note \$25,349, due August 2018, secured by vehicle.	14,076	19,021
Note payable to PG&E, payable in monthly installments of \$1,169, including interest at 0%, original note \$70,131, due November 2018, unsecured.	40,910	54,936
Note payable to PG&E, payable in monthly installments of \$2,083, including interest at 0%, original note \$100,000, due February 2019, unsecured.	79,167	0
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.	17,579	22,594
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.	17,579	22,594
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.	17,379	22,184
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.	22,338	28,430

Note 5 NOTES PAYABLE – (Continued)

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.	25,314	31,228
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.	23,149	28,100
Note payable to PG&E, payable in monthly installments of \$1,267, including interest at 0%, original note \$75,996, due February 2020, unsecured.	63,330	0
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.	24,901	0
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.	25,076	0
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.	26,016	0
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.	1,666,881	1,944,695
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).	1,238,227	1,425,200
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.	<u>6,800,000</u>	<u>7,600,000</u>
Total Notes Payable	10,473,291	11,834,838
Less Current Portion	(<u>1,654,948</u>)	(<u>1,625,365</u>)
LONG-TERM PORTION	\$ <u>8,818,343</u>	\$ <u>10,209,473</u>

Note 5 NOTES PAYABLE – (Continued)

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

<u>Year Ending</u>	
December 31, 2016	\$ 1,654,948
December 30, 2017	1,501,392
December 29, 2018	1,424,042
December 28, 2019	1,381,883
December 26, 2020	1,359,509
Thereafter	3,151,517
TOTAL NOTES PAYABLE	\$ <u>10,473,291</u>

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 26, 2015 and December 27, 2014.

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 26, 2015 and December 27, 2014 were \$4,552,853 and \$4,334,192, respectively. Future minimum payments under these leases are as follows:

<u>Year Ending</u>	
December 31, 2016	\$ 4,008,385
December 30, 2017	3,849,117
December 29, 2018	3,574,250
December 28, 2019	3,321,573
December 26, 2020	2,784,105
Thereafter	<u>17,719,041</u>
TOTAL FUTURE MINIMUM LEASE PAYMENTS	\$ <u>35,256,471</u>

Many of these leases have renewal options and require payment of property taxes and insurance. At December 26, 2015, 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 26, 2015 and December 27, 2014 consists of:

	<u>2015</u>	<u>2014</u>
Fixtures and equipment	\$ 625,680	\$ 791,271
Less accumulated depreciation	(406,963)	(496,086)
LEASED PROPERTY, NET	\$ <u>218,717</u>	\$ <u>295,185</u>

Note 7 CAPITALIZED LEASES – (Continued)

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 26, 2015:

<u>Year Ending</u>		
December 31, 2016	\$	63,248
December 30, 2017		47,011
December 29, 2018		45,512
December 28, 2019		10,665
December 26, 2020		686
Thereafter		0
Total Minimum Lease Payments		<u>167,122</u>
Less amount representing interest and executors costs	(<u>44,399</u>)
Present Value of Net Minimum Lease Payments		<u>122,723</u>
Less Current Portion	(<u>58,318</u>)
LONG-TERM PORTION	\$	<u><u>64,405</u></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 discretionary; additional contributions may be made at the discretion of the Board of Directors. The expense for the profit sharing plan was \$0 for the year ended December 26, 2015 and December 27, 2014.

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 company expensed \$1,866,959 as a result of additions to the ESOP during the year ended December 26, 2015. The company expensed \$719,360 as a result of additions to the ESOP during the year ended December 27, 2014.

Note 10 INCOME TAX EXPENSE

Income tax expense consists of the following for the year ending December 26, 2015 and December 27, 2014:

	2015	2014
Federal income tax	\$ 0	\$ 0
Federal income tax – deferred	0	0
State income tax	119,931	98,428
State income tax – deferred	<u>2,870</u>	<u>741</u>
INCOME TAX EXPENSE (BENEFIT)	\$ <u><u>122,801</u></u>	\$ <u><u>99,169</u></u>

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.

Note 10 INCOME TAX EXPENSE – (continued)

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

	2015		2014	
	State	Total	State	Total
Deferred tax current	\$ (1,779)	\$ (1,779)	\$ (2,829)	\$ (2,829)
Deferred tax non-current	(15,227)	(15,227)	(12,048)	(12,048)
NET DEFERRED TAX				
ASSETS (LIABILITIES)	\$ (17,006)	\$ (17,006)	\$ (14,877)	\$ (14,877)

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 26, 2015 and December 27, 2014:

	2015	2014
Interest Paid	\$ 518,161	\$ 806,356
Income Taxes Paid	\$ 144,057	\$ 37,100

Note 12 STOCK TRANSACTIONS

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 RELATED PARTY TRANSACTIONS

The Company leases stores and office facilities from a related party. Rent expense for these facilities for the year ended December 26, 2015 and December 27, 2014 were \$626,268 and \$612,324 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 26, 2015 and December 27, 2014 is \$1,238,227 and \$1,425,200, respectively.

The Company had a loan with the 54% shareholder and a related party. The balances as of December 26, 2015 and December 27, 2014 are \$0 and \$0, respectively. The shareholder and related party secured a note with Rabobank. The loan was paid off in 2014 using the proceeds from the new loan with National Cooperative Bank.

Note 14 SUBSEQUENT EVENTS

Subsequent to the year end, 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 in 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.

As a result of the transaction Notes Payable will increase by \$25,000,000. The Common Stock account will be reduced by \$6,000 to a balance of \$5,140. Additional Paid in Capital will be reduced by \$4,606,134 to a balance of \$0. The remaining \$25,387,866 will reduce the Retained Earnings account to a negative balance of \$18,290,715.

Management has evaluated subsequent events through August 25, 2016, 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 26, 2015 and December 27, 2014

	2015		2014	
	AMOUNT	%	AMOUNT	%
SALES:				
Grocery	\$ 59,708,947	30.4	\$ 58,917,375	30.8
Grocery DSD	28,559,178	14.5	26,897,638	14.1
Produce	23,462,672	11.9	22,883,121	11.9
Liquor	18,960,571	9.7	17,502,589	9.2
Meat	16,157,035	8.2	15,165,180	7.9
Meat/Deli	15,180,228	7.7	14,749,398	7.7
Bakery	13,648,376	7.0	12,623,612	6.6
Fuel	10,447,907	5.3	12,614,270	6.6
General merchandise	6,693,347	3.4	6,583,428	3.4
Bakery/Deli	4,374,923	2.2	4,226,574	2.2
Discounts	(684,457)	(.3)	(700,731)	(.4)
TOTAL SALES	196,508,727	100.0	191,462,454	100.0
COST OF SALES:				
Grocery	43,815,199	22.3	43,249,249	22.6
Grocery DSD	20,478,657	10.4	19,370,235	10.1
Produce	16,565,703	8.4	15,959,570	8.3
Liquor	14,687,831	7.5	13,517,082	7.1
Meat	11,729,723	6.0	11,538,691	6.0
Meat/Deli	10,562,389	5.4	10,260,040	5.4
Bakery	8,113,073	4.1	7,597,452	4.0
Fuel	9,438,535	4.8	11,711,731	6.1
General merchandise	4,506,775	2.3	4,518,559	2.4
Bakery/Deli	2,805,139	1.4	2,760,754	1.4
TOTAL COST OF SALES	142,703,024	72.6	140,483,363	73.4
GROSS PROFIT:				
Grocery	15,893,748	26.6	15,668,126	26.6
Grocery DSD	8,080,521	28.3	7,527,403	28.0
Produce	6,896,969	29.4	6,923,551	30.3
Liquor	4,272,740	22.5	3,985,507	22.8
Meat	4,427,312	27.4	3,626,489	23.9
Meat/Deli	4,617,839	30.4	4,489,358	30.4
Bakery	5,535,303	40.6	5,026,160	39.8
Fuel	1,009,372	9.7	902,539	7.2
General Merchandise	2,186,572	32.7	2,064,869	31.4
Bakery/Deli	1,569,784	35.9	1,465,820	34.7
Discounts	(684,457)	(100.0)	(700,731)	(100.0)
TOTAL GROSS PROFIT	\$ 53,805,703	27.4	\$ 50,979,091	26.6

See accountant's report.

NORTH STATE GROCERY, INC.
SCHEDULES OF OPERATING EXPENSES
For The Year Ended December 26, 2015 and December 27, 2014

	2015		2014	
	AMOUNT	%	AMOUNT	%
OPERATING EXPENSE:				
Wages	\$ 19,241,363	9.8	\$ 18,807,920	9.8
Employee benefits	5,519,777	2.8	4,371,185	2.3
Occupancy costs	4,802,302	2.4	4,690,929	2.4
Utilities	3,278,817	1.7	3,372,845	1.8
Bank charges	1,915,637	1.0	1,820,011	1.0
Payroll taxes	1,896,041	1.0	1,905,782	1.0
Operating supplies	1,740,609	.9	1,697,647	.9
Depreciation and amortization	1,524,680	.8	1,296,753	.7
Worker's compensation	1,326,114	.7	1,560,199	.8
Repairs and maintenance	1,255,870	.6	1,019,974	.5
Legal and accounting	769,800	.4	437,335	.2
Promotions	682,651	.3	634,661	.3
Dues and subscriptions	583,682	.3	454,980	.2
Training	562,922	.3	359,262	.2
Insurance	412,021	.2	444,444	.2
Janitorial and laundry	271,535	.1	281,564	.2
Telephone	252,190	.1	252,023	.1
Advertising	183,712	.1	178,789	.1
Taxes and licenses	177,977	.1	181,703	.1
Other contract services	167,956	.1	107,816	.1
Office supplies	119,374	.1	132,616	.1
Auto expense	100,947	.1	154,322	.1
Travel	71,604	.0	24,898	.0
Equipment rent	29,028	.0	9,586	.0
Security	28,535	.0	36,718	.0
Cash shortage	27,543	.0	19,989	.0
Bad debts	5,223	.0	2,531	.0
Settlements	0	.0	4,750	.0
TOTAL OPERATING EXPENSES	\$ 46,947,910	23.9	\$ 44,261,232	23.1

See accountant's report.