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

FORM 10-K

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

For the fiscal year ended December 25, 2016

or

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

Commission file number 001-36104

POTBELLY CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	**36-4466837**
(State of incorporation)	**(I.R.S. Employer Identification No.)**
111 N. Canal Street, Suite 850 Chicago, Illinois	**60606**
(Address of principal executive offices)	**(Zip Code)**

Registrant's telephone number, including area code (312) 951-0600

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $.01 par value	**The Nasdaq Stock Market LLC (Nasdaq Global Select Market)**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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, and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

Indicate by check mark whether registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer	☐	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 Act). Yes ☐ No ☒

As of June 26, 2016, the last trading day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the registrant's outstanding common equity held by non-affiliates was $250.6 million, based on the closing price of the registrant's common stock on such date as reported on the Nasdaq Global Select Market.

As of February 17, 2017, 25,071,577 shares of the registrant's common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for its 2017 Annual Meeting to be filed with the Securities and Exchange Commission not later than 120 days after the end of the year covered by this Annual Report are incorporated by reference into Part III of this Annual Report.

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CAUTIONARY STATEMENT ON FORWARD-LOOKING STATEMENTS

Forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), are made throughout this Annual Report and are intended to come within the safe harbor protection provided by those sections. These forward-looking statements can generally be identified by the use of forward-looking terminology, including the terms "believes," "estimates," "anticipates," "expects," "strives," "goal," "seeks," "projects," "intends," "forecasts," "plans," "may," "will" or "should" or, in each case, their negative or other variations or comparable terminology. They appear in a number of places throughout this Annual Report and include statements regarding our intentions, beliefs or current expectations concerning, among other things, our results of operations, financial condition, liquidity, prospects, growth, strategies and the industry in which we operate.

By their nature, forward-looking statements involve risks and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future. We believe that these risks and uncertainties include, but are not limited to, those described in "Risk Factors" in Item 1A, which include, but are not limited to, the following:

- competition in the restaurant industry, which is highly competitive and includes many larger, more well-established companies;
- changes in economic conditions, including the effects of consumer confidence and discretionary spending; the future cost and availability of credit; and the liquidity or operations of our suppliers and other service providers;
- fluctuation in price and availability of commodities, including but not limited to items such as beef, poultry, grains, dairy and produce and energy supplies, where prices could increase or decrease more than we expect;
- our ability to identify and secure new locations and expand our operations (which is dependent upon various factors such as the availability of attractive sites for new shops), negotiate suitable lease terms, obtain all required governmental permits including zoning approvals on a timely basis, control construction and development costs and obtain capital to fund such costs, and recruit, train and retain qualified operating personnel;
- changes in consumer tastes and lack of acceptance or awareness of our brand in existing or new markets; damage to our reputation caused by, for example, any perceived reduction in the quality of our food, service or staff or an adverse change in our culture, concerns regarding food safety and food-borne illness or adverse opinions about the health effects of our menu offerings;
- local, regional, national and international economic and political conditions; the seasonality of our business; demographic trends; traffic patterns and our ability to effectively respond in a timely manner to changes in traffic patterns; the cost of advertising and media; inflation or deflation; unemployment rates; interest rates; and increases in various costs, such as real estate and insurance costs;
- adverse weather conditions, local strikes, natural disasters and other disasters, especially in local or regional areas in which our shops are concentrated;
- litigation or legal complaints alleging, among other things, illness, injury or violations of federal and state workplace and employment laws and our ability to obtain and maintain required licenses and permits;
- government actions and policies; tax and other legislation; regulation of the restaurant industry; and accounting standards or pronouncements;
- our reliance on a limited number of suppliers for our major products and on a distribution network with a limited number of distribution partners for the majority of our national distribution program;
- security breaches of confidential customer information in connection with our electronic processing of credit and debit card transactions or the failure of our information technology system;
- our ability to adequately protect our intellectual property; and
- other factors discussed under "Business" in Item 1, "Risk Factors" in Item 1A and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7.

These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements included in this document. These risks and uncertainties, as well as other risks of which we are not aware or which we currently do not believe to be material, may cause our actual future results to be materially different than those expressed in our forward-looking statements. We do not undertake to update our forward-looking statements, whether as a result of new information, future events or otherwise, except as may be required by law.

PART I

ITEM 1. BUSINESS

The Neighborhood Sandwich Shop

Potbelly is a fast-growing neighborhood sandwich concept offering toasty warm sandwiches, signature salads and other fresh menu items served by engaging people in an environment that reflects the Potbelly brand. Our combination of product, people and place is how we deliver on our passion to be "The Best Place for Lunch." Our sandwiches, salads and hand-dipped milkshakes are all made fresh to order and our cookies are baked fresh each day. Our employees are trained to engage with our customers in a genuine way to provide a personalized experience. Our shops feature vintage design elements and locally-themed décor inspired by the neighborhood that we believe create a lively atmosphere. Through this combination, we believe we are creating a devoted base of Potbelly fans that return again and again and that we are expanding one sandwich shop at a time.

We believe that a key to our past and future success is our culture. It is embodied in *The Potbelly Advantage*, which is an expression of our Vision, Mission, Passion and Values, and the foundation of everything we do. Our Vision is for our customers to feel that we are their "Neighborhood Sandwich Shop" and to tell others about their great experience. Our Mission is to make people really happy, to make more money and to improve every day. Our Passion is to be "The Best Place for Lunch." Our Values embody both how we lead and how we behave and form the cornerstone of our culture. We use simple language that resonates from the frontline associate to the most senior levels of the organization, creating shared expectations and accountabilities in how we approach our day-to-day activities. We strive to be a fun, friendly and hardworking group of people who enjoy taking care of our customers, while at the same time taking care of each other.

We believe executing on *The Potbelly Advantage* at a high level creates a distinct competitive advantage and drives our operating and financial results, as illustrated by the following:

- As of December 25, 2016, we had a domestic base of 441 shops in 29 states and the District of Columbia. Of these, the company operates 411 shops and franchisees operate 30 shops. In addition, there are 13 international franchised shops, including 11 shops in the Middle East, 1 shop in the United Kingdom and 1 shop in Canada. Total shop growth was 11.3% over the prior year;
- We achieved positive annual comparable store sales growth for the past five years, with levels of 3.4%, 1.5%, 0.1%, 4.4% and 1.4% in 2012, 2013, 2014, 2015 and 2016, respectively (comparable store sales reflect the change in year-over-year sales of shops open for 15 or more months);
- From 2015 to 2016, we increased our total revenue 9.2% to $407.1 million, our net income attributable to Potbelly 45.9% to $8.2 million, and our adjusted EBITDA 15.3% to $48.0 million; and
- From 2012 to 2016, we generated shop-level profit margin of 20.7%, 20.2%, 19.2%, 19.4% and 19.7% in 2012, 2013, 2014, 2015 and 2016, respectively (shop-level profit margin measures net shop sales less shop operating expenses as a percentage of net shop sales).

Shop-level profit margin and adjusted EBITDA are not required by, nor presented in accordance with, U.S. generally accepted accounting principles ("GAAP"). See "Selected Financial Data" in Item 6 for a discussion of adjusted EBITDA, adjusted EBITDA margin and shop-level profit margin and a reconciliation of the differences between adjusted EBITDA and net income (loss) and shop-level profit and income (loss) from operations, as well as a calculation of shop-level profit margin. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 for a definition of comparable store sales.

Our History

Potbelly started in 1977 as a small antique store on Lincoln Avenue in Chicago. To boost sales, the original owner began offering toasty warm sandwiches to customers. Soon, people who had no interest in antiques were stopping by to enjoy the delicious sandwiches, homemade desserts and live music featured in the shop. As time passed, Potbelly became a well-known neighborhood destination with a loyal following of regulars and frequent lines out the door.

We opened our second shop in 1997 and continued to open shops in more neighborhoods reaching 100 shops in 2005, 200 shops in 2008, 300 shops in 2013 and 400 shops in 2016. Throughout our growth, each new shop has maintained a similar look, vibe and experience that defines the Potbelly brand. Though our shops vary in size and shape, we maintain core elements in each new location, such as fast and efficient line flow, vintage décor customized with local details and exceptional customer focus.

Just like our first shop on Lincoln Avenue, we are committed to building deep community roots in all the neighborhoods we serve.

Our Competitive Strengths

We believe the following competitive strengths provide a platform for us to achieve continued growth:

Simple, Made-to-Order Food. Our menu features items made from high quality ingredients, such as fresh vegetables, hearth-baked bread and all-natural, white meat chicken. We also use whole muscle turkey, ham and roast beef, rather than chopped and formed deli meats. See "—Our Food—Our Menu" for more information on our ingredients. Our sandwiches are made fresh to order, and many are based on the original recipes from 1977. They are served toasty warm on our signature multigrain or regular bread or on our multigrain Flats, all of which are delivered to our shops. We slice our meats and cheeses daily in each shop to ensure freshness. Our sandwiches can be customized with a variety of toppings, including our unique Potbelly hot peppers that are made with a combination of spices exclusively for us. We make our sandwiches to have the right balance of ingredients with the last bite tasting as good as the first. Our generously sized cookies are baked fresh daily in each shop, and our hand-dipped shakes, malts and smoothies are made from real ingredients and come with our signature butter cookie on the straw. Our menu regularly evolves based on consumer trends and customer feedback. Among other things, we solicit customer feedback quarterly via in-person "Customer Advisories" in our major markets and conduct an annual customer survey to help determine trends. See "—Our Food—Customer Feedback" for more information about these surveys. We believe our simple menu and freshly-made food offer ease of ordering and broad appeal and help us create loyal Potbelly fans that return again and again.

Differentiated Customer Experience That Delivers a Neighborhood Feel. We strive to provide a positive customer experience that is driven by both our employees and the atmosphere of our shops. We look to hire employees that are outgoing people and train them to interact with our customers in a genuine way while providing fast service. To support the neighborhood feel of our shops, most of our managers live in the neighborhood where their shop is located. We believe this allows them to get to know their customers, understand the unique character of each neighborhood and form deep roots within the community. Each of our shops features vintage décor and shared design elements, such as the use of wood, wallpaper motifs and our signature Potbelly stove. In addition, our shops display locally-themed photos and other decorative items inspired by the neighborhood. We aim to enhance our atmosphere with live, local musicians that perform weekly in the majority of our shops. Every Potbelly location strives to be "The Neighborhood Sandwich Shop," creating devoted fans who tell others about their experience. We believe our shops are strongly integrated into the neighborhood through the use of local managers, musicians and locally-themed décor and engage with customers through initiatives such as fundraising for local causes and other promotions that cater to local interests. The unique Potbelly experience encourages repeat customer visits and drives increased sales.

Attractive Shop Economics. Our shop model is designed to generate, and has generated, strong cash flow, attractive shop-level financial results and high returns on investment. We operate our shops successfully in a wide range of geographic markets, population densities and real estate settings. We aim to generate average shop-level profit margins, a non-GAAP measure, above 20% and target cash-on-cash returns, on new company-operated shops, above 25% after two full years of operation. Our ability to achieve such margins and returns depends on a number of factors. For example, we face increasing labor and commodity costs, which we have partially offset by increasing menu prices. Although there is no guarantee that we will be able to maintain these returns, we believe our attractive shop economics support our ability to profitably grow our brand in new and existing markets.

Management Team with Substantial Operating Experience. Our senior management team has extensive operating experience across disciplines in the restaurant and retail sectors, including store operations, marketing, human resources, innovation, real estate, supply chain and finance. This team has an average of 15 years of restaurant industry experience, and many of our executives have experience at large public companies. In 2008, we hired our President and CEO, Aylwin Lewis. Aylwin was previously with Yum! Brands, Inc. from 1991 to 2004, most recently as President and Chief Multibranding and Operating Officer, as well as with Sears Holdings from 2004 to 2008, most recently as President and CEO. We believe our experienced leadership team is a key driver of our success and positions us to execute our long-term growth strategy.

Distinct, Deep-Rooted Culture: The Potbelly Advantage. We believe our culture is a key to our success. It is embodied in *The Potbelly Advantage*, which is an expression of our Vision, Mission, Passion and Values. *The Potbelly Advantage* is the written mission statement for our company that is shared with everyone who works at our company, from our top executives to shop associates. We believe such a mission statement serves as the foundation of everything we do, including how we plan and manage our business. Our Vision is to create Potbelly fans nationwide. We want our customers to feel we are their "Neighborhood Sandwich Shop" and to become Potbelly fans and advocates. Our Mission is to make our customers and employees happy, to make more money and to improve our business every day. Our Passion is to be "The Best Place for Lunch." We strive to emphasize our Values of integrity, teamwork, accountability, positive energy and coaching throughout all levels of our organization including in our hiring process and training programs. We also place importance on values for our leaders, such as delivering results through execution and building and inspiring teams. The Potbelly Values form a common language across our organization that we believe makes Potbelly a place our employees love to work. Through our Ethics Code of Conduct, ongoing training and evaluations, we encourage our employees to perform at their personal best and help them to work together as a team to make sure we deliver a positive experience to everyone who

works here. See "—Shop Operations and Management—Our People." Our culture helps us attract and retain employees and has contributed to our hourly employee turnover rate of 88% for the year ended December 25, 2016. We believe *The Potbelly Advantage* allows us to deliver operational excellence and grow our business and our base of devoted Potbelly fans.

Our Growth Strategy

We strive to grow profitability and create value for our stockholders by working to achieve the goals listed below. While we cannot provide assurances that we will achieve and maintain these objectives, we consider each of them to be a core strategy of our business.

Run Great Shops. We believe that continued excellence in shop-level execution is fundamental to our growth strategy. To maintain our operational standards, we use a Balanced Scorecard approach to measure People, Customers, Sales and Profits at each of our shops. Hiring the right people and maintaining optimal staffing levels enable us to run efficient operations. We track metrics such as peak hour throughput, mystery shopper scores and neighborhood engagement activities, such as fundraisers for local causes, to improve the customer experience. Shop sales and profitability are benchmarked against prior year periods and budget, and we focus on achieving targets on a shop-by-shop basis. To support our shop operators, we invest in systems and technology that can meaningfully improve shop-level execution. For example, we have enhanced capabilities around in-line order-taking by using a proprietary tablet system in approximately 64% of our shops as of December 25, 2016 to further increase throughput by increasing accuracy and speed of order taking. In addition, we are expanding our backline businesses, including catering, delivery and online ordering, which we view as additional growth drivers.

Find and Build Great Shops. Our company-operated shops are successful in diverse markets in 22 states and the District of Columbia, and we intend to continue to build company-operated shops in both new and existing markets utilizing our thoughtful site selection process. We evaluate a number of metrics to assess the optimal sites for our new shops, including neighborhood daytime population, site visibility, traffic and accessibility, along with an on-the-ground qualitative assessment of the characteristics of each unique trade area. This location-specific approach to development allows us to leverage our versatile shop format, which does not have standardized requirements with respect to size, shape or location, to achieve strong returns across a wide range of real estate settings. See "—Site Selection and Expansion—Shop Design" for more information about our shop requirements. In 2014, 2015 and 2016, we opened 39, 43 and 40 new company-operated shops, respectively, and expanded into Denver, Salt Lake City, San Antonio, El Paso and Indianapolis. In those same time periods, we closed one shop, six shops and two shops, respectively, due to under-performance or lease expirations. Additionally, during July 2015 and April 2016, the Company purchased a total of two franchise shops, converting them into company-operated shops. Over the long term, we plan to grow the number of Potbelly shops at least 10% annually. We cannot provide assurance that we will be able to grow the number of Potbelly shops by 10% in any year or over any period of time or that we will be able to open any specific number of shops in any year.

Achieve High Margins and Returns. Our approach to margin enhancement begins with continuous efforts to improve the financial results of our shops. We focus on cash-on-cash returns to the company and look to grow shop-level profitability each year through sales growth and productivity improvements. From 2012 to 2016, we generated shop-level profit margin, a non-GAAP measure, of 20.7%, 20.2%, 19.2%, 19.4% and 19.7% in 2012, 2013, 2014, 2015 and 2016, respectively. We also focus on cash flow generation, which supports our self-funded development model of sourcing our liquidity and capital resource needs primarily from operating activities and cash and cash equivalents. We also have a credit facility to provide another source of liquidity and to manage cash flow timing. Currently, we have no amounts outstanding under the credit facility. We believe we exercise strong financial discipline in managing expenses and by encouraging employee efficiency with the goal of achieving and maintaining general and administrative expenses under 10% of revenue. In addition, we expect our sales and shop-level profit margin to grow faster than general and administrative expenses. For fiscal 2016, our general and administrative expenses as a percentage of total revenues were 9.9%. Our intention is to maintain average shop-level profit margins over 20% as we continue to grow. However, we cannot provide assurances that we will be able to maintain our shop-level profit margin levels or that we will be able to achieve or maintain low levels of expenses.

Become a Global Iconic Brand. We believe that our premise of a "Neighborhood Sandwich Shop" has broad appeal across a wide range of market types and geographies. We believe that Potbelly is a recognized brand beyond the neighborhoods in which we currently operate. Based on our management's experience, we believe a significant contributor to this success is word-of-mouth publicity by our customers who enjoy their Potbelly experience and tell others about it. We learn from the formal customer feedback we solicit (See "—Our Food—Customer Feedback"), and from managers and employees who interact with customers in our shops, that many customers in new markets report positive recommendations from friends and family members who live in regions with established Potbelly shops. We believe that our positive brand perception helps drive interest in our shops in both existing and new markets.

Be a Great Franchisor. In 2010, we initiated a program to franchise shops in selected markets in the U.S. As of December 25, 2016, we had domestic franchise shops in Arkansas, Iowa, Illinois, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Carolina, North Dakota, Ohio, Pennsylvania, South Dakota, Tennessee, Texas and Virginia. As we develop our franchise program, we intend to expand the number of franchise shops on a disciplined basis. We perform a market analysis and focus on markets we believe have appropriate characteristics for our franchise shops and on franchisees that are compatible with the Potbelly culture. As of December 25, 2016, our franchisees operated 30 shops domestically. In addition, we have signed international franchise development agreements to open franchises in the Middle East; Ontario, Canada; and London, England. We have a franchise development agreement with the Alshaya Trading Company W.L.L. ("Alshaya"), a leading franchisee of retail brands, to develop shops in the Middle East. As of December 25, 2016, Alshaya operated 11 shops in Kuwait and the United Arab Emirates. In 2014, we entered into a franchise development agreement with Buraq Leisure (La Martina) Limited ("Buraq"), pursuant to which Buraq has the exclusive right to develop Potbelly shops in London for a period of five years. We expect Buraq to open up to ten Potbelly shops in London during that period. The first Potbelly shop in London opened in July 2015. In 2015, we entered into a franchise development agreement with Halsted Hospitality Ltd., pursuant to which Halsted has the exclusive right to develop Potbelly shops in the province of Ontario, Canada for a period of ten years. We expect Halsted to open up to 15 Potbelly shops in the first five years of the development agreement. The first Potbelly shop in Toronto, Ontario, opened in October 2016. See "—Franchising" for more information about our domestic and international franchise programs. Although we do not expect franchise activities to result in significant revenue in the near term, we see the selective expansion of our franchising efforts to be a valuable potential growth opportunity over time.

Our Food

Our Menu

Each of our shops offers freshly-made food with high quality ingredients from a simple menu. The majority of our sales are generated during lunchtime hours, but dinner and breakfast (in locations with high early morning traffic) are also important to our business. Our menu currently includes toasty warm sandwiches, signature salads, soups, chili, sides, desserts and, in our breakfast locations, breakfast sandwiches and steel cut oatmeal.

Every toasty warm sandwich on the Potbelly menu is made-to-order and customizable, with many based on the original recipes from 1977. Sandwiches are made with our signature multigrain or regular bread as "Originals" (our "regular" size), "Bigs" (30% bigger) or "Skinnys" (less meat and cheese starting under 400 calories); or on "Flats" (thin multigrain bread which is 90 calories less than our Originals). We slice our meats and cheeses daily in each shop to ensure freshness, and each of our sandwiches can be customized with a variety of toppings, including our unique Potbelly hot peppers that are made with a combination of spices exclusively for us. We believe our sandwiches have the right balance of ingredients with the last bite tasting as good as the first.

Our core sandwich offerings include Turkey Breast, Italian, Grilled Chicken and Cheddar, Smoked Ham, A Wreck, Chicken Salad, Meatball, Pizza Sandwich, Mediterranean, Roast Beef and Tuna Salad. Customers can also order off-menu sandwiches and variations on our sandwiches, including the "Wrecking Ball" (A Wreck plus meatballs), the "Lucky Seven" (which includes all seven of our sliced meat choices) and the "Cheeseburger" (the Meatball with cheddar cheese and no marinara). These items are on what our loyal fans call the "Underground Menu," which contributes to the special connection between Potbelly and our customers.

Our shops also offer salads which are made fresh to order with high quality ingredients. Our signature salads include the Uptown Salad, Farmhouse Salad, Chicken Salad Salad, A Wreck Salad, Mediterranean Salad and Powerhouse Salad. Customers may order any of our salads without meat for a vegetarian option and may customize a salad as they desire. Salads come with a choice of dressing, including Potbelly Vinaigrette, Balsamic Vinaigrette, Buttermilk Ranch and Non-Fat Vinaigrette. We believe our signature salads are key to diversifying our menu and help ensure that there is something for everyone at our shops.

We also offer soups, chili and side dishes. Different soups are offered daily, including varieties such as Broccoli Cheddar, Chicken Noodle, Loaded Baked Potato, Chicken Enchilada and Tomato soup. We also have a vegan soup option, our Garden Vegetable. Our chili is available seven days a week and is a hearty recipe of ground beef, kidney beans, onions and bell peppers sweetened with a touch of molasses. Additionally, customers can choose side dishes of coleslaw, macaroni salad, potato salad, potato chips or a whole dill pickle.

Our hand-dipped shakes and smoothies are made with real ingredients and come with our signature butter cookie on the straw. Our classic shake and smoothie flavors are vanilla, chocolate, strawberry, banana, mixed berry, coffee and Oreo ®, and include real fruit. Our varieties of cookies are baked fresh in each shop daily and include Oatmeal Chocolate Chip, Sugar and Chocolate Brownie cookies. Customers can also order an ice cream sandwich, with their choice of cookies and ice cream, or our signature chocolate and caramel Dream Bar.

Certain of our shops in areas with high early morning traffic also offer breakfast selections. As of December 25, 2016, approximately 29% of our shops offered breakfast selections. Our breakfast menu includes made-to-order breakfast sandwiches on our Flats or our signature multigrain or regular bread and include Egg & Cheddar Cheese; Bacon, Egg & Cheddar Cheese; Sausage, Egg & Cheddar Cheese; and Ham, Mushroom, Egg & Swiss Cheese. Like our lunch and dinner sandwiches, our breakfast sandwiches are served toasty warm and any of our toppings can be added. We also offer steel cut oatmeal with toppings such as raisins, brown sugar, bananas, walnuts, apples and cranberries, and have other breakfast items available such as bagels and dark roast coffee.

Our shops use high quality ingredients such as fresh produce which is delivered two to three times per week, hearth-baked bread, and whole-block cheeses sliced daily in our shops. We use all-natural white meat chicken in our sandwiches and salads. Our turkey, hickory-smoked ham and black angus roast beef are all whole-muscle meats sliced daily in our shops. Our dry-cured salami is made with fresh garlic and real red wine and we use white albacore tuna in our home-made tuna salad.

Overall, we believe our menu of high quality food at reasonable prices offers considerable value to our customers. In fiscal 2016, our system-wide average check was approximately $7.96. We generally do not discount our menu items in order to help ensure that we are able to maintain our high standards, as opposed to the discounting programs implemented by some other restaurant operators aimed at increasing traffic and revenue but that may impact profitability and quality.

Customer Feedback

We seek customer feedback on our food and operations in various ways. For example, we conduct an annual customer survey via email to learn what our customers think about us. We circulate a voluntary online survey to each customer listed in our company-wide email database, which includes email addresses obtained through our website, customer complaints and compliments, our in-shop business card drop, our Facebook page and other methods. In 2016, we sent the online survey to approximately 340,000 customers, with 20,000 customers electing to participate. Customers who take the annual survey were entered into a drawing for a nominal Potbelly gift card.

We also solicit feedback via quarterly in-person “Customer Advisories” in each of our major markets of Chicago, Washington, D.C. and Dallas. At each “Customer Advisory,” certain executives and local managers meet with approximately ten customers to get feedback on our products and initiatives. The customers who participate are selected from those listed in our company-wide email database as having recently dined at Potbelly. Our marketing team strives to have participants who are representative of the diverse customers who patronize the specific shop. Customer participants in each “Customer Advisory” receive a nominal Potbelly gift card as a thank you for their participation.

Evolution of Our Menu

We have selectively expanded our menu offerings in response to shifts in customer tastes and demand. For example, we began offering breakfast items in 2001, Bigs and Skinnys in 2008 and Flats in 2014. We also introduced the all-veggie Mediterranean sandwich in 2012, the Mediterranean salad in 2014 and the Powerhouse salad in 2016, as well as periodic limited time offers. We will continue to respond to consumer trends and customer feedback as we believe menu innovations are a way for us to continue to grow our business.

When we enter new markets, we employ a “lifecycle” approach to introducing our menu. Shops opened in new markets initially offer only our Original sandwiches to introduce new customers to our core menu items. Additionally, this approach simplifies our line operations and allows our new shops to focus on execution and speed of service. We gradually increase our menu offerings at these shops until the full range of Potbelly offerings are available.

Food Preparation and Safety

Food safety is a top priority, and we dedicate substantial resources, including our supply chain team and quality assurance teams, to help ensure that our customers enjoy safe, quality food products. We have taken various steps to mitigate food quality and safety risks, including having personnel focused on this goal together with our supply chain team. Our shops undergo third-party food safety reviews, internal safety audits and routine health inspections. We also consider food safety and quality assurance when selecting our distributors and suppliers.

Shop Operations and Management

We believe having an excellent manager in each shop is a critical factor in achieving continuous excellence in operations. Managers hire our employees, help ensure consistent execution of our menu items and strive to achieve specific targets that are evaluated on a quarterly basis. We devote significant time and resources to identifying, selecting and training our managers who plan,

manage and operate their shops and who, along with our employees, provide a positive customer experience to our Potbelly fans. We believe our comprehensive processes for developing business leaders, such as our shop managers, are a key factor in driving our success.

Potbelly Operations

Our operations are structured around the elements of People, Customers, Sales and Profits. During our peak hours of 11:30 a.m. to 1:30 p.m., our employees greet our customers and take their orders (in some shops, while they wait in line by using a proprietary tablet system to communicate with our food preparation employees). We focus on effective communication, technology and management to provide a quick and seamless experience for our customers. In addition, each shop completes quarterly tactical plans designed to help the shop achieve its targets relative to each element. In order to better assess and improve the Potbelly experience, we use a Balanced Scorecard that tracks elements such as sales and profitability metrics, employee turnover and a "mystery shopper" score, which essentially is a survey of customer satisfaction with the Potbelly experience. We review overall scores locally, regionally and nationally in order to assess our operational progress and identify areas of operational focus. Attaining certain ratings on the Balanced Scorecard allows a shop to be eligible for incentive targets paid quarterly and annual merit awards.

Our People

We look to attract, hire and retain smart, talented and outgoing people who share and demonstrate our values. We value friendly employees who engage with our customers in a genuine way to provide a personalized experience. We select employees using interview questions based on our values to determine the extent of candidate fit. All employees attend culture training classes that include team exercises and scenarios to practice utilizing the tools relative to our values of integrity, teamwork, accountability, positive energy and coaching. We strive to empower our employees to do what is right and encourage them to perform at their personal best. We believe we make expectations and accountabilities clear through our culture training and our Ethics Code of Conduct, which summarizes employee conduct guidelines and is required to be reviewed and signed by every employee upon hire and repeated annually. We believe we encourage each employee to perform at their personal best by establishing personal and professional goals through an ongoing continuous development plan. We believe the success of these programs is evident in our turnover rates and our internal promotion rates. Employees are further encouraged to perform at their personal best through an ongoing scorecard measuring system that is tied directly to a pay for performance compensation program. We believe our sustainable process to hire, train and develop our people enables us to deliver a positive customer experience. A typical Potbelly shop consists of one manager, one assistant manager and as many as 12 to 16 employees during our peak hours.

Most of our managers live in the neighborhood in which their shop is located. We believe this allows them to get to know their customers, understand the unique character of each neighborhood and form deep roots within the community. The shop manager has primary responsibility for the day-to-day operation of the shop and is required to abide by Potbelly's operating standards. Our Management Training Program provides new managers with six to eight weeks of training that emphasizes culture, standards, strategy and procedures to prepare them for success, and is followed by on-going, in-shop coaching with their District or Market manager. Our shop managers report to District or Market Managers who typically report to a Zone Manager, and ultimately to our Senior Vice President of Operations. In addition, members of senior management visit shops regularly to help ensure that our culture, strategy and quality standards are being adhered to in all aspects of our operations.

Shop managers are responsible for selecting and training the employees for each new shop. The training period for new non-management employees lasts approximately eight weeks and is characterized by on-the-job supervision by an experienced employee. Ongoing employee training remains the responsibility of the shop manager, but, as noted above, we provide specific training for our employees around *The Potbelly Advantage* several times a year. Special emphasis is placed on the consistency and quality of food preparation and service, which is monitored through ongoing meetings with managers. In addition, we have other continuing communications with all of our employees.

The Potbelly Experience

We seek to deliver a positive experience for every customer at every opportunity through our tasty food, unique atmosphere and outgoing and engaging employees. We seek to staff each shop with experienced teams to ensure consistent and attentive customer service. We look to hire employees who are friendly and responsive to the needs of our customers as they assist them in selecting menu items complementing individual preferences. We strive to staff at 110% during peak hours to ensure a fast yet personal Potbelly experience for each customer, with face-to-face interaction from start to finish. We also provide backline services, including catering, delivery and online ordering to serve our Potbelly fans.

In addition, music has been integral to the Potbelly culture since our first shop opened in 1977 and adds a neighborhood vibe. Local musicians frequently perform live at Potbelly shops creating a distinctive dining experience.

We believe the combination of our great food, people and atmosphere makes Potbelly "The Best Place for Lunch."

Site Selection and Expansion

We believe we are well positioned to continue growth in our existing markets and have significant expansion potential in new geographic areas throughout the United States. As of December 25, 2016, we had a domestic base of 441 shops in 29 states and the District of Columbia. Of these, the company operates 411 shops and franchisees operate 30 shops. In addition, there are 13 international franchised shops, including 11 shops in the Middle East, one shop in the United Kingdom, and one shop in Canada.

Over the long-term, we plan to grow the number of Potbelly shops by at least 10% annually. In 2014, 2015 and 2016, we opened 39, 43 and 40 new company-operated shops, respectively, and expanded into Denver, Salt Lake City, San Antonio, El Paso and Indianapolis. Additionally, during July 2015 and April 2016, the Company purchased a total of two franchise shops, converting them into company-operated shops. We cannot provide assurance that we will be able to grow the number of Potbelly shops by 10% in any year or over any period of time or that we will be able to open any specific number of shops in any year.

Our proven shop model is designed to generate strong cash flow, attractive shop-level financial results and high returns on investment. With an average new shop investment of approximately $600,000 and average unit volumes in excess of $1 million, which represent the average net sandwich shop sales for all shops on an annual basis, we strive to generate average shop-level profit margins, a non-GAAP measure, above 20% and cash-on-cash returns, on new company-operated shops, above 25% after two full years of operation. However, we cannot provide any assurances that we will achieve and maintain similar profit margins or cash returns in the future.

Site Selection Process

We consider the location of a shop to be a critical variable in its long-term success and as such, we devote significant effort to the investigation and evaluation of potential locations. We actively develop shops in both new and existing markets and plan to continue to expand in selected regions throughout the United States. Our Real Estate Committee, which includes most of our senior management team, meets weekly to discuss all aspects of our development program. The process for selecting locations incorporates management's experience and expertise and includes extensive data collection and analysis. We proactively seek new shop locations based on specific criteria, such as demographic characteristics, daytime population thresholds and traffic patterns, along with the potential visibility of, and accessibility to, the shop. Additionally, we use information and intelligence gathered from managers and other shop personnel that live in or near the neighborhoods we are considering. New shops are built with only one purpose in mind: to generate cash flow that meets or exceeds those modeled in our return targets. We are disciplined in our development, and we routinely forego sites that have many positive attributes, including strong visibility and street presence, but have challenging economics, such as high occupancy costs.

Since we do not have standardized requirements with respect to size, shape or location, we are flexible in our site selection process. This allows us to choose and open shops with a wide variety of shapes in a wide variety of areas, including in urban central business districts and suburban areas near shopping malls or other high-traffic locations. Proposed locations are visited, reviewed and approved by key members of our Real Estate Committee.

Shop Design

We strive to create a unique customer experience that delivers a neighborhood feel for each shop. We typically design the interior of our shops in-house, utilizing outside architects when necessary. Our design team sources most furnishings and decorations for our shops. Each of our shops features vintage décor and shared design elements, such as the use of wood, wallpaper motifs and our signature Potbelly stove. Consistent with *The Potbelly Advantage*, our shops display locally-themed photos and other decorative items inspired by the neighborhood. Most of our shops also feature a space for musicians to perform. Our shop size averages approximately 2,300 square feet; however, we currently target shop sizes between 1,800 and 2,500 square feet for new openings. The dining area of a typical shop can seat anywhere from 40 to 60 people. Some of our shops incorporate larger dining areas and outdoor patios. We believe the unique atmosphere and local music creates a lively place where friends and family can get together, encourages repeat visits by our customers and drives increased sales.

Construction

Construction of a new shop generally takes approximately 50 to 70 days from the date the location is leased or under contract and fully permitted. Each new shop requires a total cash investment of approximately $600,000, but this figure could be materially higher or lower depending on the market, shop size and condition of the premises upon landlord delivery. We generally construct shops in third-party leased retail space but also construct free-standing buildings on leased properties. In the future, we intend to

continue converting existing third-party leased retail space or constructing new shops in the majority of circumstances. For additional information regarding our leases, see "—Properties" in Item 2.

Franchising

In 2010, we initiated a program to selectively franchise our shops to take advantage of incremental growth opportunities. We intend to expand the number of franchise shops on a disciplined basis as we develop our franchise program. As of December 25, 2016, we had 30 domestic franchised shops in 16 states. In 2011, our first international franchise shop opened with Alshaya, our first international franchise partner. As of December 25, 2016, Alshaya operated 11 franchised shops in Kuwait and the United Arab Emirates and has exclusive franchising rights in the Middle East. Our agreement with Alshaya provides that Alshaya may also open shops in Bahrain, Egypt, Jordan, Lebanon, Oman, Qatar and Saudi Arabia. In 2014, we entered into a franchise development agreement with Buraq, pursuant to which Buraq has the exclusive right to develop Potbelly shops in London for a period of five years. We expect Buraq to open up to ten Potbelly shops in London during that period. The first Potbelly shop in London opened in July 2015. In 2015, we entered into a franchise development agreement with Halsted Hospitality Ltd., pursuant to which Halsted has the exclusive right to develop Potbelly shops in the province of Ontario, Canada for a period of ten years. The first Potbelly shop in Toronto, Ontario opened in October 2016. We expect Halsted to open a total of up to 15 Potbelly shops in the first five years of the development agreement.

We look for franchisees who love working with a team and have solid business experience, financial qualifications and personal motivation. Our franchise arrangements grant third parties a license to establish and operate a shop using our systems and our trademarks. The franchisee pays us for the ideas, strategy, marketing, operating system, training, purchasing power and brand recognition. All new U.S. franchisees participate in an eight to twelve-week training program consisting of real life experience in our company-operated shops, as well as training at our Potbelly Support Center in Chicago. Franchised shops must be operated in compliance with our methods, standards and specifications, regarding menu items, ingredients, materials, supplies, services, fixtures, furnishings, décor and signs. Although we do not expect franchise activities to result in significant revenue in the near term, we see the selective expansion of our franchising efforts to be a valuable potential growth opportunity over time.

Advertising and Marketing

We believe our shops appeal to a broad base of loyal customers who return again and again for our great food and fun environment staffed by friendly people. Historically, one to two percent of our annual revenue has been spent on marketing efforts. A portion of our marketing budget is spent at the shop level, with the goal of building relationships within our neighborhoods to increase the frequency of return visits and attract new customers. Our methods of marketing and advertising promote and maintain the Potbelly brand image and, among other things, generate awareness of shop locations and new menu offerings.

Neighborhood Shop Marketing

Consistent with our neighborhood approach, a portion of our marketing investments are made at the shop level. Neighborhood shops frequently hire local musicians and hold a variety of community events, including fundraisers. For example, during a "Shake Fundraiser" for smaller community organizations, Potbelly donates a portion of sales for each customized milkshake sold. For larger organizations, Potbelly sponsors local cause fundraisers, where 25% of sales gathered at the event are donated to the organization's cause. Our shops promote these events and other events through social media, public relations, in-shop materials and local support, which results in increased traffic. Additionally, we engage in a variety of promotional activities, such as contributing food, time and money to charitable, civic and cultural programs, in order to give back to the communities we serve and increase public awareness and appreciation of our shops and our employees.

Advertising

We also promote our shops through local media in markets in which we have scale. The uses of digital and outdoor media are the most common advertising vehicles used in these markets. Additionally, we rely on in-shop materials to communicate and market to our customers. Our internal corporate production staff is responsible for the creative work around our advertising and other forms of communication. In the end, our best advertising comes from our customers. We believe the Potbelly experience fosters strong customer loyalty and encourages our fans to promote the brand through word-of-mouth marketing.

E-Marketing and Social Media

We have increased our use of e-marketing tools, which enable us to reach a significant number of people in a timely and targeted fashion at a fraction of the cost of traditional media. We believe that our customers are frequent internet users and will use

social media to make dining decisions or to share dining experiences. We have a Facebook page, Instagram and Twitter feed and advertise on various social media and other websites.

Sourcing and Supply Chain

Our supply chain team sources, negotiates and purchases food supplies for our shops. We believe in using high quality ingredients while maintaining our value position in the marketplace. We benchmark our products against the competition using consumer panels. We contract with Distribution Market Advantage, Inc., or DMA, a cooperative of multiple food distributors located throughout the nation. DMA is a broker with whom we negotiate and gain access to third-party food distributors and suppliers. For fiscal year 2016, distributors through our DMA arrangement supplied us with approximately 90%-96% of our food supplies through five primary distributors: Reinhart FoodService, L.L.C., Ben E. Keith Company, Food Services of America, Shamrock Foods and Nicholas & Co. Our remaining food supplies are distributed by other distributors under separate contracts. Our distributors deliver supplies to our shops approximately two to three times per week.

We negotiate pricing and volume terms directly with certain of our suppliers and distributors or through DMA. Our supply chain team utilizes a mix of forward pricing protocols for certain items under which we agree with our supplier on fixed prices for deliveries at some time in the future, fixed pricing protocols under which we agree on a fixed price with our supplier for the duration of that protocol, and formula pricing protocols under which the prices we pay are based on a specified formula related to the prices of the goods, such as spot prices. Our use of any forward pricing arrangements varies substantially from time to time and these arrangements tend to cover relatively short periods (i.e., typically 12 months or less).

Currently we have pricing arrangements of varying lengths with our distributors and suppliers, including distributors and suppliers of meats, dairy, bread, cookie dough and other products. Meats represent about 26% of our product purchasing composition. In fiscal year 2016, more than 97% of our meat products were sourced from 10 suppliers under non-exclusive contracts. We have a non-exclusive contract with Campagna-Turano Bakery, Inc. for our signature multigrain bread. Campagna-Turano Bakery, Inc. produces bread items in a primary and secondary production facility. We have secondary suppliers in place for many of our significant meats, and we believe we would be able to source our meat and bread requirements from different suppliers if doing so became necessary. However, changes in the price or availability of certain products may affect the profitability of certain items, our ability to maintain existing prices and our ability to purchase sufficient amounts of items to satisfy our customers' demands.

Many of our products, ingredients and supplies are currently sourced from multiple suppliers. Additionally, our supply chain team has established contingency plans for many key products. For example, manufacturers of certain products maintain alternative production facilities capable of satisfying our requirements should the primary facility experience interruptions. For other products, we believe we have identified alternate suppliers that could meet our requirements at competitive prices or, in some cases, have identified a product match that could be used in our shops. Our supply chain team regularly updates our procurement strategies to include contingency plans for new products and ingredients, as well as additional secondary and alternate suppliers. We believe these strategies would collectively enable us to obtain sufficient product quantities from other sources at competitive prices without material disruption should a current supplier be unable to fulfill its commitment to us.

Management Information Systems

Shop-level financial and accounting controls are handled through a point-of-sale computer system and network in each shop that communicates with our corporate headquarters. The POS system is also used to authorize and transmit credit card sales transactions and to manage the business and control costs, such as labor. Our company-operated shops are connected through data centers and a portal to provide our corporate employees with access to business information and tools that allow them to collaborate, communicate, train and share information between shops and the corporate office. We believe our systems currently comply with all credit card industry security standards for processing of credit and gift cards.

Competition

We compete in the restaurant industry, primarily in the limited-service restaurant segment but also with restaurants in the full-service restaurant segment, and face significant competition from a wide variety of restaurants, convenience stores and other outlets on a national, regional and local level. We believe that we compete primarily based on product quality, restaurant concept, service, convenience, value perception and price. Our competition continues to intensify as competitors increase the breadth and depth of their product offerings and open new units. Although new competitors may emerge at any time due to the low barriers to entry, our competitors include: Chipotle, Jimmy John's, Panera Bread and Subway, among others. Additionally, we compete with limited-service restaurants, specialty restaurants and other retail concepts for prime shop locations.

Government Regulation

We and our franchisees are subject to various federal, state, local and international laws affecting our business. Each of our shops is subject to licensing and regulation by a number of governmental authorities, which may include, among others, health and safety, nutritional menu labeling, health care, environmental and fire agencies in the state, municipality or country in which the shop is located. Difficulty in obtaining or failing to obtain the required licenses or approvals could delay or prevent the development of a new shop in a particular area. Additionally, difficulties or inabilities to retain or renew licenses, or increased compliance costs due to changed regulations, could adversely affect operations at existing shops.

Our shop operations are also subject to federal and state labor laws, including the U.S. Fair Labor Standards Act and the U.S. Immigration Reform and Control Act of 1986, governing such matters as minimum wages, overtime and worker conditions. Significant numbers of our food service and preparation personnel are paid at rates related to the applicable minimum wage, and further increases in the minimum wage or other changes in these laws could increase our labor costs. Our ability to respond to minimum wage increases by increasing menu prices will depend on the responses of our competitors and customers. Our distributors and suppliers also may be affected by higher minimum wage and benefit standards, which could result in higher costs for goods and services supplied to us.

We and our franchisees may also be subject to lawsuits from our employees, the U.S. Equal Employment Opportunity Commission or others alleging violations of federal and state laws regarding workplace and employment matters, discrimination and similar matters.

The Patient Protection and Affordability Act of 2010 (the “PPACA”) enacted in March 2010 requires chain restaurants with 20 or more locations in the United States to comply with federal nutritional disclosure requirements. The FDA issued final regulations with regard to restaurant menu labeling that is expected to become effective May 5, 2017. A number of states, counties and cities have also enacted menu labeling laws requiring multi-unit restaurant operators to disclose certain nutritional information to customers, or have enacted legislation restricting the use of certain types of ingredients in restaurants. Although the federal legislation is intended to preempt conflicting state or local laws on nutrition labeling, until we are required to comply with the federal law we will be subject to a patchwork of state and local laws and regulations regarding nutritional content disclosure requirements. Many of these requirements are inconsistent or are interpreted differently from one jurisdiction to another. While our ability to adapt to consumer preferences is a strength of our concepts, the effect of such labeling requirements on consumer choices, if any, is unclear at this time.

There is also a potential for increased regulation of certain food establishments in the United States, where compliance with a Hazard Analysis and Critical Control Points (“HACCP”) approach may now be required. HACCP refers to a management system in which food safety is addressed through the analysis and control of potential hazards from production, procurement and handling, to manufacturing, distribution and consumption of the finished product. Many states have required restaurants to develop and implement HACCP Systems and the United States government continues to expand the sectors of the food industry that must adopt and implement HACCP programs. For example, the Food Safety Modernization Act (“FSMA”), signed into law in January 2011, granted the United States Food and Drug Administration (the “FDA”) new authority regarding the safety of the entire food system, including through increased inspections and mandatory food recalls. Although restaurants are specifically exempted from or not directly implicated by some of these new requirements, we anticipate that the new requirements may impact our industry. Additionally, our suppliers may initiate or otherwise be subject to food recalls that may impact the availability of certain products, result in adverse publicity or require us to take actions that could be costly for us or otherwise harm our business.

We and our franchisees are subject to the Americans with Disabilities Act (the “ADA”), which, among other things, requires our shops to meet federally mandated requirements for the disabled. The ADA prohibits discrimination in employment and public accommodations on the basis of disability. Under the ADA, we and our franchisees could be required to expend funds to modify our shops to provide service to, or make reasonable accommodations for the employment of, disabled persons. In addition, our employment practices are subject to the requirements of the Immigration and Naturalization Service relating to citizenship and residency. Government regulations could affect and change the items we procure for resale. We and our franchisees may also become subject to legislation or regulation seeking to tax and/or regulate high-fat and high-sodium foods, particularly in the United States, which could be costly to comply with. Our results can be impacted by tax legislation and regulation in the jurisdictions in which we operate and by accounting standards or pronouncements.

We and our franchisees are also subject to laws and regulations relating to information security, privacy, cashless payments, gift cards and consumer credit, protection and fraud, and any failure or perceived failure to comply with these laws and regulations could harm our reputation or lead to litigation, which could adversely affect our financial condition.

Our franchising activities are subject to the rules and regulations of the Federal Trade Commission (“FTC”) and various state laws regulating the offer and sale of franchises. The FTC’s franchise rule and various state laws require that we furnish a franchise

disclosure document (“FDD”) containing certain information to prospective franchisees and a number of states require registration of the FDD with state authorities. Substantive state laws that regulate the franchisor-franchisee relationship exist in a substantial number of states, and bills have been introduced in Congress from time to time that would provide for federal regulation of the franchisor-franchisee relationship. The state laws often limit, among other things, the duration and scope of non-competition provisions, the ability of a franchisor to terminate or refuse to renew a franchise and the ability of a franchisor to designate sources of supply. We believe that our FDDs, together with any applicable state versions or supplements, and franchising procedures comply in all material respects with both the FTC franchise rule and all applicable state laws regulating franchising in those states in which we have offered franchises.

See “Risk Factors” in Item 1A for a discussion of risks relating to federal, state, local and international regulation of our business.

Seasonality

Our business is subject to seasonal fluctuations. Historically, customer spending patterns for our established shops are lowest in the first quarter of the year. Our quarterly results have been and will continue to be affected by the timing of new shop openings and their associated pre-opening costs. As a result of these and other factors, our financial results for any quarter may not be indicative of the results that may be achieved for a full fiscal year.

Employees

As of December 25, 2016, we employed approximately 7,400 persons, of which approximately 200 are corporate personnel, 670 are shop management personnel and the remainder are hourly shop personnel.

Intellectual Property and Trademarks

We regard our “Potbelly” and “Potbelly Sandwich Works” trademarks as having significant value and as being important factors in the marketing of our shops. We have also obtained trademarks for several of our other menu items, such as “A Wreck,” and for various advertising slogans, including “Good Vibes, Great Sandwiches” and “A First Class Dive.” We are aware of names and marks similar to the trademarks of ours used by other persons in certain geographic areas in which we have shops. However, we believe such uses will not adversely affect us. Our policy is to pursue registration of our intellectual property whenever possible and to oppose vigorously any infringement thereof.

We license the use of our registered trademarks to franchisees through franchise arrangements. The franchise arrangements restrict franchisees’ activities with respect to the use of our trademarks and impose quality control standards in connection with goods and services offered in connection with the trademarks.

Available Information

We were incorporated in Delaware in June 2001 as Potbelly Sandwich Works, Inc. and changed our name to Potbelly Corporation in 2002. Our principal offices are located at 111 North Canal Street, Suite 850, Chicago, Illinois 60606 and our telephone number is (312) 951-0600. We maintain a website with the address www.potbelly.com. On our website, we make available at no charge our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, all amendments to those reports, and our proxy statement, as soon as reasonably practicable after these materials are filed with or furnished to the SEC. Our filings are also available on the SEC’s website at www.sec.gov. The public may read and copy any materials that we file with the SEC at the SEC’s Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. The public may also obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The contents of our website are not incorporated by reference into this Form 10-K.

ITEM 1A. RISK FACTORS

You should carefully consider the following factors, which could materially affect our business, financial condition or results of operations. You should read these Risk Factors in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 7 and our consolidated financial statements and the related notes to those statements included in Item 8.

Risks Related to Our Business and Industry

We face significant competition for customers and our inability to compete effectively may affect our traffic, sales and shop-level profit margins, which could adversely affect our business, financial condition and results of operations.

The restaurant industry is intensely competitive with many well-established companies that compete directly and indirectly with us with respect to food quality, ambience, service, price and value and location. We compete in the restaurant industry with national, regional and locally-owned limited-service restaurants and full-service restaurants. Some of our competitors have significantly greater financial, marketing, personnel and other resources than we do, and many of our competitors are well established in markets in which we have existing shops or intend to locate new shops. In addition, many of our competitors have greater name recognition nationally or in some of the local markets in which we have shops. Any inability to successfully compete with the restaurants in our markets will place downward pressure on our customer traffic and may prevent us from increasing or sustaining our revenues and profitability. Consumer tastes, nutritional and dietary trends, traffic patterns and the type, number and location of competing restaurants often affect the restaurant business, and our competitors may react more efficiently and effectively to those conditions. Further, we face growing competition from the supermarket industry, with the improvement of their "convenient meals" in the deli section, and from limited-service and fast casual restaurants, as a result of higher-quality food and beverage offerings by those restaurants. In addition, some of our competitors have in the past implemented programs which provide price discounts on certain menu offerings, and they may continue to do so in the future. If we are unable to continue to compete effectively, our traffic, sales and shop-level profit margins could decline and our business, financial condition and results of operations would be adversely affected.

Economic conditions in the United States could materially affect our business, financial condition and results of operations.

The restaurant industry depends on consumer discretionary spending. During periods of economic downturn, continuing disruptions in the overall economy, including the impacts of high unemployment and financial market volatility and unpredictability, may cause a related reduction in consumer confidence, which could negatively affect customer traffic and sales throughout our industry. These factors, as well as national, regional and local regulatory and economic conditions, gasoline prices, disposable consumer income and consumer confidence, affect discretionary consumer spending. If economic conditions worsen, customer traffic could be adversely impacted if our customers choose to dine out less frequently or reduce the amount they spend on meals while dining out. If negative economic conditions persist for a long period of time or become pervasive, consumer changes to their discretionary spending behavior, including the frequency with which they dine out, could be more permanent. The U.S. economy is likely to be affected by many national and international factors that are beyond our control. If sales decrease, our profitability could decline as we spread fixed costs across a lower level of sales. Prolonged negative trends in shop sales could cause us to, among other things, reduce the number and frequency of new shop openings, close shops or delay remodeling of our existing shops or take asset impairment charges.

Increased commodity, energy and other costs could decrease our shop-level profit margins or cause us to limit or otherwise modify our menus, which could adversely affect our business.

Our profitability depends in part on our ability to anticipate and react to changes in the price and availability of food commodities, including among other things beef, poultry, grains, dairy and produce. Prices may be affected due to market changes, increased competition, the general risk of inflation, shortages or interruptions in supply due to weather, disease or other conditions beyond our control, or other reasons. Other events could increase commodity prices or cause shortages that could affect the cost and quality of the items we buy or require us to further raise prices or limit our menu options. These events, combined with other more general economic and demographic conditions, could impact our pricing and negatively affect our sales and shop-level profit margins. We enter into certain forward pricing arrangements with our suppliers from time to time, which may result in fixed or formula-based pricing with respect to certain food products. See "Quantitative and Qualitative Disclosures about Market Risk—Commodity Price Risk" in Item 7A. However, these arrangements generally are relatively short in duration and may provide only limited protection from price changes, and the extent to which we use these arrangements varies substantially from time to time. In addition, the use of these arrangements may limit our ability to benefit from favorable price movements.

Our profitability is also adversely affected by increases in the price of utilities, such as natural gas, whether as a result of inflation, shortages or interruptions in supply, or otherwise. Our profitability is also affected by the costs of insurance, labor, marketing, taxes and real estate, all of which could increase due to inflation, changes in laws, competition or other events beyond our control. Our ability to respond to increased costs by increasing menu prices or by implementing alternative processes or products will depend on our ability to anticipate and react to such increases and other more general economic and demographic conditions, as well as the responses of our competitors and customers. All of these things may be difficult to predict and beyond our control. In this manner, increased costs could adversely affect our performance.

Our inability to identify qualified individuals for our workforce could slow our growth and adversely impact our ability to operate our shops.

Our success depends in part upon our ability to attract, motivate and retain a sufficient number of qualified managers and associates to meet the needs of our existing shops and to staff new shops. A sufficient number of qualified individuals to fill these positions may be in short supply in some communities. Competition in these communities for qualified staff could require us to pay higher wages and provide greater benefits. In addition, significant improvement in regional or national economic conditions could increase the difficulty of attracting and retaining qualified individuals and could result in the need to pay higher wages and provide greater benefits. We place a heavy emphasis on the qualification and training of our personnel and spend a significant amount of time and money on training our employees. Any inability to recruit and retain qualified individuals may result in higher turnover and increased labor costs, and could compromise the quality of our service, all of which could adversely affect our business. Any such inability could also delay the planned openings of new shops and could adversely impact our existing shops. Any such inability to retain or recruit qualified employees, increased costs of attracting qualified employees or delays in shop openings could adversely affect our business and results of operations.

Our business operations and future development could be significantly disrupted if we lose key members of our management team.

The success of our business continues to depend to a significant degree upon the continued contributions of our senior officers and key employees, both individually and as a group. Our future performance will be substantially dependent in particular on our ability to retain and motivate Aylwin Lewis—our Chief Executive Officer, Michael Coyne—our Senior Vice President and Chief Financial Officer, Julie Younglove-Webb—our Senior Vice President and Chief Operations Officer, and other members of our senior leadership team. We currently have employment agreements in place with all of the members of our senior leadership team. The loss of the services of any of these executive officers or other key employees could have a material adverse effect on our business and plans for future development. In addition, we may have difficulty finding appropriate replacements and our business could suffer. We also do not maintain any key man life insurance policies for any of our employees.

Food safety and food-borne illness concerns may have an adverse effect on our business by reducing demand and increasing costs.

Food safety is a top priority, and we dedicate substantial resources to help ensure that our customers enjoy safe, quality food products. However, food-borne illnesses and food safety issues have occurred in the food industry in the past, and could occur in the future. Any report or publicity linking us to instances of food-borne illness or other food safety issues, including food tampering or contamination, could adversely affect our brand and reputation as well as our revenues and profits. In addition, instances of food-borne illness, food tampering or food contamination occurring solely at restaurants of our competitors could result in negative publicity about the food service industry generally and adversely impact our sales.

Furthermore, our reliance on third-party food suppliers and distributors increases the risk that food-borne illness incidents could be caused by factors outside of our control and that multiple locations would be affected rather than a single shop. We cannot assure that all food items are properly maintained during transport throughout the supply chain and that our employees will identify all products that may be spoiled and should not be used in our shops. If our customers become ill from food-borne illnesses, we could be forced to temporarily close some shops. Furthermore, any instances of food contamination, whether or not at our shops, could subject us or our suppliers to a food recall pursuant to the FSMA.

Our long-term success is highly dependent on our ability to successfully identify and secure appropriate sites and develop and expand our operations in existing and new markets.

One of the key means of achieving our growth strategies will be through opening new shops and operating those shops on a profitable basis. We expect this to be the case for the foreseeable future. We opened 40 new company-operated shops in 2016. We must identify target markets where we can enter or expand, taking into account numerous factors such as the location of our current shops, demographics, traffic patterns and information gathered from local employees. We may not be able to open our planned new shops on a timely basis, if at all, given the uncertainty of these factors. In the past, we have experienced delays in opening some shops and that could happen again. Delays or failures in opening new restaurants could adversely affect our business and results of operations. As we operate more shops, our rate of expansion relative to the size of our restaurant base will eventually decline.

The number and timing of new shops opened during any given period may be negatively impacted by a number of factors including, without limitation:

- the identification and availability of attractive sites for new shops and the ability to negotiate suitable lease terms;
- competition in new markets, including competition for appropriate sites;

- anticipated commercial, residential and infrastructure development near our new shops;
- the proximity of potential sites to an existing shop;
- the cost and availability of capital to fund construction costs and pre-opening expenses;
- our ability to control construction and development costs of new shops;
- recruitment and training of qualified operating personnel in the local market;
- our ability to obtain all required governmental permits, including zoning approvals, on a timely basis;
- unanticipated increases in costs, any of which could give rise to delays or cost overruns; and
- avoiding the impact of inclement weather, natural disasters and other calamities.

We cannot assure you that we will be able to successfully expand or acquire critical market presence for our brand in new geographical markets, as we may encounter well-established competitors with substantially greater financial resources. We may be unable to find and secure attractive locations, build name recognition, successfully market our brand or attract new customers. Competitive circumstances and consumer characteristics and preferences in new market segments and new geographical markets may differ substantially from those in the market segments and geographical markets in which we have substantial experience. If we are unable to expand in existing markets or penetrate new markets, our ability to increase our revenues and profitability may be harmed.

Our expansion into new markets may present increased risks.

We plan to open shops in markets where we have little or no operating experience. Shops we open in new markets may take longer to reach expected sales and profit levels on a consistent basis and may have higher construction, occupancy or operating costs than shops we open in existing markets, thereby affecting our overall profitability. New markets may have competitive conditions, consumer tastes and discretionary spending patterns that are more difficult to predict or satisfy than our existing markets. We may need to make greater investments than we originally planned in advertising and promotional activity in new markets to build brand awareness. We may find it more difficult in new markets to hire, motivate and keep qualified employees who share our values. We may also incur higher costs from entering new markets if, for example, we assign area managers to manage comparatively fewer shops than we assign in more developed markets. As a result, these new shops may be less successful or may achieve target shop-level profit margins at a slower rate. If we do not successfully execute our plans to enter new markets, our business, financial condition or results of operations could be adversely affected.

New shops, once opened, may not be profitable, and the increases in comparable store sales that we have experienced in the past may not be indicative of future results.

Our results have been, and in the future may continue to be, significantly impacted by the timing of new shop openings (often dictated by factors outside of our control), including associated shop pre-opening costs and operating inefficiencies, as well as changes in our geographic concentration due to the opening of new shops. We typically incur the most significant portion of pre-opening expenses associated with a given shop within the five months immediately preceding and the month of the opening of the shop. Our experience has been that labor and operating costs associated with a newly opened shop for the first several months of operation are materially greater than what can be expected after that time, both in aggregate dollars and as a percentage of revenues. Our new shops commonly take 10 to 13 weeks to reach planned operating levels due to inefficiencies typically associated with new shops, including the training of new personnel, lack of market awareness, inability to hire sufficient qualified staff and other factors. We may incur additional costs in new markets, particularly for transportation, distribution and training of new personnel, which may impact the profitability of those shops. Accordingly, the volume and timing of new shop openings may have a meaningful impact on our profitability.

Although we target specified operating and financial metrics, new shops may not meet these targets or may take longer than anticipated to do so. Any new shops we open may not be profitable or achieve operating results similar to those of our existing shops. For example, in 2015, we closed six shops, including the closure of airport locations as a result of airport redevelopment and planned closures for underperforming shops with expiring leases. In 2016, we closed two underperforming shops. If our new shops do not perform as planned, our business and future prospects could be harmed. In addition, if we are unable to achieve our expected comparable store sales, our business, financial condition or results of operations could be adversely affected.

Our sales and profit growth could be adversely affected if comparable store sales are less than we expect.

The level of comparable store sales, which represent the change in year-over-year sales for company-operated shops open for 15 months or longer, will affect our sales growth and will continue to be a critical factor affecting profit growth. Our ability to increase

comparable store sales depends in part on our ability to successfully implement our initiatives to build sales. It is possible such initiatives will not be successful, that we will not achieve our target comparable store sales growth or that the change in comparable store sales could be negative, which may cause a decrease in sales and profit growth that would adversely affect our business, financial condition or results of operations.

Our failure to manage our growth effectively could harm our business and operating results.

Our growth plan includes a significant number of new shops. Our existing management systems, financial and management controls and information systems may not be adequate to support our planned expansion. Our ability to manage our growth effectively will require us to continue to enhance these systems, procedures and controls and to locate, hire, train and retain management and operating personnel. We may not be able to respond on a timely basis to all of the changing demands that our planned expansion will impose on management and on our existing infrastructure, or be able to hire or retain the necessary management and operating personnel, which could harm our business, financial condition or results of operations.

The planned rapid increase in the number of our shops may make our future results unpredictable.

In 2016, we opened 40 company-operated shops, ten franchisee-operated shops and also purchased a franchise shop, converting it into a company-operated shop, and we plan to continue to increase the number of our shops in the next several years. This growth strategy and the substantial investment associated with the development of each new shop may cause our operating results to fluctuate and be unpredictable or adversely affect our profits. Our future results depend on various factors, including successful selection of new markets and shop locations, local market acceptance of our shops, consumer recognition of the quality of our food and willingness to pay our prices, the quality of our operations and general economic conditions. In addition, as has happened when other restaurant concepts have tried to expand, we may find that our concept has limited appeal in new markets or we may experience a decline in the popularity of our concept in the markets in which we operate. Newly opened shops or our future markets and shops may not be successful or our average net sandwich shop sales may not increase at historical rates, which could adversely affect our business, financial condition or results of operations.

Opening new shops in existing markets may negatively affect sales at our existing shops.

The consumer target area of our shops varies by location, depending on a number of factors, including population density, other local retail and business attractions, area demographics and geography. As a result, the opening of a new shop in or near markets in which we already have shops could adversely affect the sales of those existing shops. Existing shops could also make it more difficult to build our consumer base for a new shop in the same market. Our business strategy does not entail opening new shops that we believe will materially affect sales at our existing shops, but we may selectively open new shops in and around areas of existing shops that are operating at or near capacity to effectively serve our customers. Sales cannibalization between our shops may become significant in the future as we continue to expand our operations and could affect our sales growth, which could, in turn, adversely affect our business, financial condition or results of operations.

We are subject to risks associated with leasing property subject to long-term non-cancelable leases.

We do not own any real property and all of our company-owned shops are located in leased premises. The leases for our shop locations generally have initial terms of ten years and typically provide for two renewal options in five-year increments as well as for rent escalations. Generally, our leases are net leases that require us to pay our share of the costs of real estate taxes, utilities, building operating expenses, insurance and other charges in addition to rent. We generally cannot cancel these leases. Additional sites that we lease are likely to be subject to similar long-term non-cancelable leases. If we close a shop, we nonetheless may be obligated to perform our monetary obligations under the applicable lease, including, among other things, payment of the base rent for the balance of the lease term. In addition, as each of our leases expire, we may fail to negotiate renewals, either on commercially acceptable terms or at all, which could cause us to close shops in desirable locations. For example, while we are currently advocating to officials of the City of Chicago to retain our shop at Midway International Airport, we can give no assurance that our lease for that shop will be renewed. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Results of Operations—Fiscal Year 2016 (52 Weeks) Compared to Fiscal Year 2015 (52 Weeks)—Revenues" in Item 7.

Damage to our reputation or lack of acceptance of our brand in existing or new markets could negatively impact our business, financial condition and results of operations.

We believe we have built our reputation on the high quality of our food, service and staff, as well as on our unique culture and the ambience in our shops, and we must protect and grow the value of our brand to continue to be successful in the future. Any incident that erodes consumer affinity for our brand could significantly reduce its value and damage our business. For example, our brand value could suffer and our business could be adversely affected if customers perceive a reduction in the quality of our food,

service or staff, or an adverse change in our culture or ambience, or otherwise believe we have failed to deliver a consistently positive experience.

We may be adversely affected by news reports or other negative publicity (regardless of their accuracy), regarding food quality issues, public health concerns, illness, safety, injury or government or industry findings concerning our shops, restaurants operated by other foodservice providers, or others across the food industry supply chain. The risks associated with such negative publicity cannot be completely eliminated or mitigated and may materially harm our results of operations and result in damage to our brand.

Also, there has been a marked increase in the use of social media platforms, including blogs, social media websites and other forms of Internet-based communications which allow individuals access to a broad audience of consumers and other interested persons. The availability of information on social media platforms is virtually immediate as is its impact. Many social media platforms immediately publish the content their subscribers and participants can post, often without filters or checks on accuracy of the content posted. The opportunity for dissemination of information, including inaccurate information, is seemingly limitless and readily available. Information concerning our company may be posted on such platforms at any time. Information posted may be adverse to our interests or may be inaccurate, each of which may harm our performance, prospects or business. The harm may be immediate without affording us an opportunity for redress or correction. Such platforms also could be used for dissemination of trade secret information, compromising valuable company assets. In sum, the dissemination of information online could harm our business, prospects, financial condition and results of operations, regardless of the information's accuracy.

Our marketing programs may not be successful.

We incur costs and expend other resources in our marketing efforts to attract and retain customers. These initiatives may not be successful, resulting in expenses incurred without the benefit of higher revenues. Additionally, some of our competitors have greater financial resources, which enable them to spend significantly more on marketing and advertising than we are able to. Should our competitors increase spending on marketing and advertising or our marketing funds decrease for any reason, or should our advertising and promotions be less effective than our competitors, there could be a material adverse effect on our results of operations and financial condition.

Our business is subject to seasonal fluctuations.

Historically, customer spending patterns for our established shops are lowest in the first quarter of the year. Our quarterly results have been and will continue to be affected by the timing of new shop openings and their associated pre-opening costs. As a result of these and other factors, our financial results for any quarter may not be indicative of the results that may be achieved for a full fiscal year.

Because many of our shops are concentrated in local or regional areas, we are susceptible to economic and other trends and developments, including adverse weather conditions, in these areas.

Our financial performance is highly dependent on shops located in Illinois, Texas, Michigan, Maryland, and Washington, D.C., which comprised approximately 62% of our total domestic shops as of December 25, 2016. Shops located in the Chicago metropolitan area comprised approximately 26% of our total domestic shops as of such date. As a result, adverse economic conditions in any of these areas could have a material adverse effect on our overall results of operations. In addition, given our geographic concentrations, negative publicity regarding any of our shops in these areas could have a material adverse effect on our business and operations, as could other regional occurrences such as local strikes, terrorist attacks, increases in energy prices, or natural or man-made disasters.

In particular, adverse weather conditions, such as regional winter storms, floods, severe thunderstorms and hurricanes, could negatively impact our results of operations. For example, during the first quarter of 2014, nearly 80% of our shops were located in areas that were negatively impacted by extreme cold temperatures, heavy snowfall, or a combination of both, for a majority of the operating days in that fiscal quarter. Temporary or prolonged shop closures may occur and customer traffic may decline due to the actual or perceived effects of future weather related events.

Legislation and regulations requiring the display and provision of nutritional information for our menu offerings, and new information or attitudes regarding diet and health or adverse opinions about the health effects of consuming our menu offerings, could affect consumer preferences and negatively impact our results of operations.

Government regulation and consumer eating habits may impact our business as a result of changes in attitudes regarding diet and health or new information regarding the health effects of consuming our menu offerings. These changes have resulted in, and may continue to result in, the enactment of laws and regulations that impact the ingredients and nutritional content of our menu offerings, or laws and regulations requiring us to disclose the nutritional content of our food offerings.

For example, a number of states, counties and cities have enacted menu labeling laws requiring multi-unit restaurant operators to disclose certain nutritional information to customers, or have enacted legislation restricting the use of certain types of ingredients in restaurants. Furthermore, the Patient Protection and Affordable Care Act of 2010, establishes a uniform, federal requirement for certain restaurants to post certain nutritional information on their menus. Specifically, the PPACA amended the Federal Food, Drug and Cosmetic Act to require chain restaurants with 20 or more locations operating under the same name and offering substantially the same menus to publish the total number of calories of standard menu items on menus and menu boards, along with a statement that puts this calorie information in the context of a total daily calorie intake. The PPACA also requires covered restaurants to provide to consumers, upon request, a written summary of detailed nutritional information for each standard menu item, and to provide a statement on menus and menu boards about the availability of this information. An unfavorable report on, or reaction to, our menu ingredients, the size of our portions or the nutritional content of our menu items could negatively influence the demand for our offerings.

Compliance with current and future laws and regulations regarding the ingredients and nutritional content of our menu items may be costly and time-consuming. Additionally, if consumer health regulations or consumer eating habits change significantly, we may be required to modify or discontinue certain menu items, and we may experience higher costs associated with the implementation of those changes. Additionally, some government authorities are increasing regulations regarding trans-fats and sodium, which may require us to limit or eliminate trans-fats and sodium from our menu offerings or switch to higher cost ingredients or may hinder our ability to operate in certain markets. If we fail to comply with these laws or regulations, our business could experience a material adverse effect.

We cannot make any assurances regarding our ability to effectively respond to changes in consumer health perceptions or our ability to successfully implement the nutrient content disclosure requirements and to adapt our menu offerings to trends in eating habits. The imposition of menu-labeling laws could have an adverse effect on our results of operations and financial position, as well as the restaurant industry in general.

We are subject to many federal, state and local laws with which compliance is both costly and complex.

The restaurant industry is subject to extensive federal, state and local laws and regulations, including those relating to building and zoning requirements and those relating to the preparation and sale of food. The development and operation of restaurants depend to a significant extent on the selection and acquisition of suitable sites, which are subject to zoning, land use, environmental, traffic and other regulations and requirements. We are also subject to licensing and regulation by state and local authorities relating to health, sanitation, safety and fire standards.

We are subject to federal and state laws governing our relationships with employees (including the Fair Labor Standards Act of 1938, the Immigration Reform and Control Act of 1986 and applicable requirements concerning the minimum wage, overtime, family leave, working conditions, safety standards, immigration status, unemployment tax rates, workers' compensation rates and state and local payroll taxes) and federal and state laws which prohibit discrimination. As significant numbers of our associates are paid at rates related to the applicable minimum wage, further increases in the minimum wage or other changes in these laws could increase our labor costs. Our ability to respond to minimum wage increases by increasing menu prices will depend on the responses of our competitors and customers.

In March 2010, the United States federal government enacted comprehensive health care reform legislation which, among other things, includes guaranteed coverage requirements, eliminates pre-existing condition exclusions and annual and lifetime maximum limits, restricts the extent to which policies can be rescinded and imposes new and significant taxes on health insurers and health care benefits. The legislation imposes implementation effective dates that began in 2010 and extend through 2020, and many of the changes require additional guidance from government agencies or federal regulations. To date, we have not experienced material costs related to such legislation. It is anticipated that there will be changes to the legislation, but we cannot predict what those changes will be or when they will take effect. It is difficult to determine at this time what impact the health care reform legislation, or any changes to the legislation, will have on our financial results. Possible adverse effects could include increased costs, exposure to expanded liability and requirements for us to revise the ways in which we provide healthcare and other benefits to our employees.

There is also a potential for increased regulation of certain food establishments in the United States, where compliance with a HACCP approach may now be required. HACCP refers to a management system in which food safety is addressed through the analysis and control of potential hazards from production, procurement and handling, to manufacturing, distribution and consumption of the finished product. Many states have required restaurants to develop and implement HACCP Systems, and the United States government continues to expand the sectors of the food industry that must adopt and implement HACCP programs. For example, the FSMA, signed into law in January 2011, granted the FDA new authority regarding the safety of the entire food system, including through increased inspections and mandatory food recalls. Although restaurants are specifically exempted from or not directly implicated by some of these new requirements, we anticipate that the new requirements may impact our industry. Additionally, our

suppliers may initiate or otherwise be subject to food recalls that may impact the availability of certain products, result in adverse publicity or require us to take actions that could be costly for us or otherwise impact our business.

We are subject to the Americans with Disabilities Act, which, among other things, requires our shops to meet federally mandated requirements for the disabled. The ADA prohibits discrimination in employment and public accommodations on the basis of disability. Under the ADA, we could be required to expend funds to modify our shops to provide service to, or make reasonable accommodations for the employment of, disabled persons. In addition, our employment practices are subject to the requirements of the Immigration and Naturalization Service relating to citizenship and residency. Government regulations could also affect and change the items we procure for resale such as commodities.

In addition, our domestic franchising activities are subject to laws enacted by a number of states, rules and regulations promulgated by the U.S. Federal Trade Commission and certain rules and requirements regulating franchising activities in foreign countries. Failure to comply with new or existing franchise laws, rules and regulations in any jurisdiction or to obtain required government approvals could negatively affect our franchise sales and our relationships with our franchisees.

The impact of current laws and regulations, the effect of future changes in laws or regulations that impose additional requirements and the consequences of litigation relating to current or future laws and regulations, or our inability to respond effectively to significant regulatory or public policy issues, could increase our compliance and other costs of doing business and, therefore, have an adverse effect on our results of operations. Failure to comply with the laws and regulatory requirements of federal, state and local authorities could result in, among other things, revocation of required licenses, administrative enforcement actions, fines and civil and criminal liability. In addition, certain laws, including the ADA, could require us to expend significant funds to make modifications to our shops if we failed to comply with applicable standards. Compliance with all of these laws and regulations can be costly and can increase our exposure to litigation or governmental investigations or proceedings.

Failure to obtain and maintain required licenses and permits or to comply with food control regulations could lead to the loss of our food service licenses and, thereby, harm our business.

Restaurants are required under various federal, state and local government regulations to obtain and maintain licenses, permits and approvals to operate their businesses and such regulations are subject to change from time to time. The failure to obtain and maintain these licenses, permits and approvals could adversely affect our operating results. Typically, licenses must be renewed annually and may be revoked, suspended or denied renewal for cause at any time if governmental authorities determine that our conduct violates applicable regulations. Difficulties or failure to maintain or obtain the required licenses and approvals could adversely affect our existing shops and delay or result in our decision to cancel the opening of new shops, which would adversely affect our business.

Shortages or interruptions in the supply or delivery of fresh food products could adversely affect our operating results.

We are dependent on frequent deliveries of fresh food products that meet our specifications. Shortages or interruptions in the supply of fresh food products caused by problems in production or distribution, inclement weather, unanticipated demand or other conditions could adversely affect the availability, quality and cost of ingredients, which would adversely affect our operating results.

We have a limited number of suppliers for our major products and rely on a distribution network with a limited number of distribution partners for the majority of our national distribution program in the U.S. If our suppliers or distributors are unable to fulfill their obligations under their contracts, it could harm our operations.

We have a limited number of suppliers for our major products, such as bread. In 2016, we purchased almost all of our bread from one supplier, Campagna-Turano Bakery, Inc., and more than 97% of our meat products from ten suppliers. In addition, we contract with a distribution network with a limited number of distribution partners located throughout the nation to provide the majority of our food distribution services in the U.S. Through our arrangement, our food supplies are largely distributed through five primary distributors. Although we believe that alternative supply and distribution sources are available, there can be no assurance that we will be able to identify or negotiate with such sources on terms that are commercially reasonable to us. If our suppliers or distributors are unable to fulfill their obligations under their contracts or we are unable to identify alternative sources, we could encounter supply shortages and incur higher costs. See “Business—Sourcing and Supply Chain” in Item 1.

Information technology system failures or breaches of our network security could interrupt our operations and adversely affect our business.

We rely on our computer systems and network infrastructure across our operations, including point-of-sale processing at our shops. In addition, we are increasingly relying on cloud computing and other technologies that result in third parties holding customer

information on our behalf. Our operations depend upon our and our third party vendors' ability to protect our computer equipment and systems against damage from physical theft, fire, power loss, telecommunications failure or other catastrophic events, as well as from internal and external security breaches, viruses and other disruptive problems. Any damage or failure of our computer systems or network infrastructure that causes an interruption in our operations could have a material adverse effect on our business and subject us to litigation or actions by regulatory authorities.

Security breaches of confidential customer information in connection with our electronic processing of credit and debit card transactions may adversely affect our business.

The majority of our sales are by credit or debit cards. Other restaurants and retailers have experienced security breaches in which credit and debit card information of their customers has been stolen. We may in the future become subject to lawsuits or other proceedings for purportedly fraudulent transactions arising out of the actual or alleged theft of our customers' credit or debit card information. In addition, most states have enacted legislation requiring notification of security breaches involving personal information, including credit and debit card information. Any such claim or proceeding, or any adverse publicity resulting from these allegations, may have a material adverse effect on our business.

Changes to estimates related to our property, fixtures and equipment or operating results that are lower than our current estimates at certain shop locations may cause us to incur impairment charges on certain long-lived assets, which may adversely affect our results of operations.

In accordance with accounting guidance as it relates to the impairment of long-lived assets, we make certain estimates and projections with regard to individual shop operations, as well as our overall performance, in connection with our impairment analyses for long-lived assets. When impairment triggers are deemed to exist for any location, the estimated undiscounted future cash flows are compared to its carrying value. If the carrying value exceeds the undiscounted cash flows, an impairment charge equal to the difference between the carrying value and the sum of the discounted cash flows is recorded. The projections of future cash flows used in these analyses require the use of judgment and a number of estimates and projections of future operating results. If actual results differ from our estimates, additional charges for asset impairments may be required in the future. We have experienced significant impairment charges in past years. If future impairment charges are significant, our reported operating results would be adversely affected.

We may not be able to adequately protect our intellectual property, which, in turn, could harm the value of our brands and adversely affect our business.

Our ability to implement our business plan successfully depends in part on our ability to further build brand recognition using our trademarks, service marks and other proprietary intellectual property, including our name and logos and the unique ambiance of our shops. We have registered or applied to register a number of our trademarks. We cannot assure you that our trademark applications will be approved. Third parties may also oppose our trademark applications, or otherwise challenge our use of the trademarks. In the event that our trademarks are successfully challenged, we could be forced to rebrand our goods and services, which could result in loss of brand recognition, and could require us to devote resources to advertising and marketing new brands. If our efforts to register, maintain and protect our intellectual property are inadequate, or if any third party misappropriates, dilutes or infringes on our intellectual property, the value of our brands may be harmed, which could have a material adverse effect on our business and might prevent our brands from achieving or maintaining market acceptance. We may also face the risk of claims that we have infringed third parties' intellectual property rights. If third parties claim that we infringe upon their intellectual property rights, our operating profits could be adversely affected. Any claims of intellectual property infringement, even those without merit, could be expensive and time consuming to defend, require us to rebrand our services, if feasible, divert management's attention and resources or require us to enter into royalty or licensing agreements in order to obtain the right to use a third party's intellectual property.

Restaurant companies have been the target of class action lawsuits and other proceedings alleging, among other things, violations of federal and state workplace and employment laws. Proceedings of this nature are costly, divert management attention and, if successful, could result in our payment of substantial damages or settlement costs.

Our business is subject to the risk of litigation by employees, consumers, suppliers, stockholders or others through private actions, class actions, administrative proceedings, regulatory actions or other litigation. The outcome of litigation, particularly class action and regulatory actions, is difficult to assess or quantify. In recent years, restaurant companies have been subject to lawsuits, including class action lawsuits, alleging violations of federal and state laws regarding workplace and employment matters, discrimination and similar matters. A number of these lawsuits have resulted in the payment of substantial damages by the defendants.

Occasionally, our customers file complaints or lawsuits against us alleging that we are responsible for some illness or injury they suffered at or after a visit to one of our shops, including actions seeking damages resulting from food-borne illness or accidents in

our shops. We are also subject to a variety of other claims from third parties arising in the ordinary course of our business, including contract claims. The restaurant industry has also been subject to a growing number of claims that the menus and actions of restaurant chains have led to the obesity of certain of their customers. We may also be subject to lawsuits from our employees, the U.S. Equal Employment Opportunity Commission or others alleging violations of federal and state laws regarding workplace and employment matters, discrimination and similar matters.

Regardless of whether any claims against us are valid or whether we are liable, claims may be expensive to defend and may divert time and money away from our operations. In addition, they may generate negative publicity, which could reduce customer traffic and sales. Although we maintain what we believe to be adequate levels of insurance, insurance may not be available at all or in sufficient amounts to cover any liabilities with respect to these or other matters. A judgment or other liability in excess of our insurance coverage for any claims or any adverse publicity resulting from claims could adversely affect our business and results of operations.

Our insurance may not provide adequate levels of coverage against claims.

We believe that we maintain insurance customary for businesses of our size and type. However, there are types of losses we may incur that cannot be insured against or that we believe are not economically reasonable to insure. Such losses could have a material adverse effect on our business and results of operations.

Unionization activities or labor disputes may disrupt our operations and affect our profitability.

Although none of our employees are currently covered under collective bargaining agreements, our employees may elect to be represented by labor unions in the future. If a significant number of our employees were to become unionized and collective bargaining agreement terms were significantly different from our current compensation arrangements, it could adversely affect our business, financial condition or results of operations. In addition, a labor dispute involving some or all of our employees may harm our reputation, disrupt our operations and reduce our revenues, and resolution of disputes may increase our costs.

As an employer, we may be subject to various employment-related claims, such as individual or class actions or government enforcement actions relating to alleged employment discrimination, employee classification and related withholding, wage-hour, labor standards or healthcare and benefit issues. Such actions, if brought against us and successful in whole or in part, may affect our ability to compete or could adversely affect our business, financial condition or results of operations.

We have limited control with respect to the operations of our franchisees which could have a negative impact on our business.

Our franchisees are obligated to operate their shops according to the specific guidelines we set forth. We provide training opportunities to these franchisees to integrate them into our operating strategy. However, since we do not have control over these shops, we cannot give assurance that there will not be differences in product quality, operations, marketing or profitably or that there will be adherence to all of our guidelines at these shops. The failure of these shops to operate effectively could adversely affect our cash flows from those operations or have a negative impact on our reputation or our business.

In addition, franchisees may not have access to the financial or management resources that they need to open the shops contemplated by their agreements with us, or be able to find suitable sites on which to develop them, or they may elect to cease development for other reasons. Franchisees may not be able to negotiate acceptable lease or purchase terms for the sites, obtain the necessary permits and governmental approvals or meet construction schedules. Any of these problems could slow our growth from franchise operations and reduce our franchise revenues. Additionally, financing from banks and other financial institutions may not always be available to franchisees to construct and open new shops. The lack of adequate financing could adversely affect the number and rate of new shop openings by our franchisees and adversely affect our future franchise revenues.

Risks Related to Ownership of Our Common Stock

Our stock price could be extremely volatile and, as a result, you may not be able to resell your shares at or above the price you paid for them.

Volatility in the market price of our common stock may prevent you from being able to sell your shares at or above the price you paid for your shares. The stock market in general has been highly volatile, and this may be especially true for our common stock given our growth strategy and stage of development. As a result, the market price of our common stock is likely to be similarly volatile. You may experience a decrease, which could be substantial, in the value of your stock, including decreases unrelated to our operating performance or prospects, and could lose part or all of your investment. The price of our common stock could be subject to wide fluctuations in response to a number of factors, including those described elsewhere in this Annual Report and others such as:

- actual or anticipated fluctuations in our quarterly or annual operating results and the performance of our competitors;
- publication of research reports by securities analysts about us, our competitors or our industry;
- our failure or the failure of our competitors to meet analysts' projections or guidance that we or our competitors may give to the market;
- additions and departures of key personnel;
- sales, or anticipated sales, of large blocks of our stock or of shares held by our stockholders, directors or executive officers;
- strategic decisions by us or our competitors, such as acquisitions, divestitures, spin-offs, joint ventures, strategic investments or changes in business strategy;
- the passage of legislation or other regulatory developments affecting us or our industry;
- speculation in the press or investment community, whether or not correct, involving us, our suppliers or our competitors;
- changes in accounting principles;
- litigation and governmental investigations;
- terrorist acts, acts of war or periods of widespread civil unrest;
- a food-borne illness outbreak;
- severe weather, natural disasters and other calamities; and
- changes in general market and economic conditions.

As we operate in a single industry, we are especially vulnerable to these factors to the extent that they affect our industry or our products. In the past, securities class action litigation has often been initiated against companies following periods of volatility in their stock price. This type of litigation could result in substantial costs and divert our management's attention and resources, and could also require us to make substantial payments to satisfy judgments or to settle litigation.

Provisions in our certificate of incorporation and by-laws and Delaware law may discourage, delay or prevent a change of control of our company or changes in our management and, therefore, may depress the trading price of our stock.

Our certificate of incorporation and by-laws include certain provisions that could have the effect of discouraging, delaying or preventing a change of control of our company or changes in our management, including, among other things:

- our board is classified into three classes of directors with only one class subject to election each year, with the classified board being phased out by our fifth annual meeting of stockholders following our initial public offering;
- restrictions on the ability of our stockholders to fill a vacancy on the board of directors;
- our ability to issue preferred stock with terms that the board of directors may determine, without stockholder approval, which could be used to significantly dilute the ownership of a hostile acquirer;
- the inability of our stockholders to call a special meeting of stockholders;
- our directors may only be removed from the board of directors for cause by the affirmative vote of the holders of at least 66-2/3% of the voting power of outstanding shares of our capital stock entitled to vote generally in the election of directors;

- the absence of cumulative voting in the election of directors, which may limit the ability of minority stockholders to elect directors;
- advance notice requirements for stockholder proposals and nominations, which may discourage or deter a potential acquirer from soliciting proxies to elect a particular slate of directors or otherwise attempting to obtain control of us; and
- our by-laws may only be amended by the affirmative vote of the holders of at least 66-2/3% of the voting power of outstanding shares of our capital stock entitled to vote generally in the election of directors or by our board of directors.

Section 203 of the Delaware General Corporation Law may affect the ability of an "interested stockholder" to engage in certain business combinations, including mergers, consolidations or acquisitions of additional shares, for a period of three years following the time that the stockholder becomes an "interested stockholder." An "interested stockholder" is defined to include persons owning directly or indirectly 15% or more of the outstanding voting stock of a corporation.

We are an "emerging growth company," and any decision on our part to comply only with certain reduced reporting and disclosure requirements applicable to emerging growth companies could make our common stock less attractive to investors.

We are an "emerging growth company," as defined in the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. For as long as we continue to be an "emerging growth company," we may choose to take advantage of exemptions from various reporting requirements applicable to other public companies but not to "emerging growth companies," including, but not limited to, not being required to have our independent registered public accounting firm audit our internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We may choose to take advantage of some but not all of these reduced burdens until we are no longer an "emerging growth company." We will remain an emerging growth company until the earlier of (1) the last day of the fiscal year (a) following the fifth anniversary of the completion of our initial public offering, (b) in which we have total annual gross revenue of at least $1.0 billion, or (c) in which we are deemed to be a large accelerated filer, which means the market value of our common stock that is held by non-affiliates exceeds $700 million as of the prior June 30th, or (2) the date on which we have issued more than $1.0 billion in non-convertible debt securities during the prior three-year period. We cannot predict if investors will find our common stock less attractive if we choose to rely on these exemptions. If some investors find our common stock less attractive as a result of any choices to reduce future disclosure, there may be a less active trading market for our common stock and our stock price may be more volatile.

Under the JOBS Act, emerging growth companies can delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have irrevocably elected not to avail ourselves of this exemption from new or revised accounting standards, and, therefore, we will be subject to the same new or revised accounting standards as other public companies that are not emerging growth companies.

If securities analysts or industry analysts downgrade our stock, publish negative research or reports, or do not publish reports about our business, our stock price and trading volume could decline.

The trading market for our common stock is influenced by the research and reports that industry or securities analysts publish about us, our business and our industry. If one or more analysts adversely change their recommendation regarding our stock or our competitors' stock, our stock price would likely decline. If one or more analysts cease coverage of us or fail to regularly publish reports on us, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline.

Because we have no plans to pay regular cash dividends on our common stock for the foreseeable future, you may not receive any return on investment unless you sell your common stock for a price greater than that which you paid for it.

We may retain future earnings, if any, for future operations, expansion and debt repayment and have no current plans to pay any cash dividends for the foreseeable future. Any decision to declare and pay dividends in the future will be made at the discretion of our board of directors and will depend on, among other things, our results of operations, financial condition, cash requirements, contractual restrictions and other factors that our board of directors may deem relevant. In addition, our ability to pay dividends may be limited by covenants of any existing and future outstanding indebtedness we or our subsidiaries incur, including our credit facility. As a result, you may not receive any return on an investment in our common stock unless you sell our common stock for a price greater than that which you paid for it.

Our ability to raise capital in the future may be limited, which could make us unable to fund our capital requirements.

Our business and operations may consume resources faster than we anticipate. In the future, we may need to raise additional funds through the issuance of new equity securities, debt or a combination of both. Additional financing may not be available on favorable terms or at all. If adequate funds are not available on acceptable terms, we may be unable to fund our capital requirements. If we issue new debt securities, the debt holders would have rights senior to common stockholders to make claims on our assets, and the terms of any debt could restrict our operations, including our ability to pay dividends on our common stock. If we issue additional equity securities, existing stockholders may experience dilution, and the new equity securities could have rights senior to those of our common stock. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, our stockholders bear the risk of our future securities offerings reducing the market price of our common stock and diluting their interest.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We do not own any real property. As of December 25, 2016, we had the following number of company-operated shops located in the following areas:

Location	Number of Shops	Location	Number of Shops
Illinois	107	Colorado	7
Texas	64	Indiana	7
Michigan	31	Massachusetts	6
Maryland	27	Oregon	6
District of Columbia	24	Utah	6
Virginia	21	Kansas	5
Minnesota	20	Pennsylvania	3
Ohio	19	New Jersey	2
New York	17	Connecticut	1
Arizona	12	Kentucky	1
Washington	12	Missouri	1
Wisconsin	12		
		Total	**411**

Initial lease terms for our company-operated properties are generally ten years, with the majority of the leases providing for an option to renew for two additional five-year terms. Nearly all of our leases provide for a minimum annual rent, and some of our leases call for additional rent based on sales volume at the particular location over specified minimum levels. Generally, the leases are net leases that require us to pay our share of the costs of real estate taxes, utilities, building operating expenses, insurance and other charges in addition to rent. For additional information regarding our leases, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Contractual Obligations" in Item 7.

During 2015, we moved our headquarters to the new office space in Chicago. As of December 25, 2016, we occupied approximately 32,000 square feet of office space in Chicago, Illinois under an 11 year lease for our corporate headquarters.

ITEM 3. LEGAL PROCEEDINGS

As previously disclosed in prior reports filed with the SEC, the Company received notice of a potential claim alleging that the Company violated the Fair Labor Standards Act by not paying overtime to our assistant managers, whom we have classified as exempt employees. Although we have always believed that our assistant managers are properly classified as exempt under both federal and state laws, and have always intended to defend any such lawsuits vigorously, we agreed to mediate the matter. On February 20, 2017, the parties entered into a Settlement Agreement and Release whereby participating assistant managers will release the Company from all federal and/or state wage and hour claims in exchange for a gross settlement amount of $1.3 million. As part of the settlement process, a complaint was filed on February 17, 2017 in the Circuit Court of the Fifteenth Judicial Circuit in and for Palm Beach County, Florida, and a motion seeking the Court's preliminary approval of the settlement was filed on February 21, 2017. As of December 25, 2016, the Company recorded a liability of $1.3 million for this matter. The settlement of this action did not have a material adverse effect on our financial position or results of operations and cash flows.

We are subject to legal proceedings, claims and liabilities, such as employment-related claims and slip and fall cases, which arise in the ordinary course of business and are generally covered by insurance. In the opinion of management, the amount of ultimate liability with respect to those actions should not have a material adverse impact on our financial position or results of operations and cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Common Stock Market Prices and Dividends

The following table describes the per share range of high and low sales prices for shares of our common stock for the quarterly periods indicated, as reported by the NASDAQ. Our common stock trades on the NASDAQ under the symbol "PBPB".

	2016		2015	
	High	Low	High	Low
First Quarter	$ 13.95	$ 10.15	$ 16.56	$ 12.19
Second Quarter	14.87	12.37	15.81	12.60
Third Quarter	13.60	12.11	13.90	10.09
Fourth Quarter	14.40	11.90	12.50	10.79

On February 17, 2017, the closing price of our common stock on the Nasdaq Global Select Market was $13.50 per share.

Holders

As of December 25, 2016, there were 46 stockholders of record of our common stock. This number excludes stockholders whose stock is held in nominee or street name by brokers.

Dividend Policy

We currently intend to retain all available funds and any future earnings to fund the development and growth of our business and therefore we do not anticipate paying any cash dividends in the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors, subject to compliance with covenants in future agreements governing our indebtedness, and will depend upon our results of operations, financial condition, capital requirements and other factors that our board of directors deems relevant. In addition, in certain circumstances, our revolving credit facility restricts our ability to pay dividends. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Credit Facility" in Item 7.

Purchases of Equity Securities by the Issuer

The following table contains information regarding purchases of our common stock made by or on behalf of Potbelly Corporation during the 13 weeks ended December 25, 2016:

Period	Total Number of Shares Purchased	Average Price Paid per Share (1)	Total Number of Shares Purchased as Part of Publicly Announced Program (2)	Maximum Value of Shares that May Yet be Purchased Under the Program (2)
September 26, 2016 – October 23, 2016	72,368	$ 12.85	72,368	$ 28,624,080
October 24, 2016 – November 20, 2016	56,918	$ 12.72	56,918	$ 27,900,206
November 21, 2016 – December 25, 2016	15,900	$ 13.67	15,900	$ 27,682,861
Total	145,186		145,186	

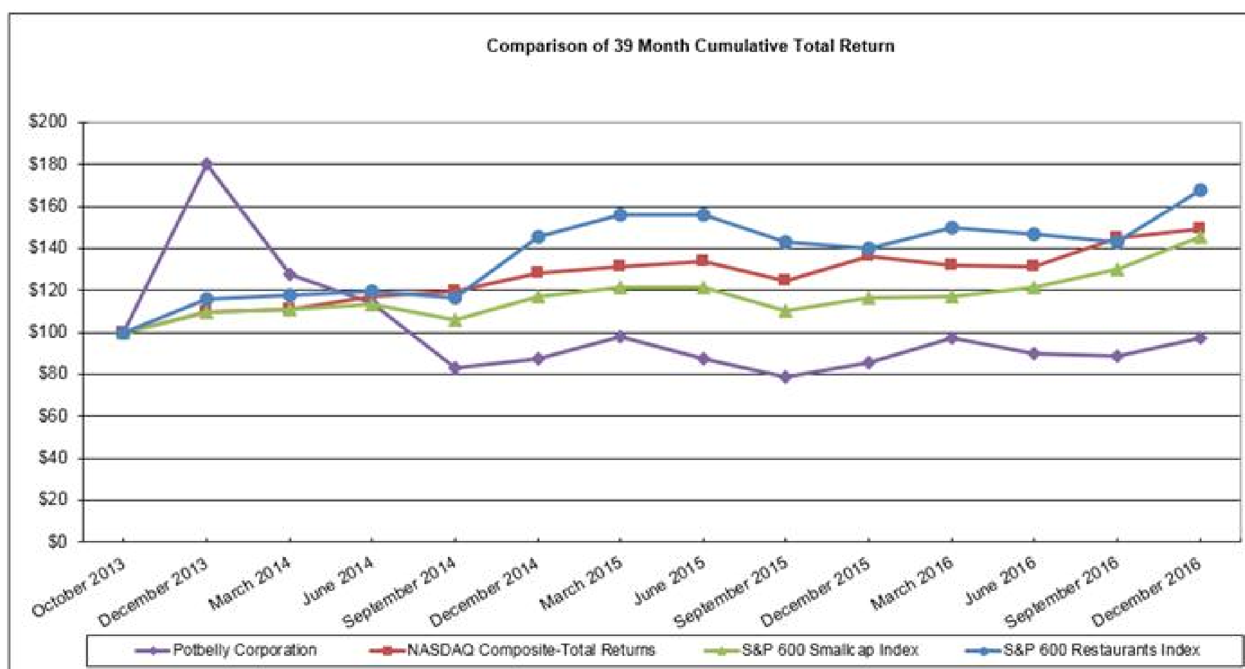
(1) Average price paid per share excludes commissions.

(2) On September 8, 2016, we announced that our Board of Directors approved a share repurchase program, authorizing us to repurchase up to $30.0 million of our common stock. Our previous $35.0 million share repurchase program, authorized in September 2015, was completed in July 2016. The new program permits us, from time to time, to purchase shares in the open market (including in pre-arranged stock trading plans in accordance with the guidelines specified in Rule 10b5-1 under the Exchange Act) or in privately negotiated transactions. No time limit has been set for the completion of the repurchase program, and the program may be suspended or discontinued at any time.

Performance Graph

The following graph and accompanying table show the cumulative total return to stockholders of Potbelly Corporation's common stock relative to the cumulative total returns of the NASDAQ Composite Index, S&P 600 Smallcap Index and S&P 600 Restaurants Index. The graph tracks the performance of a $100 investment in our common stock and in each of the indices (with the

reinvestment of dividends) from October 4, 2013 (the date our common stock commenced trading on the NASDAQ) to December 25, 2016. The stock price performance included in this graph is not necessarily indicative of future stock price performance.



ITEM 6. SELECTED FINANCIAL DATA

The following table sets forth our selected consolidated financial and other data as of the dates and for the periods indicated. We derived the consolidated statements of operations data presented below for the fiscal years ended December 25, 2016, December 27, 2015 and December 28, 2014 and selected balance sheet data presented below as of December 25, 2016 and December 27, 2015 from our audited consolidated financial statements included in Part II, Item 8, “Financial Statements and Supplementary Data” of this Annual Report on Form 10-K. The selected consolidated statements of operations data for the fiscal years ended December 29, 2013 and December 30, 2012 and the selected balance sheet data as of December 28, 2014, December 29, 2013 and December 30, 2012 have been derived from audited consolidated financial statements not included in this Annual Report on Form 10-K. Our historical results are not necessarily indicative of our results in any future period.

Operating results are reported on a 52-week fiscal year calendar, with a 53-week year occurring every fifth or sixth year. Our fiscal year ends on the last Sunday of each calendar year. Fiscal years 2016, 2015, 2014 and 2013 were 52-week years. Fiscal year 2012 included a 53rd week. The first three quarters of our fiscal year consist of 13 weeks and our fourth quarter consists of 13 weeks for 52-week fiscal years and 14 weeks for 53-week fiscal years.

Our selected consolidated financial and other data should be read in conjunction with the disclosure set forth under "Risk Factors" in Item 1A, "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 and our consolidated financial statements and the related notes included in Part II, Item 8, "Financial Statements and Supplementary Data" of this Annual Report on Form 10-K.

	Fiscal Year Ended				
	December 25, 2016	December 27, 2015	December 28, 2014	December 29, 2013	December 30, 2012
			($ in thousands)		
Total revenues	$ 407,131	$ 372,849	$ 326,979	$ 299,712	$ 274,914
Expenses:					
Sandwich shop operating expenses:					
Cost of goods sold, excluding depreciation	111,026	105,614	93,688	87,380	79,847
Labor and related expenses	117,838	106,628	93,165	83,579	77,479
Occupancy expenses	52,444	46,762	41,389	36,394	32,016
Other operating expenses	43,738	39,869	34,669	30,781	28,119
General and administrative expenses	40,411	37,322	32,420	39,656	29,624
Depreciation expense	22,734	21,476	19,615	17,875	16,219
Pre-opening costs	1,786	2,160	1,634	1,437	2,051
Impairment and loss on disposal of property and equipment	4,141	3,589	3,128	1,135	994
Total expenses	394,118	363,420	319,708	298,237	266,349
Income from operations	13,013	9,429	7,271	1,475	8,565
Interest expense, net	134	221	179	387	541
Other expense	—	—	—	2	6
Income before income taxes	12,879	9,208	7,092	1,086	8,018
Income tax expense (benefit) (1)	4,443	3,466	2,748	(204)	(15,994)
Net income	8,436	5,742	4,344	1,290	24,012
Net income (loss) attributable to non-controlling interests (2)	224	114	(14)	32	(34)
Net income attributable to Potbelly Corporation	8,212	5,628	4,358	1,258	24,046
Dividend declared and paid to common and preferred stockholders	—	—	—	(49,854)	—
Accretion of redeemable convertible preferred stock to maximum redemption value	—	—	—	(15,097)	(10,495)
Net income (loss) attributable to common stockholders	$ 8,212	$ 5,628	$ 4,358	$ (63,693)	$ 13,551

	Fiscal Year Ended				
	December 25, 2016	December 27, 2015	December 28, 2014	December 29, 2013	December 30, 2012
	($ in thousands, except per share data)				
Net income (loss) per common share attributable to common stockholders (3):					
Basic	$ 0.32	$ 0.20	$ 0.15	$ (6.29)	$ 0.72
Diluted	$ 0.31	$ 0.20	$ 0.14	$ (6.29)	$ 0.66
Weighted average shares outstanding:					
Basic	25,623,809	28,002,005	29,209,298	10,132,805	4,013,414
Diluted	26,231,367	28,634,396	30,275,061	10,132,805	4,388,822
Statement of Cash Flows Data:					
Net cash provided by (used in):					
Operating activities	45,969	40,320	26,554	29,880	25,085
Investing activities	(37,820)	(36,058)	(29,209)	(28,098)	(25,936)
Financing activities	(16,776)	(35,261)	(3,919)	45,202	(700)
Selected Other Data:					
Total company-operated shops (end of period)	411	372	334	296	264
Change in company-operated comparable store sales	1.4%	4.4%	0.1%	1.5%	3.4%
Operating income margin (4)	3.2%	2.5%	2.2%	0.5%	3.1%
Shop-level profit margin (5)	19.7%	19.4%	19.2%	20.2%	20.7%
Capital expenditures	36,712	35,725	29,209	28,098	25,936
Adjusted EBITDA (6)	48,000	41,637	36,849	35,222	31,451
Adjusted EBITDA margin (6)	11.8%	11.2%	11.3%	11.8%	11.4%

	December 25, 2016	December 27, 2015	December 28, 2014	December 29, 2013	December 30, 2012
	($ in thousands)				
Balance Sheet Data:					
Cash and cash equivalents	$ 23,379	$ 32,006	$ 63,005	$ 69,579	$ 22,595
Working capital	10,736	24,599	59,334	63,093	15,170
Total assets	175,445	174,507	191,947	186,080	126,699
Total debt	—	—	1,008	1,092	15,169
Total redeemable convertible preferred stock	—	—	—	—	250,343
Total equity (deficit)	124,236	130,213	156,325	153,273	(168,728)

(1) The fiscal year ended December 30, 2012 included a $16.9 million tax benefit related to the release of a valuation allowance against substantially all of our deferred tax assets. The fiscal year ended December 29, 2013 included a $0.6 million benefit related to increasing the federal statutory rate to measure our deferred tax assets.

(2) Non-controlling interests represent a non-controlling partner's share of the assets, liabilities and operations related to five joint venture investments. We have ownership interests ranging from 51-80% in these consolidated joint ventures.

(3) Net income (loss) per common share attributable to common stockholders is calculated using the weighted average number of common shares outstanding for the period. For fiscal year ending December 30, 2012, net income (loss) per common share attributable to common stockholders was calculated under the two-class method as our redeemable convertible preferred stock participated in the undistributed earnings of the company. Earnings of the company were allocated between the common and preferred stockholders to account for the accretion of the redeemable convertible preferred stock to its maximum redemption value, thereby reducing the earnings of the company attributable to common stockholders. Upon completion of the initial public offering on October 9, 2013, the redeemable convertible preferred stock was automatically converted to common stock.

(4) Income from operations as a percentage of total revenues.

(5) Shop-level profit is not required by, or presented in accordance with, GAAP, and is defined as income (loss) from operations less franchise royalties and fees, general and administrative expenses, depreciation expense, pre-opening costs and impairment and loss on disposal of property and equipment. Shop-level profit is a supplemental measure of operating performance of our shops and our calculation thereof may not be comparable to that reported by other companies. Shop-level profit margin represents shop-level profit expressed as a percentage of net company-operated sandwich shop sales. Shop-level profit and shop-level profit margin have limitations as analytical tools, and you should not consider them in isolation or as a substitute for analysis of our results as reported under GAAP. Management believes shop-level profit margin is an important tool for investors because it is a widely used metric within the restaurant industry to evaluate restaurant-level productivity, efficiency and performance. Management uses shop-level profit margin as a key metric to evaluate the profitability of incremental sales at our shops, to evaluate our shop performance across periods and to evaluate our shop financial performance compared with our

competitors. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 7 for a discussion of shop-level profit margin and other key performance indicators. A reconciliation of shop-level profit to income (loss) from operations and a calculation of shop-level profit margin is provided below:

	Fiscal Year Ended				
	December 25, 2016	December 27, 2015	December 28, 2014	December 29, 2013	December 30, 2012
			($ in thousands)		
Income from operations	$ 13,013	$ 9,429	$ 7,271	$ 1,475	$ 8,565
Less: Franchise royalties and fees	2,257	1,895	1,515	1,138	844
General and administrative expenses	40,411	37,322	32,420	39,656	29,624
Depreciation expense	22,734	21,476	19,615	17,875	16,219
Pre-opening costs	1,786	2,160	1,634	1,437	2,051
Impairment and loss on disposal of property and equipment	4,141	3,589	3,128	1,135	994
Shop-level profit [Y]	$ 79,828	$ 72,081	$ 62,553	$ 60,440	$ 56,609
Total revenues	$ 407,131	$ 372,849	$ 326,979	$ 299,712	$ 274,914
Less: Franchise royalties and fees	2,257	1,895	1,515	1,138	844
Sandwich shop sales, net [X]	$ 404,874	$ 370,954	$ 325,464	$ 298,574	$ 274,070
Shop-level profit margin [Y÷X]	19.7%	19.4%	19.2%	20.2%	20.7%

(6) Adjusted EBITDA is a supplemental measure of financial performance that is not required by, or presented in accordance with, GAAP. We define adjusted EBITDA as net income (loss) before depreciation and amortization expense, interest expense, provision for income taxes and pre-opening costs, adjusted to eliminate the impact of other items set forth in the reconciliation below, including certain non-cash as well as certain other items that we do not consider representative of our ongoing operating performance. Adjusted EBITDA margin is calculated by dividing adjusted EBITDA by total revenues. Adjusted EBITDA has limitations as an analytical tool and our calculation thereof may not be comparable to that reported by other companies; accordingly, you should not consider it in isolation or as a substitute for analysis of our results as reported under GAAP. Adjusted EBITDA is included in this Annual Report because it is a key metric used by management. Additionally, adjusted EBITDA is frequently used by analysts, investors and other interested parties to evaluate companies in our industry. We use adjusted EBITDA, alongside GAAP measures such as operating income (loss) and net income (loss), to measure profitability, as a key profitability target in our annual and other budgets, and to compare our performance against that of peer companies. We believe that adjusted EBITDA provides useful information facilitating operating performance comparisons from period to period and company to company. A reconciliation of adjusted EBITDA to net income attributable to Potbelly Corporation is provided below:

	Fiscal Year Ended				
	December 25, 2016	December 27, 2015	December 28, 2014	December 29, 2013	December 30, 2012
			($ in thousands)		
Net income attributable to Potbelly Corporation	$ 8,212	$ 5,628	$ 4,358	$ 1,258	$ 24,046
Depreciation expense	22,734	21,476	19,615	17,875	16,219
Interest expense, net	134	221	179	387	541
Income tax expense (benefit)	4,443	3,466	2,748	(204)	(15,994)
EBITDA	$ 35,523	$ 30,791	$ 26,900	$ 19,316	$ 24,812
Impairment and closures (a)	4,265	4,006	3,885	1,132	1,181
Pre-opening costs (b)	1,786	2,160	1,634	1,437	2,051
Stock-based compensation (c)	3,057	2,399	2,542	11,610	2,825
Legal settlement (d)	1,300	—	—	—	—
Public company costs (e)	2,069	2,281	1,888	1,727	582
Adjusted EBITDA	$ 48,000	$ 41,637	$ 36,849	$ 35,222	$ 31,451

(a) This adjustment includes costs related to impairment of long-lived assets, gain or loss on disposal of property and equipment and shop closure expenses. Additionally, fiscal years 2014 and 2015 reflects costs associated with our plans to move our corporate headquarters.

(b) This adjustment includes expenses directly associated with the opening of new shops and are incurred prior to the opening of the shop.

(c) This adjustment includes non-cash stock-based compensation. As a result of the consummation of our initial public offering, we recorded one-time charges of $10.0 million in fiscal year 2013 related to stock-based compensation, which primarily consist of a $7.6 million charge related to the cumulative expense for the periods in which the performance conditions were not met.

(d) This adjustment relates to a one-time, non-recurring legal expense incurred to establish an accrual related to a Fair Labor Standards claim.

(e) This adjustment includes on-going public company costs. Additionally, fiscal years 2012, 2013 and 2014 include one-time costs associated with our initial public offering. Both these costs primarily consist of legal and accounting fees.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with "Selected Financial Data" in Item 6 and our consolidated financial statements and the related notes to those statements included in Item 8. The discussion contains forward-looking statements involving risks, uncertainties and assumptions that could cause our results to differ materially from expectations. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those described in "Risk Factors" in Item 1A and elsewhere in this report.

Overview

Potbelly is a fast-growing neighborhood sandwich concept offering toasty warm sandwiches, signature salads and other fresh menu items served by engaging people in an environment that reflects the Potbelly brand. Our combination of product, people and place is how we deliver on our passion to be "The Best Place for Lunch." Our sandwiches, salads and hand-dipped milkshakes are all made fresh to order and our cookies are baked fresh each day. Our employees are trained to engage with our customers in a genuine way to provide a personalized experience. Our shops feature vintage design elements and locally-themed décor inspired by the neighborhood that we believe create a lively atmosphere. Through this combination, we believe we are creating a devoted base of Potbelly fans that return again and again and that we are expanding one sandwich shop at a time.

We believe that a key to our past and future success is our culture. It is embodied in *The Potbelly Advantage*, which is an expression of our Vision, Mission, Passion and Values, and the foundation of everything we do. Our Vision is for our customers to feel that we are their "Neighborhood Sandwich Shop" and to tell others about their great experience. Our Mission is to make people really happy, to make more money and to improve every day. Our Passion is to be "The Best Place for Lunch." Our Values embody both how we lead and how we behave, and form the cornerstone of our culture. We use simple language that resonates from the frontline associate to the most senior levels of the organization, creating shared expectations and accountabilities in how we approach our day-to-day activities. We strive to be a fun, friendly and hardworking group of people who enjoy taking care of our customers, while at the same time taking care of each other.

We own and operate Potbelly Sandwich Works sandwich shops in the United States. We also have domestic and international franchise operations of Potbelly Sandwich Works sandwich shops. Our chief operating decision maker is our Chief Executive Officer. Based on how our Chief Executive Officer reviews financial performance and allocates resources on a recurring basis, the company has one operating segment and one reportable segment.

The table below sets forth a rollforward of company-operated and franchise-operated activities:

	Company-Operated	Franchise-Operated			Total Company
		Domestic	International	Total	
Shops as of December 29, 2013	296	11	12	23	319
Shops opened	39	6	1	7	46
Shops closed	(1)	—	(1)	(1)	(2)
Shops as of December 28, 2014	**334**	**17**	**12**	**29**	**363**
Shops opened	43	8	2	10	53
Shop purchased from franchisee	1	(1)	—	(1)	—
Shops closed	(6)	—	(2)	(2)	(8)
Shops as of December 27, 2015	**372**	**24**	**12**	**36**	**408**
Shops opened	40	7	3	10	50
Shop purchased from franchisee	1	(1)	—	(1)	—
Shops closed	(2)	—	(2)	(2)	(4)
Shops as of December 25, 2016	**411**	**30**	**13**	**43**	**454**

Fiscal Year

Operating results are reported on a 52-week fiscal year calendar, with a 53-week year occurring every fifth or sixth year. Our fiscal year ends on the last Sunday of each calendar year. Fiscal years 2016, 2015 and 2014 were 52-week years. The first three quarters of our fiscal year consist of 13 weeks and our fourth quarter consists of 13 weeks for 52-week fiscal years and 14 weeks for 53-week fiscal years.

Outlook

Potbelly operates in a highly competitive segment of the restaurant industry. We compete with sandwich concepts that have significant scale and presence, as well as with the multitude of locally-owned sandwich shops. Additionally, we compete with many non-sandwich concepts that fall into the limited-service restaurants category. However, we believe that we will continue to succeed in the marketplace based on our combination of excellent product, people and place. The following competitive strengths provide a platform for us to achieve continued growth:

- *Simple, Made-to-Order Food*. Our menu features items made from high quality ingredients such as fresh vegetables, hearth-baked bread, and all-natural white-meat chicken. Our sandwiches are made fresh to order and served toasty warm on our signature multigrain or regular bread or on our multigrain Flats, all of which are delivered to our shops. Our menu also features a variety of cookies baked fresh daily in each shop, and our hand-dipped shakes, malts and smoothies are made from real ingredients. We believe the unique Potbelly experience encourages repeat customer visits and drives increased sales.
- *Differentiated Customer Experience That Delivers a Neighborhood Feel*. We strive to provide a positive customer experience that is driven by both our employees and the atmosphere of our shops. We look to hire employees that are outgoing people and train them to interact with our customers in a genuine way while providing fast service. We believe our atmosphere is enhanced by live, local musicians that perform weekly in the majority of our shops. Every Potbelly location strives to be "The Neighborhood Sandwich Shop," creating devoted fans who tell others about their experience.
- *Attractive Shop Economics*. Our shop model is designed to generate, and has generated, strong cash flow, with above 20% shop-level profit margins, a non-GAAP measure, and targeted cash-on-cash returns, on new company-operated shops, above 25% after two full years of operation. Our ability to maintain such margins and returns depends on a number of factors. For example, we face increasing labor and commodity costs, which we have partially offset by increasing menu prices. Although there is no guarantee that we will be able to maintain these returns, we believe our shop economics support our ability to profitably grow our brand in new and existing markets.
- *Management Team with Substantial Operating Experience*. Our senior management team has extensive operating experience across disciplines in the restaurant and retail sectors. Our senior team led by our CEO, Aylwin Lewis, averages 15 years of restaurant industry experience and embraces the daily intensity needed to deliver growth in existing shops as well as growing the business in new neighborhoods. We believe our experienced leadership team is a key driver of our success and positions us to execute our long-term growth strategy.
- *Distinct, Deep-Rooted Culture: The Potbelly Advantage*. We believe our culture is a key to our success. It is embodied in *The Potbelly Advantage*, which is an expression of our Vision, Mission, Passion and Values. *The Potbelly Advantage* is a statement of our intentions and is the foundation of everything we do, including how we plan and manage our business. It allows us to deliver operational excellence and grow our business and our base of devoted fans.

We believe the combination of these strengths provides a competitive advantage in the marketplace. Continuing to execute at a high level across all aspects of our business is imperative to realize the growth potential for Potbelly. We are confident in our strategies, our people and the opportunity to make Potbelly a "Global Iconic Brand."

Key Performance Indicators

In assessing the performance of our business, we consider a variety of performance and financial measures. The key measures for determining how our business is performing are comparable store sales, number of shop openings, shop-level profit margins and adjusted EBITDA.

Company-Operated Comparable Store Sales

Comparable store sales reflect the change in year-over-year sales for the comparable company-operated store base. We define the comparable store base to include those shops open for 15 months or longer. As of the fiscal years ended December 28, 2014, December 27, 2015 and December 25, 2016, there were 286, 312 and 355 shops, respectively, in our comparable company-operated store base. Comparable store sales growth can be generated by an increase in entree counts and/or by increases in the average check amount resulting from a shift in menu mix and/or increase in price. This measure highlights performance of existing shops as the impact of new shop openings is excluded. Entrees are defined as sandwiches, salads and bowls of soup.

Number of Company-Operated Shop Openings

The number of company-operated shop openings reflects the number of shops opened during a particular reporting period. Before we open new shops, we incur pre-opening costs, which are defined below. Often, new shops open with an initial start-up period of higher than normal sales volumes, which subsequently decrease to stabilized levels. While sales volumes are generally higher during the initial opening period, new shops typically experience normal inefficiencies in the form of higher cost of sales, labor and other direct operating expenses and as a result, shop-level profit margins are generally lower during the start-up period of operation. The average start-up period is 10 to 13 weeks. The number and timing of shop openings has had, and is expected to continue to have, an impact on our results of operations.

Shop-Level Profit Margin

Shop-level profit margin is defined as net company-operated sandwich shop sales less company-operated sandwich shop operating expenses, including cost of goods sold, labor and related expenses, other operating expenses and occupancy expenses, as a percentage of net company-operated sandwich shop sales. Shop-level profit margin is not required by, or presented in accordance with, GAAP. We believe shop-level profit margin is important in evaluating shop-level productivity, efficiency and performance.

Adjusted EBITDA

We define adjusted EBITDA as net income before depreciation and amortization, interest expense and provision for income taxes, adjusted for the impact of the following items that we do not consider representative of our ongoing operating performance: stock-based compensation expense, impairment and shop closure expenses, gain or loss on disposal of property and equipment, pre-opening expenses and public company costs as well as costs associated with our plans to move our corporate headquarters and other one-time, non-recurring charges. We believe that adjusted EBITDA is a more appropriate measure of operating performance, as it provides a clearer picture of operating results by eliminating expenses that are not reflective of underlying business performance.

Key Financial Definitions

Revenues

We generate revenue from net company-operated sandwich shop sales and our franchise operations. Net company-operated shop sales consist of food and beverage sales, net of promotional allowances and employee meals. Company-operated shop sales are influenced by new shop openings, shop closures and comparable store sales. Franchise royalties and fees consist of an initial franchise fee, a franchise development agreement fee and royalty income from the franchisee.

Cost of Goods Sold

Cost of goods sold consists primarily of food and beverage related costs. The components of cost of goods sold are variable in nature, change with sales volume, are influenced by menu mix and are subject to increases or decreases based on fluctuations in commodity costs.

Labor and Related Expenses

Labor and related expenses include all shop-level management and hourly labor costs, including salaries, wages, benefits and performance incentives, labor taxes and other indirect labor costs.

Occupancy Expenses

Occupancy expenses include fixed and variable portions of rent, common area maintenance and real estate taxes.

Other Operating Expenses

Other operating expenses include all other shop-level operating costs, the major components of which are credit card fees, operating supplies, utilities, repair and maintenance costs, shop-level marketing costs and musician expense.

General and Administrative Expenses

General and administrative expenses is comprised of expenses associated with corporate and administrative functions that support the development and operations of shops, including compensation and benefits, travel expenses, stock-based compensation

costs, legal and professional fees, advertising costs, costs related to abandoned new shop development sites and other related corporate costs.

Depreciation Expense

Depreciation expense includes the depreciation of fixed assets and capitalized leasehold improvements.

Pre-Opening Costs

Pre-opening costs consist of costs incurred prior to opening a new shop and are made up primarily of travel, employee payroll and training costs incurred prior to the shop opening, as well as occupancy costs incurred from when we take site possession to shop opening. Shop pre-opening costs are expensed as incurred.

Impairment and Loss on Disposal of Property and Equipment

We review long-lived assets, such as property and equipment and intangibles, for impairment when events or circumstances indicate the carrying value of the assets may not be recoverable and record an impairment charge when appropriate. The impairment loss recognized is the excess of the carrying value of the asset over its fair value. Typically, the fair value of the asset is determined by estimating undiscounted future cash flows associated with the asset. Loss on disposal of property and equipment represents the net book value of property and equipment less proceeds received, if applicable, on assets abandoned or sold. These losses are related to normal disposals in the ordinary course of business, along with disposals related to shop closures and selected shop remodeling activities.

Interest Expense

Interest expense consists of interest on the note payable, unused commitment fees and deferred financing fees.

Non-controlling Interests

Non-controlling interests represent a non-controlling partner’s share of the assets, liabilities and operations related to five joint venture investments. We have ownership interests ranging from 51-80% in these consolidated joint ventures.

Results of Operations

Fiscal Year 2016 (52 Weeks) Compared to Fiscal Year 2015 (52 Weeks)

The following table presents information comparing the components of net income for the periods indicated (dollars in thousands):

	Fiscal Year					
	2016	% of Revenues	2015	% of Revenues	Increase (Decrease)	Percent Change
Revenues						
Sandwich shop sales, net	$ 404,874	99.4%	$ 370,954	99.5%	$ 33,920	9.1%
Franchise royalties and fees	2,257	0.6	1,895	0.5	362	19.1
Total revenues	407,131	100.0	372,849	100.0	34,282	9.2
Expenses						
Sandwich shop operating expenses						
Cost of goods sold, excluding depreciation	111,026	27.3	105,614	28.3	5,412	5.1
Labor and related expenses	117,838	28.9	106,628	28.6	11,210	10.5
Occupancy expenses	52,444	12.9	46,762	12.5	5,682	12.2
Other operating expenses	43,738	10.7	39,869	10.7	3,869	9.7
General and administrative expenses	40,411	9.9	37,322	10.0	3,089	8.3
Depreciation expense	22,734	5.6	21,476	5.8	1,258	5.9
Pre-opening costs	1,786	0.4	2,160	0.6	(374)	(17.3)
Impairment and loss on disposal of property and equipment	4,141	1.0	3,589	1.0	552	15.4
Total expenses	394,118	96.8	363,420	97.5	30,698	8.4
Income from operations	13,013	3.2	9,429	2.5	3,584	38.0
Interest expense, net	134	*	221	0.1	(87)	(39.4)
Income before income taxes	12,879	3.2	9,208	2.5	3,671	39.9
Income tax expense	4,443	1.1	3,466	0.9	977	28.2
Net income	8,436	2.1	5,742	1.5	2,694	46.9
Net income attributable to non-controlling interests	224	*	114	*	110	96.5
Net income attributable to Potbelly Corporation	$ 8,212	2.0%	$ 5,628	1.5%	$ 2,584	45.9%

* Amount is less than 0.1%

Revenues

Revenues increased by $34.3 million, or 9.2%, to $407.1 million for fiscal year 2016, from $372.8 million for fiscal year 2015. Company-operated non-comparable store sales contributed $32.7 million, or 95%, of the total revenue increase, company-operated comparable store sales contributed $5.1 million, or 15%, of the total revenue increase and franchise shops contributed $0.4 million, or 1%, of the total revenue increase. This is partially offset by a decrease in revenues of $3.9 million, or 11%, related to closed stores. The increase in company-operated comparable store sales resulted from certain menu price increases and menu mix.

In February 2017, the City of Chicago's Department of Aviation approved the award of the Midway International Airport dining concessions to a development group whose proposal does not include an extension of our lease at the airport. The winning bidders must still sign a contract which is subject to final approval by the Chicago City Council. We are currently advocating to city officials to retain our shop at Midway; we can give no assurance that we will succeed. For the year ended December 25, 2016, our Midway shop represented approximately $7.8 million in revenue and approximately $2.0 million in income before income taxes.

Cost of Goods Sold

Cost of goods sold increased by $5.4 million, or 5.1%, to $111.0 million for fiscal year 2016, compared to $105.6 million for fiscal year 2015, primarily due to the increase in revenues. As a percentage of revenues, cost of goods sold decreased to 27.3% for fiscal year 2016, from 28.3% for fiscal year 2015, primarily driven by certain menu price increases, as well as decreases in certain food commodity costs.

Labor and Related Expenses

Labor and related expenses increased by $11.2 million, or 10.5%, to $117.8 million for fiscal year 2016, from $106.6 million for fiscal year 2015, primarily due to new shop openings. As a percentage of revenues, labor and related expenses increased to 28.9% for fiscal year 2016, from 28.6% for fiscal year 2015, primarily due to wage inflation in certain states as a result of statutory minimum wage increases. These increases were partially offset by improvements in labor productivity and certain menu price increase.

Occupancy Expenses

Occupancy expenses increased by $5.6 million, or 12.2%, to $52.4 million for fiscal year 2016, from $46.8 million for fiscal year 2015, primarily due to new shop openings. As a percentage of revenues, occupancy expenses increased to 12.9% for fiscal year 2016, from 12.5% for fiscal year 2015, primarily due to rent renewals and inflation on common area maintenance and real estate taxes.

Other Operating Expenses

Other operating expenses increased by $3.8 million, or 9.7%, to $43.7 million for fiscal year 2016, from $39.9 million for fiscal year 2015, primarily due to new shop openings as well as increased fees associated with credit card usage in our shops. As a percentage of revenues, other operating expenses remained consistent at 10.7% for fiscal year 2016 and fiscal year 2015.

General and Administrative Expenses

General and administrative expenses increased by $3.1 million, or 8.3%, to $40.4 million for fiscal year 2016, from $37.3 million for fiscal year 2015. The increase is primarily driven by increased headcount for our field management and a one-time legal settlement, partially offset by decreases in our performance-based incentives. As a percentage of revenues, general and administrative expenses decreased to 9.9% for fiscal year 2016, from 10.0% for fiscal year 2015, driven by leverage of the primarily fixed Support Center cost.

Depreciation Expense

Depreciation expense increased by $1.2 million, or 5.9%, to $22.7 million for fiscal year 2016, from $21.5 million for fiscal year 2015, primarily due to a higher depreciable base resulting from new shops. As a percentage of revenues, depreciation decreased to 5.6% for fiscal year 2016, from 5.8% for fiscal year 2015, driven by lower depreciation associated with new shops with lower build-out costs and longer expected useful lives for leasehold improvements, as well as leasehold improvements at legacy shops with higher build-out costs and shorter expected useful lives being fully depreciated.

Pre-Opening Costs

Pre-opening costs decreased by $0.4 million, or 17.3%, to $1.8 million for fiscal year 2016, from $2.2 million for fiscal year 2015, primarily due to four fewer new company-operated shops opening in 2016 as compared to fiscal year 2015, as well as pre-opening rent for the new corporate office location of $0.2 million incurred during fiscal year 2015.

Impairment and Loss on Disposal of Property and Equipment

Impairment and loss on disposal of property and equipment increased by $0.5 million, or 15.4%, to $4.1 million for fiscal year 2016, from $3.6 million for fiscal year 2015. As a result of performing a periodic review of our shops during each fiscal quarter of 2016, it was determined that indicators of impairment were present for certain shops as a result of underperformance of shop profitability. We performed an impairment analysis related to these shops and recorded an impairment charge of $4.0 million related to the excess of the carrying amounts recorded on our balance sheet over the estimated fair values, as compared to $3.4 million in fiscal year 2015.

Interest Expense

Interest expense decreased by $0.1 million, or 39.4%, to $0.1 million for fiscal year 2016, from $0.2 million for fiscal year 2015. Interest expense for the fiscal year ended December 25, 2016 is attributable to unused commitment fees and deferred financing fees.

Income Tax Expense

Income tax expense increased by $0.9 million to $4.4 million for fiscal year 2016, from $3.5 million for fiscal year 2015, driven by higher taxable income. Our effective tax rate was 34.5% for fiscal year 2016, compared to 37.6% for fiscal year 2015. The decrease in the effective tax rate primarily relates to recognizing more federal tax credits in fiscal year 2016 as compared to the prior year.

Results of Operations

Fiscal Year 2015 (52 Weeks) Compared to Fiscal Year 2014 (52 Weeks)

The following table presents information comparing the components of net income for the periods indicated (dollars in thousands):

	Fiscal Year					
	2015	% of Revenues	2014	% of Revenues	Increase (Decrease)	Percent Change
Revenues						
Sandwich shop sales, net	$ 370,954	99.5%	$ 325,464	99.5%	$ 45,490	14.0%
Franchise royalties and fees	1,895	0.5	1,515	0.5	380	25.1
Total revenues	372,849	100.0	326,979	100.0	45,870	14.0
Expenses						
Sandwich shop operating expenses						
Cost of goods sold, excluding depreciation	105,614	28.3	93,688	28.7	11,926	12.7
Labor and related expenses	106,628	28.6	93,165	28.5	13,463	14.5
Occupancy expenses	46,762	12.5	41,389	12.7	5,373	13.0
Other operating expenses	39,869	10.7	34,669	10.6	5,200	15.0
General and administrative expenses	37,322	10.0	32,420	9.9	4,902	15.1
Depreciation expense	21,476	5.8	19,615	6.0	1,861	9.5
Pre-opening costs	2,160	0.6	1,634	0.5	526	32.2
Impairment and loss on disposal of property and equipment	3,589	1.0	3,128	1.0	461	14.7
Total expenses	363,420	97.5	319,708	97.8	43,712	13.7
Income from operations	9,429	2.5	7,271	2.2	2,158	29.7
Interest expense, net	221	0.1	179	0.1	42	23.5
Income before income taxes	9,208	2.5	7,092	2.2	2,116	29.8
Income tax expense	3,466	0.9	2,748	0.8	718	(26.1)
Net income	5,742	1.5	4,344	1.3	1,398	32.2
Net income (loss) attributable to non-controlling interests	114	*	(14)	*	128	(914.3)
Net income attributable to Potbelly Corporation	$ 5,628	1.5%	$ 4,358	1.3%	$ 1,270	29.1%

* Amount is less than 0.1%

Revenues

Revenues increased by $45.9 million, or 14.0%, to $372.8 million for fiscal year 2015, from $327.0 million for fiscal year 2014. Company-operated non-comparable store sales contributed $31.9 million, or 69.6%, of the total revenue increase, company-operated comparable store sales contributed $13.6 million, or 29.5%, of the total revenue increase and franchise shops contributed $0.4 million, or 0.9%, of the total revenue increase. The increase in company-operated comparable store sales resulted from certain menu price increases and menu mix, and an increase in traffic.

Cost of Goods Sold

Cost of goods sold increased by $11.9 million, or 12.7%, to $105.6 million for fiscal year 2015, compared to $93.7 million for fiscal year 2014, primarily due to the increase in revenues. As a percentage of revenues, cost of goods sold decreased to 28.3% for

fiscal year 2015, from 28.7% for fiscal year 2014, primarily driven by certain menu price increases, as well as increased volume-based rebates from certain vendors.

Labor and Related Expenses

Labor and related expenses increased by $13.5 million, or 14.5%, to $106.6 million for fiscal year 2015, from $93.2 million for fiscal year 2014, primarily due to new shop openings. As a percentage of revenues, labor and related expenses increased to 28.6% for fiscal year 2015, from 28.5% for fiscal year 2014, primarily due to wage inflation in certain states as a result of statutory minimum wage increases as well as an additional incentive program to reward employees for tenure and development, which began in fiscal year 2015. These increases were partially offset by improvements in labor productivity.

Occupancy Expenses

Occupancy expenses increased by $5.4 million, or 13.0%, to $46.8 million for fiscal year 2015, from $41.4 million for fiscal year 2014, primarily due to new shop openings. As a percentage of revenues, occupancy expenses decreased to 12.5% for fiscal year 2015, from 12.7% for fiscal year 2014, primarily due to sales leverage (i.e., the ability to spread certain expenses over a higher revenue base).

Other Operating Expenses

Other operating expenses increased by $5.2 million, or 15.0%, to $39.9 million for fiscal year 2015, from $34.7 million for fiscal year 2014, primarily due to new shop openings as well as increased fees associated with credit card usage in our shops. As a percentage of revenues, other operating expenses increased to 10.7% for fiscal year 2015, from 10.6% for fiscal year 2014, primarily due to the $0.2 million cumulative adjustment recorded during the 39 weeks ended September 28, 2014, for the change in accounting estimate related to gift card breakage.

General and Administrative Expenses

General and administrative expenses increased by $4.9 million, or 15.1%, to $37.3 million for fiscal year 2015, from $32.4 million for fiscal year 2014. The increase is primarily driven by increases in our performance-based incentives, advertising and rent associated with our new office. As a percentage of revenues, general and administrative expenses increased to 10.0% for fiscal year 2015, from 9.9% for fiscal year 2014, primarily driven by the increase in performance-based incentives.

Depreciation Expense

Depreciation expense increased by $1.9 million, or 9.5%, to $21.5 million for fiscal year 2015, from $19.6 million for fiscal year 2014, primarily due to a higher depreciable base resulting from new shops. As a percentage of revenues, depreciation decreased to 5.8% for fiscal year 2015, from 6.0% for fiscal year 2014, driven by lower depreciation associated with new shops with lower build-out costs and longer expected useful lives for leasehold improvements, as well as leasehold improvements at legacy shops with higher build-out costs and shorter expected useful lives being fully depreciated.

Pre-Opening Costs

Pre-opening costs increased by $0.5 million to $2.2 million for fiscal year 2015, from $1.6 million for fiscal year 2014, primarily due to four more new company-operated shops opening in 2015 as compared to fiscal year 2014 and a transition of a franchise shop to a company-operated shop in 2015, as well as pre-opening rent for the new corporate office location of $0.2 million.

Impairment and Loss on Disposal of Property and Equipment

Impairment and loss on disposal of property and equipment increased by $0.5 million, or 14.7%, to $3.6 million for fiscal year 2015, from $3.1 million for fiscal year 2014. As a result of performing a periodic review of our shops during each fiscal quarter of 2015, it was determined that indicators of impairment were present for certain shops as a result of underperformance of shop profitability. We performed an impairment analysis related to these shops and recorded an impairment charge of $3.4 million related to the excess of the carrying amounts recorded on our balance sheet over the estimated fair values, as compared to $2.9 million in fiscal year 2014.

Interest Expense

Interest expense remained consistent at $0.2 million for fiscal year 2015 as compared to fiscal year 2014. Interest expense for the fiscal year ended December 27, 2015 is attributable to interest on the note payable, unused commitment fees and deferred financing fees.

Income Tax Expense (Benefit)

Income tax expense increased by $0.7 million to $3.5 million for fiscal year 2015, from $2.7 million for fiscal year 2014, driven by higher taxable income. Our effective tax rate was 37.6% for fiscal year 2015, compared to 38.7% for fiscal year 2014. The decrease in the effective tax rate primarily relates to recognizing more federal tax credits in fiscal year 2015 as compared to the prior year.

Quarterly Results and Seasonality

The following table sets forth certain unaudited financial and operating data in each fiscal quarter during fiscal year 2015 and 2016. The quarterly information includes all normal recurring adjustments that we consider necessary for a fair presentation of the information shown. This information should be read in conjunction with our consolidated financial statements and the related notes to those statements included Part II, Item 8, "Financial Statements and Supplementary Data" of this Annual Report on Form 10-K.

	2016 Fiscal Quarters Ended (1)			
	March 27, 2016	June 26, 2016	September 25, 2016	December 25, 2016
	(unaudited; dollars in thousands)			
Total revenues	$ 95,955	$ 105,036	$ 103,782	$ 102,358
Income from operations	1,889	5,512	2,842	2,770
Net income attributable to Potbelly Corporation	1,088	3,373	1,795	1,956
Total company-operated shops (end of period)	377	382	387	411
Change in company-operated comparable store sales	3.7%	1.7%	0.6%	0.1%

	2015 Fiscal Quarters Ended (1)			
	March 29, 2015	June 28, 2015	September 27, 2015	December 27, 2015
	(unaudited; dollars in thousands)			
Total revenues	$ 85,768	$ 95,949	$ 96,039	$ 95,093
Income from operations	948	4,084	2,379	2,018
Net income attributable to Potbelly Corporation	531	2,461	1,401	1,235
Total company-operated shops (end of period)	339	349	358	372
Change in company-operated comparable store sales	5.4%	4.9%	3.7%	3.7%

(1) Fiscal years 2016 and 2015 each consisted of 52 weeks. Each quarter of such fiscal years consisted of 13 weeks.

Historically, customer spending patterns for our established shops are lowest in the first quarter of the year. Our quarterly results have been and will continue to be affected by the timing of new shop openings and their associated pre-opening costs. As a result of these and other factors, our financial results for any quarter may not be indicative of the results that may be achieved for a full fiscal year.

Liquidity and Capital Resources

General

Our on-going primary sources of liquidity and capital resources are cash provided from operating activities, existing cash and cash equivalents and our credit facility. Our primary requirements for liquidity and capital are new shop openings, existing shop capital investments (maintenance and improvements), repurchases of our common stock, lease obligations, principal and interest payments on our debt, purchases of existing franchise-operated shops, and working capital and general corporate needs. Our requirement for working capital is not significant since our customers pay for their food and beverage purchases in cash or payment cards (credit or debit) at the time of sale. Thus, we are able to sell certain inventory items before we have to pay our suppliers for such items. Our shops do not require significant inventories or receivables. We believe that these sources of liquidity and capital will be sufficient to finance our continued operations and expansion plans for at least the next twelve months.

The following table presents summary cash flow information for the periods indicated (in thousands):

	Fiscal Year		
	2016	2015	2014
Operating activities	$ 45,969	$ 40,320	$ 26,554
Investing activities	(37,820)	(36,058)	(29,209)
Financing activities	(16,776)	(35,261)	(3,919)
Net decrease in cash	$ (8,627)	$ (30,999)	$ (6,574)

Operating Activities

Net cash provided by operating activities increased to $46.0 million for fiscal year 2016, from $40.3 million for fiscal year 2015. The $5.7 million increase is primarily attributable to an increase of $7.7 million in net shop-level profits. The remainder of the change is primarily driven by changes in certain working capital accounts mainly due to timing.

Net cash provided by operating activities increased to $40.3 million for fiscal year 2015, from $26.6 million for fiscal year 2014. The $13.7 million increase is primarily attributable to an increase of $9.5 million in net shop-level profits, a decrease of approximately $1.0 million in payments for performance-based incentives as well as a $1.6 million cash outflow for prepaid expenses related to change in terms with certain vendors incurred in the prior year with no comparable item in the current year. The remainder of the change is primarily driven by changes in certain working capital accounts mainly due to timing.

Investing Activities

Net cash used in investing activities increased to $37.8 million for fiscal year 2016, from $36.1 million for fiscal year 2015. The increase was primarily due to construction costs for 40 new company-operated shops opened for the 52 weeks ended December 25, 2016, compared to 43 new company-operated shops opened for the 52 weeks ended December 27, 2015, at a higher average cost per shop in 2016, as well as capital expenditures for future shop openings, maintaining our existing shops and certain other projects. In addition, in April 2016, we purchased a franchise shop, converting it into a company-operated shop at a cost of $1.1 million.

Net cash used in investing activities increased to $36.1 million for fiscal year 2015, from $29.2 million for fiscal year 2014. The increase was primarily due to construction costs for 43 new company-operated shops opened for the 52 weeks ended December 27, 2015, compared to 39 new company-operated shops opened for the 52 weeks ended December 28, 2014, at a lower average cost per shop in 2015, as well as capital expenditures for future shop openings, maintaining our existing shops and certain other projects. In addition, in July 2015, we purchased a franchise shop, converting it into a company-operated shop at a cost of $0.3 million.

Financing Activities

Net cash used in financing activities decreased to $16.8 million for fiscal year 2016, from $35.3 million for fiscal year 2015. The decrease in net cash used was mainly driven by $22.3 million of treasury stock repurchased during fiscal year 2016 compared to $39.8 million during fiscal year 2015.

Net cash used in financing activities increased to $35.3 million for fiscal year 2015, from $3.9 million for fiscal year 2014. The increase in net cash used was mainly driven by $39.8 million of treasury stock repurchased during fiscal year 2015 compared to $10.2 million during fiscal year 2014.

Initial Public Offering

On October 9, 2013, we completed an IPO of 8,625,000 shares of common stock at a price of $14.00 per share, which included 1,125,000 shares of common stock issued upon the exercise in full of the underwriters' option to purchase additional shares. We sold 8,474,869 shares of common stock and certain stockholders sold 150,131 shares of common stock. We received net proceeds from the offering of approximately $108.8 million, after deducting the underwriting discount and other estimated offering expenses. We used a portion of the net proceeds received from the sale of the shares in the IPO to pay a previously declared one-time cash dividend of approximately $49.9 million on shares outstanding on October 8, 2013 as well as to repay $14.0 million outstanding under the senior credit facility on October 24, 2013. During fiscal year 2014, we used approximately $10.2 million of the net proceeds to repurchase common stock pursuant to the share repurchase program authorized by our Board of Directors on August 1, 2014. The remaining proceeds were used in fiscal year 2015 for share repurchases, working capital, and general corporate purposes.

Stock Repurchase Program

On September 8, 2016, we announced that our Board of Directors authorized a share repurchase program of up to $30.0 million of the Company's common stock. Our previous $35.0 million share repurchase program, authorized in September 2015, was completed in July 2016. The new program permits us, from time to time, to purchase shares in the open market (including in pre-arranged stock trading plans in accordance with the guidelines specified in Rule 10b5-1 under the Exchange Act) or in privately negotiated transactions. During fiscal year 2016, we repurchased 1,719,502 shares of common stock for approximately $22.3 million, including cost and commission, in open market transactions. At December 25, 2016, the remaining dollar value of authorization under the share repurchase program was $27.7 million, which does not include commission.

Credit Facility

On December 9, 2015, we entered into an amended and restated five-year revolving credit facility agreement that expires in November 2020. The credit agreement provides, among other things, for a revolving credit facility in a maximum principal amount of $50 million, with possible future increases to $75 million under an expansion feature. Borrowings under the credit facility generally bear interest at our option at either (i) a eurocurrency rate determined by reference to the applicable LIBOR rate plus a margin ranging from 1.00% to 1.75% or (ii) a prime rate as announced by JP Morgan Chase plus a margin ranging from 0.00% to 0.50%. The applicable margin is determined based upon our consolidated total leverage ratio. On the last day of each calendar quarter, we are required to pay a commitment fee ranging from 0.125% to 0.20% per annum in respect of any unused commitments under the credit facility, with the specific rate determined based upon our consolidated total leverage ratio. So long as certain total leverage ratios are met, there is no limit on the "restricted payments" (primarily distributions and equity repurchases) that we may make. As of December 25, 2016, we had no amounts outstanding under the credit facility.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, synthetic leases, investments in special purpose entities or undisclosed borrowings or debt that would be required to be disclosed pursuant to Item 303 of Regulation S-K under the Exchange Act.

Contractual Obligations

The following table presents contractual obligations and commercial commitments as of December 25, 2016 (in thousands):

	Payments Due By Period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Operating leases (a)	$ 293,372	$ 46,035	$ 81,530	$ 69,729	$ 96,078
Capital leases	215	91	124	—	—
Total	$ 293,587	$ 46,126	$ 81,654	$ 69,729	$ 96,078

(a) Includes base lease terms and certain optional renewal periods that are included in the lease term in accordance with accounting guidance related to leases. Certain of these options are subject to escalation based on various market-based factors.

Impact of Inflation

Our profitability is dependent, among other things, on our ability to anticipate and react to changes in the costs of key operating resources, including food and beverages, labor, energy and other services. Substantial increases in costs and expenses could impact our operating results to the extent such increases cannot be passed along to our customers. Apart from the commodity effects discussed above, in general, we have been able to substantially offset shop and operating cost increases resulting from inflation by altering our menu items, increasing menu prices, making productivity improvements or other adjustments. However, certain areas of costs, notably labor and utilities, can be significantly volatile or subject to significant changes due to changes in laws or regulations, such as the minimum wage laws. There can be no assurance that we will continue to generate increases in comparable store sales in amounts sufficient to offset inflationary or other cost pressures.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of our consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period.

Actual results could differ from those estimates. Critical accounting policies are those that management believes are both most important to the portrayal of our financial condition and operating results, and require management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. We base our estimates on historical experience and other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Judgments and uncertainties affecting the application of those policies may result in materially different amounts being reported under different conditions or using different assumptions. Our significant accounting policies can be found in Note 2 to our consolidated financial statements in Item 8. We consider the following policies to be the most critical in understanding the judgments that are involved in preparing our consolidated financial statements.

Impairment of Long-Lived Assets and Disposal of Property and Equipment

We assess potential impairments to long-lived assets, which includes property and equipment, on a quarterly basis or whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable. Shop-level assets are grouped together for the purpose of the impairment assessment. Recoverability of an asset is measured by a comparison of the carrying amount of an asset to its estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of the asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized as the amount by which the carrying amount of the asset exceeds the fair value of the asset. The fair value of the shop assets is determined using the discounted future cash flow method of anticipated cash flows through the shop's lease-end date using fair value measurement inputs classified as Level 3. Level 3 inputs are derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable. We used a weighted average cost of capital to discount the future cash flows. A 100 basis point change in weighted average cost of capital would not have a material impact on the calculation of an impairment charge. After performing a periodic review of our shops as of December 25, 2016, December 27, 2015 and December 28, 2014, it was determined that indicators of impairment were present for certain shops as a result of continued underperformance of shop profitability. We recorded an impairment charge of $2.9 million, $3.4 million and $4.0 million for the fiscal years 2014, 2015 and 2016, respectively, which is included in impairment and loss on disposal of property and equipment in the consolidated statements of operations.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

We are subject to interest rate risk in connection with borrowings under our credit facility, which bear interest at variable rates. As of December 25, 2016, we had no amounts outstanding under our credit facility or our note payable. A 100 basis point change in the interest rate would not have a material impact on our financial condition or results of operations. We did not have any material exposure to interest rate market risks for fiscal year 2016.

Commodity Price Risk

We are also exposed to commodity price risks. Many of the food products we purchase are subject to changes in the price and availability of food commodities, including among other things beef, poultry, grains, dairy and produce. Prices may be affected due to market changes, increased competition, the general risk of inflation, shortages or interruptions in supply due to weather, disease or other conditions beyond our control, or other reasons. We work with our suppliers and use a mix of forward pricing protocols for certain items under which we agree with our supplier on fixed prices for deliveries at some time in the future, fixed pricing protocols under which we agree on a fixed price with our supplier for the duration of that protocol, and formula pricing protocols under which the prices we pay are based on a specified formula related to the prices of the goods, such as spot prices. Our use of any forward pricing arrangements varies substantially from time to time and these arrangements tend to cover relatively short periods (i.e., typically twelve months or less). We do not enter into futures contracts or other derivative instruments. Increased prices or shortages could generally affect the cost and quality of the items we buy or may require us to further raise prices or limit our menu options. These events, combined with other general economic and demographic conditions, could impact our pricing and negatively affect our sales and profit margins.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Report of Independent Registered Public Accounting Firm

To the Stockholders and Board of Directors of
Potbelly Corporation and subsidiaries
Chicago, Illinois

We have audited the accompanying consolidated balance sheets of Potbelly Corporation and subsidiaries (the "Company") as of December 25, 2016 and December 27, 2015, and the related consolidated statements of operations, equity, and cash flows for each of the three years in the period ended December 25, 2016. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 25, 2016 and December 27, 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 25, 2016, in conformity with accounting principles generally accepted in the United States of America.

/s/ Deloitte & Touche LLP
Chicago, Illinois
February 22, 2017

POTBELLY CORPORATION AND SUBSIDIARIES
Consolidated Balance Sheets

(amounts in thousands, except share and par value data)

	December 25, 2016	December 27, 2015
ASSETS		
Current assets		
Cash and cash equivalents	$ 23,379	$ 32,006
Accounts receivable, net of allowances of $78 and $14 as of December 25, 2016 and December 27, 2015, respectively	3,787	4,461
Inventories	3,365	3,159
Prepaid expenses and other current assets	8,020	10,155
Total current assets	38,551	49,781
Property and equipment, net	107,074	97,434
Indefinite-lived intangible assets	3,404	3,404
Goodwill	2,222	1,428
Deferred income taxes, non-current	19,410	18,439
Deferred expenses, net and other assets	4,784	4,021
Total assets	**$ 175,445**	**$ 174,507**
LIABILITIES AND EQUITY		
Current liabilities		
Accounts payable	$ 3,111	$ 5,762
Accrued expenses	23,082	19,277
Accrued income taxes	1,622	143
Total current liabilities	27,815	25,182
Deferred rent and landlord allowances	21,076	17,820
Other long-term liabilities	2,318	1,292
Total liabilities	51,209	44,294
Equity		
Common stock, $0.01 par value—authorized, 200,000,000 shares; outstanding 25,139,127 and 26,304,261 shares as of December 25, 2016 and December 27, 2015, respectively	309	303
Warrants	909	909
Additional paid-in-capital	407,622	399,458
Treasury stock, held at cost, 5,753,412 and 4,033,910 shares as of December 25, 2016, and December 27, 2015, respectively	(72,321)	(50,000)
Accumulated deficit	(213,034)	(221,246)
Total stockholders' equity	123,485	129,424
Non-controlling interest	751	789
Total equity	124,236	130,213
Total liabilities and equity	**$ 175,445**	**$ 174,507**

See accompanying notes to the consolidated financial statements.

POTBELLY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Operations

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

	Fiscal Year		
	2016	2015	2014
Revenues			
Sandwich shop sales, net	$ 404,874	$ 370,954	$ 325,464
Franchise royalties and fees	2,257	1,895	1,515
Total revenues	407,131	372,849	326,979
Expenses			
Sandwich shop operating expenses			
Cost of goods sold, excluding depreciation	111,026	105,614	93,688
Labor and related expenses	117,838	106,628	93,165
Occupancy expenses	52,444	46,762	41,389
Other operating expenses	43,738	39,869	34,669
General and administrative expenses	40,411	37,322	32,420
Depreciation expense	22,734	21,476	19,615
Pre-opening costs	1,786	2,160	1,634
Impairment and loss on disposal of property and equipment	4,141	3,589	3,128
Total expenses	394,118	363,420	319,708
Income from operations	13,013	9,429	7,271
Interest expense	134	221	179
Income before income taxes	12,879	9,208	7,092
Income tax expense	4,443	3,466	2,748
Net income	8,436	5,742	4,344
Net income (loss) attributable to non-controlling interest	224	114	(14)
Net income attributable to Potbelly Corporation	$ 8,212	$ 5,628	$ 4,358
Net income per common share attributable to common stockholders:			
Basic	$ 0.32	$ 0.20	$ 0.15
Diluted	$ 0.31	$ 0.20	$ 0.14
Weighted average shares outstanding:			
Basic	25,623,809	28,002,005	29,209,298
Diluted	26,231,367	28,634,396	30,275,061

See accompanying notes to the consolidated financial statements.

POTBELLY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Equity

(amounts in thousands, except share data)

	Common Stock		Treasury Stock	Warrants	Additional Paid-In-Capital	Accumulated Deficit	Non-Controlling Interest	Total Equity
	Shares	Amount						
Balance at December 29, 2013	29,148,029	$ 291	$ —	$ 909	$ 383,077	$ (231,232)	$ 228	$ 153,273
Net income	—	—	—	—	—	4,358	(14)	4,344
Issuance of unrestricted common stock	28,240	—	—	—	432	—	—	432
Exercise of stock options	585,521	7	—	—	5,052	—	—	5,059
Excess tax benefits associated with exercise of stock options	—	—	—	—	1,300	—	—	1,300
Repurchases of common stock	(827,090)	—	(10,246)	—	—	—	—	(10,246)
Distributions to non-controlling interest	—	—	—	—	—	—	(46)	(46)
Contributions from non-controlling interest	—	—	—	—	—	—	98	98
Amortization of stock-based compensation	—	—	—	—	2,111	—	—	2,111
Balance at December 28, 2014	**28,934,700**	**$ 298**	**$ (10,246)**	**$ 909**	**$ 391,972**	**$ (226,874)**	**$ 266**	**$ 156,325**
Net income	—	—	—	—	—	5,628	114	5,742
Exercise of stock options	576,381	5	—	—	4,779	—	—	4,784
Excess tax benefits associated with exercise of stock options	—	—	—	—	308	—	—	308
Repurchases of common stock	(3,206,820)	—	(39,754)	—	—	—	—	(39,754)
Distributions to non-controlling interest	—	—	—	—	—	—	(198)	(198)
Contributions from non-controlling interest	—	—	—	—	—	—	607	607
Amortization of stock-based compensation	—	—	—	—	2,399	—	—	2,399
Balance at December 27, 2015	**26,304,261**	**$ 303**	**$ (50,000)**	**$ 909**	**$ 399,458**	**$ (221,246)**	**$ 789**	**$ 130,213**
Net income	—	—	—	—	—	8,212	224	8,436
Exercise of stock options	536,332	6	—	—	5,770	—	—	5,776
Common stock issued for stock-based compensation plans	18,036	—	—	—	—	—	—	—
Excess tax deficiencies associated with exercise of stock options	—	—	—	—	(663)	—	—	(663)
Repurchases of common stock	(1,719,502)	—	(22,321)	—	—	—	—	(22,321)
Distributions to non-controlling interest	—	—	—	—	—	—	(413)	(413)
Contributions from non-controlling interest	—	—	—	—	—	—	151	151
Amortization of stock-based compensation	—	—	—	—	3,057	—	—	3,057
Balance at December 25, 2016	**25,139,127**	**$ 309**	**$ (72,321)**	**$ 909**	**$ 407,622**	**$ (213,034)**	**$ 751**	**$ 124,236**

See accompanying notes to the consolidated financial statements.

POTBELLY CORPORATION AND SUBSIDIARIES
Consolidated Statements of Cash Flows

(amounts in thousands)

	Fiscal Year		
	2016	2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 8,436	$ 5,742	$ 4,344
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	22,734	21,476	19,615
Deferred income tax	(1,659)	(72)	(289)
Deferred rent and landlord allowances	3,256	3,808	1,787
Amortization of stock-based compensation	3,057	2,399	2,543
Excess tax benefit from stock-based compensation	(31)	(308)	(1,300)
Asset impairment, store closure and disposal of property and equipment	4,243	3,818	3,679
Amortization of debt issuance costs	34	11	70
Changes in operating assets and liabilities:			
Accounts receivable, net	674	(445)	(1,013)
Inventories	(188)	(388)	(505)
Prepaid expenses and other assets	3,204	(1,155)	(4,216)
Accounts payable	(1,899)	1,876	1,301
Accrued and other liabilities	4,108	3,558	538
Net cash provided by operating activities	45,969	40,320	26,554
CASH FLOWS FROM INVESTING ACTIVITIES:			
Acquisition of franchise shop	(1,108)	(333)	—
Purchases of property and equipment	(36,712)	(35,725)	(29,209)
Net cash used in investing activities	(37,820)	(36,058)	(29,209)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Payments on note payable	—	(1,008)	(84)
Proceeds from exercise of stock options	6,165	5,825	6,137
Payment of payroll taxes related to stock-based compensation awards	(389)	(1,041)	(1,078)
Excess tax benefit from stock-based compensation	31	308	1,300
Treasury stock repurchase	(22,321)	(39,754)	(10,246)
Contributions from non-controlling interest	151	607	98
Distributions to non-controlling interest	(413)	(198)	(46)
Net cash used in financing activities	(16,776)	(35,261)	(3,919)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(8,627)	(30,999)	(6,574)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	32,006	63,005	69,579
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 23,379	$ 32,006	$ 63,005
Supplemental cash flow information :			
Income taxes paid	$ 3,663	$ 2,376	$ 3,232
Interest paid	108	183	179
Supplemental non-cash investing and financing activities :			
Unpaid liability for purchases of property and equipment	$ 2,727	$ 3,395	$ 2,690

See accompanying notes to the consolidated financial statements.

(1) Organization and Other Matters

Business

Potbelly Corporation (the "Company" or "Potbelly"), through its wholly-owned subsidiaries, operates Potbelly Sandwich Works sandwich shops in 29 states and the District of Columbia. The Company also sells and administers franchises of Potbelly Sandwich Works sandwich shops. The first franchise locations administered by the Company opened during February 2011. In July 2015, the Company opened its first franchise shop in the United Kingdom, and in October 2016, the Company opened its first franchise shop in Canada. Additionally, during each of July 2015 and April 2016, the Company transitioned one franchise shop into a company-operated shop for a purchase price of $0.3 million and $1.1 million, respectively. The Company did not record any goodwill related to the July 2015 transaction and recorded $0.8 million of goodwill related to the April 2016 transaction. The Company believes both acquisitions are immaterial.

Initial Public Offering

On October 9, 2013, the Company completed an initial public offering ("IPO") of 8,625,000 shares of common stock, which included 1,125,000 shares of common stock issued upon the exercise in full of the underwriters' option to purchase additional shares. The Company sold 8,474,869 shares of common stock and certain stockholders sold 150,131 shares of common stock. The Company received net proceeds from the offering of approximately $108.8 million, after deducting the underwriting discount and other offering expenses. The Company did not receive any proceeds from the shares sold by the selling stockholders.

The Company used the net proceeds received from the sale of its shares to pay a previously-declared one-time cash dividend of $49.9 million on shares outstanding on October 8, 2013 and also to repay borrowings of approximately $14.0 million under its senior credit facility. During fiscal year 2014, the Company used approximately $10.2 million of the net proceeds to repurchase common stock pursuant to the share repurchase program authorized by the Company's Board of Directors on August 1, 2014. The remaining proceeds were used in fiscal year 2015 for share repurchases, working capital, and general corporate purposes.

(2) Summary of Significant Accounting Policies

(a) Principles of Consolidation

The consolidated financial statements include the accounts of Potbelly Corporation; its wholly owned subsidiary, Potbelly Illinois, Inc. ("PII"); PII's wholly owned subsidiaries, Potbelly Franchising, LLC and Potbelly Sandwich Works LLC ("LLC"); eight of LLC's wholly owned subsidiaries and LLC's five joint ventures, collectively, the "Company." All significant intercompany balances and transactions have been eliminated in consolidation. For consolidated joint ventures, non-controlling interest represents a non-controlling partner's share of the assets, liabilities and operations related to the five joint venture investments. The Company has ownership interests ranging from 51-80% in these consolidated joint ventures.

The Company does not have any components of other comprehensive income (loss) recorded within its consolidated financial statements, and, therefore, does not separately present a statement of comprehensive income (loss) in its consolidated financial statements.

(b) Reporting Period

The Company uses a 52/53-week fiscal year that ends on the last Sunday of the calendar year. Approximately every five or six years a 53rd week is added. Fiscal years 2014, 2015 and 2016 each consisted of 52 weeks.

(c) Segment Reporting

The Company owns and operates Potbelly Sandwich Works sandwich shops in the United States. The Company also has domestic and international franchise operations of Potbelly Sandwich Works sandwich shops. The Company's chief operating decision maker (the "CODM") is its Chief Executive Officer. As the CODM reviews financial performance and allocates resources at a consolidated level on a recurring basis, the Company has one operating segment and one reportable segment.

(d) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the United States ("GAAP") requires management to make estimates and assumptions, primarily related to the long-lived assets and income taxes, that affect the

reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(e) Fair Value Measurements

The Company applies fair value accounting for all financial assets and liabilities and nonfinancial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis. Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities that are required to be recorded at fair value, the Company assumes the highest and best use of the asset by market participants in which the Company would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions, and credit risk.

The Company applies the following fair value hierarchy, which prioritizes the inputs used to measure fair value into three levels, and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

- Level 1—Quoted prices in active markets for identical assets or liabilities.
- Level 2—Observable inputs other than quoted prices in active markets for identical assets or liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3—Inputs that are both unobservable and significant to the overall fair value measurement reflect an entity's estimates of assumptions that market participants would use in pricing the asset or liability.

(f) Financial Instruments

The Company records all financial instruments at cost, which is the fair value at the date of transaction. The amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable and all other current liabilities approximate their fair value because of the short-term maturities of these instruments.

(g) Cash and Cash Equivalents

The Company considers all highly liquid investment instruments with an original maturity of three months or less when purchased to be cash equivalents. The Company maintains its cash in bank deposit accounts that, at times, may exceed federally insured limits; however, the Company has not experienced any losses in these accounts. The Company believes it is not exposed to any significant credit risk. These are valued within the fair value hierarchy as Level 1 measurements.

(h) Accounts Receivable, net

Accounts receivable, net consists of credit card receivables, amounts owed from vendors and miscellaneous receivables. The Company had credit card receivables of $2.0 million and $1.6 million as of December 27, 2015 and December 25, 2016, respectively.

(i) Inventories

Inventories, which consist of food products, paper goods and supplies, and promotional items, are valued at the lower of cost (first-in, first-out) or market. No adjustment is deemed necessary to reduce inventory to the lower of cost or market value due to the rapid turnover and high utilization of inventory.

(j) Property and Equipment

Property and equipment acquired is recorded at cost less accumulated depreciation. Property and equipment is depreciated based on the straight-line method over the estimated useful lives, generally ranging from three to five years for furniture and fixtures, computer equipment, computer software, and machinery and equipment. Leasehold improvements are depreciated over the shorter of their estimated useful lives or the related lease life, generally 10 to 15 years. For leases with renewal periods at the Company's option,

the Company determines the expected lease period based on whether the renewal of any options are reasonably assured at the inception of the lease.

Direct costs and expenditures for refurbishments and improvements that significantly add to the productive capacity or extend the useful life of an asset are capitalized, whereas the costs of repairs and maintenance are expensed when incurred. The Company capitalizes certain internal costs associated with the development, design, and construction of new shop locations as these costs have a future benefit to the Company. The Company capitalized costs of $0.9 million, $0.6 million and $0.6 million for the fiscal years ended December 28, 2014, December 27, 2015 and December 25, 2016, respectively. Capitalized costs are recorded as part of the asset to which they relate, primarily to leasehold improvements, and such costs are amortized over the asset's useful life. When assets are retired or sold, the asset cost and related accumulated depreciation are removed from the consolidated balance sheet and any gain or loss is recorded in the consolidated statement of operations.

The Company assesses potential impairments to its long-lived assets, which includes property and equipment, on a quarterly basis or whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable. Shop-level assets are grouped at the individual shop-level for the purpose of the impairment assessment. Recoverability of an asset is measured by a comparison of the carrying amount of an asset to its estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of the asset group exceeds its estimated undiscounted future cash flows, an impairment charge is recognized as the amount by which the carrying amount of the asset exceeds the fair value of the asset. The fair value of the shop assets is determined using the discounted future cash flow method of anticipated cash flows through the shop's lease-end date using fair value measurement inputs classified as Level 3. Level 3 inputs are derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable. The Company used a weighted average cost of capital to discount the future cash flows. After performing periodic reviews of the company-operated shops during each quarter of 2014, 2015 and 2016, it was determined that indicators of impairment were present for certain shops as a result of continued underperformance. The Company performed an impairment analysis related to these shops and recorded impairment charges of $2.9 million, $3.4 million and $4.0 million for the fiscal years 2014, 2015 and 2016, respectively, which is included in impairment and loss on disposal of property and equipment in the consolidated statements of operations.

(k) Intangible Assets

The Company reviews indefinite-lived intangible assets, which includes goodwill and tradenames, annually at fiscal year-end for impairment or more frequently if events or circumstances indicate that the carrying value may not be recoverable. An impaired asset is written down to its estimated fair value based on the most recent information available. The Company assesses the fair values of its intangible assets, and its reporting unit for goodwill testing purposes, using both an income-based approach and a market approach. Under the income approach, fair value is based on the present value of estimated future cash flows. The income approach is dependent on a number of factors, including forecasted revenues and expenses, appropriate discount rates and other variables. The market approach measures fair value by comparison to the observed fair values of comparable companies, adjusted for the relative size and profitability of these comparable companies. The annual impairment review utilizes the estimated fair value of the intangible assets and the overall reporting unit and compares the estimated fair values to the carrying values as of the testing date. If the carrying value of these intangible assets or the reporting unit exceeds the fair values, the Company would then use the fair values to measure the amount of any required impairment charge. No impairment charge was recognized for intangible assets for any of the fiscal periods presented.

(l) Pre-opening Costs

Pre-opening costs consist of costs incurred prior to opening a new shop and are made up primarily of travel, employee payroll and training costs incurred prior to the shop opening, as well as occupancy costs incurred from when the Company takes site possession to shop opening. Shop pre-opening costs are expensed as incurred.

(m) Advertising Expenses

Advertising costs are expensed as incurred and are included in general and administrative expenses in the consolidated statements of operations. Advertising expenses were $2.2 million, $2.9 million and $3.0 million in fiscal years 2014, 2015 and 2016, respectively.

(n) Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are attributable to differences between financial statement and income tax reporting. Deferred tax assets, net of any valuation allowances, represent the future tax return consequences of those differences and for operating loss and tax credit carryforwards, which will be deductible when the assets are recovered. Deferred tax assets are reduced by a valuation allowance if it is deemed more likely than not that some or all of the deferred tax assets will not be realized. In making this assessment of realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Deferred tax liabilities are recognized for temporary differences that will be taxable in future years' tax returns.

The Company accounts for uncertain tax positions under current accounting guidance, which prescribes a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. The minimum threshold is defined as a tax position that is more likely than not to be sustained upon examination by tax authorities, based on the technical merits of the position. The tax benefit to be recognized is measured as the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement.

(o) Stock-Based Compensation

The Company has granted stock options under its 2001 Equity Incentive Plan (the "2001 Plan"), 2004 Equity Incentive Plan (the "2004 Plan") and 2013 Long-Term Incentive Plan, as amended (the "2013 Plan" and together with the 2004 Plan and 2001 Plan, the "Plans"). The Plans permit the granting of awards to employees and non-employee officers, consultants, agents, and independent contractors of the Company in the form of stock appreciation rights, stock awards, and stock options. The Plans give broad powers to the Company's board of directors to administer and interpret the Plans, including the authority to select the individuals to be granted options and rights and to prescribe the particular form and conditions of each option to be granted. In September 2011, the 2001 Plan expired with options outstanding under the plan still available for exercise. On July 31, 2013, the Company's board of directors approved the adoption of the 2013 Plan, which replaced the 2004 Plan in conjunction with the Company's IPO. Upon approval of the 2013 Plan, the Company no longer issued awards under the 2004 Plan. The 2004 Plan expired in February 2014, but will continue to govern outstanding awards granted prior to its termination.

The Company accounts for its stock-based employee compensation in accordance with Accounting Standards Codification ("ASC") 718, *Stock Based Compensation*. The Company records stock compensation expense on a straight-line basis over the vesting period based on the grant-date fair value of the option, determined using the Black-Scholes option pricing valuation model.

(p) Leases

The Company leases retail shops, warehouse and office space under operating leases. Most lease agreements contain tenant improvement allowances, rent holidays, lease premiums, rent escalation clauses, and/or contingent rent provisions. For purposes of recognizing incentives, premiums, and minimum rental expenses on a straight-line basis over the terms of the leases, the Company uses the date it takes possession of the leased space for construction purposes as the beginning of the term, which is generally two to three months prior to a shop's opening date. For leases with renewal periods at the Company's option, the Company determines the expected lease period based on whether the renewal of any options are reasonably assured at the inception of the lease. In addition to rental expense, certain leases require the Company to pay a portion of real estate taxes, utilities, building operating expenses, insurance and other charges in addition to rent.

For tenant improvement allowances, rent escalations, and rent holidays, the Company records a deferred rent liability in its consolidated balance sheets and amortizes the deferred rent over the terms of the leases as reductions to occupancy expense in the consolidated statements of operations.

(q) Revenue Recognition

Revenue from retail shops are presented net of discounts and recognized when food and beverage products are sold. Sales taxes collected from customers are excluded from revenues and the obligation is included in accrued liabilities until the taxes are remitted to the appropriate taxing authorities.

Revenues from the Company's gift cards are deferred and were previously recognized upon redemption or after a period of 36 months of inactivity on gift card balances ("gift card breakage") and the Company does not have a legal obligation to remit the value of the unredeemed gift cards to the relevant jurisdictions. The Company monitors its actual patterns of redemption and updates its estimates and assumptions regarding redemption as the actual pattern changes. The Company estimates and records gift card breakage income based on its historical redemption pattern. The Company recognized an immaterial amount of gift card breakage income for the fiscal years ended 2014, 2015 and 2016, which is recorded within other operating expenses in the consolidated statements of operations.

The Company earns an initial franchise fee, a franchise development agreement fee and ongoing royalty fees under the Company's franchise agreements. Initial franchise fee revenue is recognized at the point a franchise shop opens for business to the public, as this is the point in time when the Company has substantially performed all initial services required under the franchise agreement. The Company recognized franchise fee revenue of $0.3 million, $0.4 million and $0.4 million in fiscal year 2014, 2015 and 2016, respectively. Initial franchise fee payments received by the Company before the shop opens are recorded as deferred revenue in the consolidated balance sheet. The Company had deferred revenue related to initial franchise fees of $0.5 million and $0.7 million included in accrued expenses as of December 27, 2015 and December 25, 2016, respectively. Franchise development agreement fee represents the exclusivity rights for a geographical area paid by a third party to develop Potbelly shops for a certain period of time. Franchise development agreement fee payments received by the Company are recorded as deferred revenue in the consolidated balance sheet and amortized over the life of the franchise development agreement. The Company had deferred revenue related to franchise development agreement fees of $0.4 million recorded as accrued expenses as of December 27, 2015 and December 25, 2016. Royalty fees are based on a percentage of sales and are recorded as revenue as the fees are earned and become receivable from the franchisee. The Company recognized royalty fees revenue of $1.2 million, $1.5 million and $1.9 million for fiscal years 2014, 2015, and 2016, respectively.

(r) Recent Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." The pronouncement was issued to clarify the principles for recognizing revenue and to develop a common revenue standard and disclosure requirements for U.S. GAAP and IFRS. The FASB has approved a one-year deferral of the effective date of ASU 2014-09, such that it will become effective for the annual period beginning after December 15, 2017. In addition, the FASB issued ASU 2016-08, ASU 2016-10, ASU 2016-12, and ASU 2016-20 in March 2016, April 2016, May 2016, and December 2016, respectively, to help provide interpretive clarifications on the new guidance in ASC Topic 606. The Company is currently evaluating the overall impact that ASU 2014-09 will have on the Company's consolidated financial statements, as well as the expected timing and method of adoption. Based on a preliminary assessment, the Company has determined that the adoption will not have a material impact on sandwich shop sales, but may impact gift card breakage income. The Company is continuing its assessment, which may identify additional impacts this standard will have on its consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02, "Leases", which will replace the existing guidance in ASC 840, "Leases". The pronouncement requires a dual approach for lessee accounting under which a lessee would account for leases as finance leases or operating leases. Both finance leases and operating leases will result in the lessee recognizing a right-of-use asset and a corresponding lease liability. For finance leases, the lessee would recognize interest expense and amortization of the right-of-use asset, and for operating leases, the lessee would recognize a straight-line total lease expense. The pronouncement is effective for fiscal years beginning after December 15, 2018, including annual and interim periods thereafter. In addition, the pronouncement requires the use of the modified retrospective method, which will require adjustment to all comparative periods presented in the consolidated financial statements. The Company is currently evaluating the impact ASU 2016-02 will have on its financial position, results of operations and cash flows but expect that it will result in a material increase in its long-term assets and liabilities given the Company has a significant number of leases.

In March 2016, the FASB issued ASU No. 2016-04, "Recognition of Breakage for Certain Prepaid Stored-Value Products". This pronouncement clarifies when it is acceptable to recognize the unredeemed portion of prepaid gift cards into income. This pronouncement is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company is evaluating the impact this standard will have on its financial statements and disclosures.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation – Stock Compensation (Topic 718)". The pronouncement simplifies the accounting for the taxes related to stock-based compensation, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification within the statement of cash flows. The pronouncement is effective for

annual periods beginning after December 15, 2016, including annual and interim periods thereafter. If the Company would have adopted this standard for fiscal 2016, it would have had the effect of increasing income tax expense by $0.7 million for the year.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments". The objective of this pronouncement is to eliminate the diversity in practice related to the classification of certain cash receipts and payments in the statement of cash flows, by adding or clarifying guidance on eight specific cash flow issues. The pronouncement is effective for annual periods beginning after December 15, 2017, including annual and interim periods thereafter. Early adoption is permitted. The adoption of ASU 2016-15 is not expected to have a material effect on the Company's financial statements and disclosures.

(s) Commitments and Contingencies

As previously disclosed in prior reports filed with the SEC, the Company received notice of a potential claim alleging that the Company violated the Fair Labor Standards Act by not paying overtime to its assistant managers, whom the Company has classified as exempt employees. Although the Company has always believed that its assistant managers are properly classified as exempt under both federal and state laws, and have always intended to defend any such lawsuits vigorously, the Company agreed to mediate the matter. On February 20, 2017, the parties entered into a Settlement Agreement and Release whereby participating assistant managers will release the Company from all federal and/or state wage and hour claims in exchange for a gross settlement amount of $1.3 million. As part of the settlement process, a complaint was filed on February 17, 2017 in the Circuit Court of the Fifteenth Judicial Circuit in and for Palm Beach County, Florida, and a motion seeking the Court's preliminary approval of the settlement was filed on February 21, 2017. As of December 25, 2016, the Company recorded a liability of $1.3 million for this matter. The settlement of this action did not have a material adverse effect on our financial position or results of operations and cash flows.

The Company is subject to legal proceedings, claims and liabilities, such as employment-related claims and slip and fall cases, which arise in the ordinary course of business and are generally covered by insurance. In the opinion of management, the amount of ultimate liability with respect to those actions should not have a material adverse impact on the Company's financial position, results of operations or cash flows.

Many of the food products the Company purchases are subject to changes in the price and availability of food commodities, including, among other things, beef, poultry, grains, dairy and produce. The Company works with its suppliers and uses a mix of forward pricing protocols for certain items including agreements with its supplier on fixed prices for deliveries at some time in the future and agreements on a fixed price with its supplier for the duration of that protocol. The Company also utilizes formula pricing protocols under which the prices the Company pays are based on a specified formula related to the prices of the goods, such as spot prices. The Company's use of any forward pricing arrangements varies substantially from time to time and these arrangements tend to cover relatively short periods (i.e., typically twelve months or less). Such contracts are used in the normal purchases of the Company's food products and not for speculative purposes, and as such are not required to be evaluated as derivative instruments. The Company does not enter into futures contracts or other derivative instruments.

(3) Fair Value Measurement

The carrying amounts of cash and cash equivalents, accounts receivable, accounts payable and all other current liabilities approximate fair values due to the short maturities of these balances.

The Company assesses potential impairments to its long-lived assets, which includes property and equipment, on a quarterly basis, or whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable. Shop-level assets are grouped at the individual shop-level for the purpose of the impairment assessment. Recoverability of an asset is measured by a comparison of the carrying amount of an asset to its estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of the asset group exceeds its estimated undiscounted future cash flows, an impairment charge is recognized as the amount by which the carrying amount of the asset exceeds the fair value of the asset. The fair value of the shop assets was determined using the discounted future cash flow method of anticipated cash flows through the shop's lease-end date using fair value measurement inputs classified as Level 3. Level 3 inputs are derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable. After performing a periodic review of the Company's shops during each quarter of 2014, 2015 and 2016, it was determined that indicators of impairment were present for certain shops as a result of continued underperformance of shop profitability. The Company performed an impairment analysis related to these shops and recorded impairment charges of $2.9 million, $3.4 million and $4.0 million for the fiscal years 2014, 2015 and 2016, respectively, related to the excess of the carrying amounts recorded on the Company's consolidated balance sheet over the identified shops' estimated fair values.

(4) Earnings per share

Basic and diluted income per common share attributable to common stockholders are calculated using the weighted average number of common shares outstanding for the period. Diluted income per common share attributable to common stockholders is computed by dividing the income allocated to common stockholders by the weighted average number of fully diluted common shares outstanding.

	Fiscal Year		
	2016	2015	2014
Net income attributable to Potbelly Corporation	$ 8,212	$ 5,628	$ 4,358
Weighted average common shares outstanding-basic	25,623,809	28,002,005	29,209,298
Plus: Effect of potential stock options exercise	549,578	577,156	949,142
Plus: Effect of potential warrant exercise	57,980	55,235	116,621
Weighted average common shares outstanding-diluted	26,231,367	28,634,396	30,275,061
Income per share available to common stockholders-basic	$ 0.32	$ 0.20	$ 0.15
Income per share available to common stockholders-diluted	$ 0.31	$ 0.20	$ 0.14
Potentially dilutive shares that are considered anti-dilutive:			
Common share options	1,164,047	898,966	622,879
Warrants	—	—	—

(5) Property and Equipment

Property and equipment, net consisted of the following (in thousands):

	December 25, 2016	December 27, 2015
Leasehold improvements	$ 170,196	$ 157,556
Machinery and equipment	47,668	42,840
Furniture and fixtures	32,561	28,605
Computer equipment and software	23,162	20,077
Construction in progress	5,601	3,074
	279,188	252,152
Less: Accumulated depreciation	(172,114)	(154,718)
	$ 107,074	$ 97,434

(6) Accrued Expenses

Accrued expenses consisted of the following (in thousands):

	December 25, 2016	December 27, 2015
Accrued labor and related expenses	$ 6,120	$ 7,482
Deferred gift card revenue	2,292	1,843
Accrued occupancy expenses	1,538	672
Deferred rent—current	706	813
Accrued corporate and shop expenses	2,255	1,961
Accrued utilities	1,094	1,035
Accrued sales and use tax	1,857	1,820
Accrued construction	2,329	2,271
Accrued contract termination costs (a)	28	21
Accrued legal and professional fees	1,756	136
Accrued other	3,107	1,223
Total	$ 23,082	$ 19,277

(a) The Company incurs expenses associated with exit activity for certain signed lease agreements, which are recognized in general and administrative expenses. Accrued contract termination costs consisted of the following (in thousands):

	December 25, 2016	December 27, 2015
Accrued contract termination costs—beginning balance	$ 21	$ 801
Contract termination costs incurred	24	—
Contract termination costs settled and paid	(17)	(780)
Accrued contract termination costs—ending balance	$ 28	$ 21

(7) Income Taxes

Income before income taxes for the Company's domestic and foreign operations was as follows (in thousands):

	Fiscal Year 2016	2015	2014
Domestic operations	$ 12,411	$ 8,660	$ 6,627
Foreign operations	468	548	465
Total	$ 12,879	$ 9,208	$ 7,092

Income tax expense consisted of the following (in thousands):

	Fiscal Year		
	2016	2015	2014
Federal:			
Current	$ 4,652	$ 2,450	$ 2,386
Deferred	(1,386)	209	(467)
	3,266	2,659	1,919
State and Local:			
Current	1,426	1,047	622
Deferred	(273)	(281)	178
	1,153	766	800
Foreign:			
Current	24	41	29
Deferred	—	—	—
	24	41	29
Income tax expense	$ 4,443	$ 3,466	$ 2,748

Income tax expense differed from the amounts computed by applying the U.S. federal income tax rates to income before income taxes as a result of the following (in thousands):

	Fiscal Year		
	2016	2015	2014
Computed "expected" tax expense	$ 4,508	$ 3,223	$ 2,411
Increase (reduction) resulting from:			
Minority interest	(89)	(45)	—
Permanent differences	131	51	97
State and local income taxes, net of federal income tax effect	673	533	460
FICA and other tax credits	(556)	(392)	(222)
Rate change and true-ups (a)	(224)	164	2
Change in valuation allowance	—	(68)	—
	$ 4,443	$ 3,466	$ 2,748

(a) The $(224) of rate changes and true-ups relates primarily to a favorable provision-to-return adjustment related to WOTC credits.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities reflected in the consolidated balance sheets are presented below (in thousands):

	December 25, 2016	December 27, 2015
Deferred tax assets:		
Accrued liabilities	$ 1,848	$ 2,074
Deferred revenue on gift certificates and gift cards	323	141
Stock-based compensation	8,104	8,261
Property and equipment depreciation	6,293	5,805
Deferred rent and start-up amortization	5,656	4,650
Other timing differences	234	273
FICA and other tax credits	—	43
Total deferred tax assets	22,458	21,247
Less: valuation allowance	—	—
Net deferred tax assets	22,458	21,247
Deferred tax liabilities:		
Prepaids	(635)	(547)
Intangible asset	(1,351)	(1,226)
Smallwares	(801)	(733)
Other timing differences	(261)	(302)
Total gross deferred tax liabilities	(3,048)	(2,808)
Net deferred tax assets	$ 19,410	$ 18,439

As of December 27, 2015 and December 25, 2016, the Company has no valuation allowances recorded based on management's assessment of the amount of its deferred tax assets that are more likely than not to be realized.

In accordance with its accounting policy, the Company recognizes accrued interest and penalties related to unrecognized tax benefits as a component of income tax expense. As of December 27, 2015 and December 25, 2016, the Company had no interest or penalties accrued.

The tax years prior to 2013 are generally closed for examination by the United States Internal Revenue Service. However, certain of these tax years are open for examination as a result of net operating losses generated in these years and utilized in subsequent years. The Company is currently under examination with the IRS for the 2014 tax year; no other IRS audits are currently ongoing. State statutes are generally open for audit for the 2012 to 2016 tax years. Additionally, certain tax years through 2016 are open for examination by certain state tax authorities.

(8) Long-term debt

Note payable

On March 15, 2007, the Company entered into a long-term note payable associated with the acquisition of certain assets of Pot Belly Deli, Inc., an unrelated California company, including the Pot Belly trade name, certain design marks, and other related assets. The Company records interest on the note payable under the effective interest method at an annual interest rate of 6.2% and recorded interest expense of $0.1 million in fiscal year 2014. The Company recorded an immaterial amount of interest expense on the note payable in fiscal year 2015. Payment of interest and principal is made monthly. The final repayment of the note was made on April 1, 2015.

Credit facility

JPMorgan Chase Bank, N.A.

On December 9, 2015, the Company entered into an amended and restated five-year revolving credit facility agreement that expires in November 2020. The credit agreement provides, among other things, for a revolving credit facility in a maximum principal amount of $50 million, with possible future increases to $75 million under an expansion feature. Borrowings under the credit facility generally bear interest at the Company's option at either (i) a eurocurrency rate determined by reference to the applicable LIBOR rate

plus a margin ranging from 1.00% to 1.75% or (ii) a prime rate as announced by JP Morgan Chase plus a margin ranging from 0.00% to 0.50%. The applicable margin is determined based upon the Company's consolidated total leverage ratio. On the last day of each calendar quarter, the Company is required to pay a commitment fee ranging from 0.125% to 0.20% per annum in respect of any unused commitments under the credit facility, with the specific rate determined based upon the Company's consolidated total leverage ratio. So long as certain total leverage ratios are met, there is no limit on the "restricted payments" (primarily distributions and equity repurchases) that the Company may make. As of December 25, 2016, the Company has no amounts outstanding under the credit facility. As of and for the year ended December 25, 2016, the Company has $49.3 million available for borrowing under the credit facility after reductions for outstanding letters of credit.

(9) Capital Stock and Warrants

As of December 25, 2016 and December 27, 2015, the Company had authorized an aggregate of 210,000,000 shares of capital stock, of which 200,000,000 shares were designated as common stock and 10,000,000 shares were designated as preferred stock. As of December 25, 2016, the Company had issued and outstanding 30,892,539 and 25,139,127 shares of common stock, respectively. As of December 27, 2015, the Company had issued and outstanding 30,338,171 and 26,304,261 shares of common stock, respectively.

Common Stock

As of December 25, 2016, each share of common stock has the same relative rights and was identical in all respects to each other share of common stock. Each holder of shares of common stock is entitled to one vote for each share held by such holder at all meetings of stockholders.

On September 8, 2016, the Company announced that its Board of Directors authorized a share repurchase program of up to $30.0 million of the Company's common stock. The Company's previous $35.0 million share repurchase program, authorized in September 2015, was completed in July 2016. The new program permits the Company, from time to time, to purchase shares in the open market (including in pre-arranged stock trading plans in accordance with the guidelines specified in Rule 10b5-1 under the Securities Exchange Act of 1934, as amended) or in privately negotiated transactions. During the fiscal year ended December 25, 2016, the Company repurchased 1,719,502 shares of its common stock for approximately $22.3 million, including cost and commission, in open market transactions. As of December 25, 2016, the remaining dollar value of authorization under the share repurchase program was $27.7 million, which does not include commission. Repurchased shares are included as treasury stock in the consolidated balance sheets and the consolidated statements of equity.

Warrants

As of December 27, 2015 and December 25, 2016, the Company had 241,704 warrants outstanding. During 2013, the Company modified 241,704 of warrants issued to Oxford Capital Partners, Inc. that were set to expire upon the consummation of an IPO to extend the expiration date of such warrants to five years from the date of the consummation of an IPO. In accordance with ASC Topic 718, *Compensation—Stock Compensation*, the Company recorded a charge of approximately $0.1 million related to the incremental value associated with the extension of the expiration date.

(10) Operating Leases

The Company leases office space for its corporate office and commercial spaces for its shops under various long-term operating lease agreements. The leases for the Company's shop locations generally have initial terms of 10 years and typically provide for two renewal options in five-year increments as well as for rent escalations. These leases expire or become subject to renewal clauses at various dates from 2017 to 2029. Some of the leases provide for base rent, plus additional rent based on gross sales, as defined in each lease agreement. The Company is also generally obligated to pay certain real estate taxes, utilities, building operating expenses, insurance, and various other expenses related to properties.

Rental expense under operating lease agreements were as follows (in thousands):

	Fiscal Year		
	2016	2015	2014
Minimum rentals	$ 40,252	$ 36,955	$ 33,032
Contingent rentals	1,755	1,827	1,765
Less: sublease rentals	(94)	(94)	(94)
Total	$ 41,913	$ 38,688	$ 34,703

A schedule by year of future minimum rental payments required under operating leases, excluding contingent rent, that have initial or remaining non-cancelable lease terms in excess of one year, as of December 25, 2016, is as follows (in thousands):

Years Ending	Minimum
2017	$ 46,035
2018	42,583
2019	38,947
2020	36,818
2021	32,911
Thereafter	96,078
Total minimum payments required*	$ 293,372

* Minimum payments have not been reduced by minimum sublease rentals of $0.2 million due in the future.

Certain leases have outstanding letters of credit in lieu of rent deposits expiring at various dates through September 2017. The letters of credit were $0.6 million in aggregate for each of the years ended December 28, 2014 and December 27, 2015, and $0.7 million in aggregate for the year ended December 25, 2016. Under the credit facility, outstanding letters of credit are subject to an annual fee of 1.50% and reduce the available borrowing to the Company.

(11) Employee Benefit Plan

The Company sponsors a 401(k) profit sharing plan for all employees who are eligible based upon age and length of service. The Company made matching contributions of $0.3 million for fiscal year 2014 and $0.4 million for fiscal years 2015 and 2016.

(12) Stock Based Compensation

Stock Based Compensation Granted Under the 2001 and 2004 Equity Incentive Plans and 2013 Long-Term Incentive Plan

The Company has granted stock options under its 2001 Equity Incentive Plan (the “2001 Plan”), 2004 Equity Incentive Plan (the “2004 Plan”) and 2013 Long-Term Incentive Plan, as amended (the “2013 Plan” and together with the 2004 Plan and 2001 Plan, the “Plans”). The Plans permit the granting of awards to employees and non-employee officers, consultants, agents, and independent contractors of the Company in the form of stock appreciation rights, stock awards, and stock options. The Plans give broad powers to the Company’s board of directors to administer and interpret the Plans, including the authority to select the individuals to be granted options and rights and to prescribe the particular form and conditions of each option to be granted.

Under the 2001 Plan, the Company had 746,749 shares reserved for issuance. In 2007, the Company entered into a Stock Option Agreement (the “Agreement”), which granted a certain key executive 500,000 options of non-voting common stock. In September 2011, the 2001 Plan expired with options outstanding under the plan still available for exercise. As a result of the IPO, all shares of the non-voting common stock converted into voting common stock on a 1:1 basis upon exercise.

On July 31, 2013, the Company’s board of directors approved the adoption of the 2013 Plan, which replaced the 2004 Plan in conjunction with the Company’s IPO. Upon approval of the 2013 Plan, the Company no longer issued awards under the 2004 Plan. The 2004 Plan expired in February 2014, but will continue to govern outstanding awards granted prior to its termination. As of December 25, 2016, there have been 1,646,991 options, 28,240 shares of unrestricted common stock and 88,635 shares of restricted stock units (“RSUs”) granted under the 2013 Plan and 1,099,191 shares are reserved for future issuance.

Under the Plans, the number of shares and exercise price of each option are determined by the committee designated by the Company's board of directors. The options granted are generally exercisable within a 10-year period from the date of grant. Certain options have been issued to key executives. Options issued and outstanding expire on various dates through the year 2026. The range of exercise prices of options outstanding as of December 25, 2016, is $7.00 to $20.53 per option, and the options vest over a range of immediately to five-year periods.

Activity under the Plans and the Agreement is as follows:

Options	Shares (Thousands)	Weighted Average Exercise Price	Aggregate Intrinsic Value (Thousands)	Weighted Average Remaining Term (Years)
Outstanding—December 29, 2013	5,030	$ 9.41	$ 78,575	6.31
Granted	318	19.16		
Exercised	(586)	8.67		
Canceled	(149)	11.68		
Outstanding—December 28, 2014	4,613	$ 10.10	$ 12,731	5.62
Granted	565	13.21		
Exercised	(576)	8.30		
Canceled	(234)	13.89		
Outstanding—December 27, 2015	4,368	$ 10.53	$ 9,742	5.10
Granted	369	13.65		
Exercised	(536)	10.77		
Canceled	(188)	14.40		
Outstanding—December 25, 2016	4,013	$ 10.61	$ 13,455	4.78
Vested and expected to vest—December 25, 2016	2,965	9.62	$ 10,182	3.54
Exercisable—December 25, 2016	2,989	$ 9.61	$ 12,675	3.60

The following table reflects the average assumptions utilized in the Black-Scholes option-pricing model to value the options granted for each year:

	2016	2015	2014
Risk-free interest rate	1.7%	1.9%	1.3%
Expected life (years)	7.00	7.00	7.00
Expected dividend yield	—	—	—
Volatility	49.4%	45.3%	49.2%
Weighted average common stock fair value	$ 13.65	$ 13.21	$ 19.16

The risk-free rate is based on U.S. Treasury rates in effect at the time of the grant with a similar duration of the expected life of the options. The expected life of options granted is derived from the average of the vesting period and the term of the option. The Company has not paid dividends to date (with exception to the one-time dividend paid to stockholders prior to the initial public offering) and does not plan to pay dividends in the near future. Beginning October 2015, expected volatility of the options was calculated using the Company's historical data since its initial public offering. Prior to October 2015, the Company calculated expected volatility of the options based on historical data from selected peer public company restaurants.

During fiscal year 2014, the Company issued 28,240 shares of unrestricted common stock to certain non-employee members of its Board of Directors. The unrestricted stock had a weighted average grant-date share price of $15.29 upon issuance. The Company recorded $0.4 million in stock-based compensation expense, with a corresponding increase to additional paid-in capital, related to the issuance of the common stock.

In May 2015, the Company issued 30,856 shares of "RSUs" to certain non-employee members of its Board of Directors. The RSUs had a grant-date fair value of $14.26 upon issuance. In August 2015, the Company issued 5,221 shares of RSUs to the new non-employee member of its Board of Directors. The RSUs had a grant-date fair value of $11.88 upon issuance. In May 2016, the Company issued 52,558 shares of RSUs to certain non-employee members of its Board of Directors. The RSUs had a grant-date fair

value of $13.27 upon issuance. All issued RSUs have a vesting schedule of 50% on the first anniversary of the grant date and 50% on the second anniversary of the grant date.

Stock-based Compensation Expense

In accordance with ASC Topic 718, *Compensation—Stock Compensation*, stock-based compensation is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the requisite employee service period (generally the vesting period of the grant). The Company recognized $2.5 million, $2.4 million and $3.1 million for the fiscal years 2014, 2015 and 2016, respectively, with a corresponding increase to additional paid-in-capital. Fiscal year 2014 stock-based compensation expense includes $0.4 million related to unrestricted common stock granted during 2014. As of December 25, 2016, the unrecognized stock-based compensation expense was $5.2 million, which will be recognized through fiscal year 2020. The Company records stock-based compensation expense within general and administrative expenses in the consolidated statements of operations.

(13) Quarterly Financial Data (Unaudited)

The unaudited quarterly information includes all normal recurring adjustments that the Company considers necessary for a fair presentation of the information shown. The Company's quarterly results have been and will continue to be affected by the timing of new shop openings and their associated pre-opening costs. As a result of these and other factors, the financial results for any quarter may not be indicative of the results for any future period.

The following table presents selected unaudited quarterly financial data for periods indicated (in thousands, except per share data):

	Fiscal Year 2016 (1)			
	March 27	June 26	September 25	December 25
Total revenues	$ 95,955	$ 105,036	$ 103,782	$ 102,358
Income from operations	1,889	5,512	2,842	2,770
Net income attributable to Potbelly Corporation	1,088	3,373	1,795	1,956
Income per share available to common stockholders-basic	0.04	0.13	0.07	0.08
Income per share available to common stockholders-diluted	0.04	0.13	0.07	0.08

	Fiscal Year 2015 (1)			
	March 29	June 28	September 27	December 27
Total revenues	$ 85,768	$ 95,949	$ 96,039	$ 95,093
Income from operations	948	4,084	2,379	2,018
Net income attributable to Potbelly Corporation	531	2,461	1,401	1,235
Income per share available to common stockholders-basic	0.02	0.09	0.05	0.05
Income per share available to common stockholders-diluted	0.02	0.08	0.05	0.05

(1) Fiscal years 2016 and 2015 were 52-week years. Each quarter of the fiscal year consists of 13 weeks.

(14) Commitments and Contingencies

As previously disclosed in prior reports filed with the SEC, the Company received notice of a potential claim alleging that the Company violated the Fair Labor Standards Act by not paying overtime to its assistant managers, whom the Company has classified as exempt employees. Although the Company has always believed that its assistant managers are properly classified as exempt under both federal and state laws, and have always intended to defend any such lawsuits vigorously, the Company agreed to mediate the matter. On February 20, 2017, the parties entered into a Settlement Agreement and Release whereby participating assistant managers will release the Company from all federal and/or state wage and hour claims in exchange for a gross settlement amount of $1.3 million. As part of the settlement process, a complaint was filed on February 17, 2017 in the Circuit Court of the Fifteenth Judicial Circuit in and for Palm Beach County, Florida, and a motion seeking the Court's preliminary approval of the settlement was filed on February 21, 2017. As of December 25, 2016, the Company recorded a liability of $1.3 million for this matter. The settlement of this action did not have a material adverse effect on our financial position or results of operations and cash flows.

The Company is subject to legal proceedings, claims and liabilities, such as employment-related claims and slip and fall cases, which arise in the ordinary course of business and are generally covered by insurance. In the opinion of management, the amount of ultimate liability with respect to those actions should not have a material adverse impact on the Company's financial position or results of operations and cash flows.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act")) as of December 25, 2016. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of December 25, 2016, our disclosure controls and procedures were effective in ensuring that information required to be disclosed in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission (the "SEC") and is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during our fiscal quarter ended December 25, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management's Report on Internal Control over Financial Reporting

Management, including our Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act). Our internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of our internal control over financial reporting as of December 25, 2016. In making this assessment, management used the criteria established by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control-Integrated Framework (2013). Based on this assessment, management has concluded that, as of December 25, 2016, our internal control over financial reporting was effective, at a reasonable assurance level.

Because we are an "emerging growth company" under the Jumpstart Our Business Startups Act of 2012, this Annual Report on Form 10-K does not include an attestation report of our independent registered public accounting firm.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Except as set forth below, the information required by this item will be contained in our definitive proxy statement for the 2016 Annual Meeting (our "Proxy Statement") and is incorporated herein by reference.

We have adopted an ethics code of conduct applicable to our directors, officers and employees. A copy of that code is available on our corporate website at www.potbelly.com, which does not form a part of this Annual Report on Form 10-K. Any amendments to such code, or any waivers of its requirements, will be posted on our website.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this item will be contained in our Proxy Statement and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Except as set forth below, the information required by this item will be contained in our Proxy Statement and is incorporated herein by reference.

Equity Compensation Plan Information

The following table presents certain information related to our equity incentive plans under which our equity securities are authorized for issuance as of December 25, 2016:

Plan Category	(a) Number of Securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted-average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders (1)	4,012,520	$ 10.61	1,099,191 (2)
Equity compensation plans not approved by security holders	—	—	—
Total	4,012,520	$ 10.61	1,099,191

(1) Consists of the 2001 Equity Incentive Plan, the 2004 Equity Incentive Plan and the 2013 Long-Term Incentive Plan. No further awards may be made under the 2001 Equity Incentive Plan or the 2004 Equity Incentive Plan.

(2) The total amount reported consists only of shares available for future issuance under the 2013 Long-Term Incentive Plan, which may be issued in connection with awards of stock options, stock appreciation rights, restricted stock, restricted stock units, deferred stock units, performance stock and performance stock units.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this item will be contained in our Proxy Statement and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this item will be contained in our Proxy Statement and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) Financial Statements

(1) The financial statements filed as part of this Annual Report on Form 10-K are listed in the index to the financial statements.

(2) Any financial statement schedules required to be filed as part of this Annual Report on Form 10-K are set forth in section (c) below.

(b) Exhibits

See the Exhibit Index at the end of this Annual Report on Form 10-K, which is incorporate by reference.

(c) Financial Statement Schedules

No financial statement schedules are provided because the information called for is not applicable or is shown in the financial statements or notes thereto.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, Potbelly Corporation has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

POTBELLY CORPORATION

By: /s/ Aylwin Lewis
Aylwin Lewis
Chief Executive Officer and President

Date: February 22, 2017

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Aylwin Lewis, Michael Coyne and Matthew Revord and each of them, his or her true and lawful attorneys-in-fact, each with full power of substitution, for him or her in any and all capacities, to sign any amendments to this report on Form 10-K and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact or their substitute or substitutes may do or cause to be done by virtue hereof. Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Aylwin Lewis Aylwin Lewis	Chairman, Chief Executive Officer and President (Principal Executive Officer)	February 22, 2017
/s/ Michael Coyne Michael Coyne	Senior Vice President and Chief Financial Officer (Principal Financial and Principal Accounting Officer)	February 22, 2017
/s/ Peter Bassi Peter Bassi	Director	February 22, 2017
/s/ Ann-Marie Campbell Ann-Marie Campbell	Director	February 22, 2017
/s/ Susan Chapman-Hughes Susan Chapman-Hughes	Director	February 22, 2017
/s/ Daniel Ginsberg Daniel Ginsberg	Director	February 22, 2017
/s/ Marla Gottschalk Marla Gottschalk	Director	February 22, 2017
/s/ Harvey Kanter Harvey Kanter	Director	February 22, 2017
/s/ Carl Warschausky Carl Warschausky	Director	February 22, 2017

EXHIBIT INDEX

Exhibit Number	Description of Exhibit
3.1	Seventh Amended and Restated Certificate of Incorporation of Potbelly Corporation (filed as Exhibit 3.1 to Form S-1 (File No. 333-190893) filed on August 29, 2013 and incorporated herein by reference)
3.2	Amended and Restated By-laws of Potbelly Corporation (filed as Exhibit 3.2 to Form S-1 (File No. 333-190893) filed on August 29, 2013 and incorporated herein by reference)
4.1	Fifth Amended and Restated Registration Rights Agreement (filed as Exhibit 4.1 to Form S-1 (File No. 333-190893) filed on August 29, 2013 and incorporated herein by reference)
10.1	Potbelly Corporation 2004 Equity Incentive Plan, as amended (filed as Exhibit 10.1 to Form S-1 (File No. 333-190893) filed on August 29, 2013 and incorporated herein by reference) †
10.2	Amended and Restated Potbelly Corporation 2013 Long-Term Incentive Plan (filed as Exhibit 10.1 to Form 8-K (File No. 001-36104) filed August 4, 2016 and incorporated herein by reference) †
10.3	Amended and Restated Credit Agreement, dated as of December 9, 2015, among Potbelly Sandwich Works, LLC, Potbelly Corporation, the other Loan Parties party thereto, the Lenders party thereto, JPMorgan Chase Bank, N.A., as Administrative Agent, and J.P. Morgan Securities, LLC, as Sole Bookrunner and Sole Lead Arranger (filed as Exhibit 10.1 to Form 8-K (File No. 001-36104) filed December 11, 2015 and incorporated herein by reference)
10.4	Executive Employment Contract between Potbelly Corporation and Aylwin Lewis dated August 8, 2013 (filed as Exhibit 10.6 to Form S-1 (File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †
10.5	Executive Employment Agreement, dated July 25, 2013, between Potbelly Corporation and Matthew Revord †
10.6	Amendment to Executive Employment Agreement, dated April 22, 2015, between Potbelly Corporation and Matthew Revord †
10.7	Executive Employment Agreement, dated April 3, 2015, effective May 1, 2015, between Potbelly Corporation and Michael Coyne (filed as Exhibit 10.1 to Form 8-K (File No. 001-36104) filed April 8, 2015 and incorporated herein by reference) †
10.8	Executive Employment Agreement, dated May 1, 2015, between Potbelly Corporation and Julie Younglove-Webb (filed as Exhibit 10.1 to Form 8-K (File No. 001-36104) filed May 4, 2015 and incorporated herein by reference) †
10.9	Form of stock option agreement for grants prior to January 1, 2011 for named executive officers other than Aylwin Lewis pursuant to 2004 Equity Incentive Plan (including any replacement options granted after such date for expired grants) (filed as Exhibit 10.9 to Form S-1(File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †
10.10	Form of stock option agreement for grants prior to January 1, 2011 for Aylwin Lewis pursuant to 2004 Equity Incentive Plan (filed as Exhibit 10.10 to Form S-1(File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †
10.11	Form of stock option agreement for grants during year 2011 for named executive officers other than Aylwin Lewis pursuant to 2004 Equity Incentive Plan (filed as Exhibit 10.11 to Form S-1(File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †
10.12	Form of stock option agreement for grants for directors other than Aylwin Lewis pursuant to 2004 Equity Incentive Plan (filed as Exhibit 10.13 to Form S-1(File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †
10.13	Form of stock option agreement (other than for Aylwin Lewis) pursuant to 2013 Long-Term Incentive Plan (filed as Exhibit 10.14 to Form S-1(File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †
10.14	Form of stock option agreement for Aylwin Lewis pursuant to 2013 Long-Term Incentive Plan (filed as Exhibit 10.15 to Form S-1(File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †
10.15	Form of Restricted Stock Unit Award Agreement pursuant to 2013 Long-Term Incentive Plan (filed as Exhibit 10.16 to Form S-1(File No. 333-190893) filed August 29, 2013 and incorporated herein by reference) †

Exhibit Number	Description of Exhibit
10.16	Form of Director Restricted Stock Unit Award Agreement for directors other than Aylwin Lewis pursuant to 2013 Long-Term Incentive Plan †
10.17	Form of Indemnification Agreement between Potbelly Corporation and each of its directors and executive officers (filed as Exhibit 10.17 to Form S-1 (File No. 333-190893) filed August 29, 2013 and incorporated herein by reference)
10.18	Director Compensation Plan (filed as Exhibit 10.20 to Form 10-K (File No. 001-36104) filed February 25, 2015 and incorporated herein by reference)†
10.19	Potbelly Director Compensation Plan (filed as Exhibit 10.23 to Form 10-K (File No. 001-36104) filed February 24, 2016 and incorporated herein by reference) †
10.20	Potbelly Non-Qualified Deferred Compensation Plan (filed as Exhibit 10.21 to Form 10-K (File No. 001-36104) filed February 25, 2015 and incorporated herein by reference)†
21.1	Subsidiaries of the Registrant
23.1	Consent of Deloitte & Touche LLP
24.1	Power of Attorney (included on signature page)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

† Management contract or compensatory plan

EXECUTIVE EMPLOYMENT CONTRACT

THIS EXECUTIVE EMPLOYMENT AGREEMENT (this "Agreement") is made and entered into as of July 25, 2013 (the "Effective Date") by and between Potbelly Corporation, a Delaware corporation (hereinafter referred to as "Company"), and Matthew Revord, an individual (hereinafter referred to as "Executive").

Statement of Purpose

WHEREAS, Executive is currently employed by Company and is party to an Executive Employment Contract dated as of September 10, 2009 (the "Prior Agreement"); and

WHEREAS, Company desires to continue to employ Executive as its Senior Vice President of General Counsel and Secretary from and after the Effective Date and Executive desires to continue in employment with Company from and after the Effective Date, subject to the terms and conditions of this Agreement.

NOW, THEREFORE, in consideration of the mutual covenants and agreements set forth below, it is hereby mutually covenanted and agreed by Company and Executive as follows:

1. Term, Employment and Duties.

(a) *Term.* The "Term" of this Agreement shall commence on the Effective Date and shall terminate on the date that Executive's employment with Company and its affiliates terminates for any reason (the "Termination Date"). Executive shall at all times be an at-will employee and nothing in this Agreement shall constitute or be evidence of any agreement or understanding, express or implied, that Executive has a right to continue to be employed by Company for any period of time or at any specific rate of compensation.

(b) *Title and Duties.* Effective as of the Effective Date, Company hereby agrees to continue to employ Executive, and Executive agrees to continue in the employ of Company, as Company's Senior Vice President of General Counsel and Secretary. Executive shall also have the commensurate titles and positions with such subsidiaries of affiliates of Company as determined by Company and shall serve in such positions without additional compensation. Executive shall have the duties, responsibilities and authority customary for his/her position and shall perform such other duties consistent with such position as may be assigned to Executive, from time to time, by Company.

(c) *Performance of Duties.* Executive shall devote Executive's full business time, energy, loyalty, and ability exclusively to the business, affairs, and interests of Company and its affiliates, and shall use Executive's best efforts and abilities to promote the interests of Company and its affiliates and to perform the services contemplated by this Agreement and agrees that he/she will perform his/her duties faithfully and efficiently subject to the directions of the CEO. Without the prior approval of Company's CEO or the executive to whom he/she reports, Executive shall not, during the Term, directly or indirectly, render any other employment or consulting activities or services, including as a director, to any other person, firm, corporation, or other entity; provided, however, that, to the extent that the following activities do not conflict with or detract from the performance by Executive of Executive's duties, Executive may act as a director of, and may also engage in activities involving, charitable, educational, religious, and similar types of organizations, and similar types of activities.

(d) *Confidentiality, Non-Competition, Non-Interference and Intellectual Property*. Executive hereby acknowledges and confirms that the Executive Confidentiality and Non-Compete Agreement previously signed by Executive and in effect on the Effective Date shall remain in full force and effect following the Effective Date and is hereby incorporated into and forms part of this Agreement.

2. Termination of Employment.

(a) *Termination Date.* Executive's Termination Date shall occur upon termination by Company for any reason or no reason or by Executive for any reason or no reason, including any of the following: (i) Executive's death; (ii) Executive being disabled by reason of physical and mental infirmity or both, thereby rendering Executive

unable to satisfactorily perform Executive's duties under this Agreement (a "Disability"), said Disability to be determined in good faith by the CEO in consultation with no fewer than two (2) accredited physicians selected by the CEO and reasonably approved by Executive in the event that Disability is disputed; (iii) termination of Executive's employment by Company with or without Cause (as defined below) or (iv) Executive's resignation with or without Good Reason (as defined below). Executive's Termination Date shall be considered to be on account of a "Qualifying Termination" if the Termination Date occurs due to (1) termination by Company without Cause or (2) termination by Executive with Good Reason.

(b) *Cause*. The term "Cause" as used in this Agreement shall mean [an act, action, or series of acts or actions, or omission or series of omissions, by Executive which constitute or result in: (i) intentional misrepresentation of material information by Executive in Executive's relations with Company; (ii) Executive's indictment (or its equivalent) for the commission of a crime by Executive that constitutes a felony; (iii) commission of an act involving moral turpitude; (iv) the material breach or material default by Executive of any of Executive's written agreements with Company or obligations under any material provision of this Agreement or any written policy of Company (that remains unremedied within thirty (30) days after notice to Executive); (v) the commission of fraud or embezzlement on the part of Executive; (vi) failure to comply with any lawful written direction of Company's Board of Directors (the "Board") (that, if capable of cure without damage to Company, remains unremedied within thirty (30) days after notice to Executive); or (vii) willful action taken for the purpose of harming Company or any of its affiliates. For purposes of clause (vii) of this Paragraph 2(b), no act or failure to act, on the part of Executive, shall be considered "willful" unless it is done or omitted to be done, by Executive in bad faith and without reasonable belief that Executive's action or omission was in the best interest of Company. An act, or failure to act, based upon written authority given by Company shall be conclusively presumed to be done, or omitted to be done, by Executive in good faith and in the best interest of Company.

(c) *Good Reason*. The term “Good Reason” as used in this Agreement means the occurrence, without Executive’s consent, of (i) a material reduction in either Executive’s rate of Base Salary (as defined in Paragraph 3 (a)) or Executive’s target bonus percentage (other than across the board salary or bonus reductions (target, actual or maximum) for management employees); (ii) any material reduction in the position, authority, or office of Executive with respect to Company, or in Executive’s responsibilities or duties for Company; (iii) any action or inaction by Company that constitutes a material breach of the terms of this Agreement; or (iv) any relocation of Executive’s principal place of work with Company to a place more than fifty (50) miles from Company’s headquarters at the Effective Date; provided, however, that any such occurrence under clauses (i) – (iv) above shall constitute Good Reason only if (1) Executive provides notice to Company within thirty (30) days after the occurrence, (2) Company fails to cure such occurrence with within thirty (30) days after receipt of notice from Executive, and (3) Executive terminates employment within thirty (30) days following expiration of the cure period.

3. <u>Compensation and Benefits During Employment</u>.

(a) *Base Salary*. During the term of Executive’s employment hereunder, Company shall pay to Executive a base salary at an annual rate of $310,000.00 (the "Base Salary"). The Base Salary may be increased from time to time at the recommendation of the CEO and approved by the Compensation Committee of the Board (the "Compensation Committee").

(b) *Annual Bonus*. With respect to bonus years beginning prior to an initial public offering of Company’s common stock (an “IPO”), Executive shall be eligible for a discretionary "Annual Bonus" in accordance with Company’s annual incentive plan for Senior Team Leaders (the “SLT Bonus Plan”) as in effect on the Effective Date (including in accordance with established EBITDA targets) at a target rate of 40% of his/her Base Salary. Executive’s Annual Bonus for bonus years beginning prior to an IPO shall be paid in a single lump sum cash payment after the end of the calendar year to which it relates and not later than June 15 following the conclusion of the calendar year to which the Annual Bonus relates, provided, however, that if the annual audit for such calendar year has not been issued by the Company’s outside auditors by said June 15, then payment shall be made within thirty (30) days following the issuance of such audit, but in no event shall payment be made later than the end of the calendar year following the calendar year to which Annual Bonus relates. The Executive understands that the Annual Bonus is purely discretionary, not accrued, or earned until the payout, if any, has been approved by the Board or Compensation Committee, and the target is not a guarantee of any particular bonus payout or amount. For bonus years beginning on or after an IPO, the

Annual Bonus amount and terms and conditions shall be determined in accordance with incentive plan metrics to be recommended by the CEO and approved by the Compensation Committee and shall be paid in accordance with the terms and conditions of the bonus plan in effect for such periods. Executive understands that the Annual Bonus is purely discretionary, not accrued, or earned until the payout, if any, has been approved by the Board or Compensation Committee, as applicable.

(c) *Time Off*. During the Term, Executive shall be entitled to vacation consistent with Company practice and policy for executive-level employees, but not less than five (5) weeks of vacation per year. In addition, Executive shall be entitled to those paid holidays granted to Company employees while Executive is employed.

(d) *Executive Benefits/Perquisites*. Executive shall be entitled to such other benefits, including health insurance, dental, 401(k), and other benefits and perquisites in such form and in such manner and at such times as Company shall from time to time adopt and establish for its executive-level employees generally. Executive shall be subject to eligibility and other requirements of applicable benefit plans.

(e) *Expenses*. Company shall pay or reimburse Executive for all reasonable business expenses actually incurred or paid by Executive during the Term in the performance of Executive's duties and responsibilities under this Agreement, subject to and in accordance with applicable expense reimbursement policies as in effect from time to time.

(f) *Equity Awards*. Executive shall be entitled to annual equity grants, if any, as determined by the Compensation Committee. All stock options that are outstanding on the Effective Date, shall become fully vested on the Effective Date. If Executive resigns his employment on account of retirement (which, solely for purposes of this Paragraph 3(f), shall mean a resignation by Executive with or without good reason after Executive has attained at least age 57 and completed at least 10 years of service with the Company and if such termination is not for any other reason), all vested stock options that are outstanding on the Effective Date and that continue to be outstanding on the Termination Date shall remain exercisable in accordance with the terms of the stock option agreement evidencing such stock option for five (5) years after the Termination Date (or, if less, the expiration date of such stock option). Notwithstanding the preceding sentence, if, after the Termination Date, Executive becomes employed on a full-time basis or provides consulting services on a full-time basis for another employer or entity (as determined in the reasonable judgment of the Board) (the "Reemployment Date"), then the options shall remain exercisable in accordance with the terms of the stock option agreement evidencing such stock option until the earlier of (i) ninety (90) days following the Reemployment Date or (i) the expiration date of the stock option term. All other stock options outstanding on Executive's Termination Date shall remain exercisable for ninety (90) days following the Termination Date or for such longer or shorter period specified under the stock option agreement evidencing such stock option but in no event after the expiration of the stock option term. Executive shall provide written notice to the Company of any post-Termination Date employment that could reasonably be expected to constitute full-time employment for purposes of this Paragraph 3(f).

4. Payments and Benefits on Termination of Employment.

(a) *Termination for any Reason*. If Executive's Termination Date occurs for any reason, Company shall pay or provide to Executive (i) Executive's Base Salary for the period ending on the Termination Date; (ii) Executive's earned but unpaid Annual Bonus for any bonus year ending prior to the bonus year during which the Termination Date occurs; (iii) reimbursement of Executive's incurred but unreimbursed business expenses for periods prior to Executive's Termination Date; and (iv) any other payments or benefits to be provided to Executive by Company pursuant to any employee benefit plans or arrangements of Company or required by applicable law, to the extent such amounts are due from Company. Executive will be entitled to any other benefits in accordance with the terms of the applicable benefit plan or program. Unless Executive’s Termination Date occurs as a result of a Qualifying Termination, all stock options outstanding on Executive’s Termination Date shall remain exercisable for ninety (90) days following the Termination Date or for such longer or shorter period specified under the stock option agreement evidencing such stock option but in no event after the expiration of the stock option term.

(b) *Qualifying Termination – Non-Change in Control*. If Executive's Termination Date occurs by reason of a Qualifying Termination and if the Release Requirements (as defined Paragraph 4(e)) are satisfied as of the

sixtieth (60th) day following the Termination Date (which sixtieth (60th) day shall be referred to as the "Payment Date"), then, in addition to the payments and benefits to which Executive is entitled under Paragraph 4(a), Executive will be entitled to the following payments and benefits:

(i) Company shall pay Executive a cash severance payment in a gross amount equal to twelve (12) months of Executive's Base Salary (determined as of the Termination Date without regard to any reduction thereof under circumstances which constitute Good Reason) (the "Severance Payment"). Any Severance Payment to which Executive is entitled under this Paragraph 4(b)(i) will commence on the first regular payroll date after the Payment Date and shall continue to be paid in substantially equal payroll by payroll period installments for a period of twelve (12) months thereafter.

(ii) If Executive is entitled to and elects continuation coverage under Company's group health plans pursuant to "COBRA" ("COBRA Coverage"), Company shall continue to pay on behalf of Executive the same level of employer contribution that is provided by Company for corresponding coverage for similarly-situated active employees for the lesser of (1) twelve (12) months following Executive's Termination Date or (2) the date on which COBRA Coverage terminates by its terms (the "Post-Termination Coverage Benefit"). Company shall have no obligations under this Paragraph 4(b)(ii) if the Post-Termination Coverage Benefit would subject Company or any of its affiliates to tax penalties or materially increase the cost to Company and its affiliates of providing group medical coverage to employees generally. For the period commencing on Executive's Termination Date and ending on the Payment Date, the COBRA Coverage shall be provided at Executive's expense and, if the Release Requirements are satisfied on the Payment Date, Executive shall be entitled to a lump sum payment in an amount equal to the Post-Termination Coverage Benefit that would have been provided to Executive for the period beginning on the Termination Date and ending on the Payment Date, which lump sum payment shall be made on the Payment Date or the next scheduled payroll date.

(iii) All vested stock options that are outstanding on the Effective Date and which continue to be exercisable by their terms on the Termination Date shall remain exercisable for five (5) years after the Termination Date (or, if less, the expiration date of such stock option).

If the Release Requirements are not satisfied on the Payment Date, Executive shall not be entitled to any payments or benefits under this Paragraph 4(b).

(c) *Qualifying Termination – Change in Control*. If Executive's Termination Date occurs by reason of a Qualifying Termination on or within two (2) years following a Change in Control (as defined below), then, in addition to the payments and benefits to which Executive is entitled under Paragraph 4(a), Executive will be entitled to the following payments and benefits (which shall not be subject to satisfaction of the Release Requirements):

(i) Company shall pay Executive the Severance Benefit in accordance with the provisions of Paragraph 4(b)(i).

(ii) If Executive is entitled to and elects COBRA Coverage, Company shall provide Executive with the Post-Termination Coverage Benefit in accordance with the provisions of Paragraph 4(b)(ii).

(iii) Company shall pay Executive a cash payment equal to the amount of the Annual Bonus that Executive would have received for the bonus year in which the Termination Date occurs had his/her Termination Date not occurred, based on actual Company performance and pro rated for the portion of the bonus year completed prior to the Termination Date, payable at the same time as the annual bonus is paid similarly-situated active executive employees in accordance with the terms of the applicable bonus plan of Company.

(iv) All vested stock options that are outstanding on the Effective Date and that continue to be exercisable by their terms on the Termination Date will remain exercisable for five (5) years after the Termination Date (or, if less, the expiration date of such stock option).

For purposes of this Agreement, the term "Change in Control" shall mean, (1) for periods prior to an IPO, a "Corporate Transaction" as defined in the Potbelly Corporation 2004 Equity Incentive Plan, as amended, and (2) for periods after

an IPO, a "Change in Control" as defined in the Potbelly Corporation 2012 Long-Term Incentive Plan. In no event shall an IPO be considered a Change in Control for purposes of this Agreement.

(d) *Company Property*. Upon Executive's Termination Date, Executive will promptly return to Company all the documents and/or property of or relating to Company or any of its affiliates within Executive's possession or control.

(e) *Release Requirements*. For purposes of this Agreement, the "Release Requirements" shall be satisfied as of any date if, as of such date, Executive (or, for purposes of Paragraph 4(f), the legal representative of Executive's estate) has signed a form of general release and waiver satisfactory to Company and Executive if prior to death (the "Release") and the Release has become effective in accordance with applicable law (including that the Release has not revoked and the revocation period applicable under applicable law has expired).

(f) *Termination by Reason of Death or Disability*. If Executive's Termination Date occurs by reason of death or Disability and the Release Requirements are satisfied (which, in the case of death shall be satisfied by the legal representative of Executive's estate), then, in addition to the payments and benefits to which Executive is entitled under Paragraph 4(a), Company shall pay to Executive or the legal representative of his estate, as applicable, a cash payment equal to the amount of the Annual Bonus that Executive would have received for the bonus year in which the Termination Date occurs had his/her Termination Date not occurred, based on actual Company performance and pro-rated for the portion of the bonus year completed prior to the Termination Date, payable at the same time as the annual bonus is paid to similarly-situated active executive employees in accordance with the terms of the applicable bonus plan of Company.

5. Mitigation and Set-Off. Executive shall not be required to mitigate the amount of any payment provided for in this Agreement by seeking other employment or otherwise. Company shall not be entitled to set off against the amounts payable to Executive under this Agreement any amounts earned by Executive in other employment after termination of his/her employment with Company or any amounts which might have been earned by Executive in other employment had he/she sought such other employment; provided, however that Company shall be entitled to set off against the amounts payable to Executive under this Agreement any amounts owed to Company by Executive.

6. Reimbursements. To the extent that any reimbursements under this Agreement are taxable to Executive, such reimbursements shall be paid to Executive only if (a) to the extent not specified herein, the expenses are incurred and reimbursable pursuant to a reimbursement plan that provides an objectively determinable nondiscretionary definition of the expenses that are eligible for reimbursement and (b) the expenses are incurred during the Term. With respect to any expenses that are reimbursable pursuant to the preceding sentence, the amount of the expenses that are eligible for reimbursement during one calendar year may not affect the amount of reimbursements to be provided in any subsequent calendar year, the reimbursement of an eligible expense shall be made no later than the last day of the calendar year following the calendar year in which the expense was incurred, and the right to reimbursement of the expenses shall not be subject to liquidation or exchange for any other benefit.

7. Notices. Notices and all other communications provided for in this Agreement shall be in writing and shall be delivered personally or sent by registered or certified mail, return receipt requested, postage prepaid, or sent by facsimile or prepaid overnight courier to the parties at the addresses set forth below (or such other addresses as shall be specified by the parties by like notice). Communications that are to be delivered by the U.S. mail or by overnight service are to be delivered to the addresses set forth below:

to Company:

Potbelly Corporation
222 Merchandise Mart Plaza Suite 2300
Chicago, Illinois 60654

Attention: Chief Executive Officer

or to Executive, to Executive's home address as reflected in Company's records.

Each party, by notice furnished to the other party, may modify the applicable delivery address, except that notice of change of address shall be effective only upon receipt.

8. Non-Waiver. No waiver by either party or any breach by the other party of any provision hereof shall be deemed to be a waiver of any later or other breach thereof or as a waiver of any such or other provision of this Agreement.

9. Governing Law and Choice of Forum. The construction, validity, and enforceability of this Agreement shall be governed by the laws of the State of Illinois, as that law applies to contracts made, and to be wholly performed, in the State of Illinois.

10. Binding Effect. This Agreement shall be binding upon and inure to the benefit of Company, Executive, and Executive's personal representatives, beneficiaries, heirs, and successors. Company will require any successor (whether direct or indirect, by purchase, merger, consolidation or otherwise) to all or substantially all of the business and/or assets of Company to expressly assume and agree to perform this Agreement in the same manner and to the same extent that Company would be required to perform it if no such succession has taken place.

11. Severability. If any provision of this Agreement or any part thereof be held invalid or unenforceable, the same shall not affect or impair any other provision of this Agreement or any part thereof, and the invalidity or unenforceability of any provision of this Agreement shall not have any effect on or otherwise impair or limit the other obligations of Company or Executive.

12. Counterparts. This Agreement may be executed in duplicate counterparts, each of which shall be deemed an original hereof.

13. Disputes. Except as set forth in this Paragraph 13, any dispute, claim or_difference arising between Company and Executive (each a "Party," and jointly, the "Parties"), including any dispute, claim or difference arising out of this Agreement, will be settled exclusively by binding arbitration in accordance with the rules of the Judicial Arbitration and Mediation Services, Inc. ("JAMS"). The arbitration will be held Chicago, Illinois unless the Parties mutually agree otherwise. Nothing contained in this Paragraph 13 will be construed to limit or preclude a Party from bringing any action in any court of competent jurisdiction for injunctive or other provisional relief to compel another party to comply with its obligations under this Agreement or any other agreement between or among the Parties during the pendency of the arbitration proceedings. Each Party shall bear its own costs and fees of the arbitration, and the fees and expenses of the arbitrator will be borne equally by the Parties, provided, however, if the arbitrator determines that any Party has acted in bad faith, the arbitrator shall have the discretion to require any one or more of the Parties to bear all or any portion of fees and expenses of the Parties and/or the fees and expenses of the arbitrator; provided, further that, with respect to claims that, but for this mandatory arbitration clause, could be brought against Company under any applicable federal or state labor or employment law ("Employment Law"), the arbitrator shall be granted and shall be required to exercise all discretion belonging to a court of competent jurisdiction under such Employment Law to decide the dispute, whether such discretion relates to the provision of discovery, the award of any remedies or penalties, or otherwise and provided further that Company may be required to pay filing or administrative fees in the event that requiring Executive to pay such fees would render this Paragraph 13 unenforceable under applicable law. As to claims not relating to Employment Laws, the arbitrator shall have the authority to award any remedy or relief that a Court of the State of Illinois could order or grant. The decision and award of the arbitrator shall be in writing and copies thereof shall be delivered to each Party. The decision and award of the arbitrator shall be binding on all Parties. In rendering such decision and award, the arbitrator shall not add to, subtract from or otherwise modify the provisions of this Agreement. Either Party to the arbitration may seek to have the award of the arbitrator entered in any court having jurisdiction thereof. All aspects of the arbitration shall be considered confidential and shall not be disseminated by any Party with the exception of the ability and opportunity to prosecute its claim or assert its defense to any such claim. The arbitrator shall, upon request of either Party, issue all prescriptive orders as may be required to enforce and maintain this covenant of confidentiality during the course of the arbitration and after the conclusion of same so that the result and underlying data, information, materials and other evidence are forever withheld from public dissemination with the exception of its subpoena by a court of competent jurisdiction in an unrelated proceeding brought by a third party.

14. Assignment and Survival. This Agreement is personal to Executive and shall not be assignable by Executive. This Agreement may be assigned by Company only to a successor-in interest to all or substantially all of

the business operations of Company or any of its affiliates. The rights and obligations of the parties to this Agreement shall survive its termination or expiration of this Agreement to the extent that any performance is required under this Agreement after the termination or expiration of the Agreement.

15. No Strict Construction. The language used in this Agreement will be deemed to be the language chosen by the parties to express their mutual intent, and no rule of strict construction will be used against any person.

16. Indemnification. If Executive (or his/her heirs, executors or administrators) is made a party or is threatened to be made a party to, or is involved in, any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative, by reason of the fact that Executive is or was a director or officer of Company or is or was serving at the request of Company as a director or officer of another corporation, partnership, joint venture, trust or other enterprise, Executive (and his/her heirs, executors or administrators) shall be indemnified and held harmless by Company to the fullest extent permitted by Delaware Law. To the fullest extent authorized by Delaware Law, the right to indemnification conferred in this Paragraph 16 shall also include the right to be paid by Company the expenses incurred in connection with any such proceeding in advance of its final disposition upon delivery to Company of an undertaking by or on behalf of Executive to repay such amount if it shall ultimately be determined that Executive is not entitled to be indemnified. Company's obligations under this Paragraph 16 shall survive the termination or expiration of this Agreement for any reason.

17. Withholding. All payments and benefits under this Agreement are subject to withholding of all applicable taxes.

18. Special Section 409A Rules. It is intended that this Agreement will comply with section 409A of the Internal Revenue Code of 1986, as amended (the "Code"), to the extent applicable, and this Agreement shall be interpreted and construed on a basis consistent with such intent. Notwithstanding any other provision of this Agreement to the contrary, if any payment or benefit hereunder is subject to section 409A of the Code, and if such payment or benefit is to be paid or provided on account of Executive's Termination Date (or other separation from service or termination of employment):

(a) and if Executive is a specified employee (within the meaning of section 409A(a)(2)(B) of the Code) and if any such payment or benefit is required to be made or provided prior to the earlier of (i) the first (1st) day of the seventh (7th) month following Executive's separation from service or (ii) termination of employment (the "Section 409A Payment Date"), such payment or benefit shall be delayed until the Section 409A Payment Date; and

(b) the determination as to whether Executive has had a termination of employment (or separation from service) shall be made in accordance with the provisions of section 409A of the Code and the guidance issued thereunder without application of any alternative levels of reductions of bona fide services permitted thereunder.

For purposes of section 409A of the Code, any installment payment or benefit under this Agreement shall be treated as a separate payment. If this Paragraph 18 applies to any payment or benefit hereunder, any such payments or benefits that would otherwise have been paid or provided to Executive between Executive's Termination Date and the Section 409A Payment Date, shall be paid in a lump sum on the Section 409A Payment Date.

19. Entire Agreement. This Agreement, together with Executive Confidentiality and Non-Compete Agreement in effect on the Effective Date, constitutes the entire agreement between the parties with respect to the subject matter hereof and supersedes and cancels all prior or contemporaneous oral or written agreements and understandings between them with respect to the subject matter hereof, except as otherwise specifically stated in this Agreement, including the Prior Agreement. This Agreement may not be changed or modified orally but only by an instrument in writing signed by the parties hereto, which instrument states that it is an amendment to this Agreement.

IN WITNESS WHEREOF, intending to be legally bound, Company and Executive have executed this agreement as of the date set forth below.

Dated as of July 29, 2013

POTBELLY CORPORATION

/s/ Aylwin Lewis

By: Aylwin Lewis

Its: President and Chief Executive Officer

EXECUTIVE:

/s/ Matthew Revord

By: Matthew Revord

Its: Senior Vice President, General Counsel

EXHIBIT 10.6

AMENDMENT TO EXECUTIVE EMPLOYMENT AGREEMENT

THIS AMENDMENT (this "Amendment") dated as of April 22, 2015, to the Executive Employment Agreement (the "Agreement") dated July 25, 2013, by and between Matthew Revord ("Executive") and Potbelly Corporation ("Company").

The parties desire to amend the Agreement as set forth herein.

Now, therefore, in consideration of the mutual covenants and agreements set forth herein, the parties hereby agree as follows:

1. **Amendment.** Paragraph 3(f) of the Agreement shall be deleted in its entirety and replaced with the following:

> "(f) *Equity Awards*. Executive shall be entitled to annual equity grants, if any, as determined by the Compensation Committee. All stock options that are outstanding on the Effective Date, shall become fully vested on the Effective Date. If Executive resigns his/her employment on account of retirement (which, solely for purposes of this Paragraph 3(f), shall mean a resignation by Executive with or without good reason after Executive has completed at least 10 years of service with the Company and if such termination is not for any other reason), all vested stock options that are outstanding on the Termination Date shall remain exercisable in accordance with the terms of the stock option agreement evidencing such stock option for five (5) years after the Termination Date (or, if less, the expiration date of such stock option). Notwithstanding the preceding sentence, if, after the Termination Date, Executive becomes employed on a full-time basis or provides consulting services on a full-time basis for another employer or entity (as determined in the reasonable judgment of the Board) (the "Reemployment Date"), then the options shall remain exercisable in accordance with the terms of the stock option agreement evidencing such stock option until the earlier of (i) ninety (90) days following the Reemployment Date or (ii) the expiration date of the stock option term. Executive shall provide written notice to the Company of any post-Termination Date employment that could reasonably be expected to constitute full-time employment for purposes of this Paragraph 3(f)."

2. **Counterparts**.This Amendment may be executed simultaneously in two or more counterparts, any one of which need not contain the signatures of more than one party, but all such counterparts taken together shall constitute one and the same Amendment.

3. **Miscellaneous.** Unless otherwise stated, capitalized terms are as defined or provided in the Agreement. The Agreement, as amended hereby, is ratified and affirmed in all respects and shall continue in full force and effect.

IN WITNESS WHEREOF, the parties hereto have executed this Amendment on the date first written above.

Potbelly Corporation	**Matthew Revord**
/s/ Aylwin Lewis____________________	/s/ Matthew Revord______________________
By: Aylwin Lewis	By: Matthew Revord
Its: President and Chief Executive Officer	Its: Senior Vice President, General Counsel

EXHIBIT 10.16

FORM OF DIRECTOR RESTRICTED STOCK UNIT AWARD AGREEMENT

POTBELLY CORPORATION
2013 LONG-TERM INCENTIVE PLAN
RESTRICTED STOCK UNIT AWARD AGREEMENT

* * * * *

Participant: ______________________________

Restricted Stock Unit Grant Date ("Grant Date"): ______________________________

Number of Restricted Stock Units: ______________________________

THIS RESTRICTED STOCK UNIT AWARD AGREEMENT (this "Agreement"), dated as of the Grant Date specified above, by and between Potbelly Corporation, a Delaware corporation (the "Company"), and the Participant is entered into pursuant to the Potbelly Corporation 2013 Long-Term Incentive Plan (as the same may be amended, restated, supplemented and otherwise modified from time to time, the "Plan"). All capitalized terms not otherwise defined in the text of this Agreement have the meanings attributed to them in the Plan. This Agreement is subject to the terms and conditions of the Plan.

1. Grant of Restricted Stock Units. Subject to the terms and conditions of the Plan and this Agreement, the Company hereby grants to the Participant a Full Value Award in the form of restricted stock units (the "Restricted Stock Units"). Each Restricted Stock Unit constitutes an unfunded and unsecured promise of the Company to deliver (or cause to be delivered) to the Participant, subject to the terms and conditions of the Plan and this Agreement, a share of Common Stock if and when the Restricted Stock Unit becomes vested and payable as described in Sections 2 and 3 hereof.

2. Vesting of Restricted Stock Units. Subject to the terms and conditions of this Agreement, the Restricted Stock Units granted pursuant to this Agreement shall vest as follows: fifty percent (50%) on the first anniversary of the Grant Date and fifty percent (50%) on the second anniversary of the Grant Date (each a "Vesting Date"); provided, however, that if the Participant's Termination Date occurs prior to a Vesting Date for any reason other than for cause, the Termination Date shall be an "Accelerated Vesting Date" and all Restricted Stock Units granted pursuant to this Agreement that have not have not otherwise vested shall vest on the Accelerated Vesting Date. Notwithstanding the foregoing, in the event that the Participant's Termination Date occurs prior to a Vesting Date or Accelerated Vesting Date on account of termination for cause, any portion of the Restricted Stock Units that are not vested upon the Participant's Termination Date shall immediately expire and shall be forfeited and the Participant shall have no further rights with respect thereto, including the right to acquire any shares of Common Stock hereunder with respect to such Restricted Stock Unit. Each Restricted Stock Unit which becomes vested on an applicable Vesting Date shall be referred to as a "Vested Restricted Stock Unit".

3. Payment of Restricted Stock Units. Vested Restricted Stock Units shall be paid as follows:

(a) Any Vested Restricted Stock Units that vest on a Vesting Date shall be paid promptly upon (but not more than thirty (30) days after) the applicable Vesting Date by delivery of one share of Common Stock for each such Vested Restricted Stock Unit being paid as of such date, subject to the terms of the Plan and this Agreement.

(b) Any Vested Restricted Stock Units that vest on an Accelerated Vesting Date which occurs by reason of termination on account of death or Disability (to the extent that the Disability would constitute a disability within the meaning of Section 409A of the Code ("Section 409A")) or shall be paid promptly upon (but not more than thirty (30) days after) the Accelerated Vesting Date.

(c) Any Vested Restricted Stock Units that vest on an Accelerated Vesting Date that occurs for any reason other than as specified in paragraph (b), the Participant shall be paid promptly on the Vesting Date that would otherwise have applied to such Vested Restricted Stock Units had the Termination Date not occurred (but not more than thirty (30) days thereafter).

4. Designation of Beneficiary. The Participant may designate a person or persons to receive payment in respect of the Participant's Vested Restricted Stock Units, in accordance with the terms of this Agreement, in the event that the Participant dies prior to the payment in respect of such Restricted Stock Units (a "Beneficiary"). Such designation, or any change to a prior designation of a Beneficiary, must be done by giving notice to the Committee on a form designated by the Committee. If, upon the death of the Participant, the Committee has determined that there is no designated Beneficiary for part or all of the Participant's Vested Restricted Stock Units, such Restricted Stock Units shall be paid, in accordance with the terms of the Agreement, to the Participant's estate (and the estate shall be deemed to be the Beneficiary for purposes of the Agreement).

5. Miscellaneous.

(a) *Administration.* The authority to administer and interpret the Agreement shall be vested in the Committee, and the Committee shall have all the powers with respect to the Agreement as it has with respect to the Plan. Any interpretation of the Agreement by the Committee and any decision made by it with respect to the Agreement is final and binding on all persons.

(b) *Transfer Restrictions*. This Agreement, the Participant's rights hereunder, and the Restricted Stock Units are not transferable by the Participant, except as otherwise provided in the Plan and this Agreement.

(c) *Securities Law Requirements*. Notwithstanding any other provision of this Agreement, the Company shall have no liability to make any distribution of Common Stock under this Agreement unless such delivery or distribution would comply with all applicable laws. In particular, no shares will be delivered to a

Participant unless, at the time of delivery, the shares qualify for exemption from, or are registered pursuant to, applicable federal and state securities laws.

(d) *Notices*. All notices, consents and other exchanges of written material required or implied under this Agreement shall be in writing and delivered in person or by messenger, facsimile, overnight courier or certified mail and shall be sent to the following:

If to the Company:	Potbelly Corporation 111 North Canal Street Suite 850 Chicago, Illinois 60606 Attention: Committee, General Counsel and Senior Vice President of Human Resources
If to Participant:	The address on file with the Company

All notices shall be deemed delivered and received by the receiving party (i) if delivered by messenger, on the date of delivery or on the date delivery was refused by the addressee, (ii) if delivered by facsimile transmission, upon receipt of facsimile confirmation of the party transmitting such notice, or (iii) if delivered by overnight courier or certified mail, on the date of delivery as established by the return receipt, courier service confirmation or similar documentation (or the date on which the courier or postal service, as applicable, confirms that acceptance of delivery was refused by the addressee). A party may change its notice information set forth above by giving the other party proper notice of the change, but a change to such notice information is only effective when it is actually received.

(e) *Rights Are Unsecured*. Under this Agreement, the right of a Participant or Beneficiary to receive payment hereunder shall be an unsecured claim against the general assets of the Company and neither the Participant nor any Beneficiary shall have any rights in or against any specific assets of the Company or any of its affiliates. All amounts credited to the Participant shall constitute general assets of the Company, and may be disposed of by the Company at such time and for such purposes as it may deem appropriate.

(f) *Successors and Assigns*. This Agreement shall be binding upon and inure to the benefit of all successors and assigns of the Company and the Participant, including without limitation, the estate of the Participant and the executor, administrator or trustee of such estate or any receiver or trustee in bankruptcy or representative of the Participant's creditors.

(g) *Severability*. The terms or conditions of this Agreement shall be deemed severable and the invalidity or unenforceability of any term or condition hereof shall not affect the validity or enforceability of the other terms and conditions set forth herein.

(h) *No Rights to Continued Service; No Rights as Stockholder*. The grant of the Restricted Stock Units does not constitute a contract of employment or continued service, and the grant of the Restricted Stock Units shall not give the Participant the right to be retained in the employ or service of the Company or any Related Company, nor any right or claim to any benefit under the Plan or the Agreement, unless such right or claim has specifically accrued under the terms of the Plan and the Agreement. The Participant and the Participant's Beneficiary shall not have any rights with respect to Common Stock (including voting rights) issuable upon payment of the Restricted Stock Units prior to the date on which the Restricted Stock Units are paid or settled.

(i) *Governing Law*. The grant of the Restricted Stock Units and the provisions of this Agreement are governed by, and subject to, the laws of the State of Delaware, without regard to the conflict of law provisions, as provided in the Plan. For purposes of litigating any dispute that arises under this grant or this Agreement the parties hereby submit to and consent to the exclusive jurisdiction of the State of Illinois and agree that such litigation shall be conducted in the courts of Lake County, Illinois, or the federal courts for the United States for the Northern District of Illinois, where this grant is made and/or to be performed.

(j) *Amendment.* The Board may, at any time, amend or terminate the Plan, and the Board or the Committee may amend this Agreement, provided that no amendment or termination may, in the absence of written consent to the change by the Participant (or, if the Participant is not then living, the Participant's beneficiary), adversely affect the rights of any Participant or beneficiary under this Agreement prior to the date such amendment is adopted by the Board (or the Committee, if applicable). Certain adjustments under the Plan shall not be subject to the foregoing limitations. In no event shall this Agreement be amended to provide for any provision that is inconsistent with the terms of the Plan.

(k) *Code Section 409A*. This Agreement is intended to be interpreted and operated to comply with the requirements of Section 409A. If an unintentional operational failure occurs with respect to Section 409A requirements, the Participant shall fully cooperate with the Company to correct the failure, to the extent possible, in accordance with any correction procedure established by the U.S. Internal Revenue Service.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed as of the Grant Date.

PARTICIPANT	POTBELLY CORPORATION
______________________	By: ______________________
Name: ______________________	Name: ______________________
	Its: ______________________

EXHIBIT 21.1

SUBSIDIARY NAME	STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION
Potbelly Illinois, Inc.	Illinois
Potbelly Sandwich Works, LLC	Illinois
Potbelly Franchising, LLC	Illinois
PSW 555 Twelfth Street, LLC	Illinois
PSW DC Acquisition LLC	Illinois
Potbelly Sandwich Works DC-1, LLC	Illinois
Potbelly Airport II Boston, LLC	Illinois
PSW PBD Acquisition LLC	Illinois
PSW Rockville Center, LLC	Illinois
PSW West Jackson, LLC	Illinois
Potbelly Airport Portland PDX, LLC	Illinois
Potbelly Airport Dulles IAD Joint Venture B, LLC	Illinois
Potbelly Airport Dulles IAD Joint Venture D, LLC	Illinois
Potbelly Airport Midway MDW 1, LLC	Illinois
Potbelly Airport Midway MDW 2, LLC	Illinois
Potbelly Airport Hopkins CLE JV, LLC	Illinois

EXHIBIT 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in Registration Statement No. 333-191917 on Form S-8 of our report dated February 22, 2017, relating to the consolidated financial statements of Potbelly Corporation and subsidiaries appearing in this Annual Report on Form 10-K of Potbelly Corporation and subsidiaries for the year ended December 25, 2016.

/s/ Deloitte & Touche LLP

Chicago, Illinois
February 22, 2017

EXHIBIT 31.1

Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Aylwin Lewis, certify that:

1. I have reviewed this annual report on Form 10-K of Potbelly Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 22, 2017

/s/ Aylwin Lewis
Aylwin Lewis
Chief Executive Officer and President

EXHIBIT 31.2

Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Michael Coyne, certify that:

1. I have reviewed this annual report on Form 10-K of Potbelly Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 22, 2017

/s/ Michael Coyne
Michael Coyne
Chief Financial Officer

EXHIBIT 32.1

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, Aylwin Lewis, Chief Executive Officer and President of Potbelly Corporation (the "Registrant"), and Michael Coyne, Chief Financial Officer of the Registrant, each hereby certifies that, to the best of his knowledge on the date hereof:

1. the Registrant's Annual Report on Form 10-K for the period ended December 25, 2016, to which this Certification is attached as Exhibit 32.1 (the "Annual Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. information contained in the Annual Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

Date: February 22, 2017

By: /s/ Aylwin Lewis
Aylwin Lewis
Chief Executive Officer and President

Date: February 22, 2017

By: /s/ Michael Coyne
Michael Coyne
Chief Financial Officer

This certification accompanies this Annual Report on Form 10-K pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Registrant for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Such certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Exchange Act, except to the extent that the Registrant specifically incorporates it by reference.