# Meritage Hospitality Group Inc.

**Consolidated Financial Report**
**December 31, 2023 and January 1, 2023**

## Contents

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# Independent Auditor's Report

Board of Directors
Meritage Hospitality Group Inc., Subsidiaries and Affiliate
Grand Rapids, Michigan

### *Opinion*

We have audited the consolidated financial statements of Meritage Hospitality Group Inc., Subsidiaries and Affiliate (the Company), which comprise the consolidated balance sheets as of December 31, 2023 and January 1, 2023, and the related consolidated statements of operations and comprehensive income, equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2023 and January 1, 2023, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### *Basis for Opinion*

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Responsibilities of Management for the Financial Statements*

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

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern within one year after the date that the consolidated financial statements are available to be issued.

### *Auditor's Responsibilities for the Audit of the Financial Statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

BDO USA, P.C.

Grand Rapids, Michigan
March 6, 2024

## Meritage Hospitality Group Inc.

**Consolidated Balance Sheets**
(in thousands)

| | December 31, 2023 | January 1, 2023 |
|---|---|---|
| **Assets** | | |
| **Current Assets** | | |
| Cash | $ 19,434 | $ 35,372 |
| Receivables | 2,412 | 368 |
| Inventories | 5,189 | 4,754 |
| Prepaid expenses and other current assets | 7,101 | 6,619 |
| Total Current Assets | 34,136 | 47,113 |
| **Property and Equipment** - Net (Note 2) | 152,597 | 161,163 |
| **Goodwill** | 205,703 | 177,552 |
| **Intangible Assets** - Net (Note 3) | 7,580 | 6,132 |
| **Operating Lease Right-of-Use Assets** - Net (Note 4) | 399,156 | 379,343 |
| **Other Assets** | 17,733 | 20,015 |
| Total Assets * | **$ 816,905** | **$ 791,318** |
| **Liabilities and Equity** | | |
| **Current Liabilities** | | |
| Trade accounts payable | $ 21,958 | $ 28,445 |
| Lines of credit | 26,257 | 31,848 |
| Current portion of long-term debt (Note 7) | 20,365 | 14,041 |
| Current portion of operating lease obligations payable (Note 4) | 28,091 | 25,841 |
| Accrued liabilities (Note 6) | 21,773 | 25,826 |
| Total Current Liabilities | 118,444 | 126,001 |
| **Unearned Vendor Allowances** | 2,301 | 1,154 |
| **Operating Lease Obligations Payable** - Net of current portion (Note 4) | 376,946 | 359,318 |
| **Other Long-term Liabilities** | 17,093 | 16,720 |
| **Long-term Debt -** Net of current portion and financing costs (Note 7) | 164,278 | 155,107 |
| **Deferred Income Taxes** (Note 9) | 15,803 | 15,821 |
| Total Liabilities * | $ 694,865 | $ 674,121 |
| **Equity** | 122,040 | 117,197 |
| Total Liabilities and Equity | **$ 816,905** | **$ 791,318** |

See notes to consolidated financial statements.

* Total assets of the Variable Interest Entity were $21,081 and $16,925 as of December 31, 2023 and January 1, 2023, respectively. Total liabilities were $18,446 and $14,509 as of December 31, 2023 and January 1, 2023, respectively. See Note 14 for balance sheet information of the Variable Interest Entity.

## Meritage Hospitality Group Inc.

**Consolidated Statements of Operations and Comprehensive Income**
(in thousands, except per share data)

| | Fiscal Year Ended December 31, 2023 | Fiscal Year Ended January 1, 2023 |
|---|---|---|
| **Food and Beverage Revenue** | $ 672,494 | $ 626,043 |
| **Expenses** | | |
| Food and beverage | 184,247 | 172,001 |
| Labor and related | 213,808 | 201,852 |
| Occupancy | 86,806 | 77,942 |
| Advertising (Note 1) | 26,273 | 24,442 |
| Franchise fees | 25,439 | 23,818 |
| Other operating | 62,750 | 56,143 |
| Total Operating Expenses | 599,323 | 556,198 |
| General and administrative | 32,012 | 30,809 |
| Preopening, acquisition and closing | 4,809 | 7,645 |
| Depreciation and amortization | 18,552 | 17,418 |
| Total Expenses | 654,696 | 612,070 |
| **Income from Operations** | 17,798 | 13,973 |
| **Other Expense (Income)** | | |
| Interest - Net | 11,939 | 8,156 |
| Other - Net | (1,053) | (3,858) |
| Total Other Expense | 10,886 | 4,298 |
| **Income Before Income Taxes** | 6,912 | 9,675 |
| **Income Tax Expense** (Note 9) | 888 | 586 |
| **Consolidated Net Income** | **$ 6,024** | **$ 9,089** |
| **Net (Loss) Income Attributable to Noncontrolling Interest in Variable Interest Entity** | (114) | 604 |
| **Consolidated Comprehensive Net Income Attributable to Controlling Interest** | **$ 6,138** | **$ 8,485** |
| **Other Comprehensive (Loss) Income - Net of Tax** | | |
| Change in interest rate swap valuation (Note 8) | (2,617) | 7,557 |
| **Consolidated Comprehensive Net Income** | **$ 3,521** | **$ 16,042** |
| **Earnings per share** (Note 13) | | |
| Basic | $ 0.61 | $ 0.98 |
| Diluted | $ 0.56 | $ 0.84 |
| Basic Weighted Average Shares Outstanding | 6,512 | 6,585 |
| Diluted Weighted Average Shares Outstanding | 8,264 | 8,694 |

See notes to consolidated financial statements.

## Meritage Hospitality Group Inc.

**Consolidated Statements of Equity**
(in thousands)

| | Convertible Preferred Stock | Common Stock | Additional Paid-In Capital | Accumulated Other Comprehensive Income | Retained Earnings | Noncontrolling Interest | Total |
|---|---|---|---|---|---|---|---|
| **Balance** - January 2, 2022 | $ 14 | $ 66 | $ 31,143 | $ 1,402 | $ 73,133 | $ 2,926 | $ 108,684 |
| Net income | - | - | - | - | 8,485 | 604 | 9,089 |
| Issuance of common stock | - | 1 | 167 | - | - | - | 168 |
| Repurchase of common stock | - | (1) | (2,233) | - | - | - | (2,234) |
| Repurchase of preferred stock | - | - | (16) | - | - | - | (16) |
| Common stock dividends | - | - | - | - | (1,973) | - | (1,973) |
| Preferred stock dividends | - | - | - | - | (1,653) | - | (1,653) |
| Interest rate swap - net of tax | - | - | - | 7,557 | - | - | 7,557 |
| Company-owned stock | - | - | (1,221) | - | - | - | (1,221) |
| Stock option expense | - | - | 1,277 | - | - | - | 1,277 |
| Distributions | - | - | - | - | - | (2,481) | (2,481) |
| **Balance** - January 1, 2023 | $ 14 | $ 66 | $ 29,117 | $ 8,959 | $ 77,992 | $ 1,049 | $ 117,197 |
| Net Income (loss) | - | - | - | - | 6,138 | (114) | 6,024 |
| Issuance of common stock | - | - | 120 | - | - | - | 120 |
| Issuance of preferred stock | 1 | - | 3,047 | - | - | - | 3,048 |
| Repurchase of common stock | - | (1) | (177) | - | - | - | (178) |
| Common stock dividends | - | - | - | - | (1,173) | - | (1,173) |
| Preferred stock dividends | - | - | - | - | (1,813) | - | (1,813) |
| Interest rate swap - net of tax | - | - | - | (2,617) | - | - | (2,617) |
| Company-owned stock | - | - | (148) | - | - | - | (148) |
| Stock option expense | - | - | 1,618 | - | - | - | 1,618 |
| Contributions | - | - | - | - | - | 82 | 82 |
| Distributions | - | - | - | - | - | (120) | (120) |
| **Balance** - December 31, 2023 | $ 15 | $ 65 | $ 33,577 | $ 6,342 | $ 81,144 | $ 897 | $ 122,040 |

See notes to consolidated financial statements.

## Meritage Hospitality Group Inc.

**Consolidated Statements of Cash Flows**
(in thousands)

| | Fiscal Year Ended | |
|---|---|---|
| | December 31, 2023 | January 1, 2023 |
| **Cash Flows from Operating Activities** | | |
| Net Income | $ 6,024 | $ 9,089 |
| Adjustments to reconcile net income to net cash from operating activities: | | |
| Depreciation and amortization | 18,552 | 17,418 |
| Amortization of financing costs | 633 | 592 |
| Deferred income taxes (Note 9) | 305 | 92 |
| Loss on disposal of fixed assets | 1,448 | 3,597 |
| Loss (gain) on sale and leaseback transactions (Note 5) | 88 | (4,178) |
| Change in company-owned stock (Note 11) | (148) | (1,221) |
| Stock option expense | 1,618 | 1,277 |
| Changes in operating assets and liabilities which provided (used) cash, net of acquisitions: | | |
| Receivables | (2,044) | 1,236 |
| Inventories | 5 | (316) |
| Prepaid expenses and other current assets | (482) | (460) |
| Other assets | (1,261) | 677 |
| Trade accounts payable | (10,105) | 746 |
| Accrued liabilities | (4,153) | (3,321) |
| Unearned vendor allowances | 603 | (650) |
| Other long-term liabilities | 373 | 1,170 |
| Net cash provided by operating activities | 11,456 | 25,748 |
| **Cash Flows from Investing Activities** | | |
| Purchase of property and equipment | (44,796) | (65,660) |
| Purchase of intangible assets | (559) | (1,108) |
| Proceeds from sale of asset | 651 | - |
| Acquisitions (Note 17) | (30,125) | (16,474) |
| Net cash used in investing activities | (74,829) | (83,242) |

See notes to consolidated financial statements.

## Meritage Hospitality Group Inc.

**Consolidated Statements of Cash Flows**
(in thousands)

| | Fiscal Year Ended | |
|---|---|---|
| | December 31, 2023 | January 1, 2023 |
| **Cash Flows from Financing Activities** | | |
| Proceeds from long-term debt | 30,064 | 3,756 |
| Principal payments on long-term debt | (14,867) | (14,872) |
| Proceeds from lines of credit | 26,953 | 55,659 |
| Payments on lines of credit | (1,659) | (4,749) |
| Proceeds from sale and leaseback transactions (Note 5) | 38,198 | 41,943 |
| Payments on lines of credit related to sale and leaseback transactions (Note 5) | (30,884) | (31,589) |
| Payments on financing costs | (336) | - |
| Repurchase of common stock | (178) | (2,234) |
| Repurchase of preferred stock | - | (16) |
| Proceeds from issuance of common stock | 120 | 168 |
| Proceeds from issuance of preferred stock | 3,048 | - |
| Common stock dividends paid | (1,173) | (1,973) |
| Preferred stock dividends paid | (1,813) | (1,653) |
| Contributions from noncontrolling interest | 82 | - |
| Distributions to noncontrolling interest | (120) | (1,525) |
| Net cash provided by financing activities | 47,435 | 42,915 |
| **Net Decrease in Cash** | (15,938) | (14,579) |
| **Cash** - Beginning of period | 35,372 | 49,951 |
| **Cash** - End of period | $ 19,434 | $ 35,372 |

**Supplemental Disclosure of Cash Flow Information**

| | December 31, 2023 | January 1, 2023 |
|---|---|---|
| Cash paid for: | | |
| Interest | $ 11,196 | $ 7,963 |
| Income taxes | $ 394 | $ 814 |
| Significant non-cash investing and financing activities: | | |
| Conversion of property and equipment to asset held for sale | $ - | $ 699 |
| Change in fair value of swap - net of tax (Note 8) | $ (2,617) | $ 7,557 |
| Non-cash purchases of property | $ 3,229 | $ 5,961 |
| Operating lease ROU assets and liabilities obtained through acquisition | $ 24,083 | $ - |
| VIE ownership interest obtained from promissory note | $ - | $ (956) |

See notes to consolidated financial statements.

## Note 1 - Nature of Business and Significant Accounting Policies

Meritage Hospitality Group Inc., Subsidiaries and Affiliate, hereafter referred to as the "Company", conducts its business in the quick-service and casual dining restaurant industries across 16 states. As of December 31, 2023, the Company operated 376 Wendy's quick-service restaurants under franchise agreements with its franchisor, Quality Is Our Recipe, LLC, hereafter referred to as "The Wendy's Company" or "Wendy's," six Taco John's quick-service restaurants under franchise agreements with its franchisor, Taco John's International, Inc., hereafter referred to as "Taco John's", and six independent concept restaurants.

**Principles of Consolidation** - The consolidated financial statements include the accounts of Meritage Hospitality Group Inc., (the "Company"), its wholly owned subsidiaries, its 98.5% owned subsidiary, RDG-MHG, LLC ("RDG"), a 15% partner in TRG-Meritage Bahamas, LLC ("TRG"), and its affiliate variable interest entity ("VIE"), Restaurant Holdings, LLC ("Restaurant Holdings"), for which the Company is the primary beneficiary. The VIE is consolidated because the Company has the power to direct activities that impact the VIE's economic performance, as well as the right to receive benefits or the obligation to absorb losses from the VIE.

Earnings from Restaurant Holdings are reported as a noncontrolling interest in the accompanying consolidated statements of operations. All intercompany transactions and balances between the Company, its subsidiaries and Restaurant Holdings have been eliminated in consolidation.

**Segment Information** – Operating segments are components of an entity for which discrete financial information is available and regularly reviewed by the chief operating decision maker to allocate resources and assess performance. Resource allocation decisions are made based on the chief operating decision maker's evaluation of total Company operations. Accordingly, the Company views the operating results of its Wendy's, Taco John's, and independent concept restaurants as one operating and reportable segment.

**Fiscal Period** – The Company operates on a 52/53-week fiscal year ending on the Sunday closest to December 31 of each year. Each of the two fiscal years presented ending December 31, 2023 (referred to as fiscal year 2023) and January 1, 2023 (referred to as fiscal year 2022) contained 52 weeks.

**Revenue Recognition** - Revenues consist of restaurant food and beverage sales and are recorded net of applicable sales taxes and deferred revenue associated with the Wendy's Company app-based loyalty program ("Wendy's Rewards"). Food and beverage revenue is recognized at the time food is delivered to the customer and the performance obligation is satisfied. Payment in cash or credit is accepted at the time of transaction, and there is no variability in the transaction price as discounts and allowances are recognized at the point of sale. Fees paid to third party delivery providers are reported as other operating expenses on the consolidated statements of operations and are immaterial to the consolidated financial statements. The Company's gift card activity is managed by The Wendy's Company and Taco John's International, Inc. and is immaterial to its consolidated financial position.

The Wendy's Rewards program is offered at all the Company's Wendy's restaurants. For every dollar of a qualifying customer purchase by those enrolled in the Wendy's Rewards program, ten rewards points are earned. The Company defers a portion of qualifying revenue until rewards points are redeemed, forfeited or expired within a year of the date earned. Deferred revenue associated with Wendy's Rewards was $755 and $656 as of December 31, 2023 and January 1, 2023, respectively, and is classified in accrued liabilities on the consolidated balance sheets.

**Cash** - Cash includes cash on hand in the restaurants and cash held in banks. At times, cash balances at financial institutions are in excess of FDIC insurance coverage. The cash balances are maintained at financial institutions with high credit quality ratings, and the Company believes no significant risk of loss exists with respect to those balances.

**Receivables** - Receivables consist of trade and other receivables. Trade receivables consist of gift cards redeemed at the Company's restaurants and amounts due from unsettled debit and credit card sales. No allowance for expected credit losses is deemed necessary.

**Inventories** - Inventories consist of restaurant food items, beverage and beverage supplies, and paper supplies. Inventories are stated at the lower of cost or net realizable value, with cost determined on the first-in, first-out (FIFO) method.

**Property and Equipment** - Property and equipment is stated at cost. Depreciation is computed principally using the straight-line method based upon estimated useful lives ranging from three to 15 years for furniture and equipment and up to 30 years for buildings. Leasehold improvements are amortized over the shorter of their estimated useful lives or the terms of the various leases. Repairs and maintenance costs that do not add to the value or increase the life of an asset are expensed when incurred. Interest costs on borrowings are capitalized during the construction period of the restaurant. Interest of $618 and $300 was capitalized in fiscal year 2023 and 2022, respectively (see Note 2).

**Goodwill** – The Company allocates the purchase price of acquisitions to its identifiable assets and liabilities based on the estimated fair values using all available information. For certain valuations, the Company may engage an independent third-party valuation specialist. The excess of purchase price over the amount allocated to assets and liabilities is recorded as goodwill.

The Company reviews goodwill for impairment annually in the fourth quarter or when indications of potential impairment or a triggering event occurs. If the carrying amounts of these assets are deemed to be less than fair value based upon a discounted cash flow analysis and comparison to comparable earnings multiples of peer companies, such assets are reduced to their estimated fair value and a charge is made to operations. For fiscal years 2023 and 2022, the tests indicated no goodwill impairment.

**Franchise Rights and Agreement Costs** - Franchise rights and agreement costs, capitalized in connection with the Company's Wendy's restaurants, are amortized using the straight-line method over the terms of each individual franchise agreement, including extension options, given the Company's historical pattern and economic incentive to renew. Franchise agreement costs, capitalized in connection with the Company's Taco John's restaurants, are amortized using the straight-line method over the terms of each individual franchise agreement (see Note 3).

**Financing Costs** - Financing costs are capitalized and amortized using the straight-line method, which approximates the effective interest rate method, over the terms of the various loan agreements. These costs are a reduction in the balance of the related outstanding debt (see Note 7).

**Fair Value of Financial Instruments** – Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability between market participants. Accounting standards require the Company to categorize its financial assets and liabilities into a three-level fair value hierarchy. Based on the nature of inputs used, the three levels of the fair value hierarchy under fair value accounting are described as follows:

Level I – Valuation is based upon quoted prices for identical assets or liabilities in active markets.

Level II – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level III – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. The unobservable assumptions reflect the estimates of assumptions that market participants would use in pricing the asset or liability.

The Company's financial instruments, which are not required to be measured at fair value on a recurring basis on the consolidated balance sheets, consist of the following:

Short-Term Financial Instruments – The fair values of short-term financial instruments, including cash, receivables, trade accounts payable, and accrued liabilities (Level I) approximate the carrying amounts in the accompanying consolidated financial statements due to the short maturity of such instruments. The Company's revolving line of credit is variable rate, and therefore has a fair value that approximates its carrying value (Level II).

Long-Term Obligations – The fair value of long-term debt obligations at December 31, 2023 and January 1, 2023 are based on estimated rates currently available to the Company at year-end and debt obligations with similar terms and maturities. Debt obligations carry variable rates of interest and thus approximate fair value. Debt is classified as Level II under the fair value hierarchy.

The Company's financial instruments on the consolidated balance sheets are required to be measured at fair value on a recurring basis and consist of the following Level II financial instruments:

Interest rate swaps – The Company measures its interest rate swaps at fair value on a recurring basis. The fair value of the swap is provided by a counterparty and is based primarily on inputs such as interest rates and Secured Overnight Financing Rate ("SOFR") yield curves that are observable at commonly quoted intervals and other observable market inputs.

Deferred compensation plan - Investments under the Company's deferred compensation plan are measured and carried at fair value based on the quoted prices in active markets for identical assets, and other observable inputs reflecting market assumptions that market participants would use in pricing.

**Self-Insurance** – The Company's restaurants in Michigan are self-insured for workers' compensation claims up to a $500 per claim stop-loss level with no maximum aggregate. The Company determines its liability based on estimated loss reserves provided by the Company's third-party claims administrator and on management's knowledge of open claims.

Beginning in 2023, the Company elected to act as self-insurer for group health insurance for its employees. The Company had stop-loss coverage through an insurance carrier that covers claims exceeding $175 per person, including dependents, with an aggregate limitation of $3,838. As of December 31, 2023, the Company recorded a liability of $61 for these claims, which is included in other accrued liabilities on the consolidated balance sheets. This accrual includes a provision for estimated claims incurred and not reported. The self-insured healthcare claims and premiums expensed by the Company were $2,994 for 2023.

**Unearned Vendor Allowances** - Up-front consideration received from vendors linked to future purchases is initially deferred, then recognized as earned income as the purchases occur over the term of the vendor arrangement. During fiscal years 2023 and 2022, the Company received $10,162 and $8,279, respectively, in funds that are recognized as a reduction of cost of food and beverage as products are purchased.

**Earnings per Share -** Basic earnings per common share is computed by dividing net income attributable to controlling interest, after the deduction of preferred stock dividends, by the number of weighted average common shares outstanding and dilutive shares. Diluted earnings per common share is computed on the weighted average common shares outstanding plus dilutive shares using the treasury stock method for stock options, and the if-converted method for convertible preferred shares (see Note 13).

**Interest Rate Swaps** – The Company has interest rate swap derivatives for the purpose of hedging risks related to the variability of cash flows caused by interest rate fluctuations. Interest rate swaps are measured at fair value on a recurring basis and are recognized in other assets and other long-term liabilities on the accompanying consolidated balance sheets accordingly.

The Company's interest rate swap is designated as a cash flow hedge for financial reporting purposes. Under this designation, changes in fair value are recorded in other comprehensive income, net of tax, until the hedge transaction occurs. The Company classifies the cash flows from derivatives that are accounted for as a cash flow hedge in the same category as the cash flows from the items being hedged (see Note 8).

**Stock-Based Compensation** - The Company measures compensation expense for stock options based on the fair value of the awards on the grant date. Compensation expense for grants is recognized ratably over the vesting period of the awards. Company policy recognizes forfeiture expense as incurred. The Company issues common shares when stock options are exercised (see Note 12).

**Advertising Costs** - Advertising costs and fees due under the Company's franchise agreements are based primarily on a percentage of monthly food and beverage revenue. These costs are charged to operations as incurred and are included in advertising expense on the consolidated statements of operations. Total advertising expense was $26,273 and $24,442 for fiscal years 2023 and 2022, respectively.

**Income Taxes** - A current tax liability or asset is recognized for the estimated taxes payable or refundable on tax returns for the year. Deferred tax liabilities or assets are recognized for the estimated future tax effects of temporary differences between financial reporting and tax accounting and are based on the difference between the financial statement and tax basis of assets and liabilities measured by the current tax rate. The deferred tax provision generally represents the net change in deferred tax assets and liabilities during the period including any changes in valuation allowances. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in the results of operations in the period that includes the enactment date. A valuation allowance is established when it is more likely than not that some or all of the deferred tax assets will not be realized. The Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not the tax position will be sustained on examination by the taxing authorities. The Company and its subsidiaries file a consolidated federal income tax return.

Restaurant Holdings is treated as a partnership for federal income tax purposes. Consequently, federal income taxes are not payable or provided for by Restaurant Holdings. Restaurant Holdings' members are taxed individually on their pro-rata ownership share of its earnings which is allocated among the members in accordance with the Restaurant Holdings operating agreement (see Note 9).

**Use of Estimates** - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management 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 consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. The Company bases its estimates on historical experience and on various other assumptions believed to be reasonable under the circumstances; however, actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the assessment of impairment of long-lived assets and goodwill.

(in thousands, except share data)

**New Accounting Standards –** In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. ASC 326 requires financial assets measured at amortized cost basis to be presented at the net amount expected to be collected. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. The guidance is effective for fiscal years beginning after December 15, 2022. The Company adopted ASU 2016-13 in January 2023. The adoption did not have a material effect on the consolidated financial statements and related disclosures.

**Reclassification** – Certain fiscal year 2022 amounts have been reclassified to conform to the fiscal year 2023 presentation.

**Subsequent Events** – The consolidated financial statements and related disclosures include evaluation of events up through and including March 6, 2024, the date the consolidated financial statements were issued.

## Note 2 - Property and Equipment

Property and equipment are summarized as follows:

| | 2023 | 2022 |
|---|---|---|
| Land and improvements | $ 29,201 | $ 34,505 |
| Buildings and improvements | 80,911 | 72,499 |
| Furnishings and equipment | 112,817 | 98,403 |
| Leasehold improvements | 24,099 | 23,230 |
| Construction in progress | 11,875 | 23,660 |
| Total cost | $ 258,903 | $ 252,297 |
| Accumulated depreciation | (106,306) | (91,134) |
| Net property and equipment | $ 152,597 | $ 161,163 |

As of December 31, 2023, the Company estimates costs of $1,600 to complete construction in progress.

Depreciation expense was $18,264 and $17,190 for fiscal years 2023 and 2022, respectively.

The Company owned certain land and buildings classified as assets held for sale within other assets on the consolidated balance sheets. As of December 31, 2023 and January 1, 2023, related assets were carried at an aggregate fair market value of $713 and $1,168, respectively.

(in thousands, except share data)

## Note 3 – Intangible Assets

Intangible assets consist of capitalized franchise rights and agreement costs less accumulated amortization, and are summarized as follows:

| | 2023 | 2022 |
|---|---|---|
| Franchise rights and agreement costs | $ 9,054 | $ 7,352 |
| Accumulated amortization | (1,474) | (1,220) |
| Net | $ 7,580 | $ 6,132 |

Amortization expense for franchise rights and agreement costs were $277 and $217 for fiscal years 2023 and 2022, respectively. The weighted average remaining life through the next renewal period is approximately 18 years for Wendy's and 19 years for Taco John's.

Amortization expense is projected as follows:

| | |
|---|---|
| 2024 | $ 301 |
| 2025 | 301 |
| 2026 | 301 |
| 2027 | 300 |
| 2028 | 300 |
| Thereafter | 6,077 |
| Total | $ 7,580 |

## Note 4 - Leases

The Company has operating lease agreements for unowned restaurants, the corporate office, and certain equipment. Land and building leases used in operations have remaining lease terms ranging from one to 20 years, some of which include options to renew for up to 50 years.

On the consolidated balance sheets, operating leases are included in operating lease right-of-use (“ROU”) assets, operating lease obligations payable, and current portion of operating lease obligations payable.

Upon commencement date, operating lease ROU assets and operating lease liabilities are recognized based on the present value of future minimum lease payments over the lease term. The Company's lease terms may include options to extend or terminate the lease. The present value of future minimum lease payments includes these options only when it is reasonably certain such options will be exercised.

The Company’s leases do not provide an implicit rate. In determining present value of future minimum lease payments, the Company utilized an incremental borrowing rate congruent with its primary lending agreement, which is the rate for a fully collateralized, amortizing loan with the same term as the lease. The weighted average effective discount rates were 4.9% and 4.5% as of December 31, 2023 and January 1, 2023, respectively.

(in thousands, except share data)

Base rent expense includes non-lease components such as taxes, insurance, and maintenance when required under the lease agreements and is classified as occupancy expense in the consolidated statements of operations. The Company elected the practical expedient to not separate non-lease components from the lease components to which they relate. For certain equipment leases, the Company applies a portfolio approach to effectively account for the operating lease ROU assets and liabilities.

Variable rent expense components are expensed as incurred and represent rent escalators of which the majority are contingent upon changes in the Consumer Price Index. Variable rent expense also includes percentage rentals which represent additional rent due under certain leases for which the Company is required to pay a percentage of sales in excess of minimum prescribed amounts.

Rent expense from operating leases were recognized as follows:

| | 2023 | 2022 |
|---|---|---|
| Operating lease costs: | | |
| Fixed base lease expense - real estate | $ 43,672 | $ 40,089 |
| Fixed base lease expense - equipment | 2,034 | 1,920 |
| Variable rent expense | 1,450 | 1,164 |
| Total | $ 47,156 | $ 43,173 |

Supplemental cash flow information related to operating leases was as follows:

| | 2023 | 2022 |
|---|---|---|
| Cash paid for amounts included in the measurement of lease liabilities | $ 45,397 | $ 41,952 |
| Right-of-use assets obtained in exchange for lease obligations | $ 49,873 | $ 45,320 |

The weighted-average remaining lease terms for operating leases were approximately 14 and 15 years as of December 31, 2023 and January 1, 2023, respectively.

(in thousands, except share data)

The future payments due under operating leases as of December 31, 2023 are projected as follows:

| | | |
|---|---|---|
| 2024 | $ | 46,787 |
| 2025 | | 46,053 |
| 2026 | | 41,777 |
| 2027 | | 39,591 |
| 2028 | | 38,020 |
| Thereafter | | 344,870 |
| Total | $ | 557,098 |
| Less present value discount | | (152,061) |
| Lease liability recognized | $ | 405,037 |

**Note 5 – Sale and Leasebacks**

The Company completed 16 sale and leaseback transactions in each of the fiscal years 2023 and 2022. Through these transactions, the Company netted proceeds of $38,198 and $41,943, paid down indebtedness of $30,884 and $31,589, and recorded a net loss of $88 and net gain of $4,178 for fiscal years 2023 and 2022, respectively. Resulting gains and losses were recorded in other income on the consolidated statements of operations.

**Note 6 - Accrued Liabilities**

The following is a detail of accrued liabilities:

| | | 2023 | | 2022 |
|---|---|---|---|---|
| Payroll and related payroll taxes | $ | 12,850 | $ | 14,207 |
| Property taxes | | 1,199 | | 1,391 |
| Sales tax | | 3,270 | | 3,329 |
| Self-insurance | | 1,049 | | 870 |
| Other | | 3,405 | | 6,029 |
| Total | $ | 21,773 | $ | 25,826 |

Other accrued liabilities included approximately $112 and $2,800 of settlement obligations related to the permanent closure of under-performing restaurants as of December 31, 2023 and January 1, 2023, respectively.

(in thousands, except share data)

**Note 7 - Long-Term Debt and Revolving Lines of Credit**

Long-term debt consists of the following:

| | 2023 | 2022 |
|---|---|---|
| Mortgage note payable - variable rate, due in monthly installments of $46 plus interest of SOFR plus a margin ranging from 1.85% through 2.50% (effective rate of 7.83% and 6.83% at December 31, 2023 and January 1, 2023, respectively), maturing in April 2027. | $ 14,174 | $ 14,712 |
| Term note payable - variable rate, due in monthly installments of $829 plus interest of SOFR plus a margin ranging from 1.85% through 2.50% (effective rate of 7.81% and 6.79% at December 31, 2023 and January 1, 2023, respectively), maturing in April 2027. | 97,943 | 107,632 |
| Term note payable - variable rate, due in monthly installments of $277 plus interest of SOFR plus a margin ranging from 1.85% through 2.50% (effective rate of 7.83% and 6.83% at December 31, 2023 and January 1, 2023, respectively), maturing in April 2027. | 39,006 | 42,241 |
| Term note payable - variable rate, due in monthly installments of $22 plus interest of SOFR plus a margin ranging from 1.85% through 2.50% (effective rate of 7.83% and 6.83% at December 31, 2023 and January 1, 2023, respectively), maturing in April 2027. | 3,422 | 3,673 |
| Term note payable - variable rate, due in quarterly installments of $63 plus monthly interest payments of SOFR plus 4.11% (effective rate of 9.46% and 8.47% at December 31, 2023 and January 1, 2023, respectively), maturing in May 2024. | 2,125 | 2,375 |
| Term note payable - variable rate, due in monthly installments totaling $220 including interest payments of SOFR plus 2.10% (effective rate of 7.46% at December 31, 2023), maturing in May 2028. | 20,359 | - |

(in thousands, except share data)

| | 2023 | 2022 |
|---|---|---|
| Term note payable - fixed rate, due in monthly installments totaling $10 (including interest of 4.75%), maturing in January 2033. | 866 | 925 |
| Term note payable - fixed rate, due in monthly installments totaling $23 (including interest of 7.75%), maturing in January 2028. | 964 | - |
| Term note payable - fixed rate, due in monthly installments totaling $9 (including interest of 8.50%), maturing in July 2028. | 395 | - |
| Term note payable - fixed rate, due in monthly interest only installments totaling $48 (interest of 7.50%), maturing in May 2025. | 7,500 | - |
| Total | 186,754 | 171,558 |
| Less unamortized financing costs | (2,111) | (2,410) |
| Less current portion | (20,365) | (14,041) |
| Long-term portion | $ 164,278 | $ 155,107 |

The total of the above debt matures as follows:

| | |
|---|---|
| 2024 | $ 20,365 |
| 2025 | 21,513 |
| 2026 | 17,310 |
| 2027 | 111,734 |
| 2028 | 15,336 |
| Thereafter | 496 |
| Total | $ 186,754 |

The Company has a revolving line of credit agreement with its primary lender that expires in April 2027 and allows for borrowings up to $35,000 as of December 31, 2023 and January 1, 2023, respectively. The revolving line of credit uses SOFR as the reference rate plus a margin ranging from 1.85% through 2.50%. Outstanding borrowings were $9,881 and $22,198 and had effective interest rates of 7.83% and 6.83% at December 31, 2023 and January 1, 2023, respectively.

Restaurant Holdings has a revolving line of credit agreement with its primary lender that expires March 2024. As of the date of this report, the Company is in negotiations to extend the terms of this agreement. As of December 31, 2023, the line of credit allows for borrowings up to $57,500 less the outstanding balance on the entity's term note payable of $2,125. The revolving line of credit uses SOFR as the reference rate plus a margin of 4.19%. Outstanding borrowings were $14,149 and $9,650 and had effective interest rates of 9.54% and 8.55% at December 31, 2023 and January 1, 2023, respectively.

The Company has a flexible development line of credit with its primary lender that expires in August 2024 and allows for borrowings up to $74,017 and $76,244 as of December 31, 2023 and January 1, 2023, respectively. As of the date of this report, the Company is in negotiations to extend the terms of this agreement. The flexible development line of credit uses SOFR as the reference rate plus a margin ranging from 1.85% through 2.50%. As of December 31, 2023 and January 1, 2023, outstanding borrowings were $2,227 and $0 and had effective interest rates of 7.83% and 6.83%, respectively.

Beginning in 2023, the Company had an additional flexible development line of credit with one of its secondary lenders that expires in May 2028 and allows for borrowings up to $3,500 as of December 31, 2023. The flexible development line of credit uses SOFR as the reference rate plus a margin of 2.10%. As of December 31, 2023, the line had an effective interest rate of 7.46% and zero borrowings outstanding.

Substantially all property and equipment owned by the Company is pledged as collateral for the Company's long-term debt and lines of credit.

Loan covenants of the Company's various loan agreements include requirements for the maintenance of certain financial ratios. As of December 31, 2023 and January 1, 2023, the Company was in compliance with these covenants.

## Note 8 – Interest Rate Swaps

The Company has entered into an amortizing interest rate swap agreement to economically manage variability of cash flows associated with its variable rate debt. Both the debt and interest rate swap mature in April 2027. Notional amounts outstanding were $97,943 and $107,632 at December 31, 2023 and January 1, 2023, respectively. Related fair values of the amortizing interest rate swaps were $7,448 and $10,388 at December 31, 2023 and January 1, 2023, respectively.

The Company designated its interest rate swap as a cash flow hedge of variable rate interest payments related to its term loan payable. Under this designation, changes in fair value of the interest rate swap are recognized through other comprehensive income ("OCI"), a component of equity.

The change in fair value of the swap agreement generated unrealized losses of $2,617 in 2023 and unrealized gains of $7,557 in 2022. Such gains and losses were recognized through other comprehensive income, a component of equity. Based on related debt balances, the Company anticipates the amount to be reclassified as a component of interest expense in fiscal year 2024 to be immaterial.

The Company recognized gains on the interest rate swap of $4,269 and $551 in fiscal years 2023 and 2022, respectively. Gains were reflected as a component of interest expense on the consolidated statement of operations.

(in thousands, except share data)

**Note 9 – Taxes**

Deferred tax assets and liabilities consist of:

| | 2023 | 2022 |
|---|---|---|
| Deferred tax assets: | | |
| Accrued rents | $ 1,695 | $ 1,617 |
| General business credit | 6,883 | 5,635 |
| Interest expense carryforward | 3,991 | 1,712 |
| Stock based compensation | 5,982 | 5,453 |
| Other | 1,112 | 1,809 |
| Total deferred tax assets | 19,663 | 16,226 |
| Deferred tax liabilities: | | |
| Depreciation, amortization, and basis differences | (33,780) | (30,038) |
| SWAP agreement OCI | (1,686) | (2,009) |
| Total deferred tax liabilities | (35,466) | (32,047) |
| Net deferred tax liabilities | $ (15,803) | $ (15,821) |

The Company regularly assesses the realizability of its deferred tax assets and the related need for, and amount of, a valuation allowance. Management considers many factors in determining the likelihood of future realization of the deferred tax assets including recent cumulative earnings and loss experience, future reversals of existing temporary differences, and carryforwards.

The general business credits listed above expire between 2040 and 2043.

The income tax provision reconciled to the tax computed at the statutory state and federal rates for the fiscal years ended 2023 and 2022 was as follows:

| | 2023 | 2022 |
|---|---|---|
| Tax expense at statutory rate of 21% applied to income before taxes | $ 1,407 | $ 2,072 |
| State taxes (net of federal benefit) | 332 | 326 |
| Permanent differences | 434 | 264 |
| Impact of tax credits | (1,584) | (1,657) |
| Noncontrolling interest | (58) | (206) |
| Other - net | 357 | (213) |
| | $ 888 | $ 586 |

(in thousands, except share data)

The provision for income taxes consists of the following:

| | 2023 | 2022 |
|---|---|---|
| Current expense | $ 583 | $ 494 |
| Deferred expense | 305 | 92 |
| Total income tax expense | $ 888 | $ 586 |

As of December 31, 2023 and January 1, 2023, the Company's unrecognized tax benefits were not significant. There were no significant penalties or interest recognized or accrued during 2023 and 2022.

## Note 10 - Equity

The Company has 5,000,000 authorized shares of $0.01 par value preferred stock. As of December 31, 2023 and January 1, 2023, preferred stock was designated as follows:

| | 2023 | 2022 |
|---|---|---|
| Preferred B: | | |
| Authorized: | 1,350,000 | 1,350,000 |
| Outstanding: | 805,400 | 805,400 |
| Treasury: | 3,467 | 3,467 |
| Preferred C: | | |
| Authorized: | 200,000 | 200,000 |
| Outstanding: | 160,360 | 160,360 |
| Preferred D: | | |
| Authorized: | 600,000 | 600,000 |
| Outstanding: | 310,293 | 310,293 |
| Preferred E: | | |
| Authorized: | 800,000 | 800,000 |
| Outstanding: | 128,744 | 128,744 |
| Preferred F: | | |
| Authorized: | 1,000,000 | - |
| Outstanding: | 130,606 | - |

The Series B nonvoting convertible preferred stock has a cumulative annual dividend rate of $0.80 per share. After one year from the date of issuance, shares are convertible by the shareholder into common shares at $5.57 per share and have a liquidation value of $10.00 per share. The Company may (but is not required to) redeem the preferred shares at a price of $10.00 per share plus accrued but unpaid dividends. The Series B Preferred shares of the Company are quoted on the OTC Markets under the symbol "MHGUP."

The Series C nonvoting convertible preferred stock has a cumulative annual dividend rate of $1.50 per share. After one year from the date of issuance, shares are convertible by the shareholders into common shares at $13.50 per share and have a liquidation

value of $25.00 per share. The Company may (but is not required to) redeem the preferred shares at a price of $28.00 per share plus accrued but unpaid dividends.
The Series D nonvoting convertible preferred stock has a cumulative annual dividend rate of $1.75 per share. After one year from the date of issuance, shares are convertible by the shareholders into common shares at $24.00 per share and have a liquidation value of $25.00 per share. The Company may (but is not required to) redeem the preferred shares at a price of $28.00 per share plus accrued but unpaid dividends.

The Series E nonvoting convertible preferred stock has a cumulative annual dividend rate of $1.75 per share. After one year from the date of issuance, shares are convertible by the shareholders into common shares at $21.00 per share and have a liquidation value of $25.00 per share. The Company may (but is not required to) redeem the preferred shares at a price of $28.00 per share plus accrued but unpaid dividends.

The Series F nonvoting convertible preferred stock has a cumulative annual dividend rate of $1.875 per share. After one year from the date of issuance, shares are convertible by the shareholders into common shares at $24.00 per share and have a liquidation value of $25.00 per share. During the two years from the date of issuance, the Company may (but is not required to) redeem the preferred shares at a price of $26.00 per share plus accrued but unpaid dividends. After two years from the date of issuance, the redemption price is $28.00.

The Company has 30,000,000 authorized shares of $0.01 par value common stock, with 6,517,965 and 6,503,924 shares issued and outstanding as of December 31, 2023 and January 1, 2023, respectively. There were 602,950 and 594,840 treasury shares as of December 31, 2023 and January 1, 2023, respectively. The common shares of the Company are quoted on the OTC Markets under the symbol “MHGU.”

## Note 11 - Employee Benefit Plans

The Company has a deferred compensation plan (the “Plan”) for the benefit of certain employees. Plan investments are participant directed, and vest in accordance with a predetermined vesting schedule. The Plan provides for the payment of benefits for a period of up to 10 years. Other long-term obligations related to deferred compensation under the Plan were $15,633 and $14,016 as of December 31, 2023 and January 1, 2023, respectively. Deferred compensation benefit earned was $711 and $1,178 in fiscal years ended December 31, 2023 and January 1, 2023, respectively.

The Company has funded the Plan obligation with Company-owned life insurance policies with cash surrender values of $7,549 and $6,484 at December 31, 2023 and January 1, 2023, respectively, and are included in other assets on the consolidated balance sheets. The plan is additionally funded with investments of $6,974 and $6,827 at December 31, 2023 and January 1, 2023, respectively. Of these investments, $6,970 was invested in 321,321 shares of Company Common stock and 39,375 shares of Company Series B Preferred Stock as of December 31, 2023. There was $6,822 invested in 276,674 shares of Company Common stock and 39,375 shares of Company Series B Preferred Stock as of January 1, 2023. Investments in Company-owned stock are recorded as a reduction in equity on the consolidated balance sheets.

(in thousands, except share data)

The Company sponsors a 401(k) plan for the benefit of substantially all employees. To be eligible for plan participation, employees must have completed one month of service and be 21 years of age or older. The 401(k) plan allows employees to contribute a portion of their compensation and, after one year of service, provides for the Company to make discretionary matching contributions. All contributions vest in accordance with a predetermined vesting schedule. Employer contributions to the plan were $394 and $399 for the years ended December 31, 2023 and January 1, 2023, respectively.

## Note 12 - Stock Option Plans

The Company has management and director share-based compensation plans which are described below. The compensation expenses charged against income for the plans were $1,618 and $1,277 for fiscal years 2023 and 2022, respectively. The total income tax benefit recognized in the consolidated statements of operations for share-based compensation arrangements was $198 and $166 for fiscal year 2023 and 2022, respectively.

The employee equity incentive plans provide for the discretionary grant of options. The current plan authorizes 2,000,000 shares of common stock to be granted for options that may be issued under the plan. The Board of Directors has the discretion to designate an option to be an incentive share option or a non-qualified share option. The plans provide that the exercise price is not less than the fair market value of the common stock at the date of grant. Options granted under the plans become exercisable pursuant to a vesting schedule adopted by the Board of Directors which administer the plans. Options have a term of 10 years and vest ratably over three years from the grant date.

The directors' share option plans provide for the non-discretionary grant of options to non-employee directors of the Company. The current plan allows for the grant of options for a maximum of 1,000,000 shares at option prices equal to the last closing sales price of the common stock on the date of grant. The plan provides that each non-employee director is granted options to purchase 10,000 shares on the date such person becomes a non-employee director and on the date of each annual shareholders' meeting thereafter. Additional options may be granted by the Board of Directors, from time to time, on such terms and conditions as it determines appropriate. Options granted under the plan have a term of 10 years and vest ratably over three years from the date of grant.

The fair value of each option award is estimated on the date of grant using the Black Scholes option valuation model that uses the following weighted average assumptions, ignoring dividends:

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | Low | High | Low | High |
| Risk-free Interest Rates | 3.52% | 4.53% | 1.71% | 4.31% |
| Expected Life | 5.00 | 8.66 | 5.46 | 8.55 |
| Expected Volatility | 30.41% | 33.17% | 30.36% | 33.42% |

(in thousands, except share data)

Expected volatilities are based on historical volatility of the Company's weekly stock price. The Company uses historical data to estimate option exercise and employee termination when determining the expected life within the valuation model. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

A summary of option activity under the employee plans for the years ended December 31, 2023 and January 1, 2023 is presented below:

| Options | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (in Years) |
|---|---|---|---|
| Outstanding at January 2, 2022 | 963,500 | $ 15.62 | - |
| Granted | 145,000 | 21.49 | - |
| Exercised | (22,000) | 3.55 | - |
| Forfeited or expired | (15,000) | 20.99 | - |
| Outstanding at January 1, 2023 | 1,071,500 | 16.58 | 5.6 |
| | | | |
| Outstanding at January 1, 2023 | 1,071,500 | $ 16.58 | - |
| Granted | 160,000 | 19.50 | - |
| Exercised | (10,000) | 2.75 | - |
| Forfeited or expired | (30,000) | 20.21 | - |
| Outstanding at December 31, 2023 | 1,191,500 | 17.00 | 5.0 |

The breakdown of outstanding employee stock options as of December 31, 2023 is as follows:

| Options | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (in Years) |
|---|---|---|---|
| Options excercisable | 1,019,000 | $ 16.46 | 4.4 |
| Nonvested options | 172,500 | 20.21 | 8.4 |

Total options outstanding represent aggregate intrinsic value of $3,508 and $3,535 as of December 31, 2023 and January 1, 2023, respectively. There were 10,000 and 22,000 options exercised with intrinsic value of $169 and $364 in 2023 and 2022, respectively. The fair value of stock options awarded during 2023 and 2022 was $1,212 and $1,049, respectively. As of December 31, 2023, total unrecognized compensation expense related to non-vested stock options was $1,023. This expense will be recognized over approximately 2.2 years.

(in thousands, except share data)

A summary of option activity under the directors' plans for the years ended December 31, 2023 and January 1, 2023 is presented below:

| Options | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (in Years) |
|---|---|---|---|
| Outstanding at January 2, 2022 | 503,333 | $ 12.75 | - |
| Granted | 70,000 | 19.93 | - |
| Exercised | (50,000) | 2.69 | - |
| Forfeited or expired | - | - | - |
| Outstanding at January 1, 2023 | 523,333 | 14.67 | 5.6 |
| | | | |
| Outstanding at January 1, 2023 | 523,333 | $ 14.67 | - |
| Granted | 60,000 | 17.25 | - |
| Exercised | (10,000) | 3.15 | - |
| Forfeited or expired | - | - | - |
| Outstanding at December 31, 2023 | 573,333 | 15.16 | 5.3 |

The breakdown of outstanding director stock options as of December 31, 2023 is as follows:

| Options | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (in Years) |
|---|---|---|---|
| Options excercisable | 446,666 | $ 14.08 | 4.3 |
| Nonvested options | 126,667 | 18.95 | 8.9 |

Total options outstanding represent aggregate intrinsic value of $2,520 and $2,497 as of December 31, 2023 and January 1, 2023, respectively. There were 10,000 and 50,000 options exercised with intrinsic value of $163 and $922 in 2023 and 2022, respectively. The fair value of stock options awarded during 2023 and 2022 was $463 and $605, respectively. As of December 31, 2023, total unrecognized compensation expense related to non-vested stock options was $722. This expense will be recognized over approximately 2.4 years.

(in thousands, except share data)

## Note 13 – Earnings per Share

Earnings per share as of December 31, 2023 and January 1, 2023 was calculated as follows:

| | 2023 | 2022 |
|---|---|---|
| Income attributable to controlling interest | $ 6,138 | $ 8,485 |
| Less: Preferred stock dividends | (2,186) | (2,026) |
| Income available to common shareholders | $ 3,952 | $ 6,459 |
| Weighted average basic shares outstanding | 6,512 | 6,585 |
| Basic EPS | $ 0.61 | $ 0.98 |
| | | |
| Income available to common shareholders | $ 3,952 | $ 6,459 |
| Add: Dividends on dilutive preferred stock | 645 | 885 |
| Income available to common shareholders | $ 4,597 | $ 7,344 |
| Weighted average basic shares outstanding plus assumed conversions | 8,264 | 8,694 |
| Diluted EPS | $ 0.56 | $ 0.84 |

## Note 14 – Information About Variable Interest Entity

Restaurant Holdings was formed to facilitate real estate transactions where the Company has potential economic benefits in future sale and leaseback transactions. This variable interest entity ("VIE") is owned by related parties and not directly by the Company. Restaurant Holdings is consolidated due to the Company's power to direct activities that impact its economic performance, as well as the right to receive benefits or the obligation to absorb losses from Restaurant Holdings that could potentially be significant.

The Company's senior credit facility requires the Company to finance acquisitions of real estate with a minimum of 25% of the purchase price in equity. The Company believes this requirement restricts its long-term real estate strategy. The purpose of Restaurant Holdings is to provide a source of capital to fund the purchase of restaurant real estate and, when sold, provide potential upside to the Company. Upon acquisition of real estate, Restaurant Holdings leases such real estate to the Company and utilizes rent revenue to pay the interest expense on its bank debt.

Restaurant Holdings leverages a revolving credit facility with a bank other than the Company's senior lender that allows for borrowings up to $55,375 secured by its interest in the real estate and personal guarantees of owners. Restaurant Holdings additionally entered into a note payable resulting from the purchase of a partnership interest in 2022 with an outstanding balance of $866 and $925 as of December 31, 2023 and January 1, 2023, respectively.

(in thousands, except share data)

Included in the consolidated balance sheets as of December 31, 2023 and January 1, 2023 are the following amounts related to Restaurant Holdings, before eliminating entries:

| | 2023 | 2022 |
|---|---|---|
| Assets: | | |
| Current assets | $ 386 | $ 1,450 |
| Property and equipment - net | 14,982 | 9,307 |
| Other assets | 713 | 1,168 |
| Investment in MHGI preferred stock | 5,000 | 5,000 |
| Total Assets | $ 21,081 | $ 16,925 |
| Liabilities: | | |
| Current liabilities | $ 1,305 | $ 1,559 |
| Current portion of long-term debt | 2,144 | 328 |
| Revolving line of credit | 14,149 | 9,650 |
| Long-term debt | 848 | 2,972 |
| Total Liabilities | $ 18,446 | $ 14,509 |
| Equity - Noncontrolling interest | 2,635 | 2,416 |
| Total Liabilities and Equity | $ 21,081 | $ 16,925 |

**Note 15 - Related Party Transactions**

The Company's CEO has provided personal guarantees to The Wendy's Company to facilitate the granting of certain Wendy's franchise agreements.

The Company's CEO and President are each 39.5% owners in the Company's VIE for which the Company is a primary beneficiary (see Note 1).

The Company repurchased 9,110 and 159,523 common stock shares from certain Board members at market price during fiscal years 2023 and 2022, respectively.

The Company's CEO and President were each 50.0% owners of a related party entity that leased real property to one of the Company's independent concept restaurants. During fiscal year 2022, the real property was sold to a third party and the related party relationship terminated.

**Note 16 - Guarantees, Commitments, and Contingencies**

The Company is involved in certain routine legal proceedings which are incidental to its business. All these proceedings arose in the ordinary course of the Company's business and, in the opinion of the Company, any potential liability of the Company with respect to these legal actions will not, in the aggregate, be material to the Company's consolidated financial statements. The Company maintains various types of insurance standard to the industry which would cover most liabilities incurred by actions brought against the Company.

As part of the Company's ongoing franchise relationship with The Wendy's Company, the Company entered into agreements which contain certain restaurant reimaging and development requirements, as well as agreed-upon improvements to acquired facilities. Through these agreements, the Company committed to develop 52 new restaurants by November 30, 2025 and to reimage 100% of its portfolio. Pursuant to these agreements, the Company is entitled to receive significant economic incentives which include royalty and national marketing fee relief. As of December 31, 2023, the Company has reimaged approximately 72% of its portfolio and has completed 34 of the new restaurant development commitments. Based on current costs, the Company estimates it will invest approximately $69,000 to fulfill the remaining commitments of these agreements.

In 2021, the Company entered into a development agreement with its newest franchisor, Taco John's. Subject to certain terms and conditions, the Company committed to build 55 new Taco John's restaurants by December 31, 2026 with options to develop an additional 150 restaurants thereafter. As of December 31, 2023, the Company has completed six of the 55 new restaurant developments and based on current costs, estimates it will invest approximately $118,000 to fulfill remaining commitments. The Company recently came to an agreement with Taco John's to pause the development schedule through December 31, 2024 and may restart development activities in 2025.

## Note 17 – Acquisitions

The Company acquired the business and equipment of 25 Wendy's restaurants in 2023 and six Wendy's restaurants in 2022. The Company assumed existing lease agreements with the restaurants' building owners for the 25 restaurants acquired in 2023. The Company acquired the real estate associated with five locations and entered into one new lease agreement with the restaurants' building owner in 2022. For all locations, the Company entered into new franchise agreements with its franchisor, The Wendy's Company.

The 2023 acquisition was financed with $21,000 of new debt and $9,125 of cash on hand. The transaction resulted in the recording of $28,151 of goodwill, $1,382 of equipment and leasehold improvements, $440 of inventory, $24,083 in operating lease ROU assets and lease liabilities, $625 of franchise costs, $625 in franchise rights and $1,098 of other current liabilities. Revenue in fiscal year 2023 included $27,648 from locations acquired.

The 2022 acquisition was financed with $12,520 of debt and $3,954 of cash on hand. The transaction resulted in the recording of $3,309 of goodwill, $12,833 of land and building, $300 of equipment and leasehold improvements, $30 of inventory, $29 of franchise costs, $69 in franchise rights and $96 of other liabilities. Revenue in fiscal year 2022 included $5,024 from locations acquired.

The Company expensed $437 and $306 of acquisition costs related to acquisitions completed in fiscal year 2023 and 2022, respectively.

In accordance with ASC 805-10-50-2, the Company deemed it impracticable to disclose sufficient and materially accurate pro forma revenue and net income related to the acquisitions transacted during fiscal year 2023 and 2022, as the determination of pro forma adjustments requires assumptions about the sellers' intent in the prior period that cannot be independently substantiated and requires significant estimates for which it is impossible to distinguish objective information about those estimates.

Goodwill arising from the acquisitions consists largely of synergies and economies of scale expected from combining the operations of the new locations with the Company. All the goodwill is expected to be deductible for tax purposes.

# Meritage Hospitality Group Inc.

Incorporated in Michigan
45 Ottawa Ave SW, Suite 600
Grand Rapids, MI 49503

Telephone: 616.776.2600
Corporate Website: https://meritagehospitality.com
Company Email: rschermer@mhgi.net

SIC Code: 5812

# Annual Disclosures

For Fiscal Year Ended December 31, 2023

The number of shares outstanding of our Common Stock is 6,517,965 as of end of reporting period.

The number of shares outstanding of our Common Stock was 6,503,924 as of end of previous reporting period.

Indicate by check mark whether the company is a shell company (as defined in Rule 405 of the Securities Act of 1933 and Rule 12b-2 of the Exchange Act of 1934):

Yes: ☐ No: ☑

Indicate by check mark whether a Change in Control[4] of the company has occurred over this reporting period:

Yes: ☐ No: ☑

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4 "Change in Control" shall mean any events resulting in:

(i) Any "person" (as such term is used in Sections 13(d) and 14(d) of the Exchange Act) becoming the "beneficial owner" (as defined in Rule 13d-3 of the Exchange Act), directly or indirectly, of securities of the Company representing fifty percent (50%) or more of the total voting power represented by the Company's then outstanding voting securities;

(ii) The consummation of the sale or disposition by the Company of all or substantially all of the Company's assets;

(iii) A change in the composition of the Board occurring within a two (2)-year period, as a result of which fewer than a majority of the directors are directors immediately prior to such change; or

(iv) The consummation of a merger or consolidation of the Company with any other corporation, other than a merger or consolidation which would result in the voting securities of the Company outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity or its parent) at least fifty percent (50%) of the total voting power represented by the voting securities of the Company or such surviving entity or its parent outstanding immediately after such merger or consolidation.

## Part A General Company Information

### Item 1 The exact name of the issuer and its predecessor (if any).

The name of the Company is Meritage Hospitality Group Inc. (the "Company" or "Meritage").

### Item 2 The address of the issuer's principal executive offices.

45 Ottawa Ave SW, Suite 600
Grand Rapids, MI 49503
Telephone: 616.776.2600
Facsimile: 616.328.6925
Web: www.meritagehospitality.com

### Item 3 The jurisdiction and date of the issuer's incorporation or organization.

The Company was incorporated under the laws of the State of Michigan in August 1986.

## Part B Share Structure

### Item 4 The exact title and class of securities outstanding.

The Company's Articles of Incorporation authorize 30,000,000 common shares (Par Value Per Share $0.01). There were 6,517,965 common shares outstanding at December 31, 2023. The shares are assigned CUSIP No. 59000K309 and are quoted on the OTC Markets under the symbol "MHGU".

The Company's Articles of Incorporation authorize 5,000,000 preferred shares (Par Value Per Share $0.01). Preferred shares are summarized as follows:

| Title | CUSIP No. | OTC Markets Trade Symbol |
|---|---|---|
| Series B Convertible Preferred Shares | 59000K408 | MHGUP |
| Series C Convertible Preferred Shares | 59000K507 | - |
| Series D Convertible Preferred Shares | 59000K606 | - |
| Series E Convertible Preferred Shares | 59000K705 | - |
| Series F Convertible Preferred Shares | 59000K804 | - |

## Item 5 Par or stated value and description of the security.

Common Shares: The Company most recently paid cash dividends per share of $0.18 in 2023, $0.30 in 2022, $0.32 in 2021, and $0.14 in 2020. The Company's Board of Directors regularly considers payment of additional dividends on common shares but has not adopted a dividend policy. State law and certain of the Company's governance documents and loan agreements may limit the Company's ability to declare cash dividends.

Series B Convertible Preferred Shares: The Company authorized 500,000 Series B Convertible Preferred Shares ("Series B Preferred Shares") in 2003, an additional 850,000 shares in 2015, and has 805,400 shares outstanding. The Series B Preferred Shares have an annual dividend rate of $0.80 per share. The right to payment of dividends is cumulative. The dividend is payable in equal quarterly installments on the first day of each January, April, July and October to holders of record as of the 15th day of the preceding month. The holders may convert their Series B Preferred Shares into common shares at a conversion price of $5.57 per common share. The conversion rate is subject to adjustment in the event of stock splits, stock dividends, combinations, reclassifications and similar occurrences. The Company may, upon 15 days written notice, redeem all or part of the Series B Preferred Shares at a redemption price of $10.00 per Series B Preferred Share plus accrued but unpaid dividends. Upon any dissolution or winding up, the holder of each Series B Preferred Share will be entitled to receive a liquidation value of $10.00 per Series B Preferred Share plus all accrued but unpaid dividends after the payment of all indebtedness of the Company and before any distributions to holders of common shares. No voting rights are provided except as required by law and with the exception that, if at any time the Company fails to make six quarterly dividend payments, the holders of the Series B Preferred Shares, voting as a class with each Series B Preferred Share having one vote, would be entitled to elect two directors to the Board, which members would remain on the Board as long as any dividend payment arrearages remain outstanding.

Series C Convertible Preferred Shares: The Company authorized 1,500,000 Series C Convertible Preferred Shares ("Series C Preferred Shares") in 2016, subsequently reduced to 200,000 in 2020, and has 160,360 shares outstanding. The Series C Preferred Shares have an annual dividend rate of $1.50 per share. The right to payment of dividends is cumulative. The dividend is payable in equal quarterly installments on the first day of each January, April, July and October to holders of record as of the 15th day of the preceding month. In one year from the date of issuance, the holders may convert their Series C Preferred Shares into common shares at a conversion price of $13.50 per common share. The conversion rate is subject to adjustments for subdivisions and splits of common shares. The Company may, at its option, redeem all or part of the Series C Preferred Shares at a redemption price of $28.00 per Series C Preferred Share plus accrued but unpaid dividends. Upon any dissolution or winding up, the holder of each Series C Preferred Share will be entitled to receive a liquidation value of $25.00 per Series C Preferred Share plus all accrued but unpaid dividends after the payment of all indebtedness of the Company and before any distributions to holders of common shares. No voting rights are provided except as required by law and with the exception that, if at any time the Company fails to make six quarterly dividend payments, the holders of the Series C Preferred Shares, voting as a class with each Series C Preferred Share having one vote, would be entitled to elect two directors to the Board, which members would remain on the Board as long as any dividend payment arrearages remain outstanding.

Series D Convertible Preferred Shares: The Company authorized 600,000 Series D Convertible Preferred Shares ("Series D Preferred Shares") in 2017 and has 310,293 shares outstanding. The Series D Preferred Shares have an annual dividend rate of $1.75 per share. The right to payment of dividends is cumulative. The dividend is payable in equal quarterly installments on the first day of each January, April, July and October to holders of record as of the 15th day of the preceding month. In one year from date of issuance, the holders may convert their Series D Preferred Shares into common shares at a conversion price of $24.00 per common share. The conversion rate is subject to adjustments for subdivisions and splits of common shares. The Company may, at its option, redeem all or part of the Series D Preferred Shares at a redemption price of $28.00 per Series D Preferred Share plus accrued but unpaid dividends. Upon any dissolution or winding up, the holder of each Series D Preferred Share will be entitled to receive a liquidation value of $25.00 per Series D Preferred Share plus all accrued but unpaid dividends after the payment of all indebtedness of the Company and before any distributions to holders of common shares. No voting rights are provided except as required by law and with the exception that, if at any time the Company fails to make six quarterly dividend payments, the holders of the Series D Preferred Shares, voting as a class with each Series D Preferred Share having one vote, would be entitled to elect two directors to the Board, which members would remain on the Board as long as any dividend payment arrearages remain outstanding.

Series E Convertible Preferred Shares: The Company authorized 800,000 Series E Convertible Preferred Shares ("Series E Preferred Shares") in 2018 and has 128,744 shares outstanding. The Series E Preferred Shares have an annual dividend rate of $1.75 per share. The right to payment of dividends is cumulative. The dividend is payable in equal quarterly installments on the first day of each January, April, July and October to holders of record as of the 15th day of the preceding month. In one year from date of issuance, the holders may convert their Series E Preferred Shares into common shares at a conversion price of $21.00 per common share. The conversion rate is subject to adjustments for subdivisions and splits of common shares. The Company may, at its option, redeem all or part of the Series E Preferred Shares at a redemption price of $28.00 per Series E Preferred Share plus accrued but unpaid dividends. Upon any dissolution or winding up, the holder of each Series E Preferred Share will be entitled to receive a liquidation value of $25.00 per Series E Preferred Share plus all accrued but unpaid dividends after the payment of all indebtedness of the Company and before any distributions to holders of common shares. No voting rights are provided except as required by law and with the exception that, if at any time the Company fails to make six quarterly dividend payments, the holders of the Series E Preferred Shares, voting as a class with each Series E Preferred Share having one vote, would be entitled to elect two directors to the Board, which members would remain on the Board as long as any dividend payment arrearages remain outstanding.

Series F Convertible Preferred Shares: The Company authorized 1,000,000 Series F Convertible Preferred Shares ("Series F Preferred Shares") in 2023 and has 130,606 shares outstanding. The Series F Preferred Shares have an annual dividend rate of $1.875 per share. The right to payment of dividends is cumulative. The dividend is payable in equal quarterly installments on the first day of each January, April, July and October to holders of record as of the 15th day of the preceding month. In one year from date of issuance, the holders may convert their Series F Preferred Shares into common shares at a conversion price of $24.00 per common share. The conversion rate is subject to adjustments for subdivisions and splits of common shares. During the first two years from the date of issuance, the Company may, at its option, redeem all or part of the Series F Preferred Shares at a redemption price of $26.00 per Series F Preferred Share plus accrued but unpaid dividends. After two years from the date of issuance, the redemption price is $28.00 per share plus any accrued and unpaid dividends to the redemption date. Upon any dissolution or winding up, the holder of each Series F Preferred Share will be entitled to receive a liquidation value of $25.00 per Series F Preferred Share plus all accrued but unpaid dividends after the payment of all indebtedness of the Company and before any distributions to holders of common shares. No voting rights are provided except as required by law and with the exception that, if at any time the Company fails to make six quarterly dividend payments, the holders of the Series F Preferred Shares, voting as a class with each Series F Preferred Share having one vote, would be entitled to elect two directors to the Board, which members would remain on the Board as long as any dividend payment arrearages remain outstanding.

While the Company's Charter documents do not have specific provisions designed to prevent a change in control, provisions in several documents (including the Company's articles of incorporation, bylaws, franchise agreements, loan agreements, equity award agreements, etc.) and certain provisions in the Michigan Business Corporate Act could effectively delay or hinder an attempted change in control.

## Item 6 The number of shares or total amount of the securities outstanding for each class of securities authorized.

| | 2023 | 2022 |
|---|---|---|
| Common Shares | | |
| Authorized: | 30,000,000 shares | 30,000,000 shares |
| Outstanding: | 6,517,965 shares | 6,503,924 shares |
| Freely Tradable (public float): | approx. 3,000,000 shs. | approx. 3,000,000 shs. |
| Number of beneficial holders owning at least 100 shares: | approx. 655 | approx. 684 |
| Number of record holders: | approx. 56 | approx. 56 |
| | | |
| Preferred B: | | |
| Authorized: | 1,350,000 shares | 1,350,000 shares |
| Outstanding: | 805,400 shares | 805,400 shares |
| Freely Tradable (public float): | 300,000 shares | 300,000 shares |
| Number of record holders: | 18 holders | 18 holders |
| | | |
| Preferred C | | |
| Authorized: | 200,000 shares | 200,000 shares |
| Outstanding: | 160,360 shares | 160,360 shares |
| Number of record holders: | 7 holders | 7 holders |
| | | |
| Preferred D | | |
| Authorized: | 600,000 shares | 600,000 shares |
| Outstanding: | 310,293 shares | 310,293 shares |
| Number of record holders: | 24 holders | 24 holders |
| | | |
| Preferred E | | |
| Authorized: | 800,000 shares | 800,000 shares |
| Outstanding: | 128,744 shares | 128,744 shares |
| Number of record holders: | 13 holders | 13 holders |
| | | |
| Preferred F | | |
| Authorized: | 1,000,000 shares | 0 shares |
| Outstanding: | 130,606 shares | 0 shares |
| Number of record holders: | 7 holders | 0 holders |

## Item 7 The name and address of the transfer agent.

American Stock Transfer and Trust Company, LLC (an Equiniti Company)
6201 15th Avenue
Brooklyn, NY 11219
Phone: (800) 937-5449

American Stock Transfer and Trust Company, LLC ("AST") is registered under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). AST's procedures and transactions are regulated and audited by the Securities and Exchange Commission ("SEC").

## Part C Business Information

### Item 8 The nature of the issuer's business.

**Summary**

Meritage was incorporated under the laws of the State of Michigan in August 1986 and was assigned a primary SIC Code of 5812 (Retail-Eating Places). Meritage has approximately 12,000 employees, of which approximately 2,800 are full-time. The Company's consolidated financial statements include the accounts of Meritage Hospitality Group Inc. and all of its wholly-owned subsidiaries and affiliate, consisting of MHG Food Service Inc., OCM Development, LLC, WM Limited Partnership-1998, Wen South, LLC, Wen Georgia LLC, Wen Carolina's LLC, Wen Virginia LLC, Wen Ohio LLC, Wen Oklahoma LLC, Wen Tennessee LLC, Inspired by Opportunity LLC, Uncommon Hospitality Group LLC, We Love Tacos LLC, its 98.5% owned subsidiary, RDG-MHG, LLC, ("RDG"), and its variable interest entity (VIE), Restaurant Holdings, LLC ("Restaurant Holdings"), for which the Company is a primary beneficiary. RDG is a 15% partner in TRG-Meritage Bahamas, LLC ("TRG"). All intercompany transactions and balances have been eliminated in consolidation. For convenience, Meritage is not a shell company, and its subsidiaries and affiliate are collectively referred to as "Meritage" or "the Company" throughout this report.

The Company operates on a 52/53-week fiscal year ending on the Sunday closest to December 31 of each year. Each of the two fiscal years presented ended December 31, 2023 and January 1, 2023 contained 52 weeks.

Meritage operates 376 Wendy's quick-service restaurants as a franchisee of Quality Is Our Recipe, LLC, a subsidiary of The Wendy's Company. To simplify the language in this disclosure, Quality Is Our Recipe, LLC will hereafter be referred to as "The Wendy's Company". The Company operates Wendy's restaurants in 16 states, which include eight restaurants in Arkansas, 32 in Connecticut, 59 in Florida, 51 in Georgia, 12 in Indiana, 13 in Massachusetts, 56 in Michigan, eight in Mississippi, three in Missouri, 24 in North Carolina, 15 in Ohio, 29 in Oklahoma, one in South Carolina, 34 in Tennessee, 16 in Texas and 15 in Virginia. Through its development and acquisition efforts, the Company is one of the nation's largest Wendy's franchisees.

Meritage operates six Taco John's quick-service restaurants as a franchisee of Taco John's International, Inc., hereafter referred to as "Taco John's". Of the six restaurants, five are located in Michigan and one in Ohio.

The Company also has independent restaurants operating under two concepts throughout Michigan which include three Morning Belle restaurants and one Stan's Tacos restaurant. Restaurants were launched as the Company's own original concepts, each with a unique environment and offerings tailored to consumer preferences. The Company continues to actively focus on future development and long-term growth of its Morning Belle brand. In connection with this long-term growth strategy, the Company recently closed, on a temporary basis, two of its Stan's Tacos locations for future potential rebranding.

## Risks and Governmental Regulations

Meritage is subject to numerous uncertainties and risk factors inherent in the food service industry. These include, among others: competition; changes in local and national economic conditions; changes in consumer tastes and eating habits; concerns about the nutritional quality of quick-service or casual dining menu items; concerns about consumption of beef or other menu items due to food-borne diseases; promotions and menu price discounting by competitors; severe weather; changes in travel patterns; road construction; demographic trends; the cost of food, labor, fuel and energy; the availability and cost of suitable restaurant sites; the ability to finance expansion; fluctuating interest rates; insurance costs; the availability of an adequate number of managers and hourly-paid employees; directives issued by its franchisor regarding the Company's quick-service operations; its franchisor's national marketing and advertising programs; its franchisor's advertised pricing; the general reputation of Meritage's and its franchisor's restaurants; legal claims; security, including cyber security; credit card fraud; information technology incidents and breaches; and the recurring need for renovation and capital improvements. Meritage is subject to risks and uncertainties related to the development of pandemics.

The Company is also subject to various federal, state and local laws and governmental regulations relating to, among other things: zoning; restaurant operations; public health certification regarding the preparation and sale of food; alcoholic beverage control; discharge of materials into the environment; sanitation; and minimum wage laws. The Company believes its operations would be adversely affected if these permits or other applicable permits or approvals were not obtained or renewed or were terminated. While the Company has no reason to anticipate that this may occur, it can give no assurances in this regard. In addition, changes regarding minimum wage laws or other laws governing the Company's relationship with its employees (e.g., overtime wages and tips, health care coverage, employment of minors, citizenship/immigration requirements, working conditions, etc.) could have an adverse effect on the Company's operations.

Approximately 11% of the Company's independent concept restaurant sales are attributable to the sale of alcoholic beverages. Each restaurant has licenses from regulatory authorities allowing it to sell liquor, beer and wine. The failure of a restaurant to obtain or retain liquor service licenses could adversely affect the Company's operations. Once a liquor license is obtained, Meritage is subject to "dram-shop" statutes and interpretations which generally provide that a person who is injured by an intoxicated person has the right to recover damages from an establishment that wrongfully served alcoholic beverages to the intoxicated person.

The Federal Americans with Disabilities Act prohibits discrimination on the basis of disability in public accommodations and employment. The Company's restaurants are designed to be accessible to the disabled and are in substantial compliance with all current applicable regulations relating to restaurant accommodations for the disabled. The development and construction of additional restaurants will be subject to compliance with applicable zoning, land use and environmental regulations.

See *Forward-Looking Statements* following Item 20 of this annual disclosure statement for additional details.

## Legal Proceedings

The Company is involved in various routine legal proceedings that are incidental to its business. All of these proceedings arose in the ordinary course of the Company's business and, in the opinion of the Company, any potential liability of the Company with respect to these legal proceedings will not, in the aggregate, be material to the Company's consolidated financial statements. The Company maintains various types of insurance policies standard to the industry that, subject to deductibles, are expected to insure over many claims and legal proceedings brought against the Company.

### Listing Developments

The Company has fewer than 300 record common shareholders, with shares listed on the OTC Markets under the symbol “MHGU.” The listing is under the OTCQX premium listing service intended to set apart a select group of issuers that the OTC Markets deem worthy of heightened consideration by investors. The OTCQX is designed to meet the needs of small to medium-sized, publicly traded U.S. companies.

The Company’s Series B Preferred Shares are listed on the OTC Markets using the OTCQX premium listing service under the symbol “MHGUP”.

## Item 9 The nature of products or services offered.

### Quick-Service Operations

The Company operates Wendy’s quick-service restaurants in Arkansas, Connecticut, Florida, Georgia, Indiana, Massachusetts, Michigan, Mississippi, Missouri, North Carolina, Ohio, Oklahoma, South Carolina, Tennessee, Texas, and Virginia. The Company’s Taco John’s quick-service restaurants operate in Michigan and Ohio.

*Menu*

Each Wendy’s restaurant offers a diverse menu of food items featuring hamburgers and chicken sandwiches, all of which are prepared to order with the customer’s choice of condiments. The Wendy’s menu additionally includes chili, baked and french-fried potatoes, chicken nuggets, freshly prepared salads, soft drinks, “Frosty®” desserts and children’s meals. Wendy’s breakfast menu features a variety of breakfast sandwiches and specialty coffees, including the new Frosty® Cream Cold Brew. Each Wendy’s restaurant features soft drink products supplied by the Coca-Cola Company and its respective affiliates.

Taco John’s menu features a variety of made to order items, including meat and potato burritos, stuffed grilled tacos, quesadillas, signature Potato Olés®, and crave worthy fried chicken tacos. Taco John’s also offers signature specials like taco tuesday and the everyday value menu. The breakfast menu brings a variety of breakfast burritos, scramblers, cold brew coffees, and signature Mexican donut bites to start the day. Soft drink products are supplied by PepsiCo and its respective affiliates.

Both franchisors maintain significant discretion over the menu items offered in the Company’s restaurants.

*Restaurant Layout and Operation*

The Company’s Wendy’s restaurants range from 2,200 to 3,500 square feet with seating capacity for approximately 30 to 130 people. Restaurants are generally open from 6:30 a.m. until midnight, with limited exceptions. Restaurants feature a pick-up drive-through window. Sales to drive-through customers account for approximately 72% of total 2023 restaurant sales.

The Company’s Taco John’s restaurants average 2,100 square feet. The restaurants feature a pick-up window for drive-through service, as well as dine-in seating capacity for approximately 40 people. Hours of operations are 6:30 a.m. until 10:00 p.m.

*Marketing and Promotion*

The Wendy's Company as a franchisor requires at least 4.0% of the Company's restaurant sales be contributed to an advertising and marketing fund, 3.5% of which is used to benefit all Wendy's restaurants in national advertising programs. The Wendy's National Advertising Program uses these funds to develop advertising and sales promotion materials and concepts to be implemented nationally. The remaining 0.5% is used on local advertising.

Taco John's International, Inc. as a franchisor requires 4.0% of the Company's restaurants sales to be contributed to an advertising and marketing fund for national, regional and/or local media placement, of which 2.85% is used on local advertising.

The Company typically spends local advertising dollars in support of radio advertising, print media, social media, and local promotions. In addition, digital marketing discounts provided through in-app purchases further represent the Company's overall marketing investment.

*Raw Materials and Energy*

The Company's restaurants comply with uniform recipe and ingredient specifications provided by each franchisor. Food and beverage inventories and restaurant supplies are purchased from independent vendors that are approved by the related franchisor. The Company has not experienced any significant shortages of food, equipment, fixtures or other products that are necessary to restaurant operations. While no such shortages are anticipated at this time, the Company believes that alternate suppliers are available if any shortage were to occur.

The Company's principal sources of energy for its quick-services restaurant operations are electricity and natural gas. The supply of energy available to the Company has been sufficient to maintain normal operations.

*Seasonality*

The Company's business is subject to various seasonal fluctuations. Midwest and East Coast traffic typically increases during the summer, resulting in increased revenues during those months. Traffic in the southern states typically increases during the spring, resulting in increased revenues during those months.

*Relationship with Franchisor*

Meritage operates its quick-service restaurants pursuant to various agreements (including one franchise agreement for each restaurant) with its franchisors, The Wendy's Company and Taco John's International, Inc. These agreements grant privileges to the Company such as the right to utilize trademarks, service marks, designs, and other proprietary rights in connection with the operation of its restaurants. These agreements also impose requirements on the Company regarding the preparation and quality of food products, the level of service, capital improvements, and general operating procedures. The remaining terms of the Company's Wendy's franchise agreements (including options to renew) range from one to 34 years. Taco John's franchise agreements have a 20-year base term with three, ten-year options to renew. All of the Company's Taco John's franchise agreements have approximately 19 years remaining in their base term.

Wendy's franchise agreements provide, among other things, that a change in the operational control of the Wendy's operating entity, or the removal of a guarantor of the franchise agreements, cannot occur without the prior consent of the franchisor. In addition, any proposed sale of a Wendy's restaurant, ownership interests or franchise rights therein is subject to the consent of, and a right of first refusal by, the franchisor. These agreements also grant the franchisor wide discretion over many aspects of the restaurant operations, and often require the consent of the franchisor to carry out certain operational transactions pertaining to the Wendy's restaurants. If Meritage needs the consent of its franchisor to proceed with its business plans and such consent is not obtained, Meritage will not be able to proceed with its plans which, in turn, could adversely affect Meritage's growth strategy. If Meritage were to proceed without the franchisor's consent when required, the franchisor could terminate the franchise agreements or exercise its right to purchase the Wendy's restaurants.

In addition to monthly fees, Meritage is required to pay the franchisor a technical assistance fee upon the opening of a new Wendy's restaurant. Meritage is permitted to develop new Wendy's restaurants subject to the expandability criteria and site standards of the franchisor. While the franchise agreements are in place, Meritage is prohibited from acquiring or developing any "Competing Business" as defined in the Wendy's Franchise Agreement within its designated market area ("DMA"), or outside of them if the restaurant sells hamburgers, chicken sandwiches or products similar to the franchisor, and is located within a three-mile radius of another Wendy's restaurant. For two years after the expiration or termination of the franchise agreements, Meritage is prohibited from participating in any quick-service restaurant business that sells hamburgers, chicken sandwiches or products similar to the franchisor, and is located within its DMA.

The reputation of Meritage's restaurants is largely dependent on the reputation of the entire Wendy's restaurant chain, which in turn is dependent upon the management and financial condition of The Wendy's Company and the performance of Wendy's restaurants operated by other Wendy's franchisees. Should the Wendy's Company be unable to compete effectively with similar restaurant chains in the future, Meritage would be materially and adversely affected. Furthermore, many of the attributes which lead to the success of Wendy's operations are factors over which Meritage has no control, such as national marketing, introduction of new products, quality assurance and other operational systems. Meritage cannot conduct its Wendy's operations without its affiliation with its franchisor. Any termination of the franchise agreements would have a material adverse effect on Meritage's financial condition and results of operations.

Taco John's franchise agreements provide, among other things, that any proposed sale of a Taco John's restaurant, ownership interests or franchise rights therein is subject to the consent of, and a right of first refusal by, the franchisor. These agreements also grant the franchisor wide discretion over many aspects of the restaurant operations, and often require the consent of the franchisor to carry out certain operational transactions pertaining to the Taco John's restaurants. If Meritage needs the consent of its franchisor to proceed with its business plans and such consent is not obtained, Meritage will not be able to proceed with its plans which, in turn, could adversely affect Meritage's growth strategy. If Meritage were to proceed without the franchisor's consent when required, the franchisor could terminate the franchise agreements or exercise its right to purchase the Taco John's restaurants.

Meritage is permitted to develop new Taco John's restaurants subject to the standards and approval of the franchisor. While the franchise agreements are in place, Meritage is prohibited from performing services for or have any direct or indirect interest in any "Competitive Business" as defined in the Taco John's Franchise Agreement within its Protected Territory, or outside of the Protected Territory if the restaurant offers or sells Mexican food as more than 15.0% of its menu items.

The reputation of Meritage is dependent on the reputation of the entire Taco John's restaurant chain, which in turn is dependent upon the management and financial condition of Taco John's International and the performance of restaurants operated by other Taco John's franchisees. Should Taco John's be unable to compete effectively with similar restaurant chains, Meritage would be adversely affected. Furthermore, many of the attributes which lead to the success of Taco John's operations are factors over which Meritage has no control, such as national marketing, introduction of new products, quality assurance, operational systems, and building infrastructure. Meritage cannot conduct its Taco John's operations without affiliation with its franchisor. Any termination of the franchise agreements would have an adverse effect on Meritage's financial condition and results of operations.

**Independent Concept Operations**

The Company owns six independent restaurants under two concepts throughout Michigan which include Morning Belle restaurants and Stan's Tacos.

The Company's three Morning Belle restaurants are located in Grand Rapids, Michigan. All restaurants feature a garden themed environment tailored to family and friends and include a variety of breakfast options using the best ingredients for the freshest taste. The restaurants' vibrant decor is designed to make days brighter with any one of the restaurants' crafted morning cocktails, or signature breakfast, brunch or lunch dishes.

The Company's Stan's Tacos restaurant is located in Standale, Michigan. The restaurants' upbeat décor aims to feature a unique, tailored menu which includes a variety of made-to-order tacos and specialty margaritas. In connection with this long-term growth strategy, the Company recently closed, on a temporary basis, two of its Stan's Tacos locations for future potential rebranding.

*Restaurant Menu, Layout and Operation*

Morning Belle is a bright, garden-themed breakfast restaurant that ranges from 2,400 to 5,500 square feet and features between 90 and 140 dining seats. The restaurants' décor includes white brick and shiplap walls, warm cedar accents, greenery, and vibrant fabrics. Morning Belle's menu features breakfast, brunch and lunch options which include traditional breakfast entrees, scratch-made pancakes, a kids menu, lighter options such as salads with fresh cut vegetables and grain bowls, and its own glazed donut waffle for the more indulgent palate. The concept's extensive specialty beverage menu includes, among other items, a variety of mimosas, spiked cold brews, and pomegranate lemonade.

Stan's Tacos' Standale location is a 4,700 square foot site on the end cap space of a shopping center. The restaurant features a large cabana bar as well as a 14-foot garage door to welcome the outside in. The location accommodates approximately 140 guests and exhibits a come-as-you-are atmosphere for guests of every age. The restaurant features specialty margaritas and made-to-order tacos using only the freshest ingredients.

*Marketing and Promotion*

The advertising and promotional efforts for the Company's independent concepts are aimed at building brand loyalty and emphasizing the distinctiveness of each location's food, service, atmosphere, and commitment to supporting the local economy. Their campaigns include participation in local events and support of local media outlets. Social media, digital and mobile marketing also play a large role in their advertising strategy as the online conversation and consumer review systems grow larger.

*Raw Materials and Energy*

The Company's independent concepts comply with internal recipe and ingredient specifications. Food and beverage inventories and restaurant supplies are purchased from third party suppliers. The Company has not experienced any significant shortages of food or other products that are necessary to restaurant operations. While no such shortages are anticipated at this time, the Company believes that alternate suppliers are available if any shortage were to occur.

The Company's principal sources of energy for its independent concept restaurants are electricity and natural gas. The supply of energy available to the Company has been sufficient to maintain normal operations.

## Competition and Industry Conditions

Meritage operates restaurants within the quick-service restaurant ("QSR") industry and the casual dining restaurant industry.

*Quick-Service Restaurant Industry*

Meritage operates its Wendy's and Taco John's restaurants within the quick-service restaurant ("QSR") industry. The QSR industry is characterized by customers who are looking for quick, convenient, and value-oriented meals that are ordered, paid for and picked up at a cash register. Within the quick-service industry, the hamburger segment comprises approximately half of the market and is dominated by Wendy's, McDonald's, and Burger King. Pizza, chicken, breakfast, Mexican, Asian and other sandwich market segments comprise a significant portion of the remainder of the QSR industry.

Most of the Company's quick-service restaurants are located in close proximity to principal competitors which are highly competitive on the basis of price and value perception, service, location, food quality, menu variety, speed of service, attractiveness of facilities, and effectiveness of marketing and new product development. The Company also competes within the food service industry and the QSR restaurant sector not only for customers, but also for personnel and suitable real estate sites.

The Company believes the competitive position of a Wendy's restaurant is ultimately enhanced by its unique qualities such as the use of fresh ground beef, a diverse menu, food prepared to order with an emphasis on quality, nutrition and taste, pleasant and speedy services, and atmosphere. Wendy's continues to implement its reimaging program, which includes innovative exterior and interior restaurant designs, with plans for significantly more new and reimaged restaurants which began in 2014 and continuing beyond.

*Casual Dining Restaurant Industry*

The Company operates its Morning Belle and Stan's Tacos restaurants within the casual dining industry. The casual dining restaurant industry services customers interested in high-quality, value-oriented, full-service meals with wait staff taking orders and available throughout the meal.

As with its quick-service restaurants, the Company's independent concept restaurants are located in close proximity to their principal casual dining restaurant competitors who are highly competitive on the basis of price and value perception, service, location, food quality, menu variety, quality and speed of service, attractiveness of facilities, effectiveness of marketing and new product development.

## Item 10 The nature and extent of the issuer's facilities.

Each Wendy's restaurant is built to the franchisor's specifications for exterior style and interior decor. Typical freestanding restaurants are one-story brick buildings with parking for 15 to 70 vehicles. The restaurants have a food preparation area, a dining room with seating capacity for 30 to 130 guests, and a pick-up window for drive-through service. Of the 376 Wendy's restaurants it operates, the Company (i) owns the land and buildings comprising 14 restaurants, (ii) leases the land and buildings comprising 352 restaurants, and (iii) owns the building and leases the land comprising 10 restaurants. The remaining lease terms (including options to renew) range from one to 50 years. The structures are between one and 49 years old. Meritage has performed major remodels on a number of its older Wendy's restaurants in the last several years. The land and buildings owned by the Company are held as collateral for financing.

The Company remains focused on reimaging its Wendy's restaurants. Reimaging costs inclusive of deferred maintenance items range from $400,000 to $600,000 per restaurant. Currently, 72% of the Company's Wendy's restaurant portfolio has been reimaged.

Taco John's restaurants are typically a 2,100 square foot, freestanding building with parking for roughly 30 vehicles. Similar to Wendy's, there is a food preparation area, a dining room with seating capacity for 40 guests, and a pick-up window for drive-through service. Of the six Taco John's restaurants it operates, the Company (i) owns the land and buildings comprising five restaurants and (ii) leases the land and buildings for one restaurant. The remaining lease term (including options to renew) is 50 years. The land and buildings owned by the Company are held as collateral for financing.

Of the Company's six independent restaurants, the Company (i) leases the land and buildings comprising five restaurants, and (ii) owns the building and leases the land for one restaurant. The remaining term of the building and land leases (including options to renew) are between 14 and 48 years. The remaining term of the land lease (including options to renew) is 15 years.

The Company leases office space at 45 Ottawa SW Suite 600, Grand Rapids, Michigan, which serves as the registered office and principal place of business of the Company. The lease term runs through June 2026 with three 5-year renewal options.

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## Part D Management Structure and Financial Information

### Item 11 The name of Company Officers, members of the Board of Directors, and control persons.

The table below identifies the Company's Executive Officers, members of the Board of Directors, and control persons and provides information on their beneficial ownership of Company securities as of December 31, 2023 in accordance with Securities Exchange Act of 1934 Rule 13d-3(d)(1)(i):

| Name and Age | Position | Total Shares Beneficially Owned Amount (1) | Total Shares Beneficially Owned Percentage |
|---|---|---|---|
| Robert E. Schermer, Jr., 65 | Chief Executive Officer | 2,523,424 | 31.2% |
| Gary A. Rose, 61 | President and Chief Operating Officer | 1,109,068 | 14.2% |
| Tracey A. Smith, 49 | Vice President, Chief Financial Officer, Treasurer and Secretary | 171,015 | 2.4% |
| Robert E. Schermer, Sr., 88 | Principal Shareholder | 1,334,389 | 17.5% |
| Duane F. Kluting, 74 | Director | 138,505 | 1.9% |
| Joseph L. Maggini, Sr., 84 | Director | 399,634 | 5.4% |
| Peter D. Wierenga, 69 | Director | 557,749 | 7.7% |
| Dirk J. Pruis, 63 | Director | 53,294 | 0.7% |
| Chris A. Armbruster, 62 | Director | 22,325 | 0.3% |
| John W. Inwright, 67 | Director | 4,017 | 0.1% |
| All current Executive Officers, Directors, and Principal Shareholders (10 persons) | | 6,313,420 | 63.7% |

(1) Represents beneficial ownership of Company common stock including options presently exercisable or exercisable within 60 days, as well as shares of common stock underlying Series B Convertible Preferred Shares, Series C Convertible Preferred Shares, Series D Convertible Preferred Shares, Series E Convertible Preferred Shares, and Series F Convertible Preferred Shares.

Robert E. Schermer, Jr. has been a Director of the Company since 1996. He has been Chief Executive Officer of the Company since 1998. Mr. Schermer served as President of the Company from October 1998 through May 2016. Mr. Schermer's business address is 45 Ottawa SW, Suite 600, Grand Rapids, MI 49503.

Gary A. Rose has been President since May 2016 and Chief Operating Officer since 2006. He was Vice President, Chief Financial Officer and Treasurer of the Company from 2005 through May 2016. He was Secretary from 2008 through May 2017. Mr. Rose is a CPA and spent six years with Deloitte & Touche in Grand Rapids, MI. Mr. Rose's business address is 45 Ottawa SW, Suite 600, Grand Rapids, MI 49503.

Tracey A. Smith has been Vice President, Chief Financial Officer and Treasurer since May 2016. She has been Secretary since May 2017. She was Director of Finance from 2012 through May 2016 and Controller from 2008 through 2011. Mrs. Smith's business address is 45 Ottawa SW, Suite 600, Grand Rapids, MI 49503.

Robert E. Schermer, Sr. was Chairman of the Board of Directors from 1996 through May 2023 and is currently a Principal Shareholder. Mr. Schermer, Sr. is currently retired. From 1990 through 2005, he was Senior Vice President and a Managing Director of Robert W. Baird & Co. Incorporated, an investment banking and securities brokerage firm headquartered in Milwaukee, WI. Mr. Schermer's business address is 45 Ottawa SW, Suite 600, Grand Rapids, MI 49503.

Duane F. Kluting has been a Director of the Company since 2005. Mr. Kluting is currently retired. From 1992 through 2003, Mr. Kluting served as Vice President, Chief Financial Officer and Corporate Secretary of X-Rite, Incorporated, a developer and manufacturer of color measurement instrumentation and software used in graphic arts, retail and industrial applications. Mr. Kluting's business address is 2525 Keyton Ct NW, Grand Rapids, MI 49504.

Joseph L. Maggini, Sr. has been a Director of the Company since 1996. Mr. Maggini was the President and Chairman of the Board of Magic Steel Corporation, a steel service center located in Grand Rapids, Michigan that he founded in 1974. After 40 years, Mr. Maggini sold his company in June of 2019 and is no longer affiliated with Magic Steel Sales. Mr. Maggini's business address is 3326 Vine Street SW, Grandville, MI 49418.

Peter D. Wierenga has been a Director of the Company since 2010. He is currently retired. He was the Vice President and Director of Godwin Plumbing, Inc., a plumbing and mechanical contractor, from 1987 through 2015. Concurrently, Mr. Wierenga was the President and director of Godwin Hardware Stores, a retail hardware company, since 1988. Mr. Wierenga's business address is 3319 Antigua Drive, Punta Gorda, FL 33950.

Dirk J. Pruis has served as a Director of the Company since 2018. Mr. Pruis began his career as a CPA at Touche Ross. Between 1993 and 2014 he held various leadership positions at Goldman Sachs and its subsidiaries, most recently a Managing Director and Chief of Staff in the Operations Division. Mr. Pruis is currently the Vice President for Finance and CFO at Calvin University as well as an Associate Professor and Director of the Financial Planning Program there. Mr. Pruis' business address is 3201 Burton Street SE, Grand Rapids, MI 49546.

Chris A. Armbruster has served as Director of the Company since 2020. Mr. Armbruster worked for Taco Bell Corporation from 1991 through 2013 where he held several leadership positions in finance involving acquisitions and divestitures, financial planning, and development. He spent the last six years at Taco Bell as Vice President of Development and Franchise Finance. Between 2015 and 2018 he served as Vice President of Development for the Wendy's Company. In April 2021, Mr. Arbruster co-founded Creed Unco and has been consulting with that group ever since. Mr. Armbruster's business address is 6969 Red Bank Road, Galena, OH 43021.

John Inwright has served as Director of the Company since 2022. Mr. Inwright is retired and now serves as a board member and advisor to a variety of businesses. Through 2005, he held several leadership positions at Unified Foodservice Purchase Co-op, a Yum! Brands Co-op. Between 2005 to 2007 he served as Chief Procurement Officer for US Foods, and then as Executive Vice President and General Manager for Nice-Pack Products, Inc, a global expert providing infection control products and prevention methods for the foodservice and healthcare industries from 2007 to 2009. Most recently, he served as President & CEO of Wendy's Quality Supply Chain Co-op until 2021. He also served on the Board of the Dave Thomas Foundation for Adoption for 10 years. Mr. Inwright's business address is 810 Greenwillow Way, Louisville KY 40223.

The non-employee directors are compensated in accordance with the compensatory plans outlined in Item 16 below. In fiscal 2023, each of the non-employee directors received an option grant of 10,000 common shares priced at $17.25 per share (the closing price on the date of the grant). In fiscal 2023, the non-employee directors received compensation for attendance at Board and Committee meetings as follows: Mr. Kluting: $43,182 (paid in 2,051 common shares and $3,063 in cash); Mr. Pruis: $51,632 (paid in 1,053 common shares and $31,320 in cash); Mr. Maggini: $13,380 (paid in 684 common shares); Mr. Wierenga: $13,380 (paid in 684 common shares); Mr. Armbruster: $15,463 (paid in 684 common shares and $2,083 in cash); Mr. Inwright: $13,380 (paid in 684 common shares); and Mr. Schermer, Sr.: $6,609 (paid in 333 common shares).

The Board of Directors establishes and oversees the Company's executive officer compensation policies and incentive awards. Mr. Schermer, Jr. earned a base salary of $355,700 plus an annual car allowance of $10,500. Mr. Rose earned a base salary of $314,700 plus an annual car allowance of $8,400. Mrs. Smith earned a base salary of $248,100. In fiscal 2023, Mr. Schermer, Jr. and Mr. Rose each also received 30,000 stock option grants priced at $19.50 per share (the closing price on the date of the grant). Mrs. Smith received 15,000 grants priced at $19.50 per share (the closing price on the date of the grant). The Company also has a deferred compensation program and a bonus program in place for executive officers. Deferred compensation earned and accrued in fiscal 2023 was $261,000 each for Mr. Schermer, Jr. and Mr. Rose. Deferred compensation earned and accrued in fiscal 2023 for Mrs. Smith was $62,000. Bonuses earned and accrued in fiscal 2023 were $483,000 each for Mr. Schermer, Jr. and Mr. Rose. Bonus earned and accrued in fiscal 2023 for Mrs. Smith was $193,000.

*Beneficial Owners*

Other than certain Meritage officers, directors, and principal shareholders identified above, no other shareholders are believed by the Company to beneficially own 5% or more of the Company's outstanding common shares.

*Legal/Disciplinary History*

None.

*Disclosure of Family Relationships*

Robert E. Schermer, Sr. is the father of Robert E. Schermer, Jr. In addition, Mr. Schermer, Jr. is the sole owner of Terra Libre, LLC, a Michigan limited liability company that owns 521,921 shares of MHGU common stock.

*Related Party Transactions*

Robert E. Schermer, Jr. has provided personal guarantees to The Wendy's Company for the Wendy's franchise agreements, as well as personal guarantees to certain vendors.

Robert E. Schermer, Jr. and Gary A. Rose are 39.52% and 39.55% owners, respectively, in the Company's variable interest entity, Restaurant Holdings, of which the Company is a primary beneficiary.

During the prior year, the Company repurchased 9,110 shares of Company common stock from certain Board members at market price.

*Conflicts of Interest*

None.

## Item 12 Financial information for the issuer's most recent fiscal period.

See audited consolidated financial statements for fiscal year ended December 31, 2023, separately posted on the OTC Markets website (www.otcmarkets.com/otcqx/home) for Meritage and incorporated by reference in this Annual Report. The audited consolidated financial statements include the following reports:

(1) balance sheets;
(2) statements of operations;
(3) statements of equity;
(4) statements of cash flows;
(5) notes to financial statements; and
(6) report of independent auditor

## Item 13 Similar financial information for such part of the preceding two fiscal years as the issuer or its predecessor has been in existence.

See audited financial statements for the Company's preceding two fiscal years separately posted on the OTC Markets website (www.otcmarkets.com/otcqx/home) for Meritage and incorporated by reference in this Annual Report. Each year's audited consolidated financial statements include the following comparative reports:

(1) balance sheets;
(2) statements of operations;
(3) statements of equity;
(4) statements of cash flows;
(5) notes to financial statements; and
(6) report of independent auditor

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**Item 14 The name, address, telephone number, and email address of each of the following outside providers that advise the issuer on matters relating to the operations, business development and disclosure:**

Legal Counsel:
Keating Muething & Klekamp PLL
c/o F. Mark Reuter, Esq.
One East Fourth Street, Suite 1400
Cincinnati, OH 45202-3752
(513) 579-6400
mreuter@kmklaw.com

Auditors:
BDO USA P.C.
License #: 1101026824 (State of Michigan)
c/o Lyle VanKlompenberg
200 Ottawa Avenue NW, Suite 300
Grand Rapids, MI 49503
(616) 774-7000
lvanklompenberg@bdo.com

BDO USA P.C. conducted an audit of the consolidated financial statements of Meritage in accordance with generally accepted auditing standards.

**Item 15 Management's Discussion and Analysis or Plan of Operations.**

*Refer to Forward-Looking Statements following Item 20 of this annual disclosure statement.*

**Overview**

Meritage operates in the quick-service and casual dining restaurant industries. The Company has experienced significant growth through acquisitions, newly built locations, reimaging campaigns, and investment in independent concept restaurants.

The Company has committed significant capital resources to the Wendy's brand initiatives, including a commitment to build 52 new restaurants by November 30, 2025 under a development agreement with Wendy's. As of the date of this report, the Company has completed approximately 34 of the new restaurant commitments. Additionally, since 2009, the Company has acquired 295 Wendy's restaurants through 28 separate transactions making it one of the largest franchisees in the Wendy's system. As part of its long-term growth strategy, the Company continues to evaluate acquisition and development opportunities in the Wendy's system, as well as other growth opportunities in the restaurant industry.

As part of the Company's continued growth initiatives, the Company entered into a franchise relationship and associated Area Development Agreement with its newest quick-service franchisor, Taco John's. Subject to certain terms and conditions of the Area Development Agreement, the Company committed to build 55 new Taco John's restaurants by December 31, 2026, with options to develop an additional 150 restaurants thereafter. As of December 31, 2023, the Company operated six Taco John's quick-service restaurants. Of these restaurants, five are located in Michigan and one in Ohio. The Company recently came to an agreement to pause the development schedule through December 31, 2024.

As of December 31, 2023, the Company operated 376 Wendy's quick-service restaurants under franchise agreements with The Wendy's Company. Of the Wendy's restaurants, eight restaurants are located in Arkansas, 32 in Connecticut, 59 in Florida, 51 in Georgia, 12 in Indiana, 13 in Massachusetts, 56 in Michigan, eight in Mississippi, three in Missouri, 24 in North Carolina, 15 in Ohio, 29 in Oklahoma, one in South Carolina, 34 in Tennessee, 16 in Texas and 15 in Virginia.

The Company also has six independent restaurants under two concepts. All six restaurants are located in Michigan.

A schedule of Company restaurants is as follows:

| | Wendy's | Taco John's | Independent Concepts | Total Restaurants |
|---|---|---|---|---|
| Restaurants as of January 2, 2022 | 337 | - | 8 | 345 |
| Acquired restaurants | 6 | - | - | 6 |
| Newly opened restaurants | 15 | 1 | 1 | 17 |
| Closed restaurants | (9) | - | - | (9) |
| Sold restaurants | - | - | (3) | (3) |
| Restaurants as of January 1, 2023 | 349 | 1 | 6 | 356 |
| Acquired restaurants | 25 | - | - | 25 |
| Newly opened restaurants | 5 | 5 | - | 10 |
| Closed restaurants | (3) | - | - | (3) |
| Restaurants as of December 31, 2023 | 376 | 6 | 6 | 388 |

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## **Results of Operations**

Results of operations are summarized below:

| | 2023 (in thousands) | | 2022 (in thousands) | |
|---|---|---|---|---|
| Food and Beverage Revenue | $ 672,494 | 100.0% | $ 626,043 | 100.0% |
| Expenses | | | | |
| Food and beverage | 184,247 | 27.4% | 172,001 | 27.5% |
| Labor and related | 213,808 | 31.8% | 201,852 | 32.2% |
| Occupancy | 86,806 | 12.9% | 77,942 | 12.4% |
| Advertising | 26,273 | 3.9% | 24,442 | 3.9% |
| Franchise fees | 25,439 | 3.8% | 23,818 | 3.8% |
| Other operating | 62,750 | 9.3% | 56,143 | 9.0% |
| Total Operating Expenses | 599,323 | 89.1% | 556,198 | 88.8% |
| General and administrative | 32,012 | 4.8% | 30,809 | 4.9% |
| Preopening, acquisition and closing | 4,809 | 0.7% | 7,645 | 1.2% |
| Depreciation and amortization | 18,552 | 2.8% | 17,418 | 2.8% |
| Total Expenses | 654,696 | 97.4% | 612,070 | 97.7% |
| Income from Operations | 17,798 | 2.6% | 13,973 | 2.3% |
| Other Expense (Income) | | | | |
| Interest - Net | 11,939 | 1.8% | 8,156 | 1.3% |
| Other - Net | (1,053) | (0.2%) | (3,858) | (0.6%) |
| Total Other Expense | 10,886 | 1.6% | 4,298 | 0.7% |
| Income Before Income Taxes | 6,912 | 1.0% | 9,675 | 1.6% |
| Income Tax Expense | 888 | 0.1% | 586 | 0.1% |
| Consolidated Net Income | $ 6,024 | 0.9% | $ 9,089 | 1.5% |
| Net (Loss) Income Attributable to Noncontrolling Interest in Variable Interest Entity | (114) | 0.0% | 604 | 0.1% |
| Consolidated Comprehensive Net Income Attributable to Controlling Interest | $ 6,138 | 0.9% | $ 8,485 | 1.4% |
| Other Comprehensive (Loss) Income - Net of Tax Change in interest rate swap valuation | (2,617) | (0.4%) | 7,557 | 1.2% |
| Consolidated Comprehensive Net Income | $ 3,521 | 0.5% | $ 16,042 | 2.6% |

**Food and Beverage Revenue**

The Company reported revenues of $672.5 million in fiscal 2023, an increase of 7.4% over prior year's revenues of $626.0 million. Total Company "same store sales" (i.e., food and beverage revenue for stores in full operation on a per period basis for both fiscal years) decreased by 0.8% in 2023 over prior year's sales. The annual decline in same store sales was largely due to a decline in transactions resulting from the global impact of economic inflation and evolving market conditions.

The Company's Wendy's restaurants reported sales of $663.0 million in fiscal 2023, an increase of 7.1% over the prior year's sales of $618.8 million. The sales increase is primarily due to the net addition of restaurants achieved through acquisition and new build efforts. The Company's Wendy's restaurants experienced a "same store sales" decrease of 0.4% over prior year's sales.

The Company's Taco John's restaurants reported revenue of $3.7 million in fiscal 2023, versus nominal revenue from its first location opening in December 2022.

The Company's independent concept restaurants reported sales of $5.2 million, a decrease of 27.1% from prior year's sales of $7.1 million. The decrease is partially due to the sale of three of the Company's restaurants in the first half of 2022. Independent concept restaurants experienced a "same store sales" decrease of 37.1% from prior year's sales.

**Cost of Food and Beverages**

The cost of food and beverage as a percent of revenue remained consistent when compared to the prior year. While comparable, costs as a percent of revenue were favorably impacted by the Company's value pricing strategy deployed late in 2023, as well as strategic price increases taken throughout the year. Results were partially offset by a 9.3% increase in the average cost of chicken for fiscal 2023 when compared to the prior year.

In response to the ongoing impact of inflation and evolving market conditions, the Company continues to assess and deploy strategic price increases where applicable.

**Labor and Related Expenses**

Labor and related expenses decreased to 31.8% of revenue for fiscal 2023 from 32.2% of revenue in fiscal 2022. The decrease represents a slight decline in average wage rates from the Company's sustained focus on reducing the impact of inflation on market wages. The Company additionally realized a reduction in labor hours resulting from the impact of the decline in transactions on its transaction-based labor guide.

**Occupancy Expenses**

Occupancy expenses increased to 12.9% of revenue for fiscal 2023 from 12.4% of revenue for fiscal 2022. The increase primarily reflects the inflationary impact of certain utility rates and property tax values.

**Other Operating Expenses**

Other operating expenses increased to 9.3% of revenue for fiscal 2023 from 9.0% of revenue in fiscal 2022. The increase primarily represents the industry-wide inflation on repair and maintenance costs and certain associated supplies.

**General and Administrative Expenses**

General and administrative expenses as a percentage of revenue remained consistent when compared to prior year.

**Preopening, Acquisition and Closing Expenses**

Preopening and acquisition expenses generally represent costs associated with opening new locations, concepts, or product lines in addition to restaurant reimaging and acquisitions.

Closing expenses generally represent actual and estimated costs related to the closure of under-performing restaurants which are limited in quantity and subject to standard approvals by the franchisor, the Wendy's Company. These strategic closures are expected to be ongoing in a continued effort to improve the Company's portfolio position for stronger earnings growth going forward.

**Depreciation and Amortization**

Depreciation and amortization as a percent of revenue remained consistent when compared to the prior year.

**Interest Expense**

The increase in interest expense resulted from the Company's effective interest rate on its variable debt increasing 14.6% over the prior year. The Company's effective interest rate on its fixed debt remained the same.

The Company entered into an interest rate swap agreement with its 2021 refinancing for approximately 50.0% of its debt. The interest rate swap agreement hedges risks related to the variability of cash flows caused by interest rate fluctuations, and significantly mitigated the effective interest rate's potential impact in fiscal 2023.

**Other (Income)**

Other (Income) primarily represents the gain or loss on real estate transactions completed throughout the year as well as stock option expense. The decrease in other income for fiscal 2023 is due to reduced profitability of the Company's real estate transactions, primarily resulting from increased interest rates as well as increased development and construction costs. This decrease was offset by the impact of Employee Retention Credits from the CARES Act recognized in the second quarter of 2023.

**Income Tax Expense**

Income tax expense is summarized as follows:

| | 2023 (in thousands) | 2022 (in thousands) |
|---|---|---|
| Federal income tax expense | $ 219 | $ 220 |
| State and local income tax expense | 364 | 269 |
| Change in deferred income taxes | 305 | 97 |
| Income tax expense | $ 888 | $ 586 |

The Company had net deferred tax liabilities totaling approximately $15.8 million as of both December 31, 2023 and January 1, 2023. The Company's federal income tax expense was reduced by tax credits of $1.6 million and $1.7 million in fiscal years 2023 and 2022, respectively.

## Financial Condition

Management monitors short and long-term cash needs and currently believes that with its ongoing operations and current cash balances, the Company has sufficient capital to meet its ongoing operational needs. Loan covenants of the Company's various loan agreements include requirements for the maintenance of certain financial ratios. At December 31, 2023 and January 1, 2023, the Company was in compliance with these covenants.

### Off-Balance Sheet Arrangements

There were no off-balance sheet arrangements as of December 31, 2023.

## Part E Issuance History

### Item 16 List of securities offerings and shares issued for services in the past two years.

Common Shares Issued for services in: Fiscal Years 2022 and 2023:

| Transaction | Date | Shares Issued |
|---|---|---|
| Director Comp – 1st Quarter 2022 | 04/03/2022 | 1,472 |
| Director Comp – 2nd Quarter 2022 | 07/03/2022 | 1,510 |
| Director Comp – 3rd Quarter 2022 | 10/02/2022 | 1,622 |
| Director Comp – 4th Quarter 2022 | 01/01/2023 | 1,770 |
| Director Comp – 1st Quarter 2023 | 04/02/2023 | 1,359 |
| Director Comp – 2nd Quarter 2023 | 07/02/2023 | 1,304 |
| Director Comp – 3rd Quarter 2023 | 10/01/2023 | 1,762 |
| Director Comp – 4th Quarter 2023 | 12/31/2023 | 1,748 |

### Management Compensation Plans

2017 Directors' Compensation Plan ("2017 Plan"). The 2017 Plan was adopted by the Board of Directors in May 2017. Pursuant to the Plan, all non-employee directors currently receive a fee of $3,385 for attendance at meetings of the Board of Directors and $6,765 for attendance at meetings of the audit committee of the Board. Compensation is paid quarterly in arrears in the form of cash or Company common shares which are priced at the average fair market value during the five trading days prior to the end of the fiscal quarter. A director who is also an employee of Meritage is not separately compensated for serving as a director. This Plan will terminate pursuant to its terms on January 1, 2027.

2008 Directors' Share Equity Plan ("2008 Directors' Plan"), and 2018 Directors' Share Equity Plan ("2018 Directors' Plan"). The 2008 Directors' Plan was adopted by the Board of Directors in March 2008 and amended in May 2014 to extend the Plan's term to May 2024. The 2018 Directors' Plan was adopted by the Board of Directors in March 2018. Under the terms of the 2018 Directors' Plan, non-employee directors are granted an option to purchase 10,000 common shares upon initial election to the Board, and another option to purchase 10,000 common shares upon each subsequent election. The Plan allows for discretionary issuance of additional shares, pending Board approval. The 2008 Directors' Plan will terminate pursuant to its terms in May 2024. The 2018 Directors' Plan will terminate pursuant to its terms in May 2028.

2002 Management Equity Incentive Plan ("2002 Incentive Plan"), 2008 Management Equity Incentive Plan ("2008 Incentive Plan") and 2017 Management Equity Incentive Plan ("2017 Incentive Plan"). The 2002 Incentive Plan authorized up to 1,000,000 common shares for use in the 2002 Incentive Plan. The 2008 Incentive Plan authorized up to 750,000 common shares for use in the 2008 Incentive Plan. The 2017 Incentive Plan was adopted by the Board of Directors in May 2017 and authorized up to 2,000,000 common shares for use in the 2017 Incentive Plan. The purpose of these Plans is to (i) further the long-term growth of Meritage by offering competitive incentive compensation related to long-term performance goals to employees who are largely responsible for planning and directing such growth, (ii) reinforce the commonality of interest between Meritage's shareholders and its employees and (iii) aid in attracting and retaining employees of outstanding abilities and specialized skills. These Plans allow for the award of (i) incentive and non-qualified stock options, (ii) stock appreciation rights which may be issued in tandem with stock options or as freestanding rights, (iii) restricted and unrestricted stock, (iv) performance shares conditioned upon meeting performance criteria, and (v) other awards based in whole or in part by reference to, or otherwise based on, securities of Meritage. The 2002 Incentive Plan terminated pursuant to its terms in May 2012. The 2008 Incentive Plan terminated in May 2018 pursuant to its terms. The 2017 Incentive Plan will terminate pursuant to its terms in May 2027.

## Part F Exhibits

### Item 17 Material Contracts.

Material contracts are separately posted on the OTC Markets website for Meritage and can be accessed at www.otcmarkets.com/otcqx/home or can be found in previous Forms 10-K and other SEC EDGAR filings which can be accessed on the SEC website at www.sec.gov. In addition, the following material contracts are included with this Annual Report:

None.

### Item 18 Articles of Incorporation and Bylaws.

The Articles of Incorporation and Bylaws of the Company are separately posted on the OTC Markets website and can be accessed at www.otcmarkets.com/otcqx/home.

## Item 19 Purchases of Equity Securities by the Issuer and Affiliated Purchasers.

The following table summarizes Meritage's purchases of its common shares, par value $0.01 per share, for the fiscal year ended December 31, 2023:

### Company's Purchase of Equity Securities

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Shares Purchased as Part of Publicly Announced Programs | Shares That May Yet Be Purchased Under the Program (1) |
|---|---|---|---|---|
| Month #1 01/02/23-01/29/23 | 9,110 | $19.45 | --- | 947,050 |
| Month #2 01/30/23-02/05/23 | --- | --- | --- | 947,050 |
| Month #3 02/06/23-04/02/23 | --- | --- | --- | 947,050 |
| Month #4 04/03/23-04/30/23 | --- | --- | --- | 947,050 |
| Month #5 05/01/23-06/04/23 | --- | --- | --- | 947,050 |
| Month #6 06/05/23-07/02/23 | --- | --- | --- | 947,050 |
| Month #7 07/03/23-07/30/23 | --- | --- | --- | 947,050 |
| Month #8 07/31/23-09/03/23 | --- | --- | --- | 947,050 |
| Month #9 09/04/23-10/01/23 | --- | --- | --- | 947,050 |
| Month #10 10/02/23-10/29/23 | --- | --- | --- | 947,050 |
| Month #11 10/30/23-12/03/23 | --- | --- | --- | 947,050 |
| Month #12 12/04/23-12/31/23 | --- | --- | --- | 947,050 |

**(1)** The Board of Directors authorized the Company to repurchase from time to time, subject to capital availability, up to 550,000 shares of Meritage's common stock through open market transactions or otherwise. In May 2022, the Board authorized an additional 1,000,000 shares for repurchase, subject to capital availability. There is no expiration date relating to this program, and the Board is permitted to rescind the program at any time.

**(2)** The Board of Directors authorized the Company to repurchase from time to time, subject to capital availability, up to 100,000 shares of Meritage's preferred stock. There is no expiration date relating to this program, and the Board is permitted to rescind the program at any time. During fiscal 2023, there were no preferred shares repurchased. As of fiscal year ended December 31, 2023, there were 96,533 shares that may yet be purchased under this program.

## Item 20 Issuer's Certifications.

I, Robert E. Schermer, Jr., Chief Executive Officer, certify that:

1. I have reviewed this annual disclosure statement of Meritage Hospitality Group Inc.;

2. Based on my knowledge, this disclosure statement 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 disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

March 6, 2024

Robert E. Schermer, Jr.
Chief Executive Officer

I, Tracey A. Smith, Chief Financial Officer, certify that:

1. I have reviewed this annual disclosure statement of Meritage Hospitality Group Inc.

2. Based on my knowledge, this disclosure statement 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 disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

March 6, 2024

Tracey A. Smith
Chief Financial Officer

FORWARD-LOOKING STATEMENTS

*Certain statements contained in the reports we submit to the OTC, including this report, that are not historical facts constitute forward-looking statements. These statements may be identified by words such as "estimates," "anticipates," "hopes," "projects," "plans," "expects," "believes," "should," "would," and similar expressions (including the negative versions), and by the context in which they are used. Such statements are based only upon Meritage's current expectations. Any forward-looking statement speaks only as of the date made. Reliance should not be placed on forward-looking statements because they involve known and unknown risks, uncertainties and other factors which may cause actual results, performance, or achievements to differ materially from those expressed or implied. Meritage undertakes no obligation to update any forward-looking statements to reflect events or circumstances after the date on which they are made.*

*Statements concerning expected financial performance, business strategies and actions which Meritage intends to pursue to achieve its strategic objectives, constitute forward-looking statements. Implementation of strategies and achievement of financial performance are subject to numerous conditions, uncertainties, and risk factors, which could cause actual performance to differ materially from the forward-looking statements. These include, without limitation: competition; changes in the national or local economy; changes in consumer preferences, tastes and eating habits; concerns about the nutritional quality of our restaurant menu items; concerns about the nutritional quality of our restaurant menu items; economic recessions, disruptions to or reductions in business operations, liquidity, prospects or supply chains due to pandemics, epidemics, widespread health emergencies, or outbreaks of infectious diseases, its variants and developments related to these types of events; concerns about the consumption of beef or other menu items due to diseases or other food safety issues, including, without limitation, E. coli bacteria; promotions and price discounting by competitors; severe weather and natural disasters including, without limitation, tropical storms, hurricanes, or tornadoes; changes in travel patterns; road construction; demographic trends; failure to manage social media trends; inflation, including related increases in the cost of food, labor and energy; supply chain interruptions; the availability and cost of suitable restaurant sites; the ability to finance expansion; interest rates; insurance costs; the availability of adequate managers and hourly-paid employees; risks associated with leasing real property; directives issued by the franchisor regarding operations and menu pricing; the general reputation of Meritage's and its franchisors' restaurants; the relationships between Meritage and its franchisors; legal claims; security, including cyber security and information technology security; credit card fraud; Meritage's ability to consummate acquisitions or, if consummated, to successfully integrate acquired businesses into Meritage's operations; Meritage's execution of growth initiatives; the recurring need for restaurant renovation and capital improvements; government regulations relating to, among other things, zoning, public health, sanitation, alcoholic beverage control, environment, food preparation, minimum and overtime wages and tips, employment of minors, citizenship requirements, working conditions, other labor and employment matters, and the operation of its restaurants; economic changes in the state and local economies where our restaurants are located including, without limitation, Arkansas, Connecticut, Florida, Georgia, Indiana, Massachusetts, Michigan, Mississippi, Missouri, North Carolina, Ohio, Oklahoma, South Carolina, Tennessee, Texas and Virginia.*