2012 Annual Report

NOW WE'RE ROLLING

Sonic began in 1953 in Shawnee, Oklahoma. Today, we franchise and operate the largest chain of drive-in restaurants in the country, with more than 3,500 Sonic Drive-Ins from coast to coast.

Our drive-in experience, together with a unique menu and personalized Carhop service, positions us as one of the most highly differentiated concepts in the quick-service restaurant (QSR) industry. At a typical Sonic Drive-In, customers park in one of 16 to 24 canopy-covered spaces and place orders through a speaker system. A smiling Carhop delivers the customer's order car-side. Customers also may enjoy patio dining or drive-thru service at many Sonic locations.

Sonic Drive-Ins feature signature menu items, offering made-when-you-order footlong quarter pound coneys, six-inch premium beef hot dogs, hamburgers, popcorn chicken, chicken strips and chicken sandwiches. Likewise, we are famous for our fresh-made onion rings and tater tots, and we offer a full breakfast menu all day, including a delicious line-up of Breakfast Burritos. We also are known for our extensive range of Frozen Favorites® treats and Fountain Favorites® drinks, like Cherry Limeades, real fruit slushes, shakes and blasts, making Sonic Your Ultimate Drink Stop®. Sonic also offers a variety of choices for health-conscious customers, such as apple slices and many low-calorie drinks, 20,064 in fact, including a diet version of our classic Cherry Limeade.

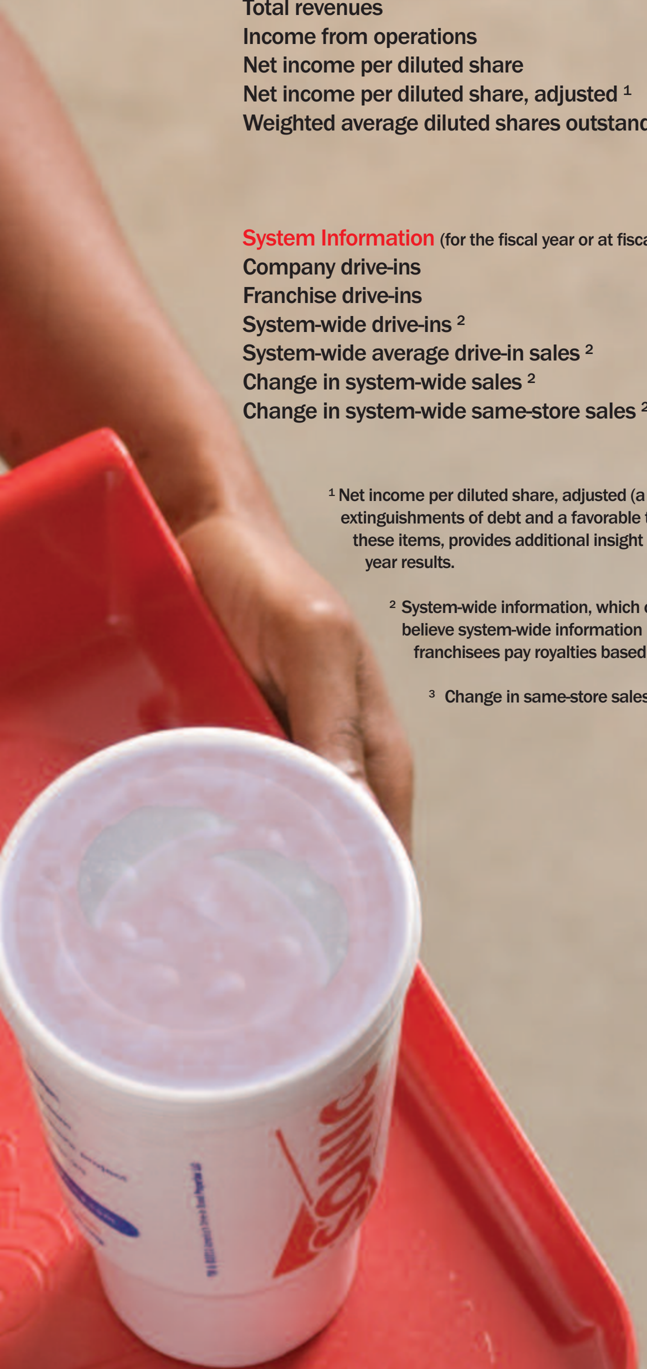
Financial Highlights

	2012	2011	Change
	($ in thousands, except per share amounts)		
Operations (for the fiscal year)			
Total revenues	$ 543,730	$ 545,951	–
Income from operations	$ 88,940	$ 83,308	7%
Net income per diluted share	$ 0.60	$ 0.31	94%
Net income per diluted share, adjusted [1]	$ 0.60	$ 0.53	13%
Weighted average diluted shares outstanding	60,172	61,943	-3%
System Information (for the fiscal year or at fiscal year's end)			
Company drive-ins	409	446	-8%
Franchise drive-ins	3,147	3,115	1%
System-wide drive-ins [2]	3,556	3,561	–
System-wide average drive-in sales [2]	$ 1,066	$ 1,037	3%
Change in system-wide sales [2]	2.7 %	1.9 %	
Change in system-wide same-store sales [2, 3]	2.2 %	0.5 %	

[1] Net income per diluted share, adjusted (a non-GAAP measure) excludes items of $0.22, net, in 2011 associated with early extinguishments of debt and a favorable tax settlement. We believe showing net income per diluted share, adjusted to exclude these items, provides additional insight into the strength of our operations and aids in the comparability of current- and prior-year results.

[2] System-wide information, which combines company and franchise drive-in information, is a non-GAAP measure. We believe system-wide information is useful in analyzing the growth of the Sonic brand as well as our revenues, since franchisees pay royalties based on a percentage of sales.

[3] Change in same-store sales based on drive-ins open for a minimum of 15 months.



To Our Shareholders:

Reporting to you this year feels different... and it feels better!

In reviewing this letter and considering where our company is, remember these three things:

- How we have improved;
- Why I believe we are on better footing; and
- How we are going to sustain this improvement, despite persistent external headwinds.

We have improved because our food quality and customer service have improved. Our customers have told us this consistently over the last four years, as we have reported to you in prior years.

We have improved because we have become more focused on customer value and pricing tiers than we were before the recession. Our customers tell us the value we offer has improved versus three and four years ago.

We have improved because our media buying and television creative, including a return to our "Two Guys" campaign, are now much more effective. Stronger vendors combined with more effective day-part strategies and product promotions are driving positive sales. This was not true 18 to 24 months ago, but it is so now. Positive feedback from customers and franchisees, along with favorable sales and profitability trends, are evidence of this.

And so, the Sonic brand is on sound footing with growing sales and profitability as a result of these improvements and others like:

- Stronger, more stable company drive-in level management;
- The addition of new talent at our company, including our new chief marketing officer, James O'Reilly, and key marketing staff members;
- Greater national media presence; we have secured the overwhelming support of our franchisees to pursue media strategies, specifically greater national presence, that should lift our brand awareness in every market and nationwide;
- A stronger product pipeline, which is now the best it has been in years;
- Lower new drive-in building costs, reduced by 15% to 20%, to improve the return on investment (ROI) for new Sonic Drive-Ins; and
- A stronger technology platform, setting us up for good things to come!

Our work to increase shareholder value relies on a multi-layered growth strategy, which incorporates sales growth, leverage from higher sales, strategic use of free cash, increasing royalty revenue and new drive-in development, to achieve double-digit earnings per share growth. We were very pleased that positive same-store sales in fiscal 2012 fueled other layers in our multi-layered growth strategy, including greater operating leverage, increased franchising revenue and strategic use of cash, which resulted in a 13% increase in earnings per share for the year to $0.60 from $0.53, on an adjusted basis, for fiscal 2011. The improvement was disproportionately greater in the latter part of the year when our earnings per share for the fourth fiscal quarter improved 25%.

We have the view that the initiatives we have planned for 2013 and beyond will only build and complement the foundational improvements made over the past three years. All of these components are expected to sustain our improvement and increase shareholder value over the near term and long term. So life is better at Sonic.

In calendar year 2013, consumers will get the word about Sonic more than ever due to reallocation of a significant portion of our media dollars from local to national cable. This media effort will more powerfully support our strengthened product pipeline. Every market, as a result, will be able to promote all five day-parts in every quarter, something not previously experienced at Sonic on a chain-wide basis.

Our new product pipeline, across all day-parts, will also strengthen in 2013, so the power of the incremental media discussed in the preceding paragraph will be even more potent!

In calendar 2013, we will also begin the implementation of a new point-of-sale system, starting with our company drive-ins. This initiative will assist every Sonic Drive-In with labor and inventory management, cash controls and the integration of our store operations more completely with an improved supply chain management system. All of this will result in considerable improvement in profitability at the drive-in level.

In 2013 and beyond, we'll continue to focus on improving customer service and, as important, the consistency of the experience customers have at Sonic. Few things could strengthen the perception of our brand more!

As same-store sales have grown, profitability at our drive-ins also has increased – by more than $11,000 per drive-in during the last fiscal year. This increasing profitability also raises our franchisees' appetite for new drive-in development. In addition to improved drive-in level sales and profitability, we have also focused on the cost of a new drive-in, the other half of the ROI equation. We have done this by achieving a $150,000 to $200,000 reduction in construction costs, while positively impacting the drive-in's throughput capacity. A half-dozen drive-ins have opened utilizing this structure and are now achieving an enhanced return on investment. This initiative results in improved returns for our franchisees and shareholders alike.

This lower cost construction and operating model positions us to focus on smaller core markets we've previously bypassed, but it will also enable us to revamp the rate of growth of new drive-ins across the system. We have added management talent and depth to this area of our company to drive the effort. The anticipated regeneration of new drive-in development will contribute to the scale of our marketing efforts and the profitability of all franchisees and our company!

The combination of these initiatives and the strong cash flow we generate each year supported our fiscal year 2012, stock repurchase program, which totaled $30 million. We executed that program in full, and our Board of Directors has approved an additional repurchase plan for fiscal year 2013 totaling $40 million.

We are confident our multi-layered growth strategy, including an expected reacceleration of new drive-in development, will enable us to achieve double-digit earnings per share growth in the near and long term. With this business update, I hope you will take away why we believe our business is stronger and will result in continued growth of our brand and our earnings. We appreciate your investment alongside us and look forward to sharing the outcome of these investments in the coming years!

Sincerely,

Clifford Hudson

Clifford Hudson
Chairman and Chief Executive Officer

FAST. FUN. FABULOUS!

It's like a party for your taste buds.

At Sonic, customers have always come for great food, great flavors, and great selection. We're THE destination for a completely customizable, all-day menu to satisfy virtually any craving - even one like a Super SONIC® Bacon Double Cheeseburger for breakfast or our Ultimate Meat & Cheese Breakfast Burrito™ for a late night snack - and everything in between. And we're still the Ultimate Drink Stop®, home to almost 400,000 different drink combinations to quench any thirst. More than 20,000 of these drink combinations have less than 60 calories.

That's good news for our customers, but not good enough for Sonic. Over the past two years, we've continued to take our diverse menu to new heights, with an increasing focus on quality and distinctive product platforms. Two years ago, we introduced Real Ice Cream for our Frozen Favorites® treats, improved our burgers, and upgraded our coney selection with the launch of a true footlong quarter pound coney. Last year, we expanded on that with a new line of premium beef hot dogs in several craveable versions, including the famous New York, Chicago and All-American Dogs.

And there's more. This year, we continued to expand our new product news with the introduction of a new line of Flatmelts™, savory combinations of steak, chicken, bacon and other delights! Recently, we markedly upgraded our offering of chicken sandwiches - grilled or crispy - taking a fresh approach on a classic favorite and incorporating a whole grain ciabatta bun, giving our customers both higher quality and an expanded selection of menu items for those who are calorie-conscious. Our introduction of a mini cup for our Real Ice Cream treats is another way that we have responded to the desire for smaller portion sizes. At Sonic, it's always been about choice.

Mt. Juliet, TENNESSEE

6 ounces of pure bliss

So good, you have to eat slow, very slow! You'll want to savor every bite. We reintroduced our Jumbo Popcorn Chicken across our system in March 2012, and cheers went out all across Sonicland.

Sonic serves Seaweed! (and Flamingo)

Sonic is the only place you can get great tasting slush flavors like Flaviator Slush, Haunted Berry Slush, Houston Texan Slush, Island Breeze Slush, Rainbow Slush, Seaweed Slush, Hulk Slush and... the Pink Flamingo.

32°

Frozen Favs

What do the best shakes, sundaes, cones, floats, splits, Sonic Blasts®, and CreamSlush® Treats have in common? They all start with Real Ice Cream. Sonic's got it. Others don't.

I'm Diving In!

Each year Sonic sells enough Cherry Limeades to fill more than 50 Olympic-sized pools.

IT'S ALWAYS TASTY.

That's a Lot of Tots

Last year, we sold enough Tater Tots that when placed end to end would circle the globe...TWICE.

"Your footlong coneys remind me of eating at the seashore when I was a **kid.**"

"I remember the first time I stopped at **Sonic.** My carhop's name was Becky."

"Real ice cream milk shakes on Friday afternoon after school have become a family **tradition.**"

"Awesome"

Fresh Thinking

Sonic's Premium Grilled Chicken Sandwich is new and improved, with a savory chicken breast filet and whole grain ciabatta bun. Now that's a FRESH approach on a CLASSIC favorite.

NOW IN A MORE CONVENIENT SIZE.

Bringing the Sonic experience to more of America.

In fiscal 2012, Sonic developed a smaller-footprint drive-in to enable our franchisees to capitalize on development opportunities. With its lower costs to build and operate, it provides an ideal vehicle for our franchisees to enter smaller markets that might not be able to sustain our traditionally larger drive-ins. On the other hand, the new smaller drive-in is a versatile way to further develop larger markets that are well established or where land availability is limited. Either way, the new small Sonic Drive-In means added flexibility in our business model, lower up-front capital and reduced operational risk.

For almost 60 years, Sonic has been a franchise-driven business, with our franchisees providing strong leadership for the brand in so many areas, including new drive-in development. We think the addition of our small-format drive-in will help reignite overall development activity over time by making the economics of expansion more attractive for franchisees. This, in turn, will contribute to a stronger development pipeline and enhanced future growth, taking us to new places like never before. You see, sometimes less can be more. More opportunity. More sales. More profit.

Bel Air, MARYLAND

25% smaller

100% Sonic

Bel Air, a town of about 10,500 people located less than 30 miles northeast of Baltimore, is a perfect place for a small-format Sonic Drive-In. With 16 drive-in spaces instead of the typical 20 to 36 found at most larger Sonic Drive-Ins, it fits neatly on a lot that is 25 to 40 percent smaller than usual. Even with its reduced size, this drive-in is booming, with no sacrifice in brand perception. In fact, the franchisee has found that with its re-engineered kitchen, food orders are prepared and delivered as fast or faster than at a traditional Sonic Drive-In, using less labor for greater operational efficiency.

Welcome Back "Guys"

The return of the two guys format during the third quarter of fiscal 2012 allowed us to reignite a multi-day-part promotional strategy with compelling products and promotions that work effectively throughout the day. In contrast to many competitors, our multi-day-part strategy is a critical element to driving consistently positive same-store sales, since more than half of our business occurs outside of lunch and dinner.

Because many customers still had high awareness of the two guys, this creative strategy provided instant brand recognition and enabled us to implement a layered day-part promotional strategy to highlight a variety of products and promote all of our day-parts more effectively in a shorter time frame. In addition, their distinctive brand of humor combined with our brand of fun provide great opportunities to expand our presence in the social media landscape.

WINNERS THRIVE HERE.

96%

Excellent Customer Service

That's the **average Sonic service satisfaction score** for our three Dr Pepper Sonic Games team medal winners below. These company drive-ins have embraced and benefitted from our sales- and profit-driving initiatives, such as an added emphasis on customer service and skating, a reduction in management layers between drive-in operations and the corporate office, and a new manager compensation structure in fiscal 2010, all of which have led to improved performance.

Perhaps nothing illustrates the resurgence of our company drive-ins better than their performance at the annual Dr Pepper Sonic Games, which pits the top qualifying teams from all across the country in competition at every key aspect of drive-in operations. In 2012, for the first time ever, company drive-ins placed first, second and third in these games. This performance helps illustrate the contributions of company drive-ins to our business, with improved sales and profitability providing meaningful value to earnings. More important, company drive-ins continue to present one of the best opportunities for enhanced earnings and shareholder value over the long term.

Silver Medal

Littleton, Colorado
Usama Khan, Supervisor (left)
Jose Ramos, Manager (right)

Gold Medal

Greenbrier, Tennessee
Kelli Linville, Supervisor (left)
Tim Busby, Manager (right)

Bronze Medal

Arvada, Colorado
James Martinez, Manager (left)
Alex Marizcurrena, Supervisor (right)

Mann Hill Hill & Twiggs
Franchise Group
Houston, Texas
Keith Twiggs (seated)
Robert Mann (left)
Ken Hill (center)
Doug Hill (right)

NO.1

The Troy Smith Award

The Mann Hill Hill & Twiggs franchise group in Houston, which operates 31 Sonic Drive-Ins, won Sonic's most prestigious award for franchisees, The Troy Smith Award, for 2012. Named for the company's founder, this annual award recognizes a high-performing franchise group that has contributed significantly to the growth of the Sonic brand, mentored newer franchisees, and helped create opportunities for others.

COMING TO A SONIC DRIVE-IN NEAR YOU.

New POS provides better business insight.

What happens when you have back-office tools, such as labor scheduling and inventory management, integrated with a state-of-the-art point-of-sale (POS) platform? You get more efficient margins and increased profitability with improved customer service. Sonic's Technology Advisory Council, composed of franchisees from across the system, selected a new POS platform that enhances drive-in level profitability, reduces operational complexity and generates higher drive-in level profit. Implementation of the new POS platform will begin in 2013 and is expected to play an important role in driving additional shareholder value in 2014 and subsequent years.

Barbara Stammer
The Merritt Group
Las Cruces, NM

Buddy McClain
McClain, Vaughn & Partners
(MVP) Sonic Group
Ridgeland, MS

Don Welsh
Simple Tie Ventures, LP
Philadelphia, PA

Mike Perry
Great Lake Sonics, LLC/MHR
Chicago, IL

James Junkin
D.L. Rogers Companies
North Richland Hills, TX

Linda Clark
Encore Restaurants, Inc.
Grapevine, TX

Joey Pierson
Boom Foods, LLC
Birmingham, AL

POS Platform

Near real-time data to:

- Reduce waste
- Manage inventory
- Improve labor management
- Streamline kitchen preparation

Supply chain management to link and better manage:

- Demand forecasting
- Suppliers
- Distributors
- Drive-in kitchens

What it means for our customers:

- Improved order accuracy
- Expedited service times
- Greater satisfaction
- An improved dining experience

What it means for our operators:

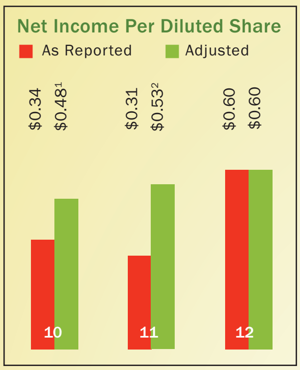
- Improved drive-in profitability
- Higher customer loyalty
- Enhanced sales opportunity

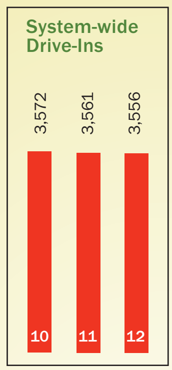
Tech Group Brings Diversity and Experience

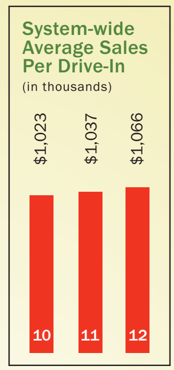
Seven franchisees, six states, varying viewpoints, one way forward. That's the way you Sonic! At Sonic, we are always thinking about how to move our business forward, and technology improvements are a big part of this effort. Remember PAYS (Pay At Your Stall), when we introduced a streamlined credit/debit card payment system years back, and the sales and profit bump it produced?

Today, like then, our technology initiatives are guided by the insight, wisdom and experience of a group of franchisees who have a real sense for our business, now and in the years to come. Recently, our Technology Advisory Council came together to ensure one of the most significant leaps forward we will make as a brand with our new POS platform.

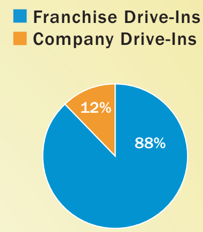
Sonic at a Glance







Business Mix



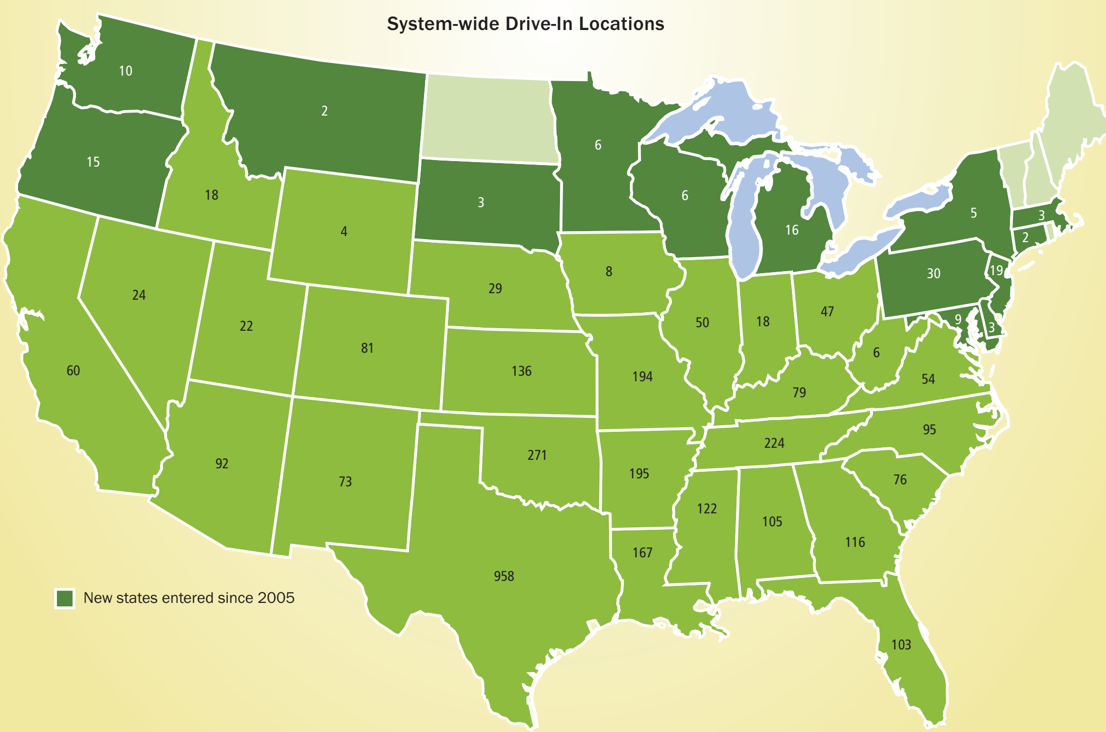
Non-GAAP Adjustments (after-tax)

[1] Excludes $0.14, net, associated with impairment provisions, stock option exchange program, refranchising program and early extinguishments of debt.

[2] Excludes $0.22, net, associated with early extinguishments of debt and a favorable tax settlement.

Locations

System-wide Drive-In Locations



Selected Financial Data

The following table sets forth selected financial data regarding the company's financial condition and operating results. One should read the following information in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" below and the company's Consolidated Financial Statements included elsewhere in this report.

	Year Ended August 31,				
(In thousands, except per share data)	**2012**	**2011**	**2010**	**2009**	**2008**
Income Statement Data:					
Company Drive-In sales	**$ 404,443**	$ 410,820	$ 414,369	$ 567,436	$ 671,151
Franchise Drive-Ins:					
Franchise royalties	**125,989**	124,127	122,385	126,706	121,944
Franchise fees	**2,024**	1,744	2,752	5,006	5,167
Lease revenue	**6,575**	6,023	6,879	3,985	1,519
Other	**4,699**	3,237	4,541	3,148	1,978
Total revenues	**543,730**	545,951	550,926	706,281	801,759
Cost of Company Drive-In sales	**347,470**	356,236	354,659	464,876	526,180
Selling, general and administrative	**65,173**	64,943	66,847	63,358	61,179
Depreciation and amortization	**41,914**	41,225	42,615	48,064	50,653
Provision for impairment of long-lived assets	**764**	824	15,161	11,163	571
Total expenses	**455,321**	463,228	479,282	587,461	638,583
Other operating income (expense), net	**531**	585	(763)	12,508	2,954
Income from operations	**88,940**	83,308	70,881	131,328	166,130
Interest expense, net[1]	**30,978**	54,929	36,073	35,657	47,927
Income before income taxes	**$ 57,962**	$ 28,379	$ 34,808	$ 95,671	$ 118,203
Net income-including noncontrolling interests	**36,085**	19,225	25,839	64,793	82,241
Net income-noncontrolling interests	**–**	–	4,630	15,351	21,922
Net income-attributable to Sonic Corp.	**$ 36,085**	$ 19,225	$ 21,209	$ 49,442	$ 60,319
Income per share:					
Basic	**$ 0.60**	$ 0.31	$ 0.35	$ 0.81	$ 1.00
Diluted	**$ 0.60**	$ 0.31	$ 0.34	$ 0.81	$ 0.97
Weighted average shares used in calculation:					
Basic	**60,078**	61,781	61,319	60,761	60,403
Diluted	**60,172**	61,943	61,576	61,238	62,270
Balance Sheet Data:					
Working capital (deficit)	**$ 26,635**	$ 22,178	$ 15,320	$ 84,813	$ (13,115)
Property, equipment and capital leases, net	**443,008**	464,875	489,264	523,938	586,245
Total assets	**680,760**	679,742	737,320	849,041	836,312
Obligations under capital leases (including current portion)	**31,676**	34,063	36,256	39,461	37,385
Long-term debt (including current portion)	**481,793**	497,013	591,621	699,550	759,422
Stockholders' equity (deficit)	**59,247**	51,696	22,566	(2,352)	(61,020)
Cash dividends declared per common share	**–**	–	–	–	–

(1) Includes net loss (gain) from early extinguishment of debt of $23.0 million, $0.3 million and $(6.4) million for fiscal years 2011, 2010 and 2009, respectively.

Overview

Description of the Business. Sonic operates and franchises the largest chain of drive-in restaurants in the United States. As of August 31, 2012, the Sonic system was comprised of 3,556 drive-ins, of which 12% were Company Drive-Ins and 88% were Franchise Drive-Ins. Sonic Drive-Ins feature signature menu items such as specialty drinks including cherry limeades and slushes, ice cream desserts, made-to-order sandwiches and hamburgers, six-inch premium beef hot dogs, footlong quarter pound coneys, hand-battered onion rings, tater tots and a unique breakfast menu. We derive our revenues primarily from Company Drive-In sales and royalties from franchisees. We also receive revenues from leasing real estate to franchisees, initial franchise fees, earnings from minority investments in franchise operations and other miscellaneous revenues.

Costs of Company Drive-In sales relate directly to Company Drive-In sales. Other expenses, such as depreciation, amortization and general and administrative expenses, relate to our franchising operations, as well as Company Drive-In operations. Our revenues and Company Drive-In expenses are directly affected by the number and sales volumes of Company Drive-Ins. Our revenues and, to a lesser extent, selling, general and administrative expenses also are affected by the number and sales volumes of Franchise Drive-Ins. Initial franchise fees and franchise royalties are directly affected by the number of Franchise Drive-In openings. Lease revenues are generated by the leasing of land and buildings for Company Drive-Ins that have been sold to franchisees.

Overview of Business Performance. Sales momentum for fiscal year 2012 continued to improve from fiscal year 2011. System-wide same-store sales increased 2.2% during fiscal year 2012 as compared to an increase of 0.5% for fiscal year 2011. Same-store sales at Company Drive-Ins increased by 2.8% during fiscal year 2012 as compared to an increase of 1.8% for 2011. We believe the initiatives we have implemented over the last few years, including product quality improvements, a greater emphasis on personalized service and a new creative strategy, have set a solid foundation for growth which is reflected in our operating results. We use a multi-layered growth strategy which incorporates sales growth, operating leverage, deployment of cash, an ascending royalty rate and new drive-in development to achieve earnings growth. Positive system-wide same-store sales is the most important layer and drives operating leverage and increased operating cash flows.

Revenues decreased slightly to $543.7 million for fiscal year 2012 from $546.0 million for the same period last year, which was primarily related to a decline in revenues resulting from the refranchising of 34 Company Drive-Ins during the second fiscal quarter of 2012, mostly offset by an increase in same-store sales. Restaurant margins at Company Drive-Ins improved by 80 basis points during fiscal year 2012, reflecting the leverage of positive same-store sales as well as moderating commodity cost inflation. Net income and diluted earnings per share for fiscal year 2012 were $36.1 million and $0.60, respectively, as compared to net income of $19.2 million or $0.31 per diluted share for fiscal year 2011. Excluding an after-tax net loss of $14.4 million from the early extinguishment of debt during fiscal year 2011 and a $1.1 million tax benefit recognized during the first quarter of fiscal year 2011 relating to the favorable settlement of state tax matters, net income and diluted earnings per share for fiscal year 2012 increased 11% and 13%, respectively.

Franchisees opened 36 new drive-ins and relocated or rebuilt 17 existing drive-ins during the fiscal year. While the number of new drive-in openings in fiscal year 2012 was down compared to the prior year, investments by franchisees in existing locations continued throughout the year, as evidenced by an increase in Franchise Drive-Ins relocated or rebuilt. We also continued our expansion in several new markets.

The growth and success of our business is built around implementation of our brand strategy, which features the following components:

- Improved revenue and margin performance of Company Drive-Ins with consistent and improved operations execution; and
- Same-store sales growth fueled by re-emphasizing our core brand strengths, including high-quality products, the introduction of new limited-time products and service differentiation with carhops.

The following non-GAAP adjustments are intended to supplement the presentation of the company's financial results in accordance with GAAP. We believe the exclusion of these items in evaluating the change in net income and diluted earnings per share for the periods below provides useful information to investors and management regarding the underlying business trends and the performance of our ongoing operations and is helpful for period-to-period and company-to-company comparisons, which management believes will assist investors in analyzing the financial results for the company and predicting future performance.

	Fiscal Year Ended August 31, 2012		Fiscal Year Ended August 31, 2011	
	Net Income	Diluted EPS	Net Income	Diluted EPS
Reported – GAAP	**$ 36,085**	**$ 0.60**	$ 19,225	$ 0.31
After-tax net loss from early extinguishment of debt	**–**	**–**	14,439	0.24
Tax benefit from favorable tax settlement	**–**	**–**	(1,073)	(0.02)
Adjusted - Non-GAAP	**$ 36,085**	**$ 0.60**	$ 32,591	$ 0.53

The following table provides information regarding the number of Company Drive-Ins and Franchise Drive-Ins operating as of the end of the years indicated as well as the system-wide change in sales and average unit volume. System-wide information includes both Company Drive-In and Franchise Drive-In information, which we believe is useful in analyzing the growth of the brand as well as the company's revenues, since franchisees pay royalties based on a percentage of sales.

	System-wide Performance Year Ended August 31,		
($ in thousands)	2012	2011	2010
Percentage increase (decrease) in sales	**2.7%**	1.9%	(5.7)%
System-wide drive-ins in operation [(1)]:			
Total at beginning of year	**3,561**	3,572	3,544
Opened	**37**	43	85
Closed (net of re-openings)	**(42)**	(54)	(57)
Total at end of year	**3,556**	3,561	3,572
Average sales per drive-in:	**$ 1,066**	$ 1,037	$ 1,023
Change in same-store sales [(2)]:	**2.2%**	0.5%	(7.8)%

(1) Drive-ins that are temporarily closed for various reasons (repairs, remodeling, relocations, etc.) are not considered closed unless the company determines that they are unlikely to reopen within a reasonable time.

(2) Represents percentage change for drive-ins open for a minimum of 15 months.

The following table provides information regarding drive-in development across the system.

	Year Ended August 31,		
	2012	2011	2010
New drive-ins:			
Company	**1**	3	5
Franchise	**36**	40	80
System-wide	**37**	43	85
Rebuilds/relocations:			
Company	**1**	3	–
Franchise	**17**	11	23
System-wide	**18**	14	23

Results of Operations

Revenues. The following table sets forth the components of revenue for the reported periods and the relative change between the comparable periods.

($ in thousands)	Revenues Year Ended August 31, 2012	2011	Increase/ (Decrease)	Percent Increase/ (Decrease)
Revenues:				
Company Drive-In sales	**$ 404,443**	$ 410,820	$ (6,377)	(1.6)%
Franchise Drive-Ins:				
Franchise royalties	**125,989**	124,127	1,862	1.5
Franchise fees	**2,024**	1,744	280	16.1
Lease revenue	**6,575**	6,023	552	9.2
Other	**4,699**	3,237	1,462	45.2
Total revenues	**$ 543,730**	$ 545,951	$ (2,221)	(0.4)%

($ in thousands)	Revenues Year Ended August 31, 2011	2010	Increase/ (Decrease)	Percent Increase/ (Decrease)
Revenues:				
Company Drive-In sales	$ 410,820	$ 414,369	$ (3,549)	(0.9)%
Franchise Drive-Ins:				
Franchise royalties	124,127	122,385	1,742	1.4
Franchise fees	1,744	2,752	(1,008)	(36.6)
Lease revenue	6,023	6,879	(856)	(12.4)
Other	3,237	4,541	(1,304)	(28.7)
Total revenues	$ 545,951	$ 550,926	$ (4,975)	(0.9)%

The following table reflects the changes in sales and same-store sales at Company Drive-Ins. It also presents information about average unit volumes and the number of Company Drive-Ins, which is useful in analyzing the growth of Company Drive-In sales.

($ in thousands)	Company Drive-In Sales Year Ended August 31, 2012	2011	2010
Company Drive-In sales	**$ 404,443**	$ 410,820	$ 414,369
Percentage decrease	**(1.6)%**	(0.9)%	(27.0)%
Company Drive-Ins in operation[1]:			
Total at beginning of year	**446**	455	475
Opened	**1**	3	5
Sold to franchisees, net	**(35)**	(5)	(16)
Closed (net of re-openings)	**(3)**	(7)	(9)
Total at end of year	**409**	446	455
Average sales per Company Drive-In	**$ 958**	$ 920	$ 893
Percentage increase (decrease)	**4.1%**	3.0%	(6.4)%
Change in same-store sales[2]	**2.8%**	1.8%	(8.8)%

(1) Drive-ins that are temporarily closed for various reasons (repairs, remodeling, relocations, etc.) are not considered closed unless the company determines that they are unlikely to reopen within a reasonable time.

(2) Represents percentage change for drive-ins open for a minimum of 15 months.

Same-store sales for Company Drive-Ins increased 2.8% for fiscal year 2012 and 1.8% for fiscal year 2011, an improving trend that we attribute to the initiatives we have implemented. In addition to the implementation of system-wide initiatives over the last few years, we have implemented a number of initiatives at Company Drive-Ins which have contributed to improved performance. These initiatives included restructuring our Company Drive-In operations to reduce excess management layers, revising the compensation program at the drive-in level, and implementing a customer service initiative to improve sales and profits. Company Drive-In sales decreased $6.4 million, or 1.6%, during fiscal year 2012 as compared to 2011. This decrease was primarily attributable to an $18.6 million reduction in sales from the refranchised drive-ins discussed earlier and a $2.3 million decrease related to drive-ins that were closed during or subsequent to fiscal year 2011 partially offset by a $11.0 million improvement in same-store sales and $3.5 million of incremental sales from new drive-in openings during fiscal year 2011.

For fiscal year 2011, Company Drive-In sales decreased $3.5 million, or 0.9%, as compared to 2010. This decrease was primarily attributable to a $7.2 million decrease in sales from the refranchising of 16 Company Drive-Ins in the second quarter of fiscal year 2010 and six drive-ins in fiscal year 2011 as well as a $4.4 million decrease related to drive-ins that were closed during or subsequent to fiscal year 2010. These decreases were partially offset by an $8.1 million increase from an improvement in same-store sales and, to a lesser extent, new drive-in openings during fiscal year 2011.

The following table reflects the change in franchising revenues (franchise royalties, franchise fees and lease revenues) as well as franchise sales, average unit volumes and the number of Franchise Drive-Ins. While we do not record Franchise Drive-In sales as revenues, we believe this information is important in understanding our financial performance since these sales are the basis on which we calculate and record franchise royalties. This information is also indicative of the financial health of our franchisees.

	Franchise Information		
	Year Ended August 31,		
($ in thousands)	**2012**	**2011**	**2010**
Franchising revenues[(1)]	**$ 134,588**	$ 131,894	$ 132,016
Percentage increase (decrease)	**2.0%**	(0.1)%	(2.7)%
Franchise Drive-Ins in operation[(2)]:			
Total at beginning of year	**3,115**	3,117	3,069
Opened	**36**	40	80
Acquired from company, net	**35**	5	16
Closed (net of re-openings)	**(39)**	(47)	(48)
Total at end of year	**3,147**	3,115	3,117
Franchise Drive-In sales	**$3,386,218**	$3,278,208	$3,205,507
Percentage change	**3.3%**	2.3%	(2.0)%
Effective royalty rate	**3.72%**	3.79%	3.82%
Average sales per Franchise Drive-In	**$ 1,081**	$ 1,054	$ 1,043
Change in same-store sales[(3)]	**2.2%**	0.4%	(7.6)%

(1) Consists of revenues derived from franchising activities, including royalties, franchise fees and lease revenues. See *Revenue Recognition Related to Franchise Fees and Royalties in the Critical Accounting Policies and Estimates* section of "Management's Discussion and Analysis of Financial Condition and Results of Operations."

(2) Drive-ins that are temporarily closed for various reasons (repairs, remodeling, relocations, etc.) are not considered closed unless the company determines that they are unlikely to reopen within a reasonable time.

(3) Represents percentage change for drive-ins open for a minimum of 15 months.

Same-store sales for Franchise Drive-Ins increased 2.2% for fiscal year 2012 and 0.4% for fiscal year 2011, an improving trend that we attribute to the initiatives we have implemented. Franchising revenues increased $2.7 million, or 2.0%, for fiscal year 2012 as compared to 2011. The increase in franchising revenues was primarily driven by a $1.9 million increase in franchise royalties. Same-store sales increases combined with incremental royalties from newly constructed and refranchised drive-ins resulted in an increase in royalties of $3.2 million, which was partially offset by a $1.3 million decrease from a lower effective royalty rate. The lower effective royalty rate is due to a temporary reduction in royalty rates from various development incentives and certain franchisee restructuring efforts. Franchisees opened 36 new drive-ins during fiscal year 2012 compared to 40 in the prior year. Franchisee investment in existing drive-ins continued during fiscal year 2012 and included the relocation or rebuilding of 17 drive-ins versus 11 in the prior year.

Franchising revenues were relatively flat in fiscal year 2011 decreasing by $0.1 million, or 0.1%, to $131.9 million as compared to $132.0 million for fiscal year 2010. Franchise royalties increased $1.7 million for fiscal year 2011, which was comprised of a $2.0 million increase from same-store sales and incremental royalties from newly constructed and refranchised drive-ins, partially offset by a $0.3 million decrease from a lower effective royalty rate. Franchise fees declined $1.0 million to $1.7 million in fiscal year 2011, which was primarily related to franchisees opening fewer drive-ins during the year as a result of the weaker overall business environment. Franchisees opened 40 new drive-ins during fiscal year 2011, down from 80 in 2010.

Other revenues increased $1.5 million to $4.7 million in fiscal year 2012 and decreased $1.3 million to $3.2 million in fiscal year 2011 as compared to prior years, primarily due to changes in income from investments in franchise operations.

Operating Expenses. The following table presents the overall costs of drive-in operations as a percentage of Company Drive-In sales. Other operating expenses include direct operating costs such as marketing, telephone and utilities, repair and maintenance, rent, property tax and other controllable expenses.

	Company Drive-In Margins Year Ended August 31,		Percentage Points
	2012	**2011**	**(Decrease)**
Costs and expenses[1]:			
Company Drive-Ins:			
Food and packaging	**28.1%**	28.1%	–
Payroll and other employee benefits[2]	**35.7**	36.4	(0.7)
Other operating expenses	**22.1**	22.2	(0.1)
Cost of sales	**85.9%**	86.7%	(0.8)

	Company Drive-In Margins Year Ended August 31,		Percentage Points Increase/
	2011	**2010**	**(Decrease)**
Costs and expenses[1]:			
Company Drive-Ins:			
Food and packaging	28.1%	27.6%	0.5
Payroll and other employee benefits[2]	36.4	35.2	1.2
Other operating expenses	22.2	22.8	(0.6)
Cost of sales	86.7%	85.6%	1.1
Noncontrolling interests[2]	–	1.1%	(1.1)
Pro forma cost of sales, including noncontrolling interests	86.7%	86.7%	–

(1) Calculated as a percentage of Company Drive-In sales.

(2) Effective April 1, 2010, we revised our compensation program at the Company Drive-In level. As a result of these changes, noncontrolling interests are immaterial for fiscal years 2012 and 2011 and have been included in payroll and other employee benefits. We have included noncontrolling interests for fiscal year 2010 in the table for comparative purposes because we believe it is helpful in understanding the impact our new compensation program had on Company Drive-In margins.

Restaurant-level margins improved by 80 basis points during fiscal year 2012 reflecting leverage from improved same-store sales and, to a lesser extent, the refranchising of 34 lower performing Company Drive-Ins during the second quarter of fiscal year 2012. Food and packaging costs remained flat during fiscal year 2012, which was a combination of moderating commodity cost inflation during the latter half of the year, effective inventory management, and moderate price increases taken over the preceding twelve months. Payroll and other employee benefits as well as other operating expenses improved by a combined 80 basis points primarily as a result of leveraging labor with improved sales.

Restaurant-level margins remained flat in fiscal year 2011 as compared to 2010. Food and packaging cost increases during fiscal year 2011 were driven by investments in product quality improvements and higher commodity costs. Payroll and other employee benefit costs increased as a result of increased compensation costs associated with our new compensation program at the Company Drive-In level which was effective April 1, 2010. As a result of our new compensation program introduced as an alternative to our traditional ownership program, compensation costs that were formerly reflected as noncontrolling interests are now included in payroll and other employee benefits. Other operating expenses decreased, as a percentage of sales, attributable to leverage from positive same-store sales.

Selling, General and Administrative ("SG&A"). SG&A expenses remained relatively flat for fiscal year 2012 as compared to the prior year, increasing by 0.4% to $65.2 million, and decreased 2.8% to $64.9 million during fiscal year 2011 as compared to fiscal 2010. The decrease in SG&A expense for fiscal year 2011 was largely attributable to a decline in stock compensation expense resulting from a revision in our long-term compensation strategy as well as declines in bad debt expense due to an improvement in sales trends.

Depreciation and Amortization. Depreciation and amortization expense increased 1.7% to $41.9 million in fiscal year 2012 and decreased 3.3% to $41.2 million in fiscal year 2011. Of the $0.7 million increase in fiscal year 2012, approximately $0.4 million was attributable to the amortization of intellectual property acquired during the second quarter of fiscal year 2012 relating to a point-of-sale system that is used by a majority of the Sonic system. The decrease in depreciation and amortization expense for fiscal year 2011 was primarily attributable to the provision for impairment of long-lived assets recorded in the fourth quarter of fiscal 2010 and, to a lesser extent, the refranchising of 16 Company Drive-Ins in fiscal year 2010.

Provision for Impairment of Long-Lived Assets. Provision for impairment of long-lived assets remained steady at $0.8 million for fiscal years 2012 and 2011 and decreased $14.3 million in fiscal year 2011 from 2010. This decrease was primarily the result of the $15.2 million non-cash impairment of long-lived assets recorded in fiscal year 2010 to reduce the carrying cost of the related operating assets to an estimated fair value. This provision primarily related to lower sales and profits for Company Drive-Ins resulting from the sustained economic downturn and weak results during fiscal 2010 for operating stores. Assets impaired included operating drive-ins, property leased to franchisees, surplus property and other assets.

Net Interest Expense. Net interest expense decreased in fiscal year 2012 as compared to the same period last year primarily as a result of a $28.2 million loss from the early extinguishment of debt related to the refinancing of our debt in May 2011. In addition, net interest expense for fiscal year 2011 included a $5.2 million gain from the early extinguishment of debt in the second quarter of fiscal year 2011, and net interest expense for fiscal year 2010 included a $0.3 million loss from the early extinguishment of debt during the third quarter of fiscal year 2010. Excluding the early extinguishments of debt, net interest expense decreased $0.9 million in fiscal year 2012 and $3.9 million in fiscal year 2011, primarily related to a decline in debt partially offset by a higher weighted average interest rate. See "Liquidity and Sources of Capital" and "Quantitative and Qualitative Disclosures About Market Risk" below for additional information on factors that could impact interest expense.

Income Taxes. The provision for income taxes reflects an effective tax rate of 37.7% for fiscal year 2012 compared with 32.3% for fiscal year 2011. The higher effective income tax rate for fiscal year 2012 was primarily attributable to a $1.1 million favorable settlement of state tax audits during the first quarter of fiscal year 2011 and the expiration of tax credit programs during the second quarter of fiscal year 2012. The provision for income taxes, excluding income attributable to noncontrolling interests, reflects an effective tax rate of 29.7% for fiscal year 2010. The increase in the tax rate for fiscal year 2011 as compared to 2010 was primarily attributable to a $1.8 million tax benefit associated with the stock option exchange program that was implemented during the third quarter of fiscal year 2010, partially offset by the $1.1 million favorable state tax settlement during 2011 discussed earlier. Our tax rate may continue to vary significantly from quarter to quarter depending on the timing of stock option exercises and dispositions by option-holders, changes in tax credit legislation, changes to uncertain tax positions, and as circumstances on other tax matters change.

Net Income - Noncontrolling Interests. As a result of the change to a new compensation program for Company Drive-Ins in April 2010, compensation costs that were formerly reflected as noncontrolling interests relating to store-level managers are now immaterial and included in payroll and other employee benefits.

Financial Position

Total assets increased $1.0 million to $680.8 million during fiscal year 2012 from $679.7 million at the end of fiscal year 2011. Current assets increased $13.7 million during the year primarily due to an increase in cash from improved sales and profitability, partially offset by capital expenditures, debt repayments and purchases under our stock repurchase programs. Non-current assets decreased $12.7 million primarily due to a $21.9 million decrease in net property, equipment and capital leases resulting primarily from depreciation during the year partially offset by capital additions. The overall decrease in non-current assets was largely offset by the reclassification of our income tax receivable, which is explained further in note 11 – Income Taxes, included in the Notes to the Consolidated Financial Statements in this Annual Report.

Total liabilities decreased $6.5 million, or 1.0%, to $621.5 million during fiscal year 2012 from $628.0 million at the end of fiscal year 2011. This decrease was primarily attributable to scheduled debt principal repayments of $15.2 million during fiscal year 2012, partially offset by an increase in income taxes payable.

Total stockholders' equity increased $7.6 million, or 14.6%, to $59.2 million during fiscal year 2012 from $51.7 million at the end of fiscal year 2011. This increase was largely attributable to current year earnings of $36.1 million partially offset by $31.1 million in purchases of common stock under our stock repurchase programs during fiscal year 2012.

Liquidity and Sources of Capital

Operating Cash Flows. Net cash provided by operating activities increased $11.0 million to $95.1 million for fiscal year 2012 as compared to $84.1 million in fiscal year 2011. This increase primarily relates to an improvement in same-store sales and profitability.

Investing Cash Flows. Cash used in investing activities increased $8.0 million to $24.1 million for fiscal year 2012 compared to $16.1 million for fiscal year 2011. During fiscal year 2012, we used $24.2 million of cash for purchases of property and equipment as outlined in the table below as well as $3.4 million of cash to purchase intellectual property related to a point-of-sale system that is used by a majority of the Sonic system. These cash outflows were partially offset by $9.9 million in proceeds primarily related to the sale of operations and a portion of the real estate for 34 Company Drive-Ins. The balance of the change relates to an increase in notes receivable and other investments. The following table sets forth the components of our investments in property and equipment for fiscal year 2012 (in millions):

Replacement equipment and technology for existing drive-ins	$ 9.5
Corporate technology investments	5.2
Acquisition of underlying real estate for drive-ins	4.5
Rebuilds, relocations and remodels of existing drive-ins	3.3
New Company Drive-Ins, including drive-ins under construction	1.3
Retrofits, drive-thru additions and LED signs in existing drive-ins	0.4
Total purchases of property and equipment	$ 24.2

Financing Cash Flows. Net cash used in financing activities decreased $76.7 million to $47.9 million for fiscal year 2012 as compared to $124.6 million in fiscal year 2011. During the third quarter of fiscal year 2011 we refinanced our previously outstanding debt as described below, which was the primary reason for the decrease. Approximately $30 million of the decrease relates to a reduction in debt payments during fiscal year 2012 as compared to fiscal year 2011, primarily due to lower mandatory principal payments under our new financing. These decreases were offset by the use of $30 million of cash during the year to purchase outstanding common stock under our stock repurchase programs as discussed below, and by changes in restricted cash related to our new debt obligations.

On May 20, 2011, various subsidiaries of ours (the "Co-Issuers") issued $500 million of Series 2011-1 Senior Secured Fixed Rate Notes, Class A-2 (the "2011 Fixed Rate Notes") in a private transaction which bears interest at 5.4% per annum. The 2011 Fixed Rate Notes have an expected life of seven years with an anticipated repayment date in May 2018 based on the terms of the debt agreement. At August 31, 2012, the balance outstanding under the 2011 Fixed Rate Notes including accrued interest totaled $482.0 million and carried a weighted-average interest cost of 5.9%, including the effect of the loan origination costs described below.

In connection with the issuance of the 2011 Fixed Rate Notes, the Co-Issuers also entered into a securitized financing facility of Series 2011-1 Senior Secured Variable Funding Notes, Class A-1 (the "2011 Variable Funding Notes"). This revolving credit facility allows for the issuance of up to $100 million of 2011 Variable Funding Notes and certain other credit instruments, including letters of credit. The 2011 Variable Funding Notes have an expected life of five years with an anticipated repayment date in May 2016 based on the terms of the debt agreement. Interest on the 2011 Variable Funding Notes is based on the one-month London Interbank Offered Rate or Commercial Paper, depending on the funding source, plus 3.75% per annum. There is a 0.5% annual commitment fee payable monthly on the unused portion of the 2011 Variable Funding Notes facility. As of August 31, 2012, there was no outstanding balance under our 2011 Variable Funding Notes.

We used the $535 million of net proceeds from the issuance of the 2011 Fixed Rate Notes and 2011 Variable Funding Notes (collectively, the "2011 Notes") to repay our existing debt in full and to pay the costs associated with the securitized financing transaction, including the existing noteholder and insurer make-whole premiums.

Before the refinancing, during the second quarter of fiscal year 2011, we repurchased $62.5 million of our prior variable funding notes in a privately negotiated transaction. We recognized a gain of $5.2 million on the extinguishment of these notes during the second fiscal quarter of 2011.

Mandatory principal payments of $15 million annually under the new financing versus mandatory principal payments paid in fiscal year 2011 of $45.4 million will significantly increase the amount of our available free cash flow which we define as net income plus depreciation, amortization, and stock compensation expense, less capital expenditures. For additional information on our 2011 Notes, see note 9 – Debt, included in the Notes to the Consolidated Financial Statements in this Annual Report.

We plan capital expenditures of approximately $30 to $40 million in fiscal year 2013. These capital expenditures primarily relate to drive-in level expenditures, technology infrastructure expenditures, the development of additional Company Drive-Ins, the implementation of a new point-of-sale system at Company Drive-Ins, and the implementation of a new supply chain management tool for use by the entire Sonic system. We expect to fund these capital expenditures through cash flow from operations as well as cash on hand.

On October 13, 2011, our Board of Directors approved a $30 million stock repurchase program. Under that program, we were authorized to purchase up to $30 million of our outstanding shares of common stock through August 31, 2012. During fiscal year 2012, we completed this stock repurchase program.

On August 15, 2012, our Board of Directors approved a new stock repurchase program. Under the new program, we are authorized to purchase up to $40 million of our outstanding shares of common stock through August 31, 2013. As of August 31, 2012, the total remaining amount authorized for repurchase was $38.9 million. Share repurchases may be made from time to time in the open market or in negotiated transactions, depending on share price, market conditions and other factors. The stock repurchase program may be extended, modified, suspended or discontinued at any time. We plan to fund the stock repurchase program from existing cash on hand at August 31, 2012 and cash flows from operations.

As of August 31, 2012, our total cash balance of $70.8 million ($52.6 million of unrestricted and $18.1 million of restricted cash balances) reflected the impact of the cash generated from operating activities, cash used for stock repurchases, refranchising, and capital expenditures mentioned above. We believe that existing cash, funds generated from operations and the $100 million available under our 2011 Variable Funding Notes will meet our needs for the foreseeable future.

Off-Balance Sheet Arrangements

The company has obligations for guarantees on certain franchisee loans, which in the aggregate are immaterial, and obligations for guarantees on certain franchisee lease agreements. Other than such guarantees and various operating leases and purchase obligations, which are disclosed below in "Contractual Obligations and Commitments" and in note 6 – Leases and 15 – Commitments and Contingencies to our Consolidated Financial Statements, the company has no other material off-balance sheet arrangements.

Contractual Obligations and Commitments

In the normal course of business, Sonic enters into purchase contracts, lease agreements and borrowing arrangements. The following table presents our commitments and obligations as of August 31, 2012 (in thousands):

		Payments Due by Fiscal Year			
	Total	Less than 1 Year (2013)	1 – 3 Years (2014 to 2015)	3 – 5 Years (2016 to 2017)	More than 5 Years (2018 and thereafter)
Contractual Obligations					
Long-term debt[1]	$ 618,312	$ 40,986	$ 79,446	$ 75,879	$ 422,001
Capital leases	41,296	5,845	11,484	9,347	14,620
Operating leases	160,886	11,877	23,451	21,221	104,337
Purchase obligations[2]	76,842	28,391	46,604	1,847	–
Other[3]	14,820	–	–	–	–
Total	$ 912,156	$ 87,099	$ 160,985	$ 108,294	$ 540,958

(1) Includes scheduled principal and interest payments on our 2011 Fixed Rate Notes and assumes these notes will be outstanding for the expected seven-year life with an anticipated repayment date in May 2018.

(2) Purchase obligations primarily relate to the company's estimated share of system-wide commitments to purchase food products. We have excluded agreements that are cancelable without penalty. These amounts require estimates and could vary due to the timing of volumes and changes in market pricing.

(3) Includes $5.5 million of unrecognized tax benefits related to uncertain tax positions and $9.3 million related to guarantees of franchisee leases and loan agreements. As we are not able to reasonably estimate the timing or amount of these payments, if any, the related balances have not been reflected in the "Payments Due by Fiscal Year" section of the table.

Impact of Inflation

We are impacted by inflation which has caused increases in our food, labor and benefits costs and has increased our operating expenses. To the extent permitted by competition, increased costs are recovered through a combination of menu price increases and reviewing, then implementing, alternative products or processes, or by implementing other cost reduction procedures.

Critical Accounting Policies and Estimates

The Consolidated Financial Statements and Notes to Consolidated Financial Statements included in this document contain information that is pertinent to management's discussion and analysis. The preparation of financial statements in conformity with generally accepted accounting principles requires management to use its judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities. These assumptions and estimates could have a material effect on our financial statements. We evaluate our assumptions and estimates on an ongoing basis using historical experience and various other factors that are believed to be relevant under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

We perform an annual review of our financial reporting and disclosure practices and accounting policies to ensure that our financial reporting and disclosures provide accurate and transparent information relative to the current economic and business environment. We believe the following significant accounting policies and estimates involve a high degree of risk, judgment and/or complexity.

Impairment of Long-Lived Assets. We review Company Drive-In assets for impairment when events or circumstances indicate they might be impaired. We test for impairment using historical cash flows and other relevant facts and circumstances as the primary basis for our estimates of future cash flows. This process requires the use of estimates and assumptions, which are subject to a high degree of judgment. These impairment tests require us to estimate fair values of our drive-ins by making assumptions regarding future cash flows and other factors. It is reasonably possible that our estimates of future cash flows could change resulting in the need to write down to fair value certain Company Drive-In assets.

We assess the recoverability of goodwill and other intangible assets related to our brand and drive-ins at least annually and more frequently if events or changes in circumstances occur indicating that the carrying amount of the asset may not be recoverable or as a result of allocating goodwill to Company Drive-Ins that are sold. Goodwill impairment testing first requires a comparison of the fair value of each reporting unit to the carrying value. We estimate fair value based on a comparison of two approaches: an income approach, using the discounted cash flow method, and a market approach, using the guideline public company method. The discounted estimates of future cash flows include significant management assumptions such as revenue growth rates, operating margins, capital expenditures, weighted average cost of capital, and future economic and market conditions. In addition, the market approach includes significant assumptions such as the use of projected cash flow and revenue multiples derived from a comparable set of public companies as well as a control premium based on recent market transactions. These assumptions are significant factors in calculating the value of the reporting units and can be affected by changes in consumer demand, commodity pricing, labor and other operating costs, our cost of capital and changes in guideline public company market multiples. If the carrying value of the reporting unit exceeds fair value, goodwill is considered impaired. The amount of the impairment is the difference between the carrying value of the goodwill and the "implied" fair value, which is calculated as if the reporting unit had just been acquired and accounted for as a business combination.

During the fourth quarter of fiscal year 2012, we performed our annual assessment of recoverability of goodwill and other intangible assets and determined that no impairment was indicated. As of the impairment testing date, the fair value of the Company Drive-In reporting unit exceeded the carrying value by approximately 12%. As of August 31, 2012, the company had $77.0 million of goodwill, of which $71.0 million was attributable to the Company Drive-Ins segment and $6.0 million was attributable to the Franchise Operations segment. If cash flows generated by our Company Drive-Ins were to decline significantly in the future or there were negative revisions to key assumptions, we may be required to record impairment charges to reduce the carrying amount of goodwill.

Revenue Recognition Related to Franchise Fees and Royalties. Initial franchise fees are recognized in income when we have substantially performed or satisfied all material services or conditions relating to the sale of the franchise and the fees are nonrefundable. Area development fees are nonrefundable and are recognized in income on a pro-rata basis when the conditions for revenue recognition under the individual area development agreements are met. Both initial franchise fees and area development fees are generally recognized upon the opening of a Franchise Drive-In or upon termination of the agreement between Sonic and the franchisee.

Our franchisees are required under the provisions of the license agreements to pay royalties to Sonic each month based on a percentage of actual sales. However, the royalty payments and supporting financial statements are not due until the following month under the terms of our franchise agreements. As a result, we accrue royalty revenue in the month earned.

Accounting for Stock-Based Compensation. We account for stock-based compensation in accordance with Accounting Standards Codification ("ASC") Topic 718, Stock Compensation. We estimate the fair value of options granted using the Black-Scholes option pricing model along with the assumptions shown in note 12 – Stockholders' Equity in the Notes to the Consolidated Financial Statements in this Annual Report. The assumptions used in computing the fair value of stock-based payments reflect our best estimates, but involve uncertainties relating to market and other conditions, many of which are outside of our control. We estimate expected volatility based on historical daily price changes of the company's stock for a period equal to the current expected term of the options. The expected option term is the number of years the company estimates that options will be outstanding prior to exercise considering vesting schedules and our historical exercise patterns. If other assumptions or estimates had been used, the stock-based compensation expense that was recorded could have been materially different. Furthermore, if different assumptions are used in future periods, stock-based compensation expense could be materially impacted.

Income Taxes. We estimate certain components of our provision for income taxes. These estimates include, among other items, depreciation and amortization expense allowable for tax purposes, allowable tax credits for items such as wages paid to certain employees, effective rates for state and local income taxes and the tax deductibility of certain other items.

We account for uncertain tax positions under ASC Topic 740, Income Taxes, which sets out criteria for the use of judgment in assessing the timing and amounts of deductible and taxable items. Although we believe we have adequately accounted for our uncertain tax positions, from time to time, audits result in proposed assessments where the ultimate resolution may give rise to us owing additional taxes. We adjust our uncertain tax positions in light of changing facts and circumstances, such as the completion of a tax audit, expiration of a statute of limitations, the refinement of an estimate, and penalty and interest accruals associated with uncertain tax positions until they are resolved. We believe that our tax positions comply with applicable tax law and that we have adequately provided for these matters. However, to the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact the provision for income taxes in the period in which such determination is made.

Our estimates are based on the best available information at the time that we prepare the provision, including legislative and judicial developments. We generally file our annual income tax returns several months after our fiscal year end. Income tax returns are subject to audit by federal, state and local governments, typically several years after the returns are filed. These returns could be subject to material adjustments or differing interpretations of the tax laws. Adjustments to these estimates or returns can result in significant variability in the tax rate from period to period.

Leases. We lease the land and buildings for certain Company Drive-Ins from third parties. Rent expense for operating leases is recognized on a straight-line basis over the expected lease term, including cancelable option periods when it is deemed to be reasonably assured that we would incur an economic penalty for not exercising the options. Judgment is required to determine options expected to be exercised. Within the terms of some of our leases, there are rent holidays and/or escalations in payments over the base lease term, as well as renewal periods. The effects of the rent holidays and escalations are reflected in rent expense on a straight-line basis over the expected lease term, including cancelable option periods when appropriate. The lease term commences on the date when we have the right to control the use of lease property, which can occur before rent payments are due under the terms of the lease. Contingent rent is generally based on sales levels and is accrued at the point in time we determine that it is probable that such sales levels will be achieved.

Accounts and Notes Receivable. We charge interest on past due accounts receivable and recognize income as it is collected. Interest accrues on notes receivable based on the contractual terms of the respective note. We monitor all accounts and notes receivable for delinquency and provide for estimated losses for specific receivables that are not likely to be collected. We assess credit risk for accounts and notes receivable of specific franchisees based on payment history, current payment patterns, the health of the franchisee's business, and an assessment of the franchisee's ability to pay outstanding balances. In addition to allowances for bad debt for specific franchisee receivables, a general provision for bad debt is estimated for accounts receivable based on historical trends. Account balances generally are charged against the allowance when we believe it is probable that the receivable will not be recovered and legal remedies have been exhausted. We continually review our allowance for doubtful accounts.

Quantitative and Qualitative Disclosures About Market Risk

Sonic's use of debt directly exposes the company to interest rate risk. Fixed rate debt, where the interest rate is fixed over the life of the instrument, exposes the company to changes in market interest rates reflected in the fair value of the debt and to the risk that the company may need to refinance maturing debt with new debt at a higher rate. Sonic is also exposed to market risk from changes in commodity prices. The company does not utilize financial instruments for trading purposes. Sonic manages its debt portfolio to achieve an overall desired position of fixed and floating rates.

Interest Rate Risk. Our exposure to interest rate risk at August 31, 2012 was primarily based on the 2011 Fixed Rate Notes with an effective rate of 5.4%, before amortization of debt-related costs. At August 31, 2012, the fair value of the 2011 Fixed Rate Notes was estimated at $510.8 million versus a carrying value of $482.0 million, including accrued interest. To derive the fair value, management used market information available for public debt transactions for companies with ratings that are similar to our ratings and information gathered from brokers who trade in our notes. Management believes this fair value is a reasonable estimate. Should interest rates and/or credit spreads increase or decrease by one percentage point, the estimated fair value of the 2011 Fixed Rate Notes would decrease or increase by approximately $24 million, respectively. The fair value estimate required significant assumptions by management.

Commodity Price Risk. The company and its franchisees purchase certain commodities such as beef, potatoes, chicken and dairy products. These commodities are generally purchased based upon market prices established with vendors. These purchase arrangements may contain contractual features that limit the price paid by establishing price floors or caps; however, we generally do not make any long-term commitments to purchase any minimum quantities under these arrangements other than as disclosed above under "Contractual Obligations and Commitments." We also do not use financial instruments to hedge commodity prices because these purchase arrangements help control the ultimate cost.

This market risk discussion contains forward-looking statements. Actual results may differ materially from this discussion based upon general market conditions and changes in financial markets.

Consolidated Balance Sheets

(In thousands)	August 31, 2012	2011
Assets		
Current assets:		
Cash and cash equivalents	**$ 52,647**	$ 29,509
Restricted cash	**10,200**	12,850
Accounts and notes receivable, net	**27,073**	24,558
Income taxes receivable	**–**	12,776
Inventories	**3,289**	3,503
Prepaid expenses	**4,399**	4,523
Other current assets	**9,543**	5,738
Total current assets	**107,151**	93,457
Noncurrent restricted cash	**7,903**	8,108
Notes receivable, net	**11,641**	11,086
Property, equipment and capital leases, net	**443,008**	464,875
Goodwill	**76,997**	81,625
Debt origination costs, net	**10,555**	13,124
Other assets, net	**23,505**	7,467
Total assets	**$ 680,760**	$ 679,742
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	**$ 11,048**	$ 11,135
Deposits from franchisees	**3,055**	2,897
Accrued liabilities	**32,607**	33,532
Income taxes payable	**14,326**	4,775
Current maturities of long-term debt and capital leases	**19,480**	18,940
Total current liabilities	**80,516**	71,279
Obligations under capital leases due after one year	**27,377**	30,302
Long-term debt due after one year	**466,613**	481,835
Deferred income taxes	**29,777**	27,228
Other noncurrent liabilities	**17,230**	17,402
Commitments and contingencies (Notes 6, 7, 14 and 15)		
Stockholders' equity:		
Preferred stock, par value $.01; 1,000,000 shares authorized; none outstanding	**–**	–
Common stock, par value $.01; 245,000,000 shares authorized; shares issued 118,309,094 in 2012 and 118,309,094 in 2011	**1,183**	1,183
Paid-in capital	**230,543**	229,399
Retained earnings	**722,614**	687,431
Treasury stock, at cost; 60,324,576 shares in 2012 and 56,315,651 shares in 2011	**(895,093)**	(866,317)
Total stockholders' equity	**59,247**	51,696
Total liabilities and stockholders' equity	**$ 680,760**	$ 679,742

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Statements of Income

(In thousands, except per share data)	Year Ended August 31, 2012	2011	2010
Revenues:			
Company Drive-In sales	**$ 404,443**	$ 410,820	$ 414,369
Franchise Drive-Ins:			
Franchise royalties	**125,989**	124,127	122,385
Franchise fees	**2,024**	1,744	2,752
Lease revenue	**6,575**	6,023	6,879
Other	**4,699**	3,237	4,541
	543,730	545,951	550,926
Costs and expenses:			
Company Drive-Ins:			
Food and packaging	**113,775**	115,516	114,281
Payroll and other employee benefits	**144,531**	149,417	145,688
Other operating expenses, exclusive of depreciation and amortization included below	**89,164**	91,303	94,690
	347,470	356,236	354,659
Selling, general and administrative	**65,173**	64,943	66,847
Depreciation and amortization	**41,914**	41,225	42,615
Provision for impairment of long-lived assets	**764**	824	15,161
	455,321	463,228	479,282
Other operating income (expense), net	**531**	585	(763)
Income from operations	**88,940**	83,308	70,881
Interest expense	**31,608**	32,600	36,707
Interest income	**(630)**	(706)	(948)
Net loss from early extinguishment of debt	**–**	23,035	314
Net interest expense	**30,978**	54,929	36,073
Income before income taxes	**57,962**	28,379	34,808
Provision for income taxes	**21,877**	9,154	8,969
Net income - including noncontrolling interests	**36,085**	19,225	25,839
Net income - noncontrolling interests	**–**	–	4,630
Net income - attributable to Sonic Corp.	**$ 36,085**	$ 19,225	$ 21,209
Basic income per share	**$ 0.60**	$ 0.31	$ 0.35
Diluted income per share	**$ 0.60**	$ 0.31	$ 0.34

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Statements of Stockholders' Equity (Deficit)

(In thousands)	Common Stock Shares	Common Stock Amount	Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Noncontrolling Interests	Total Stockholders' Equity (Deficit)
Balance at August 31, 2009	117,781	$ 1,178	$219,736	$ 649,398	$ (1,500)	$ (873,080)	$ 1,916	$ (2,352)
Comprehensive Income:								
Net income	–	–	–	21,209	–	–	4,630	25,839
Net change in deferred hedging losses, net of tax of $462	–	–	–	–	657	–	–	657
Total comprehensive income, net of income taxes								26,496
Purchases of noncontrolling interests in Company Drive-Ins	–	–	(6,725)	–	–	–	(9,277)	(16,002)
Changes to noncontrolling interests	–	–	–	–	–	–	2,340	2,340
Stock-based compensation expense	–	–	7,666	–	–	–	–	7,666
Exercise of stock options and issuance of restricted stock	532	5	3,374	(119)	–	221	–	3,481
Other	–	–	402	–	–	(78)	613	937
Balance at August 31, 2010	118,313	$ 1,183	$ 224,453	$ 670,488	$ (843)	$ (872,937)	$ 222	$ 22,566
Comprehensive Income:								
Net income	–	–	–	19,225	–	–	–	19,225
Net change in deferred hedging losses, net of tax of $522	–	–	–	–	843	–	–	843
Total comprehensive income, net of income taxes								20,068
Changes to noncontrolling interests	–	–	1,866	–	–	–	(222)	1,644
Stock-based compensation expense	–	–	5,644	–	–	–	–	5,644
Exercise of stock options and issuance of restricted stock	(4)	–	(2,267)	(2,197)	–	6,594	–	2,130
Other	–	–	(297)	(85)	–	26	–	(356)
Balance at August 31, 2011	118,309	$ 1,183	$ 229,399	$ 687,431	$ –	$ (866,317)	$ –	$ 51,696
Net income and comprehensive income	**–**	**–**	**–**	**36,085**	**–**	**–**	**–**	**36,085**
Stock-based compensation expense	**–**	**–**	**4,295**	**–**	**–**	**–**	**–**	**4,295**
Purchase of treasury stock	**–**	**–**	**–**	**–**	**–**	**(31,102)**	**–**	**(31,102)**
Exercise of stock options and issuance of restricted stock	**–**	**–**	**(820)**	**(529)**	**–**	**1,629**	**–**	**280**
Other	**–**	**–**	**(2,331)**	**(373)**	**–**	**697**	**–**	**(2,007)**
Balance at August 31, 2012	**118,309**	**$ 1,183**	**$ 230,543**	**$ 722,614**	**$ –**	**$ (895,093)**	**$ –**	**$ 59,247**

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows

(In thousands)	Year Ended August 31, 2012	2011	2010
Cash flows from operating activities			
Net income - including noncontrolling interests	**$ 36,085**	$ 19,225	$ 25,839
Adjustments to reconcile net income including noncontrolling interests to net cash provided by operating activities:			
Depreciation and amortization	**41,914**	41,225	42,615
Stock-based compensation expense	**4,295**	5,644	7,666
Noncontrolling interests	**–**	–	(4,630)
Provision for impairment of long-lived assets	**764**	824	15,161
Net loss from early extinguishment of debt	**–**	23,035	314
Other	**24**	1,580	1,091
Decrease (increase) in operating assets:			
Restricted cash	**2,586**	(5,136)	4,465
Accounts receivable and other assets	**(2,591)**	(2,124)	292
Increase (decrease) in operating liabilities:			
Accounts payable	**(932)**	(552)	(522)
Accrued and other liabilities	**(828)**	(281)	(1,440)
Income taxes	**13,811**	662	(13,247)
Total adjustments	**59,043**	64,877	51,765
Net cash provided by operating activities	**95,128**	84,102	77,604
Cash flows from investing activities			
Purchases of property and equipment	**(24,175)**	(21,200)	(24,468)
Proceeds from sale of assets	**9,929**	6,448	14,271
Other	**(9,863)**	(1,321)	814
Net cash used in investing activities	**(24,109)**	(16,073)	(9,383)
Cash flows from financing activities			
Payments on and purchases of debt	**(15,220)**	(624,171)	(106,296)
Proceeds from borrowings	**–**	535,000	–
Restricted cash for securitization obligations	**269**	6,409	(209)
Proceeds from exercise of stock options	**280**	2,130	3,404
Purchases of noncontrolling interests	**(92)**	(182)	(9,277)
Purchases of treasury stock	**(30,000)**	–	–
Debt issuance and extinguishment costs	**(57)**	(40,248)	–
Other	**(3,061)**	(3,494)	(7,404)
Net cash used in financing activities	**(47,881)**	(124,556)	(119,782)
Net increase (decrease) in cash and cash equivalents	**23,138**	(56,527)	(51,561)
Cash and cash equivalents at beginning of the year	**29,509**	86,036	137,597
Cash and cash equivalents at end of the year	**$ 52,647**	$ 29,509	$ 86,036
Supplemental cash flow information			
Cash paid during the year for:			
Interest (net of amounts capitalized of $337, $23 and $25, respectively)	**$ 29,283**	$ 29,033	$ 32,184
Income taxes (net of refunds)	**11,114**	10,523	25,534
Non-cash investing and financing activities:			
Additions to capital lease obligations	**1,692**	1,340	446
Obligation to acquire treasury stock	**1,102**	–	–
Stock options exercised by stock swap	**–**	1,572	78
Change in obligation for purchase of property and equipment	**(1,061)**	(524)	3,208

The accompanying notes are an integral part of the consolidated financial statements.

1. Summary of Significant Accounting Policies

Operations

Sonic Corp. (the "company") operates and franchises a chain of quick-service restaurants in the United States. It derives its revenues primarily from Company Drive-In sales and royalty fees from franchisees. The company also leases signs and real estate, and receives equity earnings in noncontrolling ownership in a number of Franchise Drive-Ins.

Principles of Consolidation

The accompanying financial statements include the accounts of the company, its wholly owned subsidiaries and a number of Company Drive-Ins in which a subsidiary has a controlling ownership interest. All significant intercompany accounts and transactions have been eliminated.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported and contingent assets and liabilities disclosed in the financial statements and accompanying notes. Actual results may differ from those estimates, and such differences may be material to the financial statements.

Reclassifications

Certain amounts reported in previous years, which are not material, have been combined and reclassified to conform to the current year presentation.

Cash Equivalents

Cash equivalents consist of highly liquid investments, primarily money market accounts that mature in three months or less from date of purchase, and depository accounts.

Restricted Cash

As of August 31, 2012, the company had restricted cash balances totaling $18.1 million for funds required to be held in trust for the benefit of senior noteholders under the company's debt arrangements. The current portion of restricted cash of $10.2 million represents amounts to be returned to Sonic or paid to service current debt obligations. The noncurrent portion of $7.9 million represents interest reserves required to be set aside for the duration of the debt.

Accounts and Notes Receivable

The company charges interest on past due accounts receivable and recognizes income as it is collected. Interest accrues on notes receivable based on the contractual terms of the respective note. The company monitors all accounts and notes receivable for delinquency and provides for estimated losses for specific receivables that are not likely to be collected. The company assesses credit risk for accounts and notes receivable of specific franchisees based on payment history, current payment patterns, the health of the franchisee's business, and an assessment of the franchisee's ability to pay outstanding balances. In addition to allowances for bad debt for specific franchisee receivables, a general provision for bad debt is estimated for the company's accounts receivable based on historical trends. Account balances generally are charged against the allowance when the company believes it is probable that the receivable will not be recovered and legal remedies have been exhausted. The company continually reviews its allowance for doubtful accounts.

Inventories

Inventories consist principally of food and supplies that are carried at the lower of cost (first-in, first-out basis) or market.

Property, Equipment and Capital Leases

Property and equipment are recorded at cost, and leased assets under capital leases are recorded at the present value of future minimum lease payments. Depreciation of property and equipment and amortization of capital leases are computed by the straight-line method over the estimated useful lives or the lease term, including cancelable option periods when appropriate, and are combined for presentation in the financial statements.

Accounting for Long-Lived Assets

The company reviews long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset might not be recoverable. Assets are grouped and evaluated for impairment at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets, which generally represents the individual drive-in. The company's primary test for an indicator of potential impairment is operating losses. If an indication of impairment is determined to be present, the company estimates the future cash flows expected to be generated from the use of the asset and its eventual disposal. If the sum of undiscounted future cash flows is less than the carrying amount of the asset, an impairment loss is recognized. The impairment loss is measured by comparing the fair value of the asset to its carrying amount. Fair value is typically determined to be the value of the land, since drive-in buildings and improvements are single-purpose assets and have little value to market participants. The equipment associated with a store can be easily relocated to another store, and therefore is not adjusted.

Surplus property assets are carried at the lower of depreciated cost or fair value less cost to sell. The majority of the value in surplus property is land. Fair values are estimated based upon appraisals or independent assessments of the assets' estimated sales values.

Goodwill and Other Intangible Assets

Goodwill is determined based on acquisition purchase price in excess of the fair value of identified assets. Intangible assets with lives restricted by contractual, legal, or other means are amortized over their useful lives. The company tests all goodwill and other intangible assets not subject to amortization at least annually for impairment using the fair value approach on a reporting unit basis. The company's reporting units are defined as Company Drive-Ins and Franchise Operations (see additional information regarding the company's reporting units in note 13 - Segment Information). The accounting guidance requires a two-step process for testing impairment. We test for impairment using historical cash flows and other relevant facts and circumstances as the primary basis for our estimates of future cash flows. This process requires the use of estimates and assumptions, which are subject to a high degree of judgment. These impairment tests require us to estimate fair values of our drive-ins by making assumptions regarding future cash flows and other factors.

We assess the recoverability of goodwill and other intangible assets related to our brand and drive-ins at least annually and more frequently if events or changes in circumstances occur indicating that the carrying amount of the asset may not be recoverable or as a result of allocating goodwill to Company Drive-Ins that are sold. Goodwill impairment testing first requires a comparison of the fair value of each reporting unit to the carrying value. The company estimates fair value based on a comparison of two approaches: an income approach, using the discounted cash flow method, and a market approach, using the guideline public company method. The discounted estimates of future cash flows include significant management assumptions such as revenue growth rates, operating margins, capital expenditures, weighted average cost of capital, and future economic and market conditions. In addition, the market approach includes significant assumptions such as the use of projected cash flow and revenue multiples derived from a comparable set of public companies as well as a control premium based on recent market transactions. These assumptions are significant factors in calculating the value of the reporting units and can be affected by changes in consumer demand, commodity pricing, labor and other operating costs, our cost of capital and changes in guideline public company market multiples. If the carrying value of the reporting unit exceeds fair value, goodwill is considered impaired. The amount of the impairment is the difference between the carrying value of the goodwill and the "implied" fair value, which is calculated as if the reporting unit had just been acquired and accounted for as a business combination.

The company's intangible assets subject to amortization consist primarily of acquired franchise agreements, intellectual property, franchise fees, and other intangibles. Amortization expense is calculated using the straight-line method over the asset's expected useful life. See note 5 - Goodwill and Other Intangibles for additional disclosures related to goodwill and other intangibles.

Ownership Structure

Company Drive-Ins are drive-in operations which are owned and operated by Sonic Restaurants, Inc., the company's operating subsidiary. A typical Company Drive-In is operated by a manager, two to four assistant managers, and approximately 25 hourly employees, many of whom work part-time. The manager has responsibility for the day-to-day operations of the Company Drive-In. Supervisors oversee several Company Drive-Ins and supervise the managers of those Drive-Ins. The employee compensation program for Company Drive-Ins provides managers and supervisors a guaranteed base compensation with additional significant incentive compensation based on drive-in-level performance. Prior to April 2010, Company Drive-

Ins operated as individual limited liability companies or general partnerships in which the manager and the supervisor for the respective drive-in owned a noncontrolling interest. Under this form of ownership, managers and supervisors shared in the cash flow for their Company Drive-Ins, but were also responsible for their share of any losses incurred by the drive-ins.

Refranchising of Company Drive-Ins

Gains and losses from the sale of Company Drive-Ins are recorded as other operating income (expense), net on the Consolidated Statements of Income. The company may periodically refranchise other operations when circumstances warrant.

Revenue Recognition, Franchise Fees and Royalties

Revenue from Company Drive-In sales is recognized when food and beverage products are sold. Company Drive-In sales are presented net of sales tax and other sales-related taxes.

Initial franchise fees are recognized in income when the company has substantially performed or satisfied all material services or conditions relating to the sale of the franchise and the fees are nonrefundable. Area development fees are nonrefundable and are recognized in income on a pro-rata basis when the conditions for revenue recognition under the individual area development agreements are met. Both initial franchise fees and area development fees are generally recognized upon the opening of a Franchise Drive-In or upon termination of the agreement between the company and the franchisee.

The company's franchisees are required under the provisions of the license agreements to pay the company royalties each month based on a percentage of actual sales. However, the royalty payments and supporting financial statements are not due until the following month under the terms of the franchise agreements. As a result, the company accrues royalty revenue in the month earned.

Operating Leases

Rent expense is recognized on a straight-line basis over the expected lease term, including cancelable option periods when it is deemed to be reasonably assured that the company would incur an economic penalty for not exercising the options. Within the terms of some of our leases, there are rent holidays and/or escalations in payments over the base lease term, as well as renewal periods. The effects of the holidays and escalations have been reflected in rent expense on a straight-line basis over the expected lease term, which includes cancelable option periods when appropriate. The lease term commences on the date when the company has the right to control the use of the leased property, which can occur before rent payments are due under the terms of the lease. Contingent rent is generally based on sales levels and is accrued at the point in time it is probable that such sales levels will be achieved.

Advertising Costs

Costs incurred in connection with the advertising and promoting of the company's products are included in other operating expenses and are expensed as incurred. Such costs amounted to $22.6 million in fiscal year 2012 and $22.5 million in both fiscal year 2011 and 2010.

Under the company's franchise agreements, both Company Drive-Ins and Franchise Drive-Ins must contribute a minimum percentage of revenues to a national media production fund (Sonic Brand Fund) and spend an additional minimum percentage of gross revenues on local advertising, either directly or through company-required participation in advertising cooperatives. A portion of the local advertising contributions is redistributed to a System Marketing Fund, which purchases advertising on national cable and broadcast networks and funds other national media expenses and sponsorship opportunities. As stated in the terms of existing franchise agreements, these funds do not constitute assets of the company, and the company acts with limited agency in the administration of these funds. Accordingly, neither the revenues and expenses nor the assets and liabilities of the advertising cooperatives, the Sonic Brand Fund, or the System Marketing Fund are included in the company's consolidated financial statements. However, all advertising contributions by Company Drive-Ins are recorded as expense on the company's financial statements.

Stock-Based Compensation

Stock-based compensation is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense on a straight-line basis over the requisite service period of the award (generally the vesting period of the grant) or to an employee's eligible retirement date, if earlier.

The company grants incentive stock options ("ISOs"), non-qualified stock options ("NQs") and restricted stock units ("RSUs"). For grants of NQs and RSUs, the company expects to recognize a tax benefit upon exercise of the option or vesting of the RSU. As a result, a tax benefit is recognized on the related stock-based compensation expense for these types of awards. For grants of ISOs, a tax benefit only results if the option holder has a disqualifying disposition. As a result of the limitation on the tax benefit for ISOs, the tax benefit for stock-based compensation will generally be less than the company's overall tax rate and will vary depending on the timing of employees' exercises and sales of stock. For additional information on stock-based compensation see note 12 - Stockholders' Equity.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities from a change in tax rates is recognized in income in the period that includes the enactment date.

Income tax benefits credited to equity relate to tax benefits associated with amounts that are deductible for income tax purposes but do not affect earnings. These benefits are principally generated from employee exercises of non-qualified stock options, the vesting of RSUs, and disqualifying dispositions of ISOs.

The threshold for recognizing the financial statement effects of a tax position is when it is more likely than not, based on the technical merits, that the position will be sustained upon examination by a taxing authority. Recognized tax positions are initially and subsequently measured as the largest amount of tax benefit that is more likely than not to be realized upon ultimate settlement with a taxing authority. Liabilities for unrecognized tax benefits related to such tax positions are included in other long-term liabilities unless the tax position is expected to be settled within the upcoming year, in which case the liabilities are included in accrued expenses and other current liabilities. Interest and penalties related to unrecognized tax benefits are included in income tax expense.

Additional information regarding the company's unrecognized tax benefits is provided in note 11 - Income Taxes.

Fair Value Measurements

The company's financial assets and liabilities consist of cash and cash equivalents, accounts and notes receivable, accounts payable and long-term debt. The fair value of cash and cash equivalents, accounts receivable, and accounts payable approximates their carrying amounts due to the short term nature of these assets and liabilities.

The following methods and assumptions were used by the company in estimating fair values of its financial instruments:

- *Notes receivable* - For variable rate loans with no significant change in credit risk since the loan origination, fair values approximate carrying amounts. Fair values for fixed-rate loans are estimated using discounted cash flow analysis, using interest rates that would currently be offered for loans with similar terms to borrowers of similar credit quality and/or the same remaining maturities. As of August 31, 2012 and 2011, the fair value of the company's fixed-rate loans approximated their carrying value.
- *Long-term debt* - The company prepares a discounted cash flow analysis for its fixed rate borrowings to estimate fair value each quarter. This analysis uses Level 2 inputs from market information available for public debt transactions for companies with ratings that are similar to the company's ratings and from information gathered from brokers who trade in the company's notes. The fair value estimate required significant assumptions by management. Management believes this fair value is a reasonable estimate. For more information regarding the company's long-term debt, see note 9 - Debt and note 10 - Fair Value of Financial Instruments.

Certain nonfinancial assets and liabilities are measured at fair value on a nonrecurring basis, which means these assets and liabilities are not measured at fair value on an ongoing basis but are subject to periodic impairment tests. For the company, these items primarily include long-lived assets, goodwill and other intangible assets. Refer to sections "Accounting for Long-Lived Assets" and "Goodwill and Other Intangible Assets," discussed above, for inputs and valuation techniques used to measure the fair value of these nonfinancial assets. The fair value was based upon management's assessment as well as appraisals or independent assessments which involved Level 2 and Level 3 inputs.

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

Noncontrolling Interests

Effective September 1, 2009, the company implemented Accounting Standards Codification, ("ASC") Topic 810, "Consolidation," which requires noncontrolling interests, previously called minority interests, to be presented as a separate item in the equity section of the consolidated balance sheets. It also requires the amount of consolidated net income related to noncontrolling interests to be clearly presented on the face of the consolidated statements of income. Effective April 1, 2010, the company revised its compensation program at the Company Drive-In level. As a result of these changes, noncontrolling interests are immaterial for fiscal years 2012 and 2011 and have been included in "payroll and other employee benefits" on the Consolidated Statements of Income and in "other noncurrent liabilities" on the Consolidated Balance Sheets.

New Accounting Pronouncements

In September 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2011-08, "Testing Goodwill for Impairment." This pronouncement was issued to simplify how entities test goodwill for impairment. Under this pronouncement, entities may first assess qualitative factors to determine whether it is necessary to perform the two-step goodwill impairment test. If the qualitative assessment results in a more than 50% likely result that the fair value of a reporting unit is less than the carrying amount, then the entity must continue to apply the two-step impairment test. If the entity concludes the fair value exceeds the carrying amount, then neither of the two steps in the goodwill impairment test is required. This pronouncement is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011 with early adoption permitted. The adoption of this pronouncement is not expected to have a material impact on the company's consolidated financial statements.

In July 2012, the FASB issued ASU No. 2012-02, "Testing Indefinite-Lived Intangible Assets for Impairment." This pronouncement was issued to simplify how entities test for impairment of indefinite-lived intangible assets. Under this pronouncement, an entity has the option first to assess qualitative factors to determine whether it is more likely than not that an indefinite-lived intangible asset is impaired. In conclusion of this assessment, if an entity finds that it is not more likely than not that an indefinite-lived intangible asset is impaired, then the entity is not required to take further action. However, if an entity concludes otherwise, then it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment test by comparing the fair value with the carrying amount in accordance with ASC Topic 350, "Intangibles – Goodwill and Other." This pronouncement is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012 with early adoption permitted. The adoption of this pronouncement is not expected to have a material impact on the company's consolidated financial statements.

2. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share for the years ended August 31:

	2012	2011	2010
Numerator:			
Net income – attributable to Sonic Corp.	**$ 36,085**	$ 19,225	$ 21,209
Denominator:			
Weighted average common shares outstanding – basic	**60,078**	61,781	61,319
Effect of dilutive employee stock options and unvested restricted stock units	**94**	162	257
Weighted average common shares – diluted	**60,172**	61,943	61,576
Net income per common share – basic	**$ 0.60**	$ 0.31	$ 0.35
Net income per common share – diluted	**$ 0.60**	$ 0.31	$ 0.34
Anti-dilutive securities excluded[1]	**6,705**	6,367	6,834

(1) Anti-dilutive securities consist of stock options and unvested restricted stock units that were not included in the computation of diluted earnings per share because either the exercise price of the options was greater than the average market price of the common stock or the total assumed proceeds under the treasury stock method resulted in negative incremental shares and thus the inclusion would have been anti-dilutive.

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

3. Impairment of Long-Lived Assets

During the fiscal years ended August 31, 2012, 2011 and 2010, the company identified impairments for certain drive-in assets and surplus property through regular quarterly reviews of long-lived assets. The recoverability of Company Drive-Ins is assessed by estimating the undiscounted net cash flows expected to be generated over the remaining life of the Company Drive-Ins. This involves estimating same-store sales and margins for the cash flows period. When impairment exists, the carrying value of the asset is written down to fair value.

The company's assessment of long-lived assets resulted in provisions for impairment totaling $0.8 million for both fiscal year 2012 and 2011. These write-downs were completed to reduce to fair value the carrying amount of surplus properties in both years and properties leased to franchisees in fiscal year 2011.

During fiscal year 2010, the company experienced lower sales and profits in Company Drive-Ins due to the sustained economic downturn and weaker results than anticipated during the summer months for operating stores. Accordingly, the company revised its future sales growth assumptions and estimated cash flows in assessing the recoverability of its investments in Company Drive-Ins. These analyses resulted in provisions for impairment totaling $15.2 million, which primarily consisted of $11.3 million to write down the carrying amount of building and leasehold improvements on underperforming drive-ins, $2.3 million to write down the carrying amount of property leased to franchisees and $0.6 million to reduce to fair value the carrying amount of twelve surplus properties.

4. Accounts and Notes Receivable

Accounts and notes receivable consist of the following at August 31:

	2012	2011
Current Accounts and Notes Receivable:		
Royalties and other trade receivables	**$ 17,030**	$ 17,729
Notes receivable from franchisees	**1,304**	3,220
Notes receivable from advertising funds	**4,825**	1,500
Other	**6,109**	4,806
	29,268	27,255
Allowance for doubtful accounts and notes receivable	**(2,195)**	(2,697)
	$ 27,073	$ 24,558
Noncurrent Notes Receivable:		
Notes receivable from franchisees	**$ 5,286**	$ 6,286
Notes receivable from advertising funds	**7,152**	5,469
Allowance for doubtful notes receivable	**(797)**	(669)
	$ 11,641	$ 11,086

The company's receivables are primarily due from franchisees, all of whom are in the restaurant business. Substantially all of the notes receivable from franchisees are collateralized by real estate or equipment. The notes receivable from advertising funds represent transactions in the normal course of business.

The following table summarizes the activity in the allowance for doubtful accounts related to the company's notes receivable during fiscal years 2012 and 2011:

	2012	2011
Balance at beginning of year	**$ 748**	$ 54
Additions to provision	**520**	694
Reductions for charge-offs	**(190)**	–
Balance at end of year	**$ 1,078**	$ 748

5. Goodwill and Other Intangibles

As of August 31, 2012, the company had $77.0 million of goodwill, of which $71.0 million was attributable to the Company Drive-Ins segment and $6.0 million was attributable to the Franchise Operations segment. There have been no changes in the goodwill balance attributable to the Franchise Operations segment since August 31, 2011.

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

The changes in the carrying amount of goodwill for fiscal years 2012 and 2011 were as follows:

	2012	2011
Balance at beginning of year	**$ 81,625**	$ 82,089
Goodwill acquired during the year	**–**	427
Goodwill disposed of related to the sale of Company Drive-Ins	**(4,628)**	(891)
Balance at end of year	**$ 76,997**	$ 81,625

The gross carrying amount of franchise agreements, intellectual property, franchise fees and other intangibles subject to amortization was $10.2 million and $6.8 million at August 31, 2012 and 2011, respectively. Accumulated amortization related to these intangible assets was $3.4 million and $2.6 million at August 31, 2012 and 2011, respectively. Intangible assets amortization expense for the fiscal years ended August 31, 2012, 2011 and 2010 was $0.8 million, $0.4 million and $0.5 million, respectively. At August 31, 2012, the remaining weighted-average life of amortizable intangible assets was approximately 11 years. Estimated intangible assets amortization expense is $0.9 million annually for fiscal years 2013, 2014, 2015, and 2016 and $0.8 million for fiscal year 2017.

6. Leases

Description of Leasing Arrangements

The company's leasing operations consist principally of leasing certain land, buildings and equipment (including signs) and subleasing certain buildings to franchise operators. The land and building portions of these leases are classified as operating leases with lease terms expiring through September 2030. The equipment portions of these leases are classified principally as direct financing leases and expire principally over the next nine years. These leases include provisions for contingent rentals that may be received on the basis of a percentage of sales in excess of stipulated amounts. Income is not recognized on contingent rentals until sales exceed the stipulated amounts. Some leases contain escalation clauses over the lives of the leases. Most of the leases contain one to four renewal options at the end of the initial term for periods of five years.

The company has two significant master lease agreements with franchisees as a result of previously refranchised drive-ins. These leases consist of leasing land, buildings and signs for a period of 15 years and are classified as operating leases. There are four renewal options at the end of the primary term for periods of five years for property that is owned by the company. For property owned by third parties, the lease term runs concurrent with the term of the third-party lease arrangements. These leases include provisions for contingent rentals that may be received on the basis of a percentage of sales in excess of stipulated amounts. Both leases contain escalation clauses based on sales over the life of the lease.

Certain Company Drive-Ins lease land and buildings from third parties. These leases, with lease terms expiring through August 2030, include provisions for contingent rents that may be paid on the basis of a percentage of sales in excess of stipulated amounts. For the majority of leases, the land portions are classified as operating leases, and the building portions are classified as capital leases.

Receivables as a Lessor

Components of net investment in direct financing leases are as follows at August 31:

	2012	2011
Minimum lease payments receivable	**$ 1,041**	$ 1,530
Less unearned income	**(228)**	(374)
Net investment in direct financing leases	**813**	1,156
Less amount due within one year	**(233)**	(294)
Amount due after one year	**$ 580**	$ 862

Initial direct costs incurred in the negotiations and consummations of direct financing lease transactions have not been material. Accordingly, no portion of unearned income has been recognized to offset those costs.

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

Future minimum rental payments receivable as of August 31, 2012 are as follows:

	Operating	Direct Financing
Years ending August 31:		
2013	**$ 12,488**	**$ 322**
2014	**12,273**	**238**
2015	**12,472**	**185**
2016	**12,361**	**135**
2017	**12,374**	**94**
Thereafter	**90,900**	**67**
	$152,868	**1,041**
Less unearned income		**(228)**
		$ 813

Commitments as a Lessee

Maturities under capital leases and future minimum rental payments required under operating leases that have initial or remaining noncancelable lease terms in excess of one year as of August 31, 2012 are as follows:

	Operating	Capital
Years ending August 31:		
2013	**$ 11,877**	**$ 5,845**
2014	**11,783**	**6,172**
2015	**11,668**	**5,312**
2016	**11,123**	**4,876**
2017	**10,098**	**4,471**
Thereafter	**104,337**	**14,620**
Total minimum lease payments	**$160,886**	**41,296**
Less amount representing interest averaging 6.6%		**(9,620)**
Present value of net minimum lease payments		**31,676**
Less amount due within one year		**(4,299)**
Amount due after one year		**$ 27,377**

Total rent expense for all operating leases and capital leases consist of the following for the years ended August 31:

	2012	2011	2010
Operating leases:			
Minimum rentals	**$ 14,555**	$ 14,185	$ 14,330
Contingent rentals	**103**	138	176
Sublease rentals	**(2,851)**	(2,847)	(2,993)
Capital leases:			
Contingent rentals	**799**	745	740
	$ 12,606	$ 12,221	$ 12,253

The aggregate future minimum rentals receivable under noncancelable operating and capital subleases as of August 31, 2012, was $35.3 million and $2.1 million, respectively.

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

7. Property, Equipment and Capital Leases

Property, equipment and capital leases consist of the following at August 31:

	Estimated Useful Life	2012	2011
Property and equipment:			
Home office:			
Leasehold improvements	Life of lease	**$ 4,541**	$ 4,541
Computer and other equipment	2 – 5 yrs	**61,492**	52,736
Drive-ins, including those leased to others:			
Land		**171,102**	171,813
Buildings	8 – 25 yrs	**358,887**	356,536
Equipment	5 – 7 yrs	**118,975**	126,487
Property and equipment, at cost		**714,997**	712,113
Accumulated depreciation		**(295,735)**	(273,209)
Property and equipment, net		**419,262**	438,904
Capital Leases:			
Leased home office building	Life of lease	**9,990**	9,990
Leased drive-in buildings, equipment and other assets under capital leases, including those held for sublease	Life of lease	**39,906**	38,675
Accumulated amortization		**(26,150)**	(22,694)
Capital leases, net		**23,746**	25,971
Property, equipment and capital leases, net		**$443,008**	$464,875

Depreciation expense for property and equipment was $37.2 million, $37.3 million and $38.6 million for fiscal years 2012, 2011 and 2010, respectively. Land, buildings and equipment with a carrying amount of $219.8 million at August 31, 2012 were leased under operating leases to franchisees and other parties. The accumulated depreciation related to these buildings and equipment was $69.7 million at August 31, 2012. Amortization expense related to capital leases is included within "depreciation and amortization" on the Consolidated Statements of Income. As of August 31, 2012, the company had no drive-ins under construction with costs to complete.

8. Accrued Liabilities

Accrued liabilities consist of the following at August 31:

	2012	2011
Wages and employee benefit costs	**$ 11,061**	$ 9,757
Property taxes, sales and use taxes and employment taxes	**8,869**	9,441
Unredeemed gift cards and gift certificates	**7,274**	8,864
Other	**5,403**	5,470
	$ 32,607	$ 33,532

The company sells gift cards that do not have expiration dates. Gift card balances are recorded as a liability on the company's Consolidated Balance Sheets. Breakage is the amount on a gift card that is not expected to be redeemed and that the company is not required to remit to a state under unclaimed property laws. The company estimates breakage based upon the trend in redemption patterns from previously sold gift cards utilizing its history with the program. The company's policy is to recognize the breakage using the delayed recognition method when it is apparent that there is a remote likelihood the gift card balance will be redeemed based on historical trends. The company reduces the gift card liability for the estimated breakage and uses that amount to help defray the costs of operating the gift card program.

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9. Debt

Long-term debt consists of the following at August 31:

	2012	2011
Class A-2 senior secured fixed rate notes	**$ 481,250**	$ 496,250
Class A-1 senior secured variable funding notes	**–**	–
Other	**543**	763
	481,793	497,013
Less long-term debt due within one year	**(15,180)**	(15,178)
Long-term debt due after one year	**$ 466,613**	$ 481,835

At August 31, 2012, future maturities of long-term debt were $15.2 million for fiscal year 2013, $15.3 million for fiscal year 2014, and $15.0 million annually for fiscal years 2015, 2016 and 2017.

On May 20, 2011, various subsidiaries of the company (the "Co-Issuers") issued $500 million of Series 2011-1 Senior Secured Fixed Rate Notes, Class A-2 (the "2011 Fixed Rate Notes") in a private transaction which bears interest at 5.4% per annum. The 2011 Fixed Rate Notes have an expected life of seven years with an anticipated repayment date in May 2018 based on the terms of the debt agreement. At August 31, 2012 and 2011, the balance outstanding under the 2011 Fixed Rate Notes including accrued interest totaled $482.0 million and $497.0 million, respectively, and carried a weighted-average interest cost of 5.9%, including the effect of the loan origination costs described below.

In connection with the issuance of the 2011 Fixed Rate Notes, the Co-Issuers also entered into a securitized financing facility of Series 2011-1 Senior Secured Variable Funding Notes, Class A-1 (the "2011 Variable Funding Notes"). This revolving credit facility allows for the issuance of up to $100 million of 2011 Variable Funding Notes and certain other credit instruments, including letters of credit. The 2011 Variable Funding Notes have an expected life of five years with an anticipated repayment date in May 2016 based on the terms of the debt agreement. Interest on the 2011 Variable Funding Notes is based on the one-month London Interbank Offered Rate or Commercial Paper, depending on the funding source, plus 3.75% per annum. There is a 0.5% annual commitment fee payable monthly on the unused portion of the 2011 Variable Funding Notes facility. The company borrowed $35 million under the 2011 Variable Funding Notes facility at closing, and has the ability to draw additional amounts under the facility from time to time as needed. In June 2011, the company repaid the outstanding balance under its 2011 Variable Funding Notes.

Sonic used the $535 million of net proceeds from the issuance of the 2011 Fixed Rate Notes and 2011 Variable Funding Notes (collectively, the "2011 Notes") to repay its existing Series 2006-1 Senior Secured Variable Funding Notes, Class A-1 (the "2006 Variable Funding Notes") and Series 2006-1 Senior Secured Fixed Rate Notes, Class A-2 (the "2006 Fixed Rate Notes" and, together with the 2006 Variable Funding Notes, the"2006 Notes") in full and to pay the costs associated with the securitized financing transaction, including the existing noteholder and insurer make-whole premiums.

Loan origination costs associated with the company's 2011 refinancing totaled $16.4 million and were allocated between the 2011 Notes. Loan costs are being amortized over each note's expected life. The amount of loan costs expected to be amortized over the next twelve months is reflected in "other current assets" on the Consolidated Balance Sheets.

While the 2011 Fixed Rate Notes and the 2011 Variable Funding Notes are structured to provide for seven-year and five-year lives, respectively, they have a legal final maturity date of May 2041. The company intends to repay or refinance the 2011 Notes on or before the end of their respective expected lives. In the event the 2011 Notes are not paid in full by the end of their expected lives, the Notes are subject to an upward adjustment in the interest rate of at least 5% per annum. In addition, principal payments will accelerate by applying all of the royalties, lease revenues and other fees securing the debt, after deducting certain expenses, until the debt is paid in full. Also, any unfunded amount under the 2011 Variable Funding Notes will become unavailable.

The Co-Issuers and Sonic Franchising LLC (the "Guarantor") are existing special purpose, bankruptcy remote, indirect subsidiaries of Sonic Corp. that hold substantially all of Sonic's franchising assets and real estate. As of August 31, 2012, assets for these combined indirect subsidiaries totaled $356.6 million, including receivables for royalties, certain Company and Franchise Drive-In real estate, intangible assets and restricted cash balances of $18.1 million. The 2011 Notes are secured by franchise fees, royalty payments and lease payments, and the repayment of the 2011 Notes is expected to be made solely from the income derived from the Co-Issuer's assets. In addition, the Guarantor, a Sonic Corp. subsidiary that acts as a franchisor, has guaranteed the obligations of the Co-Issuers under the 2011 Notes and pledged substantially all of its assets to secure those obligations.

Neither Sonic Corp., the ultimate parent of the Co-Issuers and the Guarantor, nor any other subsidiary of Sonic, guarantee or in any way are liable for the obligations of the Co-Issuers under the 2011 Notes. The company has, however, agreed to cause the performance of certain obligations of its subsidiaries, principally related to managing the assets included as collateral for the 2011 Notes and certain indemnity obligations relating to the transfer of the collateral assets to the Co-Issuers.

The 2011 Notes are subject to a series of covenants and restrictions customary for transactions of this type, including (i) required actions to better secure collateral upon the occurrence of certain performance-related events, (ii) application of certain disposition proceeds as note prepayments after a set time is allowed for reinvestment, (iii) maintenance of specified reserve accounts, (iv) maintenance of certain debt service coverage ratios, (v) optional and mandatory prepayments upon change in control, (vi) indemnification payments for defective or ineffective collateral, and (vii) covenants relating to recordkeeping, access to information and similar matters. If certain covenants or restrictions are not met, the 2011 Notes are subject to customary accelerated repayment events and events of default. Although management does not anticipate an event of default or any other event of noncompliance with the provisions of the debt, if such event occurred, the unpaid amounts outstanding could become immediately due and payable.

In connection with the transaction described above, the company recognized a $28.2 million loss from the early extinguishment of debt during the third quarter of fiscal year 2011, which primarily consisted of a $25.3 million prepayment premium and the write-off of unamortized deferred loan fees remaining from the refinanced debt. In addition, the company's deferred hedging loss was reclassified from accumulated other comprehensive income into earnings during the third quarter of fiscal year 2011. Prior to the refinancing, during the second quarter of fiscal year 2011, the company repurchased $62.5 million of its 2006 Variable Funding Notes in a privately negotiated transaction. The company recognized a gain of $5.2 million on the extinguishment of the notes during the second fiscal quarter of 2011. These transactions are reflected within "net loss from early extinguishment of debt" in the accompanying Consolidated Statements of Income.

As a result of the May 2011 refinancing discussed above, the company's arrangement with the third-party insurance company that guaranteed its debt payments under the company's 2006 Notes was terminated.

10. Fair Value of Financial Instruments

The fair value of financial instruments is the amount at which the instrument could be exchanged in a current transaction between willing parties. The company has no financial liabilities that are required to be measured at fair value on a recurring basis.

The company categorizes its assets and liabilities recorded at fair value based upon the following fair value hierarchy established by FASB:

- Level 1 valuations use quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date. An active market is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 valuations use inputs other than actively quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include: (a) quoted prices for similar assets or liabilities in active markets, (b) quoted prices for identical or similar assets or liabilities in markets that are not active, (c) inputs other than quoted prices that are observable for the asset or liability such as interest rates and yield curves observable at commonly quoted intervals and (d) inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3 valuations use unobservable inputs for the asset or liability. Unobservable inputs are used to the extent observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date.

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The table below sets forth our fair value hierarchy for financial assets measured at fair value on a recurring basis as of August 31, 2012 and 2011:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
August 31, 2012				
Assets:				
Cash equivalents	**$ 7,784**	**$ –**	**$ –**	**$ 7,784**
Restricted cash (current)	**10,200**	**–**	**–**	**10,200**
Restricted cash (noncurrent)	**7,903**	**–**	**–**	**7,903**
Total	**$ 25,887**	**$ –**	**$ –**	**$ 25,887**
August 31, 2011				
Assets:				
Cash equivalents	$ 11,338	$ –	$ –	$ 11,338
Restricted cash (current)	12,850	–	–	12,850
Restricted cash (noncurrent)	8,108	–	–	8,108
Total	$ 32,296	$ –	$ –	$ 32,296

At August 31, 2012, the fair value of the company's 2011 Fixed Rate Notes was estimated at $510.8 million versus a carrying value of $482.0 million, including accrued interest. At August 31, 2011, the fair value of the 2011 Fixed Rate Notes approximated the carrying value of $497.0 million, including accrued interest.

11. Income Taxes

The company's income before the provision for income taxes is classified by source as domestic income.

The components of the provision for income taxes consist of the following for the years ended August 31:

	2012	2011	2010
Current:			
Federal	**$ 17,851**	$ 5,060	$ 12,165
State	**3,892**	2,223	2,904
	21,743	7,283	15,069
Deferred:			
Federal	**180**	1,876	(5,303)
State	**(46)**	(5)	(797)
	134	1,871	(6,100)
Provision for income taxes	**$ 21,877**	$ 9,154	$ 8,969

The provision for income taxes differs from the amount computed by applying the statutory federal income tax rate due to the following for the years ended August 31:

	2012	2011	2010
Amount computed by applying a tax rate of 35%	**$ 20,287**	$ 9,933	$ 10,562
State income taxes (net of federal income tax benefit)	**1,900**	1,441	1,370
Employment related and other tax credits, net	**(1,291)**	(1,730)	(1,504)
Adjustment of prior year deferred tax items	**1,559**	–	–
Benefit from stock option exchange program	**–**	–	(1,471)
Other	**(578)**	(490)	12
Provision for income taxes	**$ 21,877**	$ 9,154	$ 8,969

During fiscal year 2012, the company conducted a reconciliation of its tax basis balance sheet and identified certain adjustments which were recorded in fiscal year 2012 to appropriately reflect the company's current and deferred tax accounts. As a result of this reconciliation process, the company recorded an additional income tax provision of $1,559 for fiscal year

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2012. Management of the company evaluated the impact of this adjustment and concluded the effect of this adjustment was immaterial to the current and prior year financial statements.

The adoption of ASC Topic 810 gives an appearance of a lower effective tax rate than the company's actual effective tax rate. The following table reconciles the difference in the effective tax rate as a result of the adoption of ASC Topic 810:

	2012	2011	2010
Effective income tax rate reconciliation:			
Effective tax rate per consolidated income statement	**37.7%**	32.3%	25.8%
Book income attributable to noncontrolling interests	**–**	–	3.9
Effective tax rate for the fiscal year	**37.7%**	32.3%	29.7%

Deferred tax assets and liabilities consist of the following at August 31:

	2012	2011
Current deferred tax assets (liabilities):		
Allowance for doubtful accounts and notes receivable	**$ 840**	$ 1,032
Capital lease liabilities and other	**1,636**	1,551
Prepaid expenses	**(1,265)**	(1,190)
Deferred income from franchisees	**461**	848
Deferred income from affiliated technology fund	**597**	353
Deferred income	**1,903**	10
Accrued liabilities and other	**649**	166
Current deferred tax assets, net	**$ 4,821**	$ 2,770
Noncurrent deferred tax assets (liabilities):		
Net investment in direct financing leases, including differences related to capitalization and amortization	**$ 526**	$ 648
Investment in partnerships, including differences in capitalization, depreciation and direct financing leases	**(2,408)**	(2,554)
State net operating losses	**7,361**	6,389
Property, equipment and capital leases	**(22,538)**	(24,834)
Deferred income from affiliated franchise fees	**915**	1,160
Intangibles and other assets	**(16,694)**	(13,321)
Deferred income from franchisees	**773**	1,481
Stock compensation	**11,899**	12,556
Debt extinguishment	**(4,191)**	(4,146)
Allowance for doubtful accounts and notes receivable	**305**	256
Deferred income	**1,355**	1,453
Accrued liabilities and other	**281**	73
	(22,416)	(20,839)
Valuation allowance	**(7,361)**	(6,389)
Noncurrent deferred tax liabilities, net	**$ (29,777)**	$ (27,228)
Deferred tax assets and (liabilities):		
Deferred tax assets (net of valuation allowance)	**$ 22,140**	$ 21,587
Deferred tax liabilities	**(47,096)**	(46,045)
Net deferred tax liabilities	**$ (24,956)**	$ (24,458)

State net operating loss carryforwards expire generally beginning in 2012. Management does not believe the company will be able to realize the state net operating loss carryforwards and therefore has provided a valuation allowance of $7.4 million and $6.4 million as of August 31, 2012 and August 31, 2011, respectively.

As of August 31, 2012, the company had approximately $5,451 of unrecognized tax benefits, including approximately $746 of interest and penalty. The liability for unrecognized tax benefits increased by $676 in fiscal year 2012. The majority of the change was due to the expiration of statutes of limitations, additions for items under audit, and the settlement of a state tax audit in the first quarter of fiscal year 2012, which resulted in a decrease to state unrecognized tax positions from prior years. The company recognizes estimated interest and penalties as a component of its income tax expense, net of federal benefit. If recognized, $1,862 of unrecognized tax benefits would favorably impact the effective tax rate. As of August 31, 2012 and 2011, an immaterial net benefit for interest and penalties was recognized in our Consolidated Statements of Income as a component of "provision for income taxes." A reconciliation of unrecognized tax benefits for fiscal years 2012 and 2011 is as follows:

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	2012	2011
Balance at beginning of year	**$ 4,775**	$ 5,628
Additions based on tax positions related to the current year	**834**	–
Additions for tax positions of prior years	**1,670**	672
Reductions for tax positions of prior years	**(469)**	–
Reductions for settlements	**(68)**	(1,104)
Reductions due to statute expiration	**(1,291)**	(421)
Balance at end of year	**$ 5,451**	$ 4,775

The company or one of its subsidiaries is subject to U.S. federal income tax and income tax in multiple U.S. state jurisdictions. The company is currently undergoing examinations or appeals by various state and federal authorities. The company anticipates that the finalization of these examinations or appeals, combined with the expiration of applicable statutes of limitations and the additional accrual of interest related to unrecognized benefits on various return positions taken in years still open for examination could result in a change to the liability for unrecognized tax benefits during the next 12 months ranging from an increase of $123 to a decrease of $4,872, depending on the timing and terms of the examination resolutions. At August 31, 2012, the company was subject to income tax examinations for its U.S. federal income taxes after fiscal year 2007 and for state and local income taxes generally after fiscal year 2007.

At August 31, 2012 and 2011, the company had an income tax receivable of $10.3 million and $12.8 million, respectively, primarily relating to expected refunds from amended tax returns. Based on new information available at August 31, 2012, the company does not anticipate receiving or being able to apply these refunds to other tax obligations during fiscal year 2013. As a result, this balance was reclassified from current assets to non-current assets during fiscal year 2012 and is included within "other assets, net" on the Consolidated Balance Sheets.

12. Stockholders' Equity

Employee Stock Purchase Plan

The company has an employee stock purchase plan ("ESPP") that permits full-time regular employees to purchase the company's common stock at a 15% discount from the stock's fair market value. Employees are eligible to purchase shares of common stock each year up to the lesser of 10% of their base compensation or $25 in the stock's fair market value. At August 31, 2012, 0.9 million shares were available for grant under the ESPP.

Stock-Based Compensation

The Sonic Corp. 2006 Long-Term Incentive Plan (the "2006 Plan") provides flexibility to award various forms of equity compensation, such as stock options, stock appreciation rights, performance shares, restricted stock and other share-based awards. At August 31, 2012, 1.8 million shares were available for grant under the 2006 Plan. The company grants stock options with contractual terms of seven to ten years and a vesting period of three years and RSUs also with a vesting period of three years. The company's policy is to issue shares from treasury stock to satisfy stock option exercises, the vesting of RSUs and shares issued under the ESPP. Prior to July 2010, the company issued new shares of common stock to satisfy these items.

Total stock-based compensation cost recognized for fiscal years 2012, 2011 and 2010 was $4.3 million, $5.6 million and $7.7 million, respectively, with related income tax benefits of $1.2 million, $1.3 million and $4.3 million, respectively. At August 31, 2012, total remaining unrecognized compensation cost related to unvested stock-based arrangements was $4.9 million and is expected to be recognized over a weighted average period of 1.7 years.

In November 2009, the company's Board of Directors authorized a stock option exchange program that allowed eligible employees the opportunity to exchange certain options granted under the 2006 Plan, the 2001 Stock Option Plan, and the 1991 Stock Option Plan for a lesser number of replacement options with a lower exercise price. The company's stockholders approved the stock option exchange program on January 14, 2010, and the company executed the program in the third quarter of fiscal year 2010. The exchange, which was accounted for as a modification of existing stock options, was on an estimated fair value neutral basis and resulted in no incremental compensation expense. The exchange resulted in a tax benefit of $1.8 million in the third quarter of fiscal year 2010 related to the conversion of eligible ISOs to NQs.

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

The company measures the compensation cost associated with stock-based payments by estimating the fair value of stock options as of the grant date using the Black-Scholes option pricing model. The company believes the valuation technique and approach utilized to develop the underlying assumptions are appropriate in calculating the fair values of the company's stock options granted during 2012, 2011 and 2010. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by the employees who receive equity awards. The fair value of RSUs granted is equal to the company's closing stock price on the date of the grant.

The per share weighted average fair value of stock options granted during 2012, 2011 and 2010 was $2.88, $4.63 and $3.50, respectively. In addition to the exercise and grant date prices of the awards, certain weighted average assumptions that were used to estimate the fair value of stock option grants in the respective periods are listed in the table below:

	2012	**2011**	**2010**
Expected term (years)	**4.9**	4.7	4.5
Expected volatility	**48%**	46%	45%
Risk-free interest rate	**0.8%**	2.0%	2.2%
Expected dividend yield	**0%**	0%	0%

The company estimates expected volatility based on historical daily price changes of the company's common stock for a period equal to the current expected term of the options. The risk-free interest rate is based on the United States treasury yields in effect at the time of grant corresponding with the expected term of the options. The expected option term is the number of years the company estimates that options will be outstanding prior to exercise considering vesting schedules and our historical exercise patterns.

Stock Options

A summary of stock option activity under the company's stock-based compensation plans for the year ended August 31, 2012 is presented in the following table:

	Options	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Life (Yrs.)**	**Aggregate Intrinsic Value**
Outstanding at September 1, 2011	**7,331**	**$ 13.06**		
Granted	**1,019**	**6.91**		
Exercised	**(31)**	**9.14**		
Forfeited or expired	**(1,061)**	**11.70**		
Outstanding at August 31, 2012	**7,258**	**$ 12.41**	**3.46**	**$ 3,330**
Exercisable at August 31, 2012	**5,467**	**$ 13.80**	**2.73**	**$ 569**

Proceeds from the exercise of stock options for fiscal years 2012, 2011 and 2010 were $0.3 million, $2.1 million and $3.4 million, respectively. The total intrinsic value of options exercised during the years ended August 31, 2012, 2011 and 2010 was $0.1 million, $0.8 million and $2.6 million, respectively.

Restricted Stock Units

A summary of the company's RSU activity during the year ended August 31, 2012 is presented in the following table:

	Restricted Stock Units	**Weighted Average Grant Date Fair Value**
Outstanding at September 1, 2011	**150**	**$ 9.20**
Granted	**46**	**6.92**
Vested	**(77)**	**9.20**
Forfeited	**–**	**–**
Outstanding at August 31, 2012	**119**	**$ 8.31**

The aggregate fair value of restricted stock that vested during the years ended August 31, 2012, 2011 and 2010 was $0.5 million, $0.7 million and $0.1 million, respectively.

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

Stock Repurchase Programs

On October 13, 2011, the company's Board of Directors approved a $30 million stock repurchase program. Under that program, the company was authorized to purchase up to $30 million of its outstanding shares of common stock through August 31, 2012. During fiscal year 2012, the company completed this stock repurchase program.

On August 15, 2012, the company's Board of Directors approved a new stock repurchase program. Under the new program, the company is authorized to purchase up to $40 million of its outstanding shares of common stock through August 31, 2013. During the fourth quarter of fiscal year 2012, approximately 0.1 million shares were acquired pursuant to this program for a total cost of $1.1 million. As of August 31, 2012, the total remaining amount authorized for repurchase was $38.9 million. Share repurchases may be made from time to time in the open market or in negotiated transactions, depending on share price, market conditions and other factors. The stock repurchase program may be extended, modified, suspended or discontinued at any time.

Comprehensive Income

Comprehensive income is defined as the change in equity of a business entity during a period from transactions and other events and circumstances from non-owner sources and is reflected in the Consolidated Statements of Stockholders' Equity (Deficit).

In August 2006, the company entered into a forward starting swap agreement with a financial institution to hedge part of the exposure to changing interest rates until new financing was closed. The forward starting swap was designated as a cash flow hedge, and was subsequently settled in conjunction with the closing of the 2006 Fixed Rate Notes, as planned. The loss resulting from settlement was recorded net of tax in accumulated other comprehensive income and amortized to interest expense over the expected term of the debt. In conjunction with the company's May 2011 refinancing discussed in note 9 – Debt, the company's deferred hedging loss was reclassified from accumulated other comprehensive income into earnings during third quarter fiscal year 2011.

13. Segment Information

Operating segments are generally defined as components of an enterprise for which separate discrete financial information is available as the basis for management to allocate resources and assess performance.

Based on internal reporting and management structure, the company has two reportable segments: Company Drive-Ins and Franchise Operations. The Company Drive-Ins segment consists of the drive-in operations in which the company owns a controlling ownership interest and derives its revenues from operating drive-in restaurants. The Franchise Operations segment consists of franchising activities and derives its revenues from royalties, initial franchise fees and lease revenues received from franchisees. The accounting policies of the segments are the same as those described in note 1 - Summary of Significant Accounting Policies. Segment information for total assets and capital expenditures is not presented as such information is not used in measuring segment performance or allocating resources between segments.

The following table presents the revenues and income from operations for each reportable segment, along with reconciliation to reported revenue, income from operations and income before income taxes:

	2012	2011	2010
Revenues:			
Company Drive-Ins	**$ 404,443**	$ 410,820	$ 414,369
Franchise Operations	**134,588**	131,894	132,016
Unallocated revenues	**4,699**	3,237	4,541
	$ 543,730	$ 545,951	$ 550,926
Income from Operations:			
Company Drive-Ins	**$ 56,973**	$ 54,584	$ 59,710
Franchise Operations	**134,588**	131,894	132,016
Unallocated income	**5,230**	3,822	3,778
Unallocated expenses:			
Selling, general and administrative	**(65,173)**	(64,943)	(66,847)
Depreciation and amortization	**(41,914)**	(41,225)	(42,615)
Provision for impairment of long-lived assets	**(764)**	(824)	(15,161)
Income from operations	**88,940**	83,308	70,881
Net interest expense	**30,978**	54,929	36,073
Income before income taxes	**$ 57,962**	$ 28,379	$ 34,808

August 31, 2012, 2011 and 2010 (In thousands, except per share data)

14. Employee Benefit and Cash Incentive Plans

The company sponsors a qualified defined contribution 401(k) plan for employees meeting certain eligibility requirements. Under the plan, employees are entitled to make pre-tax contributions. The company matches an amount equal to the employees' contributions up to a maximum of 6% of the employees' salaries depending on years of service. The company's contributions during fiscal years 2012, 2011 and 2010 were $1.7 million, $1.6 million and $1.0 million, respectively.

The company has Cash Incentive Plans (the "Incentive Plans") that apply to certain members of management, and grants of awards under the Incentive Plans are at all times subject to the approval of the company's Board of Directors. Under certain awards pursuant to the Incentive Plans, if predetermined earnings goals for a fiscal year are met, the Incentive Plans provide that a predetermined percentage of the employee's salary may be paid in the form of a bonus. The company recognized as expense incentive bonuses of $4.9 million, $5.4 million and $0.8 million during fiscal years 2012, 2011 and 2010, respectively.

15. Commitments and Contingencies

Litigation

The company is involved in various legal proceedings and has certain unresolved claims pending. Based on the information currently available, management believes that all claims currently pending are either covered by insurance or would not have a material adverse effect on the company's business, operating results or financial condition.

Lease Commitments

The company has obligations under various lease agreements with third-party lessors related to the real estate for certain Company Drive-In operations that were sold to franchisees. Under these agreements, which expire through 2024, the company remains secondarily liable for the lease payments for which it was responsible as the original lessee. As of August 31, 2012, the amount remaining under these guaranteed lease obligations totaled $8.0 million. At this time, the company does not anticipate any material defaults under the foregoing leases; therefore, no liability has been provided. In addition, capital lease obligations totaling $1.1 million are still reflected as liabilities as of August 31, 2012 for properties sold to franchisees and for which the company remains secondarily liable through 2021. At this time, the company also does not anticipate any material defaults under these leases.

Purchase Obligations

At August 31, 2012, the company had purchase obligations of approximately $77 million which primarily related to its estimated share of system-wide commitments for food products.

16. Selected Quarterly Financial Data (Unaudited)

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	2012	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**
Total revenues[1]	**$128,279**	$129,146	**$115,084**	$113,523	**$149,427**	$152,098	**$150,940**	$151,184
Income from operations	**16,754**	17,792	**10,548**	9,601	**30,736**	28,667	**30,902**	27,248
Net income (loss)[2]	**$ 5,499**	$ 7,242	**$ 1,677**	$ 4,348	**$ 14,407**	$ (4,651)	**$ 14,502**	$ 12,286
Basic income (loss) per share[3]	**$ 0.09**	$ 0.12	**$ 0.03**	$ 0.07	**$ 0.24**	$ (0.08)	**$ 0.25**	$ 0.20
Diluted income (loss) per share[3]	**$ 0.09**	$ 0.12	**$ 0.03**	$ 0.07	**$ 0.24**	$ (0.08)	**$ 0.25**	$ 0.20

(1) Revenues have been impacted by the refranchising of 34 Company Drive-Ins during the latter part of the company's second fiscal quarter of 2012.

(2) Includes a $5.2 million gain and a $28.2 million loss from early extinguishments of debt in the second and third quarters of fiscal year 2011, respectively, and a $1.1 million tax benefit recognized during the first quarter of fiscal year 2011 relating to the favorable settlement of state tax audits.

(3) The sum of per share data may not agree to annual amounts due to rounding.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of Sonic Corp.

We have audited the accompanying consolidated balance sheets of Sonic Corp. as of August 31, 2012 and 2011, and the related consolidated statements of income, stockholders' equity (deficit), and cash flows for each of the three years in the period ended August 31, 2012. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Sonic Corp. at August 31, 2012 and 2011, and the consolidated results of its operations and its cash flows for each of the three years in the period ended August 31, 2012, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Sonic Corp.'s internal control over financial reporting as of August 31, 2012, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated October 26, 2012, expressed an unqualified opinion thereon.

Ernst & Young LLP

Oklahoma City, Oklahoma
October 26, 2012

Management's Report on Internal Control Over Financial Reporting

The management of the company is responsible for establishing and maintaining adequate internal control over financial reporting. The company's internal control system was designed to provide reasonable assurance to the company's management and Board of Directors regarding the preparation and fair presentation of published financial statements. All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

The company's management assessed the effectiveness of the company's internal control over financial reporting as of August 31, 2012. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control—Integrated Framework. Based on our assessment, we believe that, as of August 31, 2012, the company's internal control over financial reporting is effective based on those criteria.

The company's independent registered public accounting firm that audited the financial statements included in this annual report has issued an attestation report on the company's internal control over financial reporting. This report appears on the following page.

Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting

The Board of Directors and Stockholders of Sonic Corp.

We have audited Sonic Corp.'s internal control over financial reporting as of August 31, 2012, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Sonic Corp.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Sonic Corp. maintained, in all material respects, effective internal control over financial reporting as of August 31, 2012, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Sonic Corp. as of August 31, 2012 and 2011, and the related consolidated statements of income, stockholders' equity (deficit), and cash flows for each of the three years in the period ended August 31, 2012 of Sonic Corp. and our report dated October 26, 2012 expressed an unqualified opinion thereon.

Ernst & Young LLP

Oklahoma City, Oklahoma
October 26, 2012

Directors and Officers

Board of Directors

J. Clifford Hudson
Chairman and Chief Executive Officer
Sonic Corp.

Douglas N. Benham [2]
President and Chief Executive Officer
DNB Advisors, LLC

Kate S. Lavelle [2]
Former Executive Vice President
and Chief Financial Officer
Dunkin' Brands, Inc.

Michael J. Maples [3]
Former Executive Vice President and
Member of the Office of the President
Microsoft Corporation

J. Larry Nichols [1, 2]
Executive Chairman of the Board
Devon Energy Corporation

Federico F. Peña [1, 3]
Senior Advisor
Vestar Capital Partners

H. E. Rainbolt [2]
Chairman
BancFirst Corp.

Frank E. Richardson [1, 2, 4]
Chairman
F. E. Richardson & Co., Inc.

Robert M. Rosenberg [1, 3]
Retired President and
Chief Executive Officer
Allied-Domecq Retailing U.S.A.

Jeffrey H. Schutz [3]
Managing Director
Centennial Ventures

Kathryn L. Taylor [2]
Attorney, McAfee & Taft
Former Mayor, City of Tulsa, and
Former Chief of Education
Strategy and Innovation
State of Oklahoma

[1] Member of the Nominating and Corporate Governance Committee
[2] Member of the Audit Committee
[3] Member of the Compensation Committee
[4] Lead Independent Director

Officers

J. Clifford Hudson
Chairman and Chief Executive Officer

W. Scott McLain
President of Sonic Corp. and
President and Chief Strategy Officer of
Sonic Industries Services Inc. (SISI)
(the company's franchising subsidiary)

Omar R. Janjua
President of Sonic Restaurants, Inc.
(the company's restaurant-operating
subsidiary) and Executive Vice
President of Operations of SISI

Stephen C. Vaughan
Executive Vice President and
Chief Financial Officer

Paige S. Bass
Vice President and General Counsel

Craig J. Miller
Senior Vice President and
Chief Information Officer

James P. O'Reilly
Senior Vice President and
Chief Marketing Officer

Robert P. Franke
Senior Vice President
Field Services – East Region

Andrew G. Ritger, Jr.
Senior Vice President of
Business Planning and Purchasing

E. Edward Saroch
Senior Vice President
Field Services – West Region

Larry G. Archibald
Vice President of Brand Technology

Tanishia M. Beacham
Vice President of Field Marketing

Michelle E. Britten
Vice President and Controller

M. Anne Burkett
Vice President of Internal Auditing

Jeffry D. Carper
Vice President of Operations Services

Carolyn C. Cummins
Vice President of Compliance and
Corporate Secretary

Mark W. Davis
Vice President of IT Production
Management and Engineering

Michael J. Gallagher
Vice President of Development and
Franchising

William I. Klearman
Vice President of Retail Systems

James A. Lebs
Vice President of Supply Chain

Dino Medina
Vice President of Design and
Construction

Clas P. Petersson
Vice President of Product and
Package

Diane L. Prem
Vice President of Operations Services
and Key Initiatives

Stephen P. Reed
Vice President of Logistics

Nancy L. Robertson
Vice President of Communications

Jean-Pierre Salama
Vice President of Training

Claudia S. San Pedro
Vice President of Investor Relations
and Treasurer

Inge P. Smith
Vice President of POS Implementation

Todd W. Smith
Vice President of Marketing

C. Nelson Taylor
Vice President of Technical Services

Anita K. Vanderveer
Vice President of People

Barbara A. Williams
Vice President of Performance
Analysis

Charles B. Woods
Vice President of Tax

Hans Wybenga
Vice President of Consumer Insights

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250 Royall Street
Canton, Massachusetts 02021
800/884-4225
web.queries@computershare.com
www.computershare.com

Independent Registered Public Accounting Firm

Ernst & Young LLP
Oklahoma City, Oklahoma

Annual Meeting

Our 2013 Annual Meeting of Shareholders will be held at 1:30 p.m. Central Standard Time on January 17, 2013, at our Corporate Offices, 4th Floor, 300 Johnny Bench Drive, Oklahoma City, Oklahoma.

Annual Report on Form 10-K

A copy of our annual report on Form 10-K for the year ended August 31, 2012, as filed with the Securities and Exchange Commission, may be obtained without charge upon written request to Stephen C. Vaughan, Executive Vice President and Chief Financial Officer, at our Corporate Offices. In addition, we make available free of charge through our website at www.sonicdrivein.com annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports filed with or furnished to the SEC. The reports are available as soon as reasonably practical after we electronically file such material with the SEC, and may be found on our website under "About/Corporate/Investors/Financial Information/SEC Filings."

Forward-Looking Statements

This annual report contains forward-looking statements within the meaning of the federal securities laws. Forward-looking statements reflect management's expectations regarding future events and operating performance and speak only as of the date thereof. These forward-looking statements involve a number of risks and uncertainties. Factors that could cause actual results to differ materially from those expressed in, or underlying, these forward-looking statements are detailed in the company's annual and quarterly report filings with the Securities and Exchange Commission. The company undertakes no obligation to publicly release revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unforeseen events, except as required to be reported under the rules and regulations of the Securities and Exchange Commission.

Stock Market Information

Our common stock trades on the NASDAQ Global Select Market under the symbol SONC. At November 19, 2012, we had approximately 14,000 shareholders, including beneficial owners holding shares in nominee or "street" name.

The table below sets forth our high and low sales prices for the company's common stock during each fiscal quarter within the two most recent fiscal years.

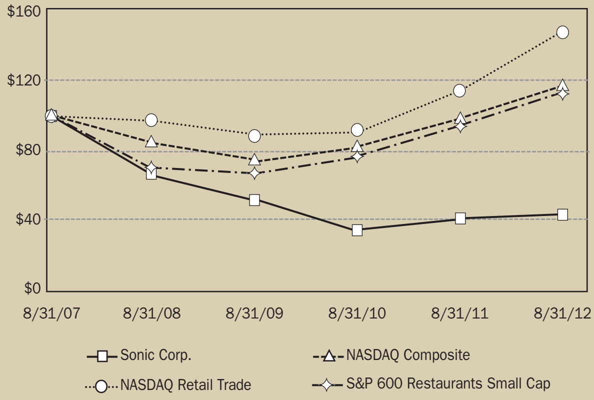
Fiscal Year Ended August 31, 2012	**High**	**Low**
First Quarter	$ 9.31	$ 6.35
Second Quarter	$ 8.45	$ 6.49
Third Quarter	$ 8.57	$ 6.84
Fourth Quarter	$10.94	$ 7.92

Fiscal Year Ended August 31, 2011	**High**	**Low**
First Quarter	$ 9.82	$ 7.30
Second Quarter	$11.53	$ 8.71
Third Quarter	$11.86	$ 8.50
Fourth Quarter	$11.45	$ 8.19

We currently anticipate that we will retain all of our earnings to support our operations and develop our business. Therefore, we do not pay any cash dividends on our outstanding common stock. Future cash dividends, if any, will be at the discretion of our Board of Directors and will depend upon, among other things, future operations and earnings, capital requirements, general financial conditions, contractual restrictions, and other factors that our Board may consider relevant.

Comparison of 5 Year Cumulative Total Return

The following graph compares the cumulative five-year return of holders of Sonic Corp.'s common stock with the cumulative total returns of the NASDAQ Composite index, the NASDAQ Retail Trade index, and the S&P 600 Restaurants Small Cap index. We are changing our industry comparison from the NASDAQ Retail Trade index to the S&P 600 Restaurants Small Cap index because we believe that the companies included in the S&P 600 Restaurants Small Cap index more appropriately reflect the scope of our operations and match our competitive market. The graph tracks the performance of a $100 investment in our common stock and in each index (with the reinvestment of all dividends) from 8/31/2007 to 8/31/2012.




SONIC
Jennifer
YOU SIP.
KIDS LEARN.®
SONIC
LIMEADES for LEARNING®

YOU SIP. KIDS LEARN®
Help give students a more fulfilling school year.

For three years running, Sonic and DonorsChoose.org have partnered to help public school teachers provide inspirational learning experiences for students in their classrooms through Limeades for Learning®. When Sonic customers ordered a drink during September 2012, they were encouraged to visit a special website, LimeadesforLearning.com, and vote for a teacher's project they wanted Sonic to fund. More than four million votes were cast by Sonic's customers and fans in the 2012 Limeades for Learning® Campaign to fund 1,495 public school classroom projects in 30 states!

Since 2009, Sonic and its generous franchisees have contributed more than $2.7 million to public school classrooms across the country through this program. Even though fall voting is over, there are still countless classrooms that could use your help. Go to LimeadesforLearning.com to see where all the votes went, and learn more about teachers' projects that still need assistance.

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