BLACKHAWK NETWORK HOLDINGS, INC
Form 10-Q
October 14, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 6, 2014
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number: 001-35882

BLACKHAWK NETWORK HOLDINGS, INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	43-2099257 (I.R.S. Employer Identification No.)
6220 Stoneridge Mall Road Pleasanton, CA	94588
(Address of Principal Executive Offices)	(Zip Code)

(925) 226-9990
(Registrant’s Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨
Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter time period that the registrant was required to submit and post such files). Yes ý No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨	Accelerated filer ý
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No ý

As of October 7, 2014, there were 12,677,000 shares of the Registrant’s Class A common stock outstanding and 40,320,000 shares of the Registrant’s Class B common stock outstanding.

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
BLACKHAWK NETWORK HOLDINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par value)
(Unaudited)

	September 6, 2014	December 28, 2013	September 7, 2013
ASSETS			
Current assets:			
Cash and cash equivalents	$ 219,851	$ 550,380	$ 103,453
Restricted cash	5,000	—	—
Overnight cash advances to Safeway	—	—	9,000
Settlement receivables, net	272,912	813,448	167,945
Accounts receivable, net	125,976	126,369	91,634
Deferred income taxes	20,145	20,145	10,499
Prepaid expenses and other current assets	71,802	67,474	57,674
Total current assets	715,686	1,577,816	440,205
Property, equipment and technology, net	95,368	79,663	71,384
Intangible assets, net	85,083	98,689	22,198
Goodwill	172,866	133,521	42,729
Deferred income taxes	727	727	983
Other assets	86,590	90,678	70,473
TOTAL ASSETS	$ 1,156,320	$ 1,981,094	$ 647,972

See accompanying notes to condensed consolidated financial statements

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BLACKHAWK NETWORK HOLDINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS (continued)
(In thousands, except par value)

	September 6, 2014	December 28, 2013	September 7, 2013
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities:			
Settlement payables	$ 472,629	$ 1,484,047	$ 351,938
Consumer and customer deposits	65,607	54,915	8,670
Accounts payable and accrued operating expenses	89,633	99,499	59,448
Current portion of note payable	8,708	—	—
Note payable to Safeway	8,473	—	—
Other current liabilities	49,695	81,270	41,817
Total current liabilities	694,745	1,719,731	461,873
Deferred income taxes	23,312	24,488	9,959
Note payable	165,446	—	—
Other liabilities	29,115	8,711	15,986
Total liabilities	912,618	1,752,930	487,818
Commitments and contingencies (see Note 8)	—	—	—
Stockholders' equity:			
Preferred stock: $0.001 par value; 10,000 shares authorized; no shares outstanding	—	—	—
Class A common stock: $0.001 par value; 125,000 shares authorized; 12,678, 12,188, and 11,550 shares outstanding, respectively	13	12	11
Class B common stock: $0.001 par value; 125,000 shares authorized; 40,297, 40,252, and 40,429 shares outstanding, respectively	41	41	41
Additional paid-in capital	125,267	107,139	95,225
Treasury stock	(508)	(126)	(50)
Accumulated other comprehensive loss	(7,556)	(2,873)	(2,930)
Retained earnings	119,730	116,975	67,713
Total Blackhawk Network Holdings, Inc. equity	236,987	221,168	160,010
Non-controlling interests	6,715	6,996	144
Total stockholders' equity	243,702	228,164	160,154
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 1,156,320	$ 1,981,094	$ 647,972

See accompanying notes to condensed consolidated financial statements

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BLACKHAWK NETWORK HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except for per share amounts)
(Unaudited)

	12 Weeks Ended		36 Weeks Ended	
	September 6, 2014	September 7, 2013	September 6, 2014	September 7, 2013
OPERATING REVENUES:				
Commissions and fees	$201,888	$ 158,270	$596,324	$ 479,564
Program, interchange, marketing and other fees	43,895	25,352	119,981	78,617
Product sales	23,244	22,374	69,781	58,727
Total operating revenues	269,027	205,996	786,086	616,908
OPERATING EXPENSES:				
Distribution partner commissions	137,506	105,361	400,123	319,496
Processing and services	46,715	34,927	133,654	101,321
Sales and marketing	41,704	30,486	126,274	98,743
Costs of products sold	21,946	21,423	66,745	55,782
General and administrative	16,163	10,320	41,700	33,115
Business acquisition expense (benefit) and amortization of acquisition intangibles	3,330	(255)	11,199	(962)
Total operating expenses	267,364	202,262	779,695	607,495
OPERATING INCOME	1,663	3,734	6,391	9,413
OTHER INCOME (EXPENSE):				
Interest income and other income (expense), net	182	59	126	432
Interest expense	(1,080)	—	(2,081)	—
INCOME BEFORE INCOME TAX EXPENSE	765	3,793	4,436	9,845
INCOME TAX EXPENSE	352	1,544	1,844	5,332
NET INCOME BEFORE ALLOCATION TO NON-CONTROLLING INTERESTS	413	2,249	2,592	4,513
Add: Net loss attributable to non-controlling interests (net of tax)	142	106	238	319
NET INCOME ATTRIBUTABLE TO BLACKHAWK NETWORK HOLDINGS, INC.	$555	$ 2,355	$2,830	$ 4,832
EARNINGS PER SHARE:				
Basic – Class A and Class B	$0.01	$ 0.05	$0.05	$ 0.09
Diluted – Class A and Class B	$0.01	$ 0.04	$0.05	$ 0.09
Weighted average shares outstanding—basic	52,609	51,615	52,450	50,811
Weighted average shares outstanding—diluted	54,304	53,074	54,035	51,982

See accompanying notes to condensed consolidated financial statements

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BLACKHAWK NETWORK HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)
(Unaudited)

	12 Weeks Ended		36 Weeks Ended	
	September 6, 2014	September 7, 2013	September 6, 2014	September 7, 2013
NET INCOME BEFORE ALLOCATION TO NON-CONTROLLING INTERESTS	$413	$2,249	$2,592	$4,513
Other comprehensive income (loss):				
Currency translation adjustments	(4,163)	(1,413)	(4,682)	(3,228)
COMPREHENSIVE INCOME (LOSS) BEFORE ALLOCATION TO NON-CONTROLLING INTERESTS	(3,750)	836	(2,090)	1,285
Add: Comprehensive loss attributable to non-controlling interests (net of tax)	145	106	237	319
COMPREHENSIVE INCOME (LOSS) ATTRIBUTABLE TO BLACKHAWK NETWORK HOLDINGS, INC.	$(3,605)	$942	$(1,853)	$1,604

See accompanying notes to condensed consolidated financial statements

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BLACKHAWK NETWORK HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	36 Weeks Ended	
	September 6, 2014	September 7, 2013
OPERATING ACTIVITIES:		
Net income before allocation to non-controlling interests	$2,592	$4,513
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	32,153	16,963
Program development cost amortization	17,779	13,259
Provision for doubtful accounts and sales adjustments	2,678	2,764
Employee stock-based compensation expense	9,769	5,279
Distribution partner mark-to-market expense	(88)	6,961
Change in fair value of contingent consideration	—	(1,255)
Reversal of reserve for patent litigation	(3,852)	—
Excess tax benefit from stock-based awards	(1,364)	(588)
Other	1,174	80
Changes in operating assets and liabilities:		
Settlement receivables	535,183	338,568
Settlement payables	(1,006,128)	(877,287)
Accounts receivable, current and long-term	8,721	15,132
Prepaid expenses and other current assets	1,450	(4,624)
Other assets	(21,466)	(19,894)
Consumer and customer deposits	6,542	(294)
Accounts payable and accrued operating expenses	(13,345)	(4,767)
Other current and long-term liabilities	(12,733)	(16,803)
Income taxes, net	(22,474)	(15,596)
Net cash used in operating activities	(463,409)	(537,589)
INVESTING ACTIVITIES:		
Change in overnight cash advances to Safeway	—	486,000
Expenditures for property, equipment and technology	(25,960)	(21,349)
Business acquisitions, net of cash received	(16,710)	—
Payment for working capital adjustment for business acquisitions, net	(1,366)	—
Cash received for assumption of liabilities from prior business acquisition	3,917	—
Change in restricted cash	(5,000)	8,968
Other	—	(250)
Net cash provided by (used in) investing activities	(45,119)	473,369

See accompanying notes to condensed consolidated financial statements

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BLACKHAWK NETWORK HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
(In thousands)
(Unaudited)

	36 Weeks Ended	
	September 6, 2014	September 7, 2013
FINANCING ACTIVITIES:		
Proceeds from issuance of note payable	175,000	—
Payments of costs for issuance of note payable	(2,451)	—
Proceeds from note payable to Safeway	8,473	—
Repayment of debt assumed in business acquisition	(7,474)	—
Payments for acquisition liability	—	(2,281)
Payments for initial public offering costs	—	(4,694)
Reimbursements for initial public offering costs	—	5,540
Proceeds from issuance of common stock from exercise of employee stock options and employee stock purchase plans	5,895	359
Excess tax benefit from stock-based awards	1,364	588
Other	(778)	(872)
Net cash provided by (used in) financing activities	180,029	(1,360)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(2,030)	(3,632)
DECREASE IN CASH AND CASH EQUIVALENTS	(330,529)	(69,212)
CASH AND CASH EQUIVALENTS—Beginning of year	550,380	172,665
CASH AND CASH EQUIVALENTS—End of period	$219,851	$103,453
Noncash investing and financing activities:		
Financing of business acquisition with stock	$1,595	$—
Financing of business acquisition with contingent consideration	$24,100	$—
Reclassification of warrant and common stock liabilities to additional paid-in capital upon initial public offering	$—	$27,121
Reclassification of redeemable equity to stockholders' equity upon initial public offering	$—	$36,171
Intangible assets recognized for the issuance of fully vested warrants	$—	$22,183

See accompanying notes to condensed consolidated financial statements

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BLACKHAWK NETWORK HOLDINGS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
1. The Company and Significant Accounting Policies
The Company
Blackhawk Network Holdings, Inc., together with its subsidiaries (we, us, our), is a leading prepaid payment network utilizing proprietary technology to offer a broad range of prepaid gift, telecom and debit cards, in physical and digital forms, as well as related prepaid products and payment services in the United States and 21 other countries. Our payment network supports our key constituents: consumers who purchase or receive the products and services we offer, content providers who offer branded gift cards and other prepaid products that are redeemable for goods and services, distribution partners who sell those products and business partners that distribute our products as incentives and rewards. Our product offerings include gift cards, prepaid telecom products and prepaid financial services products, including general purpose reloadable (GPR) cards and our reload network (collectively, prepaid products). We offer gift cards from leading consumer brands (known as closed loop) as well as branded gift and incentive cards from leading payment network card associations such as American Express, Discover, MasterCard and Visa (known as open loop) and prepaid telecom products offered by prepaid wireless telecom carriers. We also distribute GPR cards, including Green Dot and NetSpend branded cards, as well as PayPower, our proprietary GPR card. We operate a proprietary reload network named Reloadit, which allows consumers to reload funds onto their previously purchased GPR cards. We distribute products across multiple high-traffic channels such as grocery, convenience, specialty and online retailers (referred to as distribution partners) in the Americas, Europe, Africa, Australia and Asia.
Spin-Off
Prior to April 14, 2014, we were a majority-owned subsidiary of Safeway Inc. (Safeway). On April 14, 2014, Safeway distributed its remaining 37.8 million shares of our Class B common stock to Safeway stockholders (the Spin-Off). As a result of the Spin-Off, we became a stand-alone entity separate from Safeway. See Note 7—Income Taxes and Note 9—Related Party Transactions for disclosures regarding this relationship.
Basis of Presentation
The accompanying condensed consolidated financial statements of Blackhawk Network Holdings, Inc. are unaudited. We have prepared our unaudited interim condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. We have condensed or omitted certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP pursuant to such rules and regulations. Accordingly, our interim condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements and related notes included in our Annual Report on Form 10-K, filed with the SEC on March 17, 2014 (the Annual Report). We have prepared our condensed consolidated financial statements on the same basis as our annual audited consolidated financial statements and, in the opinion of management, have reflected all adjustments, which include only normal recurring adjustments, necessary to present fairly our financial position and results of operations for the interim periods presented. Our results for the interim periods are not necessarily reflective of the results to be expected for the year ending January 3, 2015 or for any other interim period or other future year. Our condensed consolidated balance sheet as of December 28, 2013, included herein was derived from our audited consolidated financial statements as of that date but does not include all disclosures required by GAAP, including notes to the financial statements.
Our condensed consolidated financial statements include Blackhawk Network Holdings, Inc., a Delaware corporation, and its wholly- or majority-owned domestic and foreign subsidiaries. All intercompany transactions and balances among us and our subsidiaries have been eliminated in consolidation. Our condensed consolidated financial statements have been prepared as if we existed on a stand-alone basis for the periods presented, but may not necessarily reflect the results of operations, financial position or cash flows that would have been achieved if we had existed on a stand-alone basis separate from Safeway during the periods presented.
Prior to the Spin-Off, our condensed consolidated financial statements included an allocation of expenses arising from certain shared services and infrastructure provided by Safeway. These expenses primarily related to facilities rental

and tax services and were allocated using actual costs or estimates based on the portion of services used by us. Management believes that the allocation methodology was reasonable and considers the charges to be a reasonable reflection of the cost of benefits received. Following the Spin-Off, Safeway continues to rent facilities to us and provide certain tax services (related to tax periods through the Spin-Off) based on similar pricing terms as prior to the Spin-Off.

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Significant Accounting Policies

There have been no material changes to our significant accounting policies, as compared to the significant accounting policies described in the audited consolidated financial statements and related notes included in the Annual Report.

Use of Estimates

The preparation of our condensed consolidated financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and the accompanying notes to the condensed consolidated financial statements. We generally base our estimates and assumptions on a combination of historical factors, current circumstances, and the experience and judgment of management. Significant estimates and assumptions include, among other things, allowances for doubtful accounts and sales adjustments, useful lives of assets, card redemption patterns and lives, delivery timing for product sales and valuation assumptions with respect to acquisition liabilities, goodwill, other intangible assets, common stock and income taxes. Actual results could differ from our estimates.

Seasonality

A significant portion of gift card sales occurs in late December of each year during the holiday selling season. As a result, we earn a significant portion of revenues, net income and cash inflows during the fourth fiscal quarter of each year and remit the majority of the cash, less commissions, to our content providers in January of the following year. The timing of our fiscal year-end, December holiday sales and the related January cash settlement with content providers significantly increases our Cash and cash equivalents, Overnight cash advances to Safeway, Settlement receivables and Settlement payables balances at the end of each fiscal year relative to normal daily balances. The cash settlement with our content providers in January accounts for the majority of the use of cash from operating activities in our condensed consolidated statements of cash flows during our first three fiscal quarters. Additionally, our operating income may fluctuate significantly during our first three fiscal quarters due to lower revenues and timing of certain expenses during such fiscal periods. As a result, quarterly financial results are not necessarily reflective of the results to be expected for the year, any other interim period or other future year.

Restatement

Subsequent to the issuance of our third quarter 2013 condensed consolidated financial statements, we identified certain IRS limitations related to stock-based compensation as a result of our initial public offering in that quarter that should have been considered in our reported income tax expense for that quarter. Therefore, we have corrected previously issued condensed consolidated financial statements for the 36 weeks ended September 7, 2013 for a $1.4 million increase in income tax expense, decrease to Net income attributable to Blackhawk Network Holdings, Inc. and related impacts to our condensed consolidated balance sheets and statements of comprehensive income and cash flows. We have also corrected Basic and Diluted Earnings per Share – Class A and Class B from previously reported amounts of $0.12 and $0.12, respectively, for the 36 weeks ended September 7, 2013. Management does not consider these amounts to be material to our previously issued unaudited condensed consolidated financial statements.

Reclassification

In the accompanying condensed consolidated balance sheets, we have reclassified amounts previously reported as Accounts payable and accrued liabilities into Consumer and customer deposits, Accounts payable and accrued expenses and Other current liabilities. We have made the corresponding reclassifications in the condensed consolidated statements of cash flows and have combined the changes of Other current liabilities and Other liabilities as Other current and long-term liabilities. Additionally, we have reclassified the Change in the provision for doubtful accounts and sales adjustments from previously reported amounts to (i) the Provision for doubtful accounts and sales adjustments, (ii) changes in operating assets and liabilities for Settlement receivables and (iii) changes in operating assets and liabilities for Accounts receivable, current and long-term.

In the accompanying consolidated statements of operations, we have reclassified certain amounts from previously reported amounts in various Operating expenses, including the change in fair value of contingent consideration and acquisition-related expenses previously reported in General and administrative expense, to Business acquisition expense (benefit) and amortization of acquisition intangibles.

Restricted Cash

Restricted cash represents funds held in an escrow account related to one of our acquisitions. See Note 2—Business Acquisitions.

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Financing Costs

We incurred debt issuance costs and paid certain costs to the group of banks in conjunction with entering into our credit agreement, which included a note payable and revolving credit facility (see Note 4—Financing). We allocated the costs paid to the group of banks between the note payable and revolving credit facility based on their relative fair values and recognized them as discount on note payable and deferred revolving credit facility costs, respectively. We present the deferred revolving credit facility costs and debt issuance costs (collectively, deferred financing costs) in Other assets and the discount on the note payable as a reduction of the carrying value of the Note payable in our accompanying condensed consolidated balance sheets. We amortize the deferred financing costs and discount on note payable on a straight-line basis over the term of the credit agreement as the difference between the straight-line method and effective interest method is immaterial to our consolidated financial statements.

Revenue Recognition

Post-Activation Program Management Fees—During the 36 weeks ended September 6, 2014, pursuant to contract amendments with certain of our card-issuing banks of our open loop Visa gift and incentive cards, the issuing banks agreed to replace certain account service fees and fund expiration fees with a program management fee, defined as a contractually-determined percentage of load value. We recognize these fees in the same manner as our other program management fees described in our Annual Report. Certain of these issuing banks agreed to compensate us under this arrangement for cards activated from January 1, 2014 or other prior periods. Certain of these amendments also provide that, in addition to the program management fee, the issuing banks will compensate us in the same amount that the issuing bank would have paid to us as account service fees and fund expiration fees on such cards to the extent that such fees exceed the program management fees previously paid to us.

Recent Accounting Pronouncement

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2014-09 Revenue from Contracts with Customers (Topic 606). ASU 2014-09 supersedes all previous revenue recognition guidance with a single revenue recognition model. This new guidance is to be applied retrospectively either to each reporting period presented or with the cumulative effect of initially applying the guidance at the date of initial application for reporting periods beginning after December 15, 2016. Early adoption is not permitted. Management is still evaluating the impact of this guidance.

2. Business Acquisitions

2014 Acquisitions

Parago, Inc.

On September 24, 2014, we entered into a definitive agreement to acquire Parago, Inc. and its subsidiaries, a leader in providing global incentive and engagement solutions, for approximately $291 million, consisting of cash purchase consideration of approximately $256 million, subject to certain adjustments for working capital, and debt assumed of approximately $35 million. The acquisition is expected to close by the end of October 2014, subject to certain conditions, including receipt of certain regulatory approvals. If consummated, this acquisition will allow us to deliver expanded capabilities and products in the consumer and corporate incentives markets. We plan to finance the purchase using cash on hand and approximately $200 million in new borrowings under an expansion of our current credit facility.

Other 2014 Acquisitions

During the 36 weeks ended September 6, 2014, we acquired CardLab, Inc. and its subsidiaries (CardLab), a leading online provider of customizable prepaid incentive and rewards cards, and Incentec Solutions, Inc. (Incentec), which provides cloud-based software solutions in the incentives and rewards industry, for total purchase consideration of $44.6 million. These acquisitions have enhanced our product and service offerings in our incentives business. We accounted for these acquisitions as business combinations and have included their results of operations in our accompanying condensed consolidated financial statements starting on the acquisition dates. The following table summarizes the components of the purchase consideration based on their fair values at the acquisition dates (in thousands):

Cash paid at closing	$18,898
Stock consideration	1,595

Contingent consideration	24,100
Total purchase consideration	$44,593

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Stock consideration consists of 61,840 shares of our Class A common stock. Contingent consideration resulting from our acquisition of CardLab consists of three cash payments: i) up to $2.5 million based on CardLab's 2014 financial results, ii) $0, $1.25 million or $2.5 million dependent upon the contract execution and subsequent launch of a certain incentive program by certain specified dates and iii) up to $46.5 million based on CardLab's 2015 financial results for certain incentive programs. We estimated the fair value of the contingent consideration based on our estimates of the probability of achieving these targets and discount rates ranging from 4.6% to 15.0%, reflecting the risk profiles of meeting these targets (see Note 3—Fair Value Measurements) and present such amounts in Other current liabilities or Other liabilities in our condensed consolidated balance sheets. We placed $5.0 million in an escrow account for the contingent consideration related to the 2014 financial results and the execution and launch of the incentive program and present such amounts as Restricted cash in the accompanying condensed consolidated balance sheets.

We allocated the total purchase consideration to tangible net assets and identifiable technology and intangible assets based on the estimated fair value of each asset and liability and recorded the excess purchase price over the fair value of the net assets as goodwill. Goodwill represents the value of the future cash flows from new customers and the launch of new incentive programs, our prior relationship with Incentec and the value of the assembled workforce. Goodwill is not expected to be deductible for income tax purposes. The following table summarizes the initial purchase price allocation, and we may make adjustments to these amounts through the one year measurement period to finalize information regarding forecasting assumptions, other relevant valuation assumptions, working capital, amounts due to or from us regarding working capital and income taxes (in thousands):

Tangible liabilities, net	$(1,112)
Debt assumed	(7,474)
Deferred taxes	756
Identifiable technology and intangible assets	11,123
Goodwill	41,300
Total purchase consideration	$44,593

We repaid all of CardLab's outstanding debt of $7.5 million on the acquisition date and present such payments as Repayment of debt assumed in business acquisition in our condensed consolidated statements of cash flows.

The following table summarizes the components of the identifiable technology and intangible assets and their estimated useful lives at the acquisition date (dollars in thousands):

	Fair Value	Useful Life
Customer relationships	$1,250	5 years
Back-log	1,610	4 months
Technology	8,180	5 years
Trade name	83	3 years
Total identifiable technology and intangible assets	$11,123	

Customer relationships represent the estimated fair value of the underlying relationships and agreements with the acquirees' customers. Back-log represents the estimated fair value resulting from cards issued prior to the acquisition date, resulting from revenues, including interchange and account service fees. Technology consists of Incentec's cloud-based software solutions and CardLab's internal-use software used for the order, fulfillment and management of customer orders. Trade name represents the fair value of the brand and name recognition associated with the acquirees.

We valued customer relationships, back-log, trade name and Incentec's technology using the income approach and CardLab's technology using the cost approach. Significant assumptions include forecasts of revenues, costs of revenue, development costs and sales, general and administrative expenses and estimated attrition rates for customers. We discounted the cash flows at various rates reflecting the different risk profiles of the assets.

Acquisition related costs totaled $0.4 million and are included in Business acquisition expense (benefit) and amortization of acquisition intangibles expense. Revenues and earnings from closing and pro forma financial information are not presented, as amounts are not material to our condensed consolidated financial statements.

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2013 Acquisitions

As discussed in our Annual Report, in the fourth quarter of 2013, we acquired Retailo AG and its subsidiaries (collectively, Retailo) and substantially all of the net assets of InteliSpend Prepaid Solutions, LLC, and its subsidiaries (collectively, InteliSpend). We have included the results of Retailo and InteliSpend in our consolidated financial statements since the acquisition dates.

The following pro forma financial information summarizes the combined results of operations of us, Retailo and InteliSpend as though we had been combined as of the beginning of fiscal 2012 (in thousands):

	12 Weeks Ended September 7, 2013	36 Weeks Ended September 7, 2013
Total revenues	$222,624	$665,545
Net income attributable to Blackhawk Network Holdings, Inc.	1,556	2,824

The pro forma financial information includes adjustments to amortize the identifiable technology and intangible assets starting at the beginning of 2012. The pro forma financial information is for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisitions had taken place at the beginning of 2012.

As discussed in our Annual Report, we had not assumed certain cardholder liabilities nor acquired the related cash for our acquisition of InteliSpend due to requirements for a state regulatory approval. In May 2014, we received such approval and subsequently assumed such liabilities and related cash of $3.9 million, which we present as Cash received for assumption of liabilities from prior business acquisition in the accompanying condensed consolidated statements of cash flows.

3. Fair Value Measurements

We measure certain assets and liabilities at fair value on a recurring basis. The table below summarizes the fair value of these assets and liabilities as of September 6, 2014, December 28, 2013 and September 7, 2013 (in thousands):

	September 6, 2014			
	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents				
Money market mutual funds	$86,100	$—	$—	$86,100
Liabilities				
Contingent consideration	$—	$—	$24,100	$24,100

	December 28, 2013			
	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents				
Money market mutual funds	$379,000	$—	$—	$379,000
Liabilities				
Contingent consideration	$—	$—	$—	$—

	September 7, 2013			
	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents				
Money market mutual funds	$28,000	$—	$—	$28,000
Liabilities				
Contingent consideration	$—	$—	$13,485	$13,485

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Level 1— Unadjusted quoted prices in active markets for identical assets or liabilities. Level 1 investments include money market mutual funds.
Level 2— Inputs other than quoted prices included in Level 1 that are either directly or indirectly observable. Level 2 investments include commercial paper. We did not classify any amounts within Level 2 as of September 6, 2014, December 28, 2013 or September 7, 2013.
In the 36 weeks ended September 6, 2014, there were no transfers between Level 1 and Level 2.
Level 3— Unobservable inputs in which little or no market activity exists, therefore requiring an entity to develop its own assumptions about the inputs that market participants would use in pricing. Level 3 includes the estimated fair value of our contingent consideration liability.
Contingent Consideration—We estimate the fair value of the contingent consideration based on our estimates of the probability of achieving the relevant targets and discount rates reflecting the risk profiles of meeting these targets. A significant increase (decrease) in our estimate of the probability of achieving the relevant targets or a significant decrease (increase) in the discount rate could materially increase (decrease) the fair value of contingent consideration.
The change in fair value of contingent consideration classified as Level 3 for the 36 weeks ended September 6, 2014 and September 7, 2013 is as follows (in thousands):

	36 Weeks Ended	
	September 6, 2014	September 7, 2013
Contingent Consideration		
Balance – Year-end	$—	$18,947
Decrease in fair value of contingent consideration	—	(1,255)
Issuance of contingent consideration for acquisition of CardLab	24,100	—
Settlements	—	(4,207)
Balance – End of period	$24,100	$13,485

The decrease in the fair value of contingent consideration is recognized in Business acquisition expense (benefit) and amortization of acquisition intangibles, is presented as a non-cash adjustment to net income in our accompanying condensed consolidated statements of cash flows and reflects the changes in the passage of time, expected timing of the contingent payments, our estimate of the probability of achieving the relevant targets and the discount rate. Settlements reflect the resolution of the contingency based on achievement of the relevant targets.
As of year-end 2013, we estimated the fair value of contingent consideration from our acquisition of Cardpool to be $0. As of September 6, 2014, the final measurement period for the Cardpool contingent consideration was concluded, and no amounts were payable based on such measurement period. As a result of our acquisition of CardLab during the 36 weeks ended September 6, 2014, we recognized the fair value of contingent consideration at its acquisition date (see Note 2—Business Acquisitions), and there was no change in the fair value from the acquisition date through September 6, 2014. We estimated the fair value of the contingent consideration based on our estimates of the probability of achieving the relevant targets and discount rates ranging from 4.6% to 15.0%, reflecting the risk profiles of meeting these targets. A significant increase (decrease) in our estimates of achieving the relevant targets or a significant decrease (increase) in the discount rates used could materially increase (decrease) the fair value of the contingent consideration liability.
As of September 7, 2013, settlements of $3.3 million were payable, and, during the 36 weeks ended September 7, 2013, we paid settlements of $2.3 million, of which $1.4 million resulted from fiscal 2012 financial and operational results, which we present as Payments for acquisition liability in our accompanying condensed consolidated statements of cash flows.

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4. Financing

On March 28, 2014, we entered into a credit agreement with a group of banks (the Credit Agreement). The Credit Agreement includes a $175 million 4-year term loan, with an option to increase such loan to $225 million, and a revolving credit facility of up to $200 million with up to an additional $100 million during the year-end holiday period for specific settlement related requirements. The revolving credit facility includes a $100 million subfacility for the issuance of letters of credit. On September 26, 2014, we exercised the option for the additional $50 million under the term loan and increased our term loan to $225 million. Borrowings under the Credit Agreement are secured by a pledge of the assets of Blackhawk Network Holdings, Inc.; substantially all of the assets of certain of its U.S. subsidiaries, including Blackhawk Network, Inc., the primary U.S. operating subsidiary; and 65% of the shares in certain foreign subsidiaries.

Loans borrowed under the Credit Agreement bear interest, in the case of LIBOR rate loans, at a per annum rate equal to the LIBOR rate plus the Applicable Margin (as defined in the Credit Agreement), which may range from 1.25% to 2.00%, based on our Consolidated Total Leverage Ratio (as defined in the Credit Agreement). Loans that are borrowed under the Credit Agreement that are not LIBOR rate loans bear interest at a per annum rate equal to (i) the highest of (A) the rate of interest announced, from time to time, by Wells Fargo Bank, National Association as its "prime rate," (B) the Federal Funds Rate plus 0.50% and (C) one-month LIBOR plus 1.00%, plus (ii) the Applicable Margin, which may range from 0.25% to 1.00%, based on our Consolidated Total Leverage Ratio. During the 36 weeks ended September 6, 2014, our interest rate for our Note payable ranged from 1.73% to 1.75%.

A letter of credit commission on the daily amount available to be drawn under letters of credit issued under the Credit Agreement is payable by us at the rate per annum equal to the Applicable Margin with respect to LIBOR rate loans, which Applicable Margin may range from 1.25% to 2.00% per annum, based on our Consolidated Total Leverage Ratio; provided, however, that the commission on letters of credit secured by cash is payable at the rate of 0.75% per annum. During the 36 weeks ended September 6, 2014, our interest rate for our letter of credit commission was 1.75%.

A commitment fee on the average daily unused portion of the revolving credit facility is payable by us at the rate per annum equal to the Applicable Margin for that fee, which may range from 0.20% to 0.35%, based on our Consolidated Total Leverage Ratio. Other fees are also payable by us, as referenced in the Credit Agreement. During the 36 weeks ended September 6, 2014, our interest rate for our commitment fee was 0.25%.

The Credit Agreement contains various loan covenants that restrict our ability to take certain actions and contains financial covenants that require us periodically to meet certain financial tests, which limit our ability to declare and pay cash dividends.

As of September 6, 2014, we had no amounts outstanding under our revolving credit facility, $44.9 million in outstanding letters of credit and $155.1 million available under our revolving credit facility.

As of September 6, 2014, we estimate the fair value of our Note payable to be approximately $175 million.

The following table presents the amounts due by maturity date, unamortized discount and net carrying amount of our Note payable as of September 6, 2014 and amounts due by maturity date as of September 26, 2014 pursuant to our exercise of our option to increase our loan to $225 million (in thousands):

	September 6, 2014	September 26, 2014
Due March 21, 2015	$8,750	$11,250
Due March 21, 2016	17,500	22,500
Due March 21, 2017	26,250	33,750
Due March 28, 2018	122,500	157,500
Total amount due	$175,000	$225,000
Unamortized discount	(846)	
Note payable, net of discount	$174,154	

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5. Condensed Consolidated Financial Statement Details

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets as of September 6, 2014, December 28, 2013 and September 7, 2013 consisted of the following (in thousands):

	September 6, 2014	December 28, 2013	September 7, 2013
Card stock	$ 19,104	$ 13,342	$ 12,230
Deferred expenses	6,970	10,126	3,416
Program development costs	3,041	5,767	7,016
Prepaid load value	6,399	10,631	10,174
Income tax receivables	14,292	8,344	2,811
Other prepaids	21,996	19,264	22,027
Total prepaid expenses and other current assets	$ 71,802	$ 67,474	$ 57,674

Goodwill

A summary of changes in our goodwill during the 36 weeks ended September 6, 2014 is as follows (in thousands):

Balance – December 28, 2013	$133,521
Retailo purchase price adjustment	78
Business acquisitions	41,300
Foreign currency translation adjustments	(2,033)
Balance – September 6, 2014	$172,866

We have finalized our information regarding working capital for our acquisitions of InteliSpend and Retailo and have settled amounts due to or from us for working capital adjustments, which we present as Payment for working capital adjustment for business acquisitions, net in the accompanying condensed consolidated statements of cash flows.

Other Assets

Other assets as of September 6, 2014, December 28, 2013 and September 7, 2013 consisted of the following (in thousands):

	September 6, 2014	December 28, 2013	September 7, 2013
Program development costs	$ 59,729	$ 58,029	$ 46,738
Other receivables	9,737	19,905	10,901
Income taxes receivable	6,376	5,555	4,962
Deferred financing costs	1,330	—	—
Other	9,418	7,189	7,872
Total other assets	$ 86,590	$ 90,678	$ 70,473

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Other Current Liabilities

Other current liabilities as of September 6, 2014, December 28, 2013 and September 7, 2013 consisted of the following (in thousands):

	September 6, 2014	December 28, 2013	September 7, 2013
Deferred revenue	$ 23,934	$ 30,540	$ 15,262
Income taxes payable	3,269	21,167	4,939
Payroll and related liabilities	15,398	20,949	10,096
Acquisition liabilities	4,350	2,279	6,867
Other payables and accrued liabilities	2,744	6,335	4,653
Total other current liabilities	$ 49,695	$ 81,270	$ 41,817

Other Liabilities

Other liabilities as of September 6, 2014, December 28, 2013 and September 7, 2013 consisted of the following (in thousands):

	September 6, 2014	December 28, 2013	September 7, 2013
Acquisition liabilities	$ 19,750	$ —	$ 9,930
Payable to content provider	6,718	6,664	4,360
Income taxes payable	906	—	—
Deferred income and other liabilities	1,741	2,047	1,696
Total other liabilities	$ 29,115	$ 8,711	$ 15,986

Business Acquisition Expense (Benefit) and Amortization of Acquisition Intangibles

Business acquisition expense (benefit) and amortization of acquisition intangibles for the 12 and 36 weeks ended September 6, 2014 and September 7, 2013 consisted of the following (in thousands):

	12 Weeks Ended		36 Weeks Ended	
	September 6, 2014	September 7, 2013	September 6, 2014	September 7, 2013
Change in fair value of contingent consideration liability (See Note 3—Fair Value Measurements)	$—	$(352)	$—	$(1,255)
Amortization of intangible assets acquired in business combination	3,005	97	10,839	293
Acquisition related expenses	325	—	360	—
Total business acquisition expense (benefit) and amortization of acquisition intangibles	$3,330	$(255)	$11,199	$(962)

6. Stock Based Compensation

During the 36 weeks ended September 6, 2014 our Board of Directors granted 26,250 restricted stock awards, 886,450 restricted stock units, 88,900 performance stock units and 559,500 stock options at a weighted-average exercise price of $26.65 per share.

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7. Income Taxes

Our effective tax rates were 46.0% and 40.7% for the 12 weeks ended September 6, 2014 and September 7, 2013, respectively and were 41.6% and 54.2% for the 36 weeks ended September 6, 2014 and September 7, 2013, respectively. The effective rate for the 12 weeks ended September 6, 2014 was higher primarily due to operating losses of certain foreign subsidiaries for which we did not recognize an income tax benefit and jurisdictional mix of income partially offset by benefits related to return-to-provision adjustments that we recorded in the 12 weeks ended September 6, 2014. The effective rate for the 36 weeks ended September 6, 2014 was lower primarily due to lower amounts of nondeductible equity based compensation expense for certain executives, which, as a result of our initial public offering, became subject to IRS limitations.

Second Amended and Restated Tax Sharing Agreement

In April 2014, we and Safeway executed the second Amended and Restated Tax Sharing Agreement (the SARTSA), which superseded the previous tax sharing agreements, with respect to the matters addressed by the SARTSA. Under the terms of the SARTSA, if the Spin-Off is treated as taxable, we and Safeway intend to continue to file a consolidated federal tax return and certain state and local tax returns through the date of the Spin-Off, rather than through the date of our initial public offering in April 2013, as discussed in the Annual Report, subject to Safeway's ultimate determination as to whether such consolidated treatment is appropriate.

Safeway previously announced that it had entered into the Agreement and Plan of Merger with AB Acquisition LLC dated March 6, 2014, which was subsequently amended on April 7, 2014 pursuant to Amendment No. 1 and on June 13, 2014 pursuant to Amendment No. 2 (as amended, the Merger Agreement). Assuming that the acquisition of Safeway by AB Acquisition LLC (the Merger) is completed as contemplated by the Merger Agreement, the Spin-Off is expected to be taxable to Safeway and Safeway's stockholders. Under the SARTSA, any corporate-level income tax incurred as a result of the Spin-Off in the event that the Merger is completed will be borne by Safeway, except that, pursuant to a separate letter agreement entered into by Safeway and us in August 2014, we will bear any incremental taxes that result from certain elections requested by us with respect to certain of our subsidiaries in connection with the Spin-Off.

The SARTSA provides that Safeway and we will make an election that is intended to give rise to a step-up in the tax basis of Blackhawk's assets if the Spin-Off is taxable (the Section 336(e) Election). The actual benefit realized by us from the step-up will depend on, among other things, our value at the time of the Spin-Off and whether we generate adequate taxable income over time to fully utilize deductions associated with any increased tax basis resulting from the Section 336(e) Election.

If the Merger is not completed, and certain other conditions are satisfied, it is intended that the Spin-Off qualify as a tax-free transaction to Safeway and its stockholders. The SARTSA provides for certain continuing restrictions and covenants applicable to both Safeway and us that are intended to preserve the ability for the Spin-Off to qualify as a tax-free spin-off. Among the restrictions on us are that (i) for up to two years following the termination of the Merger Agreement, subject to certain exceptions, we will not dispose of all or substantially all of our assets, merge with another entity, issue an amount of our stock (or securities convertible or exchangeable into our stock) in one or more transactions that would comprise 40% or more of our value or voting power, facilitate any person becoming the owner of 5% or more of our stock, or cease conducting our current business and (ii) for up to five years from the date of our initial public offering in April 2013, we will not seek to convert any class of our stock into a different class of our stock or change the absolute or relative voting rights of our classes of stock. The SARTSA provides these restrictions will lapse in certain circumstances, including the completion of the Merger or the completion of certain alternative transactions. If the Merger is not completed, each of Safeway and we would be responsible for any taxes resulting from the failure of the Spin-Off to qualify as a tax-free transaction to the extent such taxes are attributable to, or result from, any act or failure to act by Safeway or us, as applicable, or certain transactions involving Safeway or us, as applicable, following the Spin-Off. Safeway and we each would be responsible for 50 percent of taxes from the Spin-Off to the extent such taxes are not attributable to, or do not result from, any act or failure to act by either Safeway or us.

The SARTSA provides that, in the event that (i) the Merger does not occur, (ii) the Spin-Off is taxable, (iii) Safeway bears the liability for any Spin-Off taxes and (iv) certain other conditions are met, we will make payments to Safeway

over time equal to 85 percent of the amount of the tax benefits, if any, that we are deemed to realize as a result of the Section 336(e) Election. The tax benefit deemed realized will be computed by comparing our actual income tax liability (calculated based on certain assumptions) to the amount of income taxes we would have been required to pay had the Section 336(e) Election not been made. Such payments will be made by us to Safeway as we recognize the benefit of the basis step-up, or upon the occurrence of certain events, such as certain changes of control of us or material breaches by us of the provisions in the SARTSA regarding such payments.

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For any states in which we are required under state law to remit Spin-Off taxes (because Safeway does not file combined returns with us in those states), Safeway is responsible for funding the amount of such taxes; however, the SARTSA permits Safeway to determine how such taxes will be remitted to the applicable state taxing authority. To date, Safeway has determined to fund these amounts to us in exchange for promissory notes. Pursuant to the terms of the notes, Safeway will contribute the notes to us as paid-in capital when the Merger is completed (and also will do so if the Merger is not completed but the Spin-Off is nonetheless taxable as a result of the negotiation of the Merger (or an alternative acquisition)). If the Merger is not completed and certain other considerations are satisfied, it is intended that the Spin-Off qualify as a tax-free transaction. In that event, we intend to file for refunds of the Spin-Off taxes paid to these states and then repay the notes with the refunded amounts.
As of September 6, 2014, Safeway has funded approximately $8.5 million to us in exchange for promissory notes for Spin-Off taxes we directly remitted to certain state taxing authorities. The promissory notes bear interest at a per annum rate equal to the short-term applicable federal rates. We present the corresponding Spin-Off tax payments that we remitted to various state taxing authorities in Prepaid expenses and other current assets in our condensed consolidated balance sheets. On September 11, 2014, Safeway funded an additional $16.1 million in exchange for a promissory note for Spin-Off taxes that we directly remitted to various state taxing authorities.

8. Commitments and Contingencies

Legal Matters

On October 19, 2009, e2Interactive and Interactive Communications International, Inc. (collectively, InComm) filed a lawsuit against us in the United States District Court for the Western District of Wisconsin (the District Court), alleging that we infringed a recently issued patent (the Patent). InComm claimed the rights to “methods, systems and computer programs for processing a store-value card transaction request in a card data management system.” InComm sought injunctive relief, damages and attorneys’ fees. On December 2, 2009, we answered InComm’s complaint and filed counterclaims asserting, among other things, that the Patent was invalid and that InComm engaged in inequitable conduct before the U.S. Patent and Trademark Office in securing the Patent. We sought a declaration of noninfringement, invalidity and unenforceability of the Patent. On February 28, 2012, the jury found that we had infringed the Patent and awarded damages of $3.5 million plus interest to InComm for such infringement. On February 21, 2013, the District Court awarded InComm costs, such that the total damages outstanding at year end 2013 totaled $3.7 million. We appealed to the United States Court of Appeals for the Federal Circuit (the Federal Circuit). On March 12, 2014, the Federal Circuit reversed the judgment of infringement on the grounds that the asserted claims in the Patent were limited “to require use of the terminal identifier for determining if a terminal is authorized to make the requested transaction” and that we did not make such use of a terminal identifier. InComm requested rehearing en banc at the Federal Circuit. On April 29, 2014, the Federal Circuit denied InComm’s request. We filed a motion with the District Court seeking to have the previous award of damages vacated and also for discharge of the injunction, release of the bond, and for a reversal of costs. The District Court ruled in our favor, vacating the damages award, discharging the injunction, releasing the bond and reversing the costs award. All appeal deadlines have passed regarding liability. Accordingly, we reversed our previously recorded reserve of $3.9 million (including interest) during the 36 weeks ended September 6, 2014 to General and administrative expense.
There are various claims and lawsuits arising in the normal course of business pending against us, some of which seek damages and other relief which, if granted, may require future cash expenditures. Management does not believe that it is probable that the resolution of these matters would result in any liability that would materially affect our results of operations or financial condition.

Commitments

From time to time, we enter into contracts containing provisions that require us to indemnify various parties against certain potential claims from third parties. Under contracts with certain issuing banks, we are responsible to the banks for any unrecovered overdrafts on cardholders’ accounts. Under contracts with certain content and distribution partners, we are responsible for potential losses resulting from certain claims from third parties. Because the indemnity amounts associated with these agreements are not explicitly stated, the maximum amount of the obligation cannot be reasonably estimated. Historically, we have paid limited amounts pursuant to these indemnification provisions.

Contingencies

We are subject to audit related to various indirect taxes, including, but not limited to, sales and use taxes, value-added tax, and goods and services tax, in various foreign and state jurisdictions. We evaluate our exposure related to these audits and potential audits and do not believe that it is probable that any audit would hold us liable for any material amounts due.

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9. Related-Party Transactions

Intercompany Revenues and Expenses

As discussed in Note 1, until April 14, 2014, Safeway was our Parent. The following table presents the amounts of Operating revenues and Other income (expense) from (to) Safeway and Operating expenses to (from) Safeway through the Spin-Off date of April 14, 2014 included in the accompanying consolidated statements of operations (in thousands). Although we are no longer a related party with Safeway, we continue to recognize Operating revenues from Safeway and Operating expense to (from) Safeway following the Spin-Off.

	12 Weeks Ended		36 Weeks Ended	
	September 6, 2014	September 7, 2013	September 6, 2014	September 7, 2013
OPERATING REVENUES:				
Commissions and fees	$—	$376	$710	$1,493
Program, interchange, marketing and other fees	—	321	383	1,053
Product sales	—	1,669	863	3,552
Total operating revenues	—	2,366	1,956	6,098
OPERATING EXPENSES:				
Distribution partner commissions	—	9,887	11,821	30,973
Processing and services	—	(1,105)	(212)	(1,453)
Sales and marketing	—	27	—	90
Costs of products sold	—	—	—	—
General and administrative	—	611	786	1,949
Total operating expenses	—	9,420	12,395	31,559
OTHER INCOME (EXPENSE):				
Interest income and other income (expense), net	—	25	—	201
Interest expense	—	—	(50)	—

Intercompany Assets and Liabilities

The following table presents the amounts of assets and liabilities with Safeway as a related party included in the accompanying consolidated balance sheet as of December 28, 2013 (in thousands). As of April 14, 2014, Safeway was no longer a related party, and therefore we no longer separately report assets and liabilities with Safeway as related party transactions.

	December 28, 2013	September 7, 2013
ASSETS		
Overnight cash advances	$—	$9,000
Settlement receivables, net	95,317	18,011
Accounts receivable, net	1,833	2,061
Prepaid expenses and other current assets	8,268	—
Other assets	5,555	4,962
LIABILITIES		
Settlement payables	1,636	2,213
Accounts payable and accrued operating expenses	3,554	484

Cash Management and Treasury Services Agreement and Guarantees

In March 2014, Safeway and we terminated our Cash Management and Treasury Services Agreement (the CMATSA). Under the CMATSA, pursuant to unsecured promissory notes, Safeway borrowed available excess cash from us, and we borrowed from Safeway to meet our working capital and capital expenditure requirements (the Note Payable to Safeway). In conjunction with such termination, on March 28, 2014, we fully repaid amounts outstanding under the Note Payable to Safeway, which totaled $103.1 million.

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As a result of the Spin-Off, Safeway no longer provides guarantees to any of our content providers. We have replaced the Note Payable to Safeway with a credit agreement with a group of banks. See Note 4—Financing.
Pursuant to our second Amended and Restated Tax Sharing Agreement and in exchange for promissory notes issued by us, Safeway provides us funding for Spin-Off taxes that we directly remitted to certain state taxing authorities, which we present as Note payable to Safeway in our accompanying condensed consolidated balance sheets. See Note 7—Income Taxes for additional information.

10. Earnings Per Share

We compute basic earnings per share (EPS) by dividing net income available to common stockholders by the weighted average common shares outstanding during the period and compute diluted EPS by dividing earnings available to common stockholders by the weighted average shares outstanding during the period and the impact of securities that if exercised, would have a dilutive effect on EPS.
We compute EPS under the two-class method, which is a method of computing EPS when an entity has both common stock and participating securities. We consider nonvested stock as a participating security if it contains rights to receive nonforfeitable dividends at the same rate as common stock. Under the two-class method, we exclude the income and distributions attributable to participating securities from the calculation of basic and diluted EPS and exclude the participating securities from the weighted average shares outstanding.
Class A and Class B common stock have equal rights to dividends as declared by the Board. As a result, basic and diluted EPS are equivalent for Class A and Class B common stock.
The following table provides reconciliations of net income and shares used in calculating Basic EPS to those used in calculating Diluted EPS (in thousands except per share amounts):

	12 Weeks Ended September 6, 2014		12 Weeks Ended September 7, 2013	
	Basic	Diluted	Basic	Diluted
Net income attributable to Blackhawk Network Holdings, Inc.	$555	$555	$2,355	$2,355
Distributed and undistributed earnings allocated to participating securities	(1)	(1)	(14)	(14)
Net income attributable to common stockholders	$554	$554	$2,341	$2,341
Weighted-average common shares outstanding	52,609	52,609	51,615	51,615
Common share equivalents		1,695		1,459
Weighted-average shares outstanding		54,304		53,074
Earnings per share– Class A and Class B	$0.01	$0.01	$0.05	$0.04
	36 Weeks Ended September 6, 2014		36 Weeks Ended September 7, 2013	
	Basic	Diluted	Basic	Diluted
Net income attributable to Blackhawk Network Holdings, Inc.	$2,830	$2,830	$4,832	$4,832
Distributed and undistributed earnings allocated to participating securities	(47)	(47)	(153)	(151)
Net income attributable to common stockholders	$2,783	$2,783	$4,679	$4,681
Weighted-average common shares outstanding	52,450	52,450	50,811	50,811
Common share equivalents		1,585		1,171
Weighted-average shares outstanding		54,035		51,982
Earnings per share– Class A and Class B	$0.05	$0.05	$0.09	$0.09

The weighted-average common shares outstanding for diluted EPS excluded approximately 569,000 and 1,806,000 potential common stock outstanding for the 12 weeks ended September 6, 2014 and September 7, 2013, respectively, and 488,000 and 1,573,000 potential common stock outstanding for the 36 weeks ended September 6, 2014 and September 7, 2013 because the effect would have been anti-dilutive. Potential common stock outstanding results in fewer common share equivalents as a result of the treasury stock method.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q (the Quarterly Report) and our Annual Report filed on Form 10-K filed with the Securities and Exchange Commission on March 17, 2014 (the Annual Report). The following discussion has been updated to reflect the effects of the restatement to the 36 weeks ended September 7, 2013 disclosed in Note 1 to our condensed consolidated financial statements. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those discussed below. You should review the "Risk Factors" and "Special Note regarding Forward-Looking Statements" sections of the Annual Report and the "Risk Factors" section of this Quarterly Report for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.

Forward Looking Information

This Quarterly Report contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. The statements contained in this Quarterly Report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). Forward-looking statements are often identified by the use of words such as, but not limited to, "anticipate," "believe," "can," "continue," "could," "estimate," "expect," "inten "plan," "project," "seek," "should," "target," "will," "would" and similar expressions or variations intended to identify forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed or referenced in the section titled "Risk Factors" included under Part II, Item 1A below. Furthermore, such forward-looking statements speak only as of the date of this Quarterly Report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Company Overview

Blackhawk Network Holdings, Inc., together with its subsidiaries (we, us or our) is a leading prepaid payment network utilizing proprietary technology to offer a broad range of prepaid gift, telecom and debit cards, in physical and digital forms, as well as related prepaid products and payment services in the United States and 21 other countries. Our extensive prepaid network provides significant benefits to our key constituents: consumers who purchase or receive the products and services we offer; content providers who offer branded gift cards and other prepaid products that are redeemable for goods and services; distribution partners who sell those products; and business partners that distribute our products as incentives or rewards. For consumers, we provide convenience by offering a broad variety of quality brands and content through retail and online distribution locations or through loyalty, incentive and reward programs offered by our business customers. For our content providers, we drive incremental sales by providing access to millions of consumers and creating new customer relationships. For our retail distribution partners, we provide a significant, high-growth and highly productive product category that drives incremental store traffic and customer loyalty. And for our business partners, we provide a wide array of prepaid products to enhance their customer incentives and employee rewards programs. Our technology platform allows us to efficiently and seamlessly connect our network participants and offer new products and services as payment technologies evolve. We believe the breadth of our distribution network and product content, combined with our consumer reach and technology platform, creates powerful network effects that enhance value for our constituents and drive growth in our business.

Prior to April 14, 2014, we were a majority-owned subsidiary of Safeway Inc. (Safeway). On April 14, 2014, Safeway distributed its remaining 37.8 million shares of our Class B common stock to Safeway stockholders (the Spin-Off). As a result of the Spin-Off, we became a stand-alone entity separate from Safeway.

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Quarterly Results of Operations and Seasonality

Seasonal consumer spending habits, which are most pronounced in December of each year as a result of the holiday selling season, significantly affect our business. We believe this seasonality is important to understanding our quarterly operating results. A significant portion of gift card sales occurs in late December of each year during the holiday selling season. As a result, we earn a significant portion of our revenues, net income and cash flows during the fourth quarter of each year. We also experience an increase in revenues, net income and cash flows during the second quarter of each year, which we primarily attribute to the Mother’s Day, Father’s Day and graduation gifting season and the Easter holiday. Depending on when the Easter holiday occurs, the associated increase could occur in either the first or second quarter. Additionally, operating income may fluctuate significantly during the first three fiscal quarters due to lower revenues and timing of certain expenses during such fiscal periods. As a result, quarterly financial results are not necessarily reflective of the results to be expected for the year, any other interim period or other future year.

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Description of Our Revenues

Commissions and Fees—Commissions and fees consist of content provider commissions, consumer purchase fees, GPR load and reload fees and other transaction-based commissions. We account for total commissions and fees as revenues. The portion of commissions and fees that we pay to our distribution partners is accounted for as Distribution partner commissions in operating expenses.

- Content Provider Commissions—We earn the majority of our revenues from commissions paid by content providers for the marketing and distribution of their prepaid cards, which we refer to as closed loop gift cards. For closed loop gift cards and prepaid telecom cards, our commissions are based on a contractual percentage of the aggregate load value of the cards recognized during a defined period. This contractual percentage is individually negotiated with each content provider and is generally a fixed percentage. After a closed loop gift card or telecom card is activated, we have no further service obligations and recognize the commissions received as revenue at the time of activation.
- Purchase Fees—We generate a portion of our revenue from fees related to open loop gift cards, including our proprietary Visa gift card, American Express and MasterCard network-branded gift cards and GPR cards provided by Green Dot and NetSpend, the industry leaders in this product category, as well as PayPower, our own GPR card. The consumer pays a purchase fee upon activation of a network-branded card or the initial load to the GPR cards. These purchase fees vary based on the type of card purchased and the dollar amount of the load transaction. We serve as the program manager, in conjunction with the issuing banks, for our proprietary Visa gift card and PayPower GPR card and have ongoing customer service obligations after card activation. We recognize revenue for our proprietary Visa gift card purchase fee ratably in proportion to the historical redemption patterns of the card portfolio over the estimated life of the card (currently 12 months), which presently results in the recognition of approximately 90% of the purchase fee within four months of card activation. We recognize the initial load fee on the PayPower GPR card on a straight-line basis over the estimated life of the card (currently four months). For the American Express and MasterCard network-branded gift cards and the Green Dot and NetSpend branded GPR cards, we receive a contractual percentage of the consumer purchase fee, which is recognized as revenue at the time of card activation as we have no future customer service obligations.
- Reload Fees—The consumer pays a purchase fee and we earn the fee when consumers reload funds onto their PayPower GPR card or another GPR card through our Reloadit network. Revenue is recognized when the reload is processed.
- Incentive Program Fees—We receive fees from our business partners for the activation of incentive cards and the overall management of our incentives and rewards business. Incentive cards include Visa and MasterCard network-branded cards, for which we serve as program manager in conjunction with issuing banks, and Discover network-branded cards that we issue. We defer initial program fees for incentive cards ratably over the estimated card life for single use cards (currently nine months) and on a straight-line basis for reloadable cards (currently 24 months), and we recognize fees for reloading cards when the reload is processed. We may grant price concessions to certain business partners for the purchase of incentive cards. Such concessions are presented as a reduction of Commissions and fees revenue. If such concessions exceed the revenues received from the business partner, we present the net amounts in Operating expenses in Distribution partner commissions
- Merchant Commissions—Certain open-loop incentive cards are redeemable only at certain merchants utilizing our proprietary restricted authorization network technology. We receive commissions from such merchants based on a contractual percentage of the amount redeemed. Revenue is recognized when the cardholders make purchases.
- Transaction-Based and Other Fees—We receive transaction-based fees from certain telecom partners related to the use of our proprietary network. These fees vary with usage or volumes and are recognized at the time our network is accessed. We also receive fees for certain services related to our local, regional and sports team card programs such as balance tracking, customer service calls and financial settlement. Revenue is recognized in the period the services are performed.

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Program, Interchange, Marketing and Other Fees—Program, interchange, marketing and other fees consist of post-activation program management fees, settlement network interchange fees, marketing revenues from our content providers, account service fees, fund expiration fees, fund expiration revenues and other fees.

- Post-Activation Program Management Fees—We receive a program management fee from certain of our issuing banks related to our proprietary Visa gift card and certain open-loop incentive cards. This fee is based on a contractually stated percentage of load value and represents a portion of our compensation for the overall management and customer support of our proprietary Visa gift and incentive card programs. The fees are deferred and recognized over the estimated life of the card in proportion to historical redemption patterns. The fee percentages are subject to quarterly adjustment based on changes in the underlying redemption patterns, escheat obligations, regulations and other factors that change the underlying economics of the card portfolio.
- Interchange Fees—We earn payment network fees related to the cardholder's usage of our proprietary Visa gift, PayPower GPR and open loop incentive cards. Merchants are charged at varying rates established by Visa, MasterCard and Discover. These fees are contractually passed through to us by the issuing banks net of any fees paid to Visa or MasterCard, or paid directly to us by Discover for the cards that we issue. We recognize revenues when cardholders make purchases.
- Marketing Revenue—We receive funds from our content providers to promote their prepaid cards throughout our retail distribution partner network. We generally recognize revenue ratably over the period of the related marketing campaign.
- Account Service Fees—We earn a monthly fee and other transaction-based service fees on the PayPower GPR card and earn monthly fees for certain Visa gift and incentive cards, which we charge only after a predetermined amount of time has transpired since card activation. These consumer-paid service fees are collected by reducing card balances and are recognized as revenue at the time the card balance is reduced. For certain incentive cards, we earn these fees only to the extent that the fees exceed post-activation program management fees paid to us for such cards.
- Fund Expiration Revenue—We serve as issuer of Discover network-branded incentive cards and present the cardholder liability in Consumer and Customer Deposits in our consolidated balance sheets. When funds expire, we recognize revenue and derecognize the liability.
- Fund Expiration Fees—We receive fees from our issuing banks for certain Visa gift and Visa and MasterCard incentive cards, based on a contractual percentage of the unredeemed funds when the funds expire. We recognize revenue when the funds expire. For certain incentive cards, we earn these fees only to the extent that the fees exceed post-activation program management fees paid to us for such cards.
- Other Fees—In some instances, we may receive a portion of other fees such as account maintenance, interchange or referral fees for open loop cards and GPR cards other than our proprietary Visa gift card and PayPower GPR card. We also receive fees related to Safeway-branded gift cards and local, regional and sports team card programs. Typically, these fees are recognized when earned and determinable. For one open loop content provider, we receive a fee, under deferred payment terms, based on a percentage of load value and pay the content provider a fee (a portion of which is also under deferred payment terms) for meeting certain activation targets. We recognize the net amount of these fees upon activation.

Product Sales—Product sales consist of our card production sales, secondary card market sales and telecom handset sales.

- Card Production—We provide card design, development and third-party production services for certain content providers that are separate from the standard content provider contract. We outsource the physical card production to a third party and charge the content provider actual cost plus a margin for managing this process. Revenue is recognized when the cards are received by our content providers, at our distribution partners' locations or by us at our third-party warehouse.
- Secondary Card Market—We generate revenue through our wholly owned subsidiary, Cardpool, by acquiring previously owned closed loop gift cards at a discount from the remaining value on the card and then selling them at a mark-up over our costs (but still at a discount to the value on the card) to consumers. Revenue is recognized when the cards are delivered to the purchaser.

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- Telecom Handsets—We earn revenue from the sale of telecom handsets to our distribution partners to facilitate and supplement the sale of our prepaid telecom content providers' airtime cards. Revenue is generally recognized upon handset shipment to or receipt by the distribution partner based upon the shipping terms, net of estimated returns. We may grant price discounts to distribution partners to increase sales of the distribution partners' remaining inventory, which we recognize as a reduction of revenue.

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Description of Our Expenses

Distribution Partner Commissions—Distribution partner commissions represent the amounts paid to members of our distribution partner network for their distribution services related to our content providers' cards and our proprietary Visa gift card and PayPower GPR card. We compensate our distribution partners by paying them a negotiated share of the commission we receive from our content providers or the consumer purchase fee associated with open loop cards. The percentage shared is generally fixed, but may vary based on annual load value per store location. We recognize pricing concessions in excess of revenue from incentive business partners in Distribution partner commission expense. Distribution partner commission expense is recognized upon card activation, except for Visa gift, PayPower GPR and incentive cards where commission expense is capitalized and then amortized based on the same redemption pattern as the related revenue.

Processing and Services—Processing and services costs are the direct costs of generating commissions and fees, and program, interchange, marketing and other fees and include costs of development, integration, maintenance, depreciation and amortization of technology platforms and related hardware; card distribution, fulfillment, merchandising and fixture display amortization; card production for our Visa gift, PayPower GPR and incentive cards and certain other content providers' cards, data communication costs, customer support services, third-party processing, data center facilities costs and compensation costs for processing and services personnel. These costs are expensed as incurred. However, for the Visa gift, incentive and PayPower GPR cards, card production costs and upfront transaction processing fees are capitalized and expensed based on the same redemption pattern as the related revenue. We also incur significant costs to develop new technology platforms and to add functionality to our existing technology platforms. Those costs are capitalized and included in Property, equipment and technology, net and amortized to Processing and services expense over the project's estimated useful life, which is typically five years. Some costs related to operating our technology platform, including certain technology personnel costs and the cost of our in-store displays and merchandising, are fixed in nature, not increasing directly with increasing prepaid product sales, but certain costs will increase based on expected general growth of our business.

Sales and Marketing—We incur costs, both discretionary and contractual, in the form of marketing allowances, direct advertising campaigns, general marketing and trade promotions to promote content providers' prepaid cards and our Visa gift card and PayPower GPR card at our distribution partner locations. Sales and marketing expenses consist of program marketing and advertising costs, distribution partner program development expenses, compensation and travel costs for marketing and sales personnel, communication costs, mark-to-market charges and intangible amortization expense resulting from equity instruments issued to certain distribution partners, facilities costs and outside consulting fees. Additionally, sales and marketing expenses include additional compensation to certain distribution partners for the sale of certain prepaid products, for which we earn revenues included in Program, interchange, marketing and other fees. Program development expenses are generally contractually fixed and do not increase based on volume of prepaid product sales. Other sales and marketing costs do not vary directly with the volume of prepaid product sales, but certain costs will increase based on expected general growth of our business.

Costs of Products Sold—Costs of products sold include the direct costs of card production efforts, the costs to acquire previously issued prepaid cards and other direct costs related to our Cardpool secondary gift card market business and costs to acquire telecom handsets. We may receive pricing concessions from our telecom handset vendors to increase sales of remaining inventory at distribution partners, which we recognize as a reduction of expense and pass onto our distribution partners as a reduction of revenue. Most costs of products sold are variable based on the volume of product sales.

General and Administrative—General and administrative expenses include compensation and benefits for administrative staff, facilities costs, telecommunications costs and professional service fees. These costs do not vary directly with the volume of prepaid product sales, but certain costs will increase based on general growth of our business. General and administrative expenses may also include bad debt and legal expenses, which may cause significant fluctuations from period to period.

Business acquisition expense (benefit) and amortization of acquisition intangibles— Business acquisition expense (benefit) and amortization of acquisition intangibles includes the change in the estimated fair value of the Cardpool contingent consideration liability, amortization of intangible assets acquired in a business acquisition and

acquisition-related costs, such as legal, tax, audit and valuation services.

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Key Operating Statistics

The following table sets forth key operating statistics that directly affect our financial performance for the 12 and 36 weeks ended September 6, 2014 and September 7, 2013:

	12 Weeks Ended		36 Weeks Ended	
	September 6, 2014	September 7, 2013	September 6, 2014	September 7, 2013
	(in thousands, except percentages and average load transaction value)			
Load value	$2,514,561	$1,727,753	$7,321,923	$5,256,978
Commissions and fees as a % of load value	8.0 %	9.2 %	8.1 %	9.1 %
Distribution partner commissions paid as a % of commissions and fees	68.1 %	66.6 %	67.1 %	66.6 %
Number of load transactions	52,380	40,929	154,556	124,375
Average load transaction value	$48.01	$42.21	$47.37	$42.27
Adjusted operating revenues (1)	$130,428	$100,635	$385,963	$297,412
Adjusted EBITDA (1)	$14,714	$11,477	$48,225	$37,361
Adjusted EBITDA margin (1)	11.3 %	11.4 %	12.5 %	12.6 %
Adjusted net income (1)	$4,688	$4,005	$17,693	$14,703
Adjusted diluted earnings per share (1)	$0.09	$0.08	$0.33	$0.28

(1) Our Adjusted operating revenues, EBITDA, Adjusted EBITDA, Adjusted EBITDA margin, Adjusted net income and Adjusted diluted earnings per share are non-GAAP financial measures. Generally, a non-GAAP financial measure is a numerical measure of a company's performance, financial position or cash flow that either excludes or includes amounts that are not normally excluded or included in the most directly comparable measure calculated and presented in accordance with GAAP. These measures, however, should be considered in addition to, and not as a substitute for or superior to, operating revenues, operating income, operating margin, cash flows, or other measures of the financial performance prepared in accordance with GAAP.

Load Value—Represents the total dollar amount of value loaded onto any of our prepaid products during the period. The dollar amount and volume of card sales directly affect the amount of our revenues and direct costs. We measure and monitor Load value by distribution partner channel and content provider program. The significant growth in Load value over the past two years has been driven by increased consumer use of prepaid products, partly in response to distribution partner loyalty and incentive programs, expansion of product content and services we offer, our acquisitions of InteliSpend and Retailo and expansion of selling stores in our distribution partner network in the United States and internationally.

Commissions and Fees as a Percentage of Load Value—Represents the total amount of Commissions and fees recognized during the period as a percentage of Load value for the same period. Commissions as a percentage of load value is generally higher for closed loop and telecom products than the purchase, load and incentive program fees as a percentage of load value for open loop, financial services and incentive products. As a result, overall Commissions and fees as a percentage of load value is directly affected by the mix of Load value among our product offerings. This metric helps us understand and manage overall margins from our product offerings.

Distribution Partner Commissions Paid as a Percentage of Commissions and Fees—Represents Distribution partner commissions expense divided by Commissions and fees revenue during the period. This metric represents the expense recognized for the share of content provider commissions and purchase or load fees we pay to our distribution partners as a percentage of total Commissions and fees revenue recognized during the period. Distribution partner commission share percentages are individually negotiated with our distribution partners and are independent of the commission rates negotiated between us and our content providers. The distribution partner commissions paid percentage is affected by changes in the proportion of Load value and resulting Commissions and fees revenue between distribution partners with differing share percentages.

Number of Load Transactions—Represents the total number of load transactions (including reloads) for all of our prepaid products during the period.
Average Load Transaction Value—Represents Load value divided by the Number of load transactions during the period.

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We regard Adjusted operating revenues, EBITDA, Adjusted EBITDA, Adjusted EBITDA margin, Adjusted net income and Adjusted diluted earnings per share as useful measures of operational and financial performance of the business. We regard Adjusted EBITDA margin as an important financial metric that we use to evaluate the operating efficiency of our business. Adjusted EBITDA, Adjusted net income and Adjusted diluted earnings per share measures are prepared and presented to eliminate the effect of items from EBITDA, Net income and Diluted earnings per share that we do not consider indicative of our core operating performance within the period presented. Adjusted operating revenues are prepared and presented to offset the commissions paid to our distribution partners. Adjusted EBITDA margin represents Adjusted EBITDA as a percentage of Adjusted operating revenues. Our Adjusted operating revenues, Adjusted EBITDA, Adjusted EBITDA margin, Adjusted net income and Adjusted diluted earnings per share may not be comparable to similarly titled measures of other organizations because other organizations may not calculate these measures in the same manner as we do. You are encouraged to evaluate our adjustments and the reasons we consider them appropriate.

We believe Adjusted operating revenues, EBITDA, Adjusted EBITDA, Adjusted EBITDA margin, Adjusted net income and Adjusted diluted earnings per share are useful to evaluate our operating performance for the following reasons:

- adjusting our operating revenues for the issuing bank contract amendment and the commissions paid to our distribution partners is useful to understanding our operating margin;
- EBITDA and Adjusted EBITDA are widely used by investors and securities analysts to measure a company's operating performance without regard to items that can vary substantially from company to company and from period to period depending upon their financing, accounting and tax methods, the book value of their assets, their capital structures and the method by which their assets were acquired;
- Adjusted EBITDA margin provides a measure of operating efficiency based on Adjusted operating revenues and without regard to items that can vary substantially from company to company and from period to period depending upon their financing, accounting and tax methods, the book value of their assets, their capital structures and the method by which their assets were acquired;
- non-cash equity grants made to employees and distribution partners at a certain price and point in time do not necessarily reflect how our business is performing at any particular time and the related expenses are not key measures of our core operating performance;
- the issuing bank contract amendment fee adjustments are necessary to adjust operating revenues, EBITDA and Net income to recognize the revenues from these fees as if the contract amendments had been in place as of the beginning of the fiscal year, which we believe better reflects our core operating performance during those periods;
- intangible asset amortization expenses can vary substantially from company to company and from period to period depending upon the applicable financing and accounting methods, the fair value and average expected life of the acquired intangible assets, the capital structure and the method by which the intangible assets were acquired and, as such, we do not believe that these adjustments are reflective of our core operating performance; and
- non-cash fair value adjustments to contingent business acquisition liability do not directly reflect how our business is performing at any particular time and the related expense adjustment amounts are not key measures of our core operating performance.

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Reconciliation of Non-GAAP Measures:

The following tables present a reconciliation of Total operating revenues to Adjusted operating revenues, a reconciliation of Net income to EBITDA and Adjusted EBITDA, a reconciliation of Operating income margin to Adjusted EBITDA margin, a reconciliation of Net income to Adjusted net income and a reconciliation of Diluted earnings per share to Adjusted diluted earnings per share, in each case reconciling the most comparable GAAP measure to the adjusted measure, for each of the periods indicated.

	12 Weeks Ended		36 Weeks Ended	
	September 6, 2014	September 7, 2013	September 6, 2014	September 7, 2013
	(in thousands, except percentages and per share amounts)			
Adjusted operating revenues:				
Total operating revenues	$269,027	$205,996	$786,086	$616,908
Issuing bank contract amendment fee adjustment (b)	(1,093)	—	—	—
Distribution partner commissions	(137,506)	(105,361)	(400,123)	(319,496)
Adjusted operating revenues	$130,428	$100,635	$385,963	$297,412
Adjusted EBITDA:				
Net income before allocation to non-controlling interests	$413	$2,249	$2,592	$4,513
Interest income and other income (expense), net	(182)	(59)	(126)	(432)
Interest expense	1,080	—	2,081	—
Income tax expense	352	1,544	1,844	5,332
Depreciation and amortization	10,465	6,312	32,153	16,963
EBITDA	12,128	10,046	38,544	26,376
Adjustments to EBITDA:				
Employee stock-based compensation	3,679	1,817	9,769	5,279
Distribution partner mark-to-market expense (a)	—	(34)	(88)	6,961
Issuing bank contract amendment fee adjustment (b)	(1,093)	—	—	—
Change in fair value of contingent consideration (c)	—	(352)	—	(1,255)
Adjusted EBITDA	$14,714	$11,477	$48,225	$37,361
Adjusted EBITDA margin:				
Total operating revenues	$269,027	$205,996	$786,086	$616,908
Operating income	$1,663	$3,734	$6,391	$9,413
Operating margin	0.6%	1.8%	0.8%	1.5%
Adjusted operating revenues	$130,428	$100,635	$385,963	$297,412
Adjusted EBITDA	$14,714	$11,477	$48,225	$37,361
Adjusted EBITDA margin	11.3%	11.4%	12.5%	12.6%
Adjusted net income:				
Income before income tax expense	$765	$3,793	$4,436	$9,845
Employee stock-based compensation	3,679	1,817	9,769	5,279
Distribution partner mark-to-market expense (a)	—	(34)	(88)	6,961
Issuing bank contract amendment fee adjustment (b)	(1,093)	—	—	—
Change in fair value of contingent consideration (c)	—	(352)	—	(1,255)
Amortization of intangibles (d)	4,085	1,206	14,202	2,284
Adjusted income before income tax expense	7,436	6,430	28,319	23,114
Income tax expense	352	1,544	1,844	5,332
Tax expense on adjustments (e)	2,538	987	9,020	3,398
Adjusted income tax expense	2,890	2,531	10,864	8,730
Adjusted net income before allocation to non-controlling interests	4,546	3,899	17,455	14,384

Add: Net loss attributable to non-controlling interests (net of tax)	142	106	238	319
Adjusted net income attributable to Blackhawk Network Holdings, Inc.	$4,688	$4,005	$17,693	$14,703

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	12 Weeks Ended		36 Weeks Ended	
	September 6, 2014	September 7, 2013	September 6, 2014	September 7, 2013
	(in thousands, except percentages and per share amounts)			
Adjusted diluted earnings per share:				
Net income attributable to Blackhawk Network Holdings, Inc.	$555	$2,355	$2,830	$4,832
Distributed and undistributed income allocated to participating securities	(1)	(14)	(47)	(151)
Net income attributable to common shareholders	$554	$2,341	$2,783	$4,681
Diluted weighted-average shares outstanding	54,304	53,074	54,035	51,982
Diluted earnings per share	$0.01	$0.04	$0.05	$0.09
Adjusted net income attributable to Blackhawk Network Holdings, Inc.	$4,688	$4,005	$17,693	$14,703
Adjusted distributed and undistributed income allocated to participating securities	(7)	(24)	(74)	(312)
Adjusted net income attributable to common shareholders	$4,681	$3,981	$17,619	$14,391
Diluted weighted average shares outstanding	54,304	53,074	54,035	51,982
Adjusted diluted earnings per share	$0.09	$0.08	$0.33	$0.28

(a) Distribution partner equity instruments are generally marked to market at each reporting date to fair value until the instrument is vested.

(b) During 2014, we entered into contractual amendments with certain of our issuing banks that substituted a program management fee for account service fees or card expiration fees for certain open-loop gift and incentive cards. A portion of the fees related to cards sold in prior periods. Adjusted operating revenues, Adjusted EBITDA and Adjusted net income for the 12 weeks ended September 6, 2014 have been adjusted to recognized the revenues as if the contract amendment had been in force at the beginning of the fiscal year.

(c) Adjustments to reflect a contingent business acquisition liability at its estimated fair value.

(d) Non-cash expense resulting from the amortization of intangible assets, including the amortization of distribution partner relationships resulting from the issuance of fully vested warrants, recorded in Sales and marketing expense, and the amortization of intangible assets from business acquisitions, recorded in Business acquisition expense (benefit) and amortization of acquisition intangibles.

(e) Assumes our statutory tax rate adjusted for certain amounts that are not deductible for tax purposes.

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Results of Operations

Comparison of the 12 Weeks Ended September 6, 2014 and September 7, 2013
The fiscal periods presented in the accompanying tables below and throughout this Results of Operations section consist of the 12-week periods ended September 6, 2014 and September 7, 2013.
The following table sets forth the revenue and expense amounts as a percentage of total operating revenues by the line items in our condensed consolidated statements of income for the 12 weeks ended September 6, 2014 and September 7, 2013.

	12 Weeks Ended September 6, 2014	% of Total Operating Revenues	12 Weeks Ended September 7, 2013	% of Total Operating Revenues
	(in thousands, except percentages)			
OPERATING REVENUES:				
Commissions and fees	$201,888	75.0 %	$158,270	76.8 %
Program, interchange, marketing and other fees	43,895	16.3 %	25,352	12.3 %
Product sales	23,244	8.6 %	22,374	10.9 %
Total operating revenues	269,027	100.0 %	205,996	100.0 %
OPERATING EXPENSES:				
Distribution partner commissions	137,506	51.1 %	105,361	51.1 %
Processing and services	46,715	17.4 %	34,927	17.0 %
Sales and marketing	41,704	15.5 %	30,486	14.8 %
Costs of products sold	21,946	8.2 %	21,423	10.4 %
General and administrative	16,163	6.0 %	10,320	5.0 %
Business acquisition expense (benefit) and amortization of acquisition intangibles	3,330	1.2 %	(255)	(0.1)%
Total operating expenses	267,364	99.4 %	202,262	98.2 %
OPERATING INCOME	1,663	0.6 %	3,734	1.8 %
OTHER INCOME (EXPENSE):				
Interest income and other income (expense), net	182	0.1 %	59	— %
Interest expense	(1,080)	(0.4)%	—	— %
INCOME BEFORE INCOME TAX EXPENSE	765	0.3 %	3,793	1.8 %
INCOME TAX EXPENSE	352	0.1 %	1,544	0.7 %
NET INCOME BEFORE ALLOCATION TO NON-CONTROLLING INTERESTS	413	0.2 %	2,249	1.1 %
Add: Net loss attributable to non-controlling interests (net of tax)	142	— %	106	— %
NET INCOME ATTRIBUTABLE TO BLACKHAWK	$555	0.2 %	$2,355	1.1 %

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12 Weeks Ended September 6, 2014 and September 7, 2013:

Operating Revenues

The following table sets forth our consolidated operating revenues for the 12 weeks ended September 6, 2014 and September 7, 2013.

	12 Weeks Ended				
	September 6, 2014	September 7, 2013	Change		
	(in thousands, except percentages)				
OPERATING REVENUES:					
Commissions and fees	$201,888	$158,270	$43,618	27.6	%
Program, interchange, marketing and other fees	43,895	25,352	18,543	73.1	%
Product sales	23,244	22,374	870	3.9	%
Total operating revenues	$269,027	$205,996	$63,031	30.6	%

Commissions and Fees

Commissions and fees revenue increased primarily due to a 45.5%, or $786.8 million, increase in Load value, partially offset by a decrease in Commissions and fees as a percentage of load value of 120 basis points, to 8.0% for the 12 weeks ended September 6, 2014 from 9.2% for the 12 weeks ended September 7, 2013. The increase in Load value was primarily due to a 28.0% increase in the Number of load transactions and a 13.7% increase in the Average load transaction value. The increase in Number of load transactions reflects our acquisitions of InteliSpend and Retailo in the fourth quarter of 2013; improved store productivity in certain parts of our distribution network, including significant increases in Japan; the addition of new distribution partners, including our expansion into South Africa; and increases in products sold through our online and digital distribution channels. Increases in open loop, financial services and incentive products sold as a proportion of total Load Value resulted in increased Average load transaction value and decreased Commissions and fees as a percentage of load value as these products generally have higher load values with lower Commissions and fees revenue but generate higher amounts of revenues included in Program, interchange, marketing and other fees. Commissions and fees as a percentage of load value also decreased due to mix of closed loop products sold.

Program, Interchange, Marketing and Other Fees

Program, interchange, marketing and other fees increased primarily due to increases in our program-managed Visa gift and PayPower GPR cards sold, our acquisition of InteliSpend and contract amendments with certain of our issuing banks of our Visa gift cards, which collectively resulted in a 112.7%, or $10.4 million, increase in post-activation program management fees and a 133.5%, or $5.3 million, increase in net interchange fees, card expiration fees and account service fees. Additionally, program, interchange, marketing and other fees increased due to a 12.5%, or $1.3 million, increase in marketing revenues, and a $1.5 million increase in other revenues, primarily from our acquisitions of Incentec and InteliSpend.

Product Sales

Product sales increased primarily due to a 34.5%, or $4.8 million, increase in sales from Cardpool and a 8.3%, or $0.4 million, increase in card production sales, partially offset by a 106.7%, or $4.3 million, decrease in telecom handset and other product sales, primarily the result of vendor-funded pricing discounts which we passed on to our distribution partners to promote the sale of telecom handsets to end consumers.

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Operating Expenses

The following table sets forth our consolidated operating expenses for the 12