

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

**FORM 10-K**

(Mark One)

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

For the fiscal year ended **December 31, 2016**  
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 **001-33264**

**U.S. AUTO PARTS NETWORK, INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**68-0623433**  
(I.R.S. Employer  
Identification No.)

**16941 Keegan Avenue, Carson, CA 90746**  
(Address of Principal Executive Offices) (Zip Code)

**Registrant's Telephone Number, Including Area Code: (310) 735-0085**

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, \$0.001 par value per share	The NASDAQ Stock Market LLC (NASDAQ Global Market)

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

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See the definitions 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

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 Exchange Act Rule 12b-2). Yes  No

The aggregate market value of the common stock held by non-affiliates of the registrant as of July 2, 2016 was approximately \$63.5 million (based on the closing sales price of the registrant's common stock on that date). For the purposes of this calculation, shares owned by officers, directors and 10% stockholders known to the registrant have been deemed to be owned by affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of March 2, 2017, there were 34,556,623 shares of the registrant's common stock outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of our proxy statement for the 2017 Annual Meeting of Stockholders (the "Proxy Statement") are incorporated by reference in Part III hereof. Except with respect to information specifically incorporated by reference in this Form 10-K, the Proxy Statement is not deemed to be filed as a part hereof.

**U.S. AUTO PARTS NETWORK, INC.**  
**ANNUAL REPORT ON FORM 10-K**  
**FOR THE FISCAL YEAR ENDED DECEMBER 31, 2016**

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Unless the context requires otherwise, as used in this report, the terms “U.S. Auto Parts,” the “Company,” “we,” “us” and “our” refer to U.S. Auto Parts Network, Inc. and its subsidiaries. Unless otherwise stated, all amounts are presented in thousands.

U.S. Auto Parts<sup>®</sup>, U.S. Auto Parts Network<sup>™</sup>, AutoMD<sup>®</sup>, AutoMD Insta-Quotes<sup>!®</sup>, Kool-Vue<sup>™</sup>, JC Whitney<sup>®</sup>, and Stylintrucks<sup>™</sup>, amongst others, are our United States trademarks. All other trademarks and trade names appearing in this report are the property of their respective owners.

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## SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

*The statements included in this report, other than statements or characterizations of historical or current fact, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and we intend that such forward-looking statements be subject to the safe harbors created thereby. Any forward-looking statements included herein are based on management's beliefs and assumptions and on information currently available to management. We have attempted to identify forward-looking statements by terms such as "anticipates," "believes," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects," "should," "will," "would", "will likely continue," "will likely result" and variations of these words or similar expressions. These forward-looking statements include, but are not limited to, statements regarding future events, our future operating and financial results, financial expectations, expected growth and strategies, current business indicators, capital needs, financing plans, capital deployment, liquidity, contracts, litigation, product offerings, customers, acquisitions, competition and the status of our facilities. Forward-looking statements, no matter where they occur in this document or in other statements attributable to the Company involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. We discuss many of these risks in greater detail under the heading "Risk Factors" in Part I, Item 1A of this report. Given these uncertainties, you should not place undue reliance on these forward-looking statements. You should read this report and the documents that we reference in this report and have filed as exhibits to the report completely and with the understanding that our actual future results may be materially different from what we expect. Also, forward-looking statements represent our management's beliefs and assumptions only as of the date of this report. Except as required by law, we assume no obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.*

## PART I

### ITEM 1. BUSINESS

#### Overview

We are a leading online provider of automotive aftermarket parts and repair information. Our vision is that vehicle repairs and upgrades are easy and affordable. Our mission is to provide an exceptionally easy experience for our customers. Our mantra is "make it easy for our customers." Our five core values are: customer focus, teamwork, integrity, quality, and continuous improvement.

We have historically operated under two reportable operating segments. The criteria we use to identify operating segments are primarily the nature of the products we sell or services we provide and the consolidated operating results that are regularly reviewed by our chief operating decision maker to assess performance and make operating decisions. The two reportable operating segments we identified are the core auto parts business ("Base USAP") and AutoMD, Inc., an online automotive repair information source which, subsequent to year end, has closed down its *Insta-Quotes!* program described below ("AutoMD").

We principally sell our products, identified as stock keeping units ("SKUs"), to individual consumers through our network of websites and online marketplaces. Our user-friendly websites provide customers with a comprehensive selection of over 1.0 million SKUs with detailed product descriptions, attributes and photographs. We have developed a proprietary product database that maps our SKUs to product applications based on vehicle makes, models and years.

Our online sales channel and relationships with suppliers enable us to eliminate intermediaries in the traditional auto parts supply chain and to offer a broader selection of SKUs than can easily be offered by offline competition.

We were incorporated in California in 1995 as a distributor of aftermarket auto parts and launched our first website in 2000. We reincorporated in Delaware in 2006 and expanded our online operations, increasing the number of SKUs sold through our e-commerce network, adding additional websites, improving our internet marketing proficiency, and commencing sales on online marketplaces. Like most e-commerce retailers, our success depends on our ability to attract online consumers to our websites and convert them into customers in a cost-effective manner. Historically, marketing through search engine optimization provided the most efficient opportunity to reach online auto part buyers. In order to improve our business, we worked towards enhancing the process of consolidation and implementing improvements to our multiple websites in order to improve our search ranking through the increased use of paid search advertising and pursued opportunities in third-party online

marketplaces. Our efforts to improve the website purchase experience for our online customers have included our efforts to: (1) help our customers find the parts they want to buy through a customized and guided shopping experience specific to key part names; (2) increase order size across our sites through improved recommendation engines; and (3) provide leading customer service and product support.

We intend to continue to implement strategies designed to build and increase our customer lifetime value by focusing on increasing gross profit per transaction, transaction attachment rate, repeat purchases and conversion.

In October 2008, we acquired AutoMD for the purpose of developing content and a user community to educate consumers on maintenance and service of their vehicles. The AutoMD.com site provides auto information, with tools for diagnosing car troubles, locating repair shops, estimating the cost of repairs, accessing recalls and technical service bulletins, reading do-it-yourself (“DIY”) repair guides, and getting questions answered in the automotive enthusiast community forum. In 2013, AutoMD launched its *Insta-Quotes!* program which used real time data to estimate auto repair costs for consumers, and in 2014, we sold a non-controlling interest in AutoMD to outside investors and certain of our existing shareholders. In the first quarter of 2017, AutoMD repurchased the non-controlling interests and closed down the *Insta-Quotes!* program. Following the redemptions, AutoMD filed for dissolution and all of the remaining assets of AutoMD will be distributed to the Company except for certain cash reserved for creditors of AutoMD. We intend to utilize the AutoMD assets as part our media business going forward.

In August 2010, we acquired all of the issued and outstanding shares of Automotive Specialty Accessories and Parts, Inc. and its wholly-owned subsidiary Whitney Automotive Group, Inc. (referred to herein as “WAG”), at the time, the nation’s leading catalog and internet direct marketer of automotive aftermarket performance parts and accessories. The acquisition of WAG allowed us to expand of our product line, which increased our ability to reach customers in the DIY automobile and off-road accessories market.

Our flagship websites are located at [www.autopartswarehouse.com](http://www.autopartswarehouse.com), [www.carparts.com](http://www.carparts.com), [www.jcwhitney.com](http://www.jcwhitney.com) and [www.AutoMD.com](http://www.AutoMD.com) and our corporate website is located at [www.usautoparts.net](http://www.usautoparts.net).

We report on a 52/53-week fiscal year, ending on the Saturday nearest the end of December. References to 2016 and 2015 relate to the 52-week fiscal years ended December 31, 2016 and January 2, 2016. References to 2014 relate to the 53-week fiscal year ended January 3, 2015.

## **Our Products**

We offer a broad selection of aftermarket auto parts. We continually refine our product offering by introducing new brands and parts categories, while discontinuing low-selling brands and SKUs. We broadly classify our products into three subcategories by function: collision parts serving the body repair segment, engine parts to serve the replacement/wear parts market and performance parts and accessories.

*Collision Parts.* The collision parts category is primarily comprised of parts for the exterior of an automobile. Our parts in this category are typically replacement parts for original body parts that have been damaged as a result of a collision or through general wear and tear. The majority of these products are sold through our websites. In addition, we sell an extensive line of mirror products, including our own private-label brand called Kool-Vue™, which are marketed and sold as aftermarket replacement parts and as upgrades to existing parts.

*Engine Parts.* The engine parts category is comprised of engine and chassis components as well as other mechanical and electrical parts. These parts serve as replacement parts for existing engine parts and are generally used by professionals and do-it-yourselfers for engine and mechanical maintenance and repair.

*Performance Parts and Accessories.* We offer performance versions of many parts sold in each of the above categories. Performance parts and accessories generally consist of parts that enhance the performance of the automobile, upgrade existing functionality of a specific part or improve the physical appearance or comfort of the automobile.

## **Our Sales Channels**

Our sales channels include the online channel and the offline channel.

*Online Sales Channel.* Our online sales channel consists of our e-commerce websites, online marketplaces and online advertising. Our e-commerce channel includes a network of e-commerce websites, supported by our call-center sales agents. We also sell our products through online marketplaces, including third-party auction sites and shopping portals, which provide us with access to additional consumer segments. The majority of our online sales are to individual consumers. We sell online advertising and sponsorship positions on our e-commerce websites to highlight vendor brands and offer complementary

products and services that benefit our customers. Advertising is targeted to specific sections of the websites and can also be targeted to specific users based on the vehicles they drive. Advertising partners primarily include part vendors, national automotive aftermarket brands, and automobile manufacturers.

*Offline Sales Channel.* We sell and deliver to collision repair shops from our Chesapeake, Virginia warehouse facility. We also market our Kool-Vue™ products nationwide to auto parts wholesale distributors and serve consumers by operating a retail outlet store in LaSalle, Illinois.

## **Our Fulfillment Operations**

We fulfill customer orders using two primary methods: (1) stock-and-ship, where we take physical delivery of merchandise and store it in one of our distribution centers until it is shipped to a customer, and (2) drop-ship, where merchandise is shipped directly to customers from our suppliers. We believe that the flexibility of fulfilling orders using two different fulfillment methods allows us to offer a broader product selection, helps optimize product inventory and enhances our overall business profitability.

*Stock-and-Ship Fulfillment.* Our stock-and-ship products are sourced primarily from manufacturers and other suppliers located in Asia and in the U.S. and are stored in one of our distribution centers in Chesapeake, Virginia or LaSalle, Illinois. All products received into our distribution centers are entered into our inventory management systems, allowing us to closely monitor inventory availability. We consider a number of factors in determining which items to stock in our distribution centers, including which products can be purchased at a meaningful discount to domestic prices for similar items, which products have historically sold in high volumes, and which products may be out of stock when we attempt to fulfill via drop-ship.

*Drop-Ship Fulfillment.* We have developed relationships with several U.S.-based automobile parts distributors that operate their own distribution centers and can deliver products directly to our customers. We internally developed a proprietary distributor selection system, Auto-Vend™, which allows us to electronically select multiple vendors for a given order. Auto-Vend™ will attempt to first direct an order to one of our warehouses. If the product is not in stock, Auto-Vend™ will process the order to the next appropriate vendor based on customer location, cost, contractual agreements, and service level history.

## **Suppliers**

We source our products from two primary regions: (1) our private label product sourced primarily through manufacturers and distributors in the Asia-Pacific region, and (2) our branded product sourced primarily through drop-ship manufacturers and distributors located in the United States.

*Private Label Product.* Our private label suppliers offer products which are generally less expensive and we believe provide better value for our consumers. As a result, our mix shift towards private label product has continued to increase on a year-over-year basis. We stock-and-ship our private label products in our distribution centers. We currently have over 55,000 private label SKUs in our product selection.

*Branded Product.* We have developed and implemented application programming interfaces with the majority of our branded, drop ship suppliers that allow us to electronically transmit orders, check inventory availability, and receive the shipment tracking information which is easily passed on to our customers. We are a significant customer for many of our drop-ship vendors and have long standing relationships and contracts with many of these suppliers. For the fiscal year ended December 31, 2016, three of our drop-ship vendors accounted for approximately 9% of our total product purchases. We currently have over 1.0 million branded SKUs in our product selection.

## **Marketing**

Our online marketing efforts are designed to attract visitors to our websites, convert visitors into purchasing customers and encourage repeat purchases among our existing customer base. We use a variety of marketing methods, including online marketing methods to attract visitors, which include paid search advertising, search engine optimization, affiliate programs, e-mail marketing, print catalogues and inclusion in online shopping engines. To convert visitors into paying customers, we periodically run promotions for discounted products. We seek to create cross-selling opportunities by displaying complementary and related products available for sale throughout the purchasing process. We utilize several marketing techniques, including targeted e-mails about specific vehicle promotions, to increase customer awareness of our products.

## **International Operations**

In April 2007, we established offshore operations in the Philippines. Our offshore operations allow us to access a workforce with the necessary technical skills at a significantly lower cost than comparably experienced U.S.-based professionals. Our offshore operations are responsible for a majority of our website development, catalog management, and back office support. Our offshore operations also house our main call center. We had 748 employees in the Philippines as of December 31, 2016. In addition to our operations in the Philippines, we have a Canadian subsidiary; the subsidiary currently has no operations or employees. We primarily source our private label product from suppliers in the Asia-Pacific region.

## **Competition**

The auto repair information and parts industry is competitive and highly fragmented, with products distributed through multi-tiered and overlapping channels. We compete with both online and offline retailers who offer original equipment manufacturer (“OEM”), aftermarket and private label parts to either the DIY or do-it-for-me (“DIFM”) customer segments. Current or potential competitors include the following:

- national auto parts retailers such as Advance Auto Parts, AutoZone, Napa Auto Parts, CarQuest, O’Reilly Automotive and Pep Boys;
- large online marketplaces such as Amazon.com and sellers on eBay;
- other online retailers of automotive products and auto repair information websites;
- local independent retailers or niche auto parts retailers;
- wholesale aftermarket auto parts distributors such as LKQ Corporation; and
- manufacturers, brand suppliers and other distributors selling online directly to consumers.

We believe the principal competitive factors in our market are helping customers easily find their parts, educating consumers on the service and maintenance of their vehicles, maintaining a proprietary product catalog that maps individual parts to relevant vehicle applications, broad product selection and availability, price, knowledgeable customer service, rapid order fulfillment and delivery, and easy product returns. We believe we compete favorably on the basis of these factors. However, some of our competitors may be larger, may have stronger brand recognition or may have access to greater financial, technical and marketing resources or may have been operating longer than we have.

## **Government Regulation**

We are subject to federal and state consumer protection laws, including laws protecting the privacy of customer non-public information and the handling of customer complaints and regulations prohibiting unfair and deceptive trade practices. The growth and demand for online commerce has and may continue to result in more stringent consumer protection laws that impose additional compliance burdens on online companies. These laws may cover issues such as user privacy, spyware and the tracking of consumer activities, marketing e-mails and communications, other advertising and promotional practices, money transfers, pricing, product safety, content and quality of products and services, taxation, electronic contracts and other communications and information security. In addition, most states have passed laws that prohibit or limit the use of aftermarket auto parts in collision repair work and/or require enhanced disclosure or vehicle owner consent before using aftermarket auto parts in such repair work and additional legislation of this kind may be introduced in the future.

There is also great uncertainty over whether or how existing laws governing issues such as sales and other taxes, auctions, libel and personal privacy apply to the Internet and commercial online services. These issues may take years to resolve. For example, tax authorities in a number of states, as well as a Congressional advisory commission, are currently reviewing the appropriate tax treatment of companies engaged in online commerce, and new state tax regulations may subject us to additional state sales and income taxes. New legislation or regulation, the application of laws and regulations from jurisdictions whose laws do not currently apply to our business or the application of existing laws and regulations to the Internet and commercial online services could result in significant additional taxes or regulatory restrictions on our business. These taxes or restrictions could have an adverse effect on our cash flows and results of operations. Furthermore, there is a possibility that we may be subject to significant fines or other payments for any past failures to comply with these requirements.

## **Seasonality**

We believe our business is subject to seasonal fluctuations. We have historically experienced higher sales of body parts in winter months when inclement weather and hazardous road conditions typically result in more automobile collisions. Engine parts and performance parts and accessories have historically experienced higher sales in the summer months when consumers

have more time to undertake elective projects to maintain and enhance the performance of their automobiles and the warmer weather during that time is conducive for such projects. We expect the historical seasonality trends to continue, and such trends may have a material impact on our financial condition and results of operations in subsequent periods.

## **Employees**

As of December 31, 2016, we had 332 employees in the United States and 748 employees in the Philippines for a total of 1,080 employees. None of our employees are represented by a labor union, and we have never experienced a work stoppage.

## **Available Information**

Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports are available free of charge on the Investor Relations section of our corporate website located at [www.usautoparts.net](http://www.usautoparts.net) as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the Securities and Exchange Commission ("SEC"). The inclusion of our website address in this report does not include or incorporate by reference into this report any information on our website.

## **ITEM 1A. RISK FACTORS**

*Our business is subject to a number of risks which are discussed below. Other risks are presented elsewhere in this report and in our other filings with the SEC. You should consider carefully the following risks in addition to the other information contained in this report and our other filings with the SEC, including our subsequent reports on Forms 10-Q and 8-K, and any amendments thereto, before deciding to buy, sell or hold our common stock. If any of the following known or unknown risks or uncertainties actually occurs with material adverse effects on us, our business, financial condition, results of operations and/or liquidity could be seriously harmed. In that event, the market price for our common stock will likely decline and you may lose all or part of your investment.*

### **Risks Related To Our Business**

***Purchasers of aftermarket auto parts may not choose to shop online, which would prevent us from acquiring new customers who are necessary to the growth of our business.***

The online market for aftermarket auto parts is less developed than the online market for many other business and consumer products, and currently represents only a small part of the overall aftermarket auto parts market. Our success will depend in part on our ability to attract new customers and to convert customers who have historically purchased auto parts through traditional retail and wholesale operations. Specific factors that could discourage or prevent prospective customers from purchasing from us include:

- concerns about buying auto parts without face-to-face interaction with sales personnel;
- the inability to physically handle, examine and compare products;
- delivery time associated with Internet orders;
- concerns about the security of online transactions and the privacy of personal information;
- delayed shipments or shipments of incorrect or damaged products;
- increased shipping costs;  
and
- the inconvenience associated with returning or exchanging items purchased online.

If the online market for auto parts does not gain widespread acceptance, our sales may decline and our business and financial results may suffer.

***We depend on search engines and other online sources to attract visitors to our websites, and if we are unable to attract these visitors and convert them into customers in a cost-effective manner, our business and results of operations will be harmed.***

Our success depends on our ability to attract online consumers to our websites and convert them into customers in a cost-effective manner. We are significantly dependent upon search engines, shopping comparison sites and other online sources for our website traffic. We are included in search results as a result of both paid search listings, where we purchase specific search terms that will result in the inclusion of our listing, and algorithmic searches that depend upon the searchable content on our sites.

Algorithmic listings cannot be purchased and instead are determined and displayed solely by a set of formulas utilized by the search engine. Search engines, shopping comparison sites and other online sources have in the past, and will continue to revise their algorithms from time to time in an attempt to optimize their search results. For example, search engines, like Google, revise their algorithms regularly in an attempt to optimize their search results. During the past few years, we have been negatively impacted by the changes in methodology for how Google displayed or selected our different websites for customer search results, which has reduced our unique visitor count and adversely affected our financial results. We continue to address these ongoing challenges, and during fiscal 2016 our unique visitor count increased by 1.2 million, or 1.0%, to 117.9 million unique visitors compared to 116.7 million unique visitors in 2015 primarily due to an increase in paid traffic, partially offset by a decrease in organic traffic. While we have been able to offset the decrease in our organic traffic through increases in paid search traffic, there is no guarantee we will be able to continue to increase our paid traffic at the same levels in the future. In addition, if other search engines, shopping comparison sites or similar online sources on which we rely for website traffic were to modify their general methodology for how they display or select our websites in a manner similar to the changes made by Google, or if Google continues to make changes to its search results ranking algorithms that cause those algorithms to interact with our platform in a manner that continues to reduce our unique visitors count, fewer consumers may click through to our websites, and our financial results could be further adversely affected.

Similarly, if any free search engine or shopping comparison site on which we rely begins charging fees for listing or placement, or if one or more of the search engines, shopping comparison sites and other online sources on which we rely for purchased listings, increases their fees, modifies or terminates its relationship with us, our expenses could rise, we could lose customers and traffic to our websites could decrease.

***Shifting online consumer behavior for purchasers of aftermarket auto parts may shift from desktop based to mobile device based online shopping, which could impact the growth of our business and our financial results could suffer.***

Mobile device based online shopping represents an increasing part of our business. Shifting consumer behavior indicates that our customers may become more inclined to shop for aftermarket auto parts through their mobile devices. Mobile customers exhibit different behaviors than our more traditional desktop based e-commerce customers. User sophistication and technological advances have increased consumer expectations around the user experience on mobile devices, including speed of response, functionality, product availability, security, and ease of use. If we are unable to continue to adapt our mobile device shopping experience from desktop based online shopping in ways that improve our customer's mobile experience and increase the engagement of our mobile customers our sales may decline and our business and financial results may suffer.

***During fiscal 2016, we recorded net income, but we have a history of net losses which could continue in fiscal year 2017.***

During fiscal 2016, we achieved net income of \$731, compared to a net loss of \$1,281 for fiscal 2015. While we achieved net income during fiscal 2016, if our prior net losses continue in fiscal year 2017 they could severely impact our liquidity, as we may not be able to provide positive cash flows from operations in order to meet our working capital requirements. We may need to borrow additional funds from our credit facility, which under certain circumstances may not be available, sell additional assets or seek additional equity or additional debt financing in the future. In such case, there can be no assurance that we would be able to raise such additional financing or engage in such asset sales on acceptable terms, or at all. If the net losses we have experienced in previous years occur in the future for longer than we expect because our strategies to return to positive sales growth and profitability are not successful, and if we are not able to raise adequate additional financing or proceeds from asset sales to continue to fund our ongoing operations, we will need to defer, reduce or eliminate significant planned expenditures, restructure or significantly curtail our operations, file for bankruptcy or cease operations.

***Our operations are restricted by our credit agreement, and our ability to borrow funds under our credit facility is subject to a borrowing base.***

We maintain an asset-based revolving credit facility with JPMorgan Chase Bank, N.A. (the "Credit Agreement") that provides for, among other things, a revolving commitment in an aggregate principal amount of up to \$30 million subject to a borrowing base derived from certain of our receivables, inventory and property and equipment. Our Credit Agreement includes a number of restrictive covenants. These covenants could impair our financing and operational flexibility and make it difficult for us to react to market conditions and satisfy our ongoing capital needs and unanticipated cash requirements. Specifically, such covenants restrict our ability and, if applicable, the ability of our subsidiaries to, among other things:

- incur additional debt;
- make certain investments and acquisitions;
- enter into certain types of transactions with affiliates;
- use assets as security in other transactions;



- pay dividends on our capital stock or repurchase our equity interests, excluding payments of preferred stock dividends which are specifically permitted under our credit facility;
- sell certain assets or merge with or into other companies;
- guarantee the debts of others;
- enter into new lines of business;
- pay or amend our subordinated debt; and
- form any joint ventures or subsidiary investments.

In addition, our credit facility is subject to a borrowing base derived from certain of our receivables, inventory, property and equipment. In the event that components of the borrowing base are adversely affected for any reason, including adverse market conditions or downturns in general economic conditions, we could be restricted in the amount of funds we can borrow under the credit facility. Furthermore, in the event that components of the borrowing base decrease to a level below the amount of loans then-outstanding under the credit facility, we could be required to immediately repay loans to the extent of such shortfall. If any of these events were to occur, it could severely impact our liquidity and capital resources, limit our ability to operate our business and could have a material adverse effect on our financial condition and results of operations.

Under certain circumstances, our credit facility may also require us to satisfy a financial covenant, which could limit our ability to react to market conditions or satisfy extraordinary capital needs and could otherwise impact our liquidity and capital resources, restrict our financing and have a material adverse effect on our results of operations.

Our ability to comply with the covenants and other terms of our debt obligations will depend on our future operating performance. If we fail to comply with such covenants and terms, we would be required to obtain waivers from our lenders to maintain compliance with our debt obligations. In the future, if we are unable to obtain any necessary waivers and our debt is accelerated, a material adverse effect on our financial condition and future operating performance would result.

While we did not have any outstanding indebtedness under our Credit Agreement as of the end of fiscal 2016, we may have outstanding indebtedness in the future. Any outstanding indebtedness would have important consequences, including the following:

- we would have to dedicate a portion of our cash flow to making payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures, acquisitions or other general corporate purposes;
- certain levels of indebtedness may make us less attractive to potential acquirers or acquisition targets;
- certain levels of indebtedness may limit our flexibility to adjust to changing business and market conditions, and make us more vulnerable to downturns in general economic conditions as compared to competitors that may be less leveraged; and
- as described in more detail above, the documents providing for our indebtedness contain restrictive covenants that may limit our financing and operational flexibility.

Furthermore, our ability to satisfy our debt service obligations depends, among other things, upon fluctuations in interest rates, our future operating performance and ability to refinance indebtedness when and if necessary. These factors depend partly on economic, financial, competitive and other factors beyond our control. We may not be able to generate sufficient cash from operations to meet our debt service obligations as well as fund necessary capital expenditures and general operating expenses. In addition, if we need to refinance our debt, or obtain additional debt financing or sell assets or equity to satisfy our debt service obligations, we may not be able to do so on commercially reasonable terms, if at all. If this were to occur, we may need to defer, reduce or eliminate significant planned expenditures, restructure or significantly curtail our operations, file for bankruptcy or cease operations.

***We face exposure to product liability lawsuits.***

The automotive industry in general has been subject to a large number of product liability claims due to the nature of personal injuries that result from car accidents or malfunctions. As a distributor of auto parts, including parts obtained overseas, we could be held liable for the injury or damage caused if the products we sell are defective or malfunction regardless of whether the product manufacturer is the party at fault. While we carry insurance against product liability claims, if the damages in any given action were high or we were subject to multiple lawsuits, the damages and costs could exceed the limits of our insurance coverage or prevent us from obtaining coverage in the future. If we were required to pay substantial damages as a result of these lawsuits, it may seriously harm our business and financial condition. Even defending against unsuccessful claims could cause us to incur significant expenses and result in a diversion of management's attention. In addition, even if the money

damages themselves did not cause substantial harm to our business, the damage to our reputation and the brands offered on our websites could adversely affect our future reputation and our brand, and could result in a decline in our net sales and profitability.

***If our assets become impaired we may be required to record a significant charge to earnings.***

We review our long-lived assets for impairment annually, or when events or changes in circumstances indicate the carrying value may not be recoverable. Factors that may be considered are changes in circumstances indicating that the carrying value of our assets may not be recoverable include a decrease in future cash flows. For fiscal 2016, we recorded a non-cash impairment charge of \$1,130 relating to the impairment of certain AutoMD software. We may be required to record a significant charge to earnings in our financial statements during the period in which any impairment of our assets is determined, resulting in an impact on our results of operations.

***We are highly dependent upon key suppliers.***

Our top ten suppliers represented approximately 44% of our total product purchases during fiscal 2016. Our ability to acquire products from our suppliers in amounts and on terms acceptable to us is dependent upon a number of factors that could affect our suppliers and which are beyond our control. For example, financial or operational difficulties that some of our suppliers may face could result in an increase in the cost of the products we purchase from them. If we do not maintain our relationships with our existing suppliers or develop relationships with new suppliers on acceptable commercial terms, we may not be able to continue to offer a broad selection of merchandise at competitive prices and, as a result, we could lose customers and our sales could decline.

For a number of the products that we sell, we outsource the distribution and fulfillment operation and are dependent on certain drop-ship suppliers to manage inventory, process orders and distribute those products to our customers in a timely manner. For fiscal 2016, our product purchases from three drop-ship suppliers represented approximately 9% of our total product purchases. Because we outsource to suppliers a number of these traditional retail functions relating to those products, we have limited control over how and when orders are fulfilled. We also have limited control over the products that our suppliers purchase or keep in stock. Our suppliers may not accurately forecast the products that will be in high demand or they may allocate popular products to other resellers, resulting in the unavailability of certain products for delivery to our customers. Any inability to offer a broad array of products at competitive prices and any failure to deliver those products to our customers in a timely and accurate manner may damage our reputation and brand and could cause us to lose customers and our sales could decline.

In addition, the increasing consolidation among auto parts suppliers may disrupt or end our relationship with some suppliers, result in product shortages and/or lead to less competition and, consequently, higher prices. Furthermore, as part of our routine business, suppliers extend credit to us in connection with our purchase of their products. In the future, our suppliers may limit the amount of credit they are willing to extend to us in connection with our purchase of their products. If this were to occur, it could impair our ability to acquire the types and quantities of products that we desire from the applicable suppliers on acceptable terms, severely impact our liquidity and capital resources, limit our ability to operate our business and could have a material adverse effect on our financial condition and results of operations.

***We are dependent upon relationships with suppliers in Taiwan and China for the majority of our products.***

We acquire a majority of our products from manufacturers and distributors located in Taiwan and China. We do not have any long-term contracts or exclusive agreements with our foreign suppliers that would ensure our ability to acquire the types and quantities of products we desire at acceptable prices and in a timely manner or that would allow us to rely on customary indemnification protection with respect to any third party claims similar to some of our U.S. suppliers.

In addition, because many of our suppliers are outside of the United States, additional factors could interrupt our relationships or affect our ability to acquire the necessary products on acceptable terms, including:

- political, social and economic instability and the risk of war or other international incidents in Asia or abroad;
- fluctuations in foreign currency exchange rates that may increase our cost of products;
- tariffs and protectionist laws and business practices that favor local businesses;
- difficulties in complying with import and export laws, regulatory requirements and restrictions;
- natural disasters and public health emergencies;
- import shipping delays resulting from foreign or domestic labor shortages, slow downs, or stoppage; and

- the failure of local laws to provide a sufficient degree of protection against infringement of our intellectual property.

From time to time, we may also have to resort to administrative and court proceedings to enforce our legal rights with foreign suppliers. However, it may be more difficult to evaluate the level of legal protection we enjoy in Taiwan and China and the corresponding outcome of any administrative or court proceedings than in comparison to our suppliers in the United States.

***We depend on third-party delivery services to deliver our products to our customers on a timely and consistent basis, and any deterioration in our relationship with any one of these third parties or increases in the fees that they charge could harm our reputation and adversely affect our business and financial condition.***

We rely on third parties for the shipment of our products and we cannot be sure that these relationships will continue on terms favorable to us, or at all. Shipping costs have increased from time to time, and may continue to increase, and we may not be able to pass these costs directly to our customers. These increased shipping costs could harm our business, prospects, financial condition and results of operations by increasing our costs of doing business and reducing gross margins which could negatively affect our operating results. In particular, we utilize a variety of shipping methods for both inbound and outbound logistics. For inbound logistics, we rely on trucking and ocean carriers and any increases in fees that they charge could adversely affect our business and financial condition. For outbound logistics, we rely on “Less-than-Truckload” (“LTL”) and parcel freight based upon the product and quantities being shipped and customer delivery requirements. Any increases in fees or any increased use of LTL would increase our shipping costs which could negatively affect our operating results.

In addition, if our relationships with these third parties are terminated or impaired, or if these third parties are unable to deliver products for us, whether due to labor shortage, slow down or stoppage, deteriorating financial or business condition, responses to terrorist attacks or for any other reason, we would be required to use alternative carriers for the shipment of products to our customers. Changing carriers could have a negative effect on our business and operating results due to reduced visibility of order status and package tracking and delays in order processing and product delivery, and we may be unable to engage alternative carriers on a timely basis, upon terms favorable to us, or at all.

***If commodity prices such as fuel, plastic and steel increase, our margins may reduce.***

Our third party delivery services have increased fuel surcharges from time to time, and such increases negatively impact our margins, as we are generally unable to pass all of these costs directly to consumers. Increasing prices in the component materials for the parts we sell may impact the availability, the quality and the price of our products, as suppliers search for alternatives to existing materials and increase the prices they charge. We cannot ensure that we can recover all the increased costs through price increases, and our suppliers may not continue to provide the consistent quality of product as they may substitute lower cost materials to maintain pricing levels, all of which may have a negative impact on our business and results of operations.

***If we are unable to manage the challenges associated with our international operations, the growth of our business could be limited and our business could suffer.***

We maintain international business operations in the Philippines. This international operation includes development and maintenance of our websites, our main call center, and sales and back office support services. We are subject to a number of risks and challenges that specifically relate to our international operations. Our international operations may not be successful if we are unable to meet and overcome these challenges, which could limit the growth of our business and may have an adverse effect on our business and operating results. These risks and challenges include:

- difficulties and costs of staffing and managing foreign operations, including any impairment to our relationship with employees caused by a reduction in force;
- restrictions imposed by local labor practices and laws on our business and operations;
- exposure to different business practices and legal standards;
- unexpected changes in regulatory requirements;
- the imposition of government controls and restrictions;
- political, social and economic instability and the risk of war, terrorist activities or other international incidents;
- the failure of telecommunications and connectivity infrastructure;
- natural disasters and public health emergencies;
- potentially adverse tax consequences;  
and



- fluctuations in foreign currency exchange rates and relative weakness in the U.S. dollar.

***If our fulfillment operations are interrupted for any significant period of time or are not sufficient to accommodate increased demand, our sales could decline and our reputation could be harmed.***

Our success depends on our ability to successfully receive and fulfill orders and to promptly deliver our products to our customers. The majority of orders for our auto collision parts products are filled from our inventory in our distribution centers, where all our inventory management, packaging, labeling and product return processes are performed. Increased demand and other considerations may require us to expand our distribution centers or transfer our fulfillment operations to larger or other facilities in the future. If we do not successfully expand our fulfillment capabilities in response to increases in demand, our sales could decline.

In addition, our distribution centers are susceptible to damage or interruption from human error, fire, flood, power loss, telecommunications failures, terrorist attacks, acts of war, break-ins, earthquakes and similar events. We do not currently maintain back-up power systems at our fulfillment centers. We do not presently have a formal disaster recovery plan and our business interruption insurance may be insufficient to compensate us for losses that may occur in the event operations at our fulfillment center are interrupted. In addition, alternative arrangements may not be available, or if they are available, may increase the cost of fulfillment. Any interruptions in our fulfillment operations for any significant period of time, including interruptions resulting from the expansion of our existing facilities or the transfer of operations to a new facility, could damage our reputation and brand and substantially harm our business and results of operations.

***We rely on bandwidth and data center providers and other third parties to provide products to our customers, and any failure or interruption in the services provided by these third parties could disrupt our business and cause us to lose customers.***

We rely on third-party vendors, including data center and bandwidth providers. Any disruption in the network access or co-location services, which are the services that house and provide Internet access to our servers, provided by these third-party providers or any failure of these third-party providers to handle current or higher volumes of use could significantly harm our business. Any financial or other difficulties our providers face may have negative effects on our business, the nature and extent of which we cannot predict. We exercise little control over these third-party vendors, which increases our vulnerability to problems with the services they provide. We also license technology and related databases from third parties to facilitate elements of our e-commerce platform. We have experienced and expect to continue to experience interruptions and delays in service and availability for these elements. Any errors, failures, interruptions or delays experienced in connection with these third-party technologies could negatively impact our relationship with our customers and adversely affect our business. Our systems also heavily depend on the availability of electricity, which also comes from third-party providers. If we were to experience a major power outage, we would have to rely on back-up generators. These back-up generators may not operate properly through a major power outage, and their fuel supply could also be inadequate during a major power outage. Information systems such as ours may be disrupted by even brief power outages, or by the fluctuations in power resulting from switches to and from backup generators. This could disrupt our business and cause us to lose customers.

***Security threats to our IT infrastructure could expose us to liability, and damage our reputation and business***

It is essential to our business strategy that our technology and network infrastructure remain secure and is perceived by our customers to be secure. Despite security measures, however, any network infrastructure may be vulnerable to cyber-attacks by hackers and other security threats. As a leading online source for automotive aftermarket parts and repair information, we may face cyber-attacks that attempt to penetrate our network security, including our data centers, to sabotage or otherwise disable our network of websites and online marketplaces, misappropriate our or our customers' proprietary information, which may include personally identifiable information, or cause interruptions of our internal systems and services. If successful, any of these attacks could negatively affect our reputation, damage our network infrastructure and our ability to sell our products, harm our relationship with customers that are affected and expose us to financial liability.

In addition, any failure by us to comply with applicable privacy and information security laws and regulations could cause us to incur significant costs to protect any customers whose personal data was compromised and to restore customer confidence in us and to make changes to our information systems and administrative processes to address security issues and compliance with applicable laws and regulations. In addition, our customers could lose confidence in our ability to protect their personal information, which could cause them to stop shopping on our sites altogether. Such events could lead to lost sales and adversely affect our results of operations. We also could be exposed to government enforcement actions and private litigation.

Moreover, we are subject to the Payment Card Industry Data Security Standard ("PCI DSS"), issued by the PCI Council. PCI DSS contains compliance guidelines and standards with regard to our security surrounding the physical and electronic storage, processing and transmission of individual cardholder data. We cannot be certain that all of our information technology

systems are able to prevent, contain or detect any cyber-attacks, cyber terrorism, or security breaches from known malware or malware that may be developed in the future. To the extent that any disruption results in the loss, damage or misappropriation of information, we may be materially adversely affected by claims from customers, financial institutions, regulatory authorities, payment card associations and others. In addition, the cost of complying with stricter privacy and information security laws and standards could be significant to us. For example, we were recently required to transition from PCI Data Security Standard 2.0 to PCI Data Security Standard 3.2. We are in the process of conforming to the new standards which we expect to be completed by the third quarter of 2017. There is no guarantee that we will be able to conform to these new standards, and if we fail to meet these standards, we could become subject to fines and other penalties and experience a significant increase in payment card transaction costs. In addition, such failure could damage our reputation, inhibit sales, and adversely affect our business.

***We face intense competition and operate in an industry with limited barriers to entry, and some of our competitors may have greater resources than us and may be better positioned to capitalize on the growing e-commerce auto parts market.***

The auto parts industry is competitive and highly fragmented, with products distributed through multi-tiered and overlapping channels. We compete with both online and offline retailers who offer original equipment manufacturer (“OEM”) and aftermarket auto parts to either the DIY or do-it-for-me customer segments. Current or potential competitors include the following:

- national auto parts retailers such as Advance Auto Parts, AutoZone, Napa Auto Parts, CarQuest, O’Reilly Automotive and Pep Boys;
- large online marketplaces such as Amazon.com and eBay;
- other online retailers of automotive products and auto repair information websites;
- local independent retailers or niche auto parts online retailers;
- wholesale aftermarket auto parts distributors such as LKQ Corporation; and
- manufacturers, brand suppliers and other distributors selling online directly to customers.

Barriers to entry are low, and current and new competitors can launch websites at a relatively low cost. Many of our current and potential competitors have longer operating histories, larger customer bases, greater brand recognition and significantly greater financial, marketing, technical, management and other resources than we do. For example, in the event that online marketplace companies such as Amazon or eBay, who have larger customer bases, greater brand recognition and significantly greater resources than we do, focus more of their resources on competing in the aftermarket auto parts market, it could have a material adverse effect on our business and results of operations. In addition, some of our competitors have used and may continue to use aggressive pricing tactics and devote substantially more financial resources to website and system development than we do. We expect that competition will further intensify in the future as Internet use and online commerce continue to grow worldwide. Increased competition may result in reduced sales, lower operating margins, reduced profitability, loss of market share and diminished brand recognition.

Additionally, we have experienced significant competitive pressure from certain of our suppliers who are now selling their products directly to customers. Since our suppliers have access to merchandise at very low costs, they can sell products at lower prices and maintain higher gross margins on their product sales than we can. Our financial results have been negatively impacted by direct sales from our suppliers to our current and potential customers, and our total number of orders and average order value may decline due to increased competition. Continued competition from our suppliers may also continue to negatively impact our business and results of operations, including through reduced sales, lower operating margins, reduced profitability, loss of market share and diminished brand recognition. We have implemented and will continue to implement several strategies to attempt to overcome the challenges created by our suppliers selling directly to our customers and potential customers, including optimizing our pricing, continuing to increase our mix of private label products and improving our websites, which may not be successful. If these strategies are not successful, our operating results and financial conditions could be materially and adversely affected.

***If we fail to offer a broad selection of products at competitive prices or fail to maintain sufficient inventory to meet customer demands, our revenue could decline.***

In order to expand our business, we must successfully offer, on a continuous basis, a broad selection of auto parts that meet the needs of our customers, including by being the first to market with new SKUs. Our auto parts are used by consumers for a variety of purposes, including repair, performance, improved aesthetics and functionality. In addition, to be successful, our product offerings must be broad and deep in scope, competitively priced, well-made, innovative and attractive to a wide range of consumers. We cannot predict with certainty that we will be successful in offering products that meet all of these

requirements. Moreover, even if we offer a broad selection of products at competitive prices, we must maintain sufficient in-stock inventory to meet consumer demand. If our product offerings fail to satisfy our customers' requirements or respond to changes in customer preferences or we otherwise fail to maintain sufficient in-stock inventory, our revenue could decline.

***Challenges by OEMs to the validity of the aftermarket auto parts industry and claims of intellectual property infringement could adversely affect our business and the viability of the aftermarket auto parts industry.***

OEMs have attempted to use claims of intellectual property infringement against manufacturers and distributors of aftermarket products to restrict or eliminate the sale of aftermarket products that are the subject of the claims. The OEMs have brought such claims in federal court and with the United States International Trade Commission. We have received in the past, and we anticipate we may in the future receive, communications alleging that certain products we sell infringe the patents, copyrights, trademarks and trade names or other intellectual property rights of OEMs or other third parties. For instance, after approximately three and a half years of litigation and related costs and expenses, on April 16, 2009, we entered into a settlement agreement with Ford Motor Company and Ford Global Technologies, LLC that ended the two legal actions that were initiated by Ford against us related to claims of intellectual property infringement. The United States Patent and Trademark Office records indicate that OEMs are seeking and obtaining more design patents than they have in the past. To the extent that the OEMs are successful with intellectual property infringement claims, we could be restricted or prohibited from selling certain aftermarket products which could have an adverse effect on our business. Infringement claims could also result in increased costs of doing business arising from increased legal expenses, adverse judgments or settlements or changes to our business practices required to settle such claims or satisfy any judgments. Litigation could result in interpretations of the law that require us to change our business practices or otherwise increase our costs and harm our business. We may not maintain sufficient insurance coverage to cover the types of claims that could be asserted. If a successful claim were brought against us, it could expose us to significant liability.

***If we are unable to protect our intellectual property rights, our reputation and brand could be impaired and we could lose customers.***

We regard our trademarks, trade secrets and similar intellectual property such as our proprietary back-end order processing and fulfillment code and process as important to our success. We rely on trademark and copyright law, and trade secret protection, and confidentiality and/or license agreements with employees, customers, partners and others to protect our proprietary rights. We cannot be certain that we have taken adequate steps to protect our proprietary rights, especially in countries where the laws may not protect our rights as fully as in the United States. In addition, our proprietary rights may be infringed or misappropriated, and we could be required to incur significant expenses to preserve them. In the past we have filed litigation to protect our intellectual property rights. The outcome of such litigation can be uncertain, and the cost of prosecuting such litigation may have an adverse impact on our earnings. We have common law trademarks, as well as pending federal trademark registrations for several marks and several registered marks. However, any registrations may not adequately cover our intellectual property or protect us against infringement by others. Effective trademark, service mark, copyright, patent and trade secret protection may not be available in every country in which our products and services may be made available online. We also currently own or control a number of Internet domain names, including [www.usautoparts.net](http://www.usautoparts.net), [www.carparts.com](http://www.carparts.com), [www.autopartswarehouse.com](http://www.autopartswarehouse.com), [www.jcwhitney.com](http://www.jcwhitney.com) and [www.AutoMD.com](http://www.AutoMD.com), and have invested time and money in the purchase of domain names and other intellectual property, which may be impaired if we cannot protect such intellectual property. We may be unable to protect these domain names or acquire or maintain relevant domain names in the United States and in other countries. If we are not able to protect our trademarks, domain names or other intellectual property, we may experience difficulties in achieving and maintaining brand recognition and customer loyalty.

***We rely on key personnel and may need additional personnel for the success and growth of our business.***

Our business is largely dependent on the personal efforts and abilities of highly skilled executive, technical, managerial, merchandising, marketing, and call center personnel. Competition for such personnel is intense, and we cannot assure that we will be successful in attracting and retaining such personnel. The loss of any key employee or our inability to attract or retain other qualified employees could harm our business and results of operations.

***As a result of our international operations, we have foreign exchange risk.***

Our purchases of auto parts from our Asian suppliers are denominated in U.S. dollars; however, a change in the foreign currency exchange rates could impact our product costs over time. Our financial reporting currency is the U.S. dollar and changes in exchange rates significantly affect our reported results and consolidated trends. For example, if the U.S. dollar weakens year-over-year relative to currencies in our international locations, our consolidated gross profit and operating expenses would be higher than if currencies had remained constant. Similarly, our operating expenses in the Philippines are generally paid in Philippine Pesos, and as the exchange rate fluctuates, it could adversely impact our operating results.

***If our product catalog database is stolen, misappropriated or damaged, or if a competitor is able to create a substantially similar catalog without infringing our rights, then we may lose an important competitive advantage.***

We have invested significant resources and time to build and maintain our product catalog, which is maintained in the form of an electronic database, which maps SKUs to relevant product applications based on vehicle makes, models and years. We believe that our product catalog provides us with an important competitive advantage in both driving traffic to our websites and converting that traffic to revenue by enabling customers to quickly locate the products they require. We cannot assure you that we will be able to protect our product catalog from unauthorized copying or theft or that our product catalog will continue to operate adequately, without any technological challenges. In addition, it is possible that a competitor could develop a catalog or database that is similar to or more comprehensive than ours, without infringing our rights. In the event our product catalog is damaged or is stolen, copied or otherwise replicated to compete with us, whether lawfully or not, we may lose an important competitive advantage and our business could be harmed.

***Our e-commerce system is dependent on open-source software, which exposes us to uncertainty and potential liability.***

We utilize open-source software such as Linux, Apache, MySQL, PHP, Fedora and Perl throughout our web properties and supporting infrastructure although we have created proprietary programs. Open-source software is maintained and upgraded by a general community of software developers under various open-source licenses, including the GNU General Public License (“GPL”). These developers are under no obligation to maintain, enhance or provide any fixes or updates to this software in the future. Additionally, under the terms of the GPL and other open-source licenses, we may be forced to release to the public source-code internally developed by us pursuant to such licenses. Furthermore, if any of these developers contribute any code of others to any of the software that we use, we may be exposed to claims and liability for intellectual property infringement and may also be forced to implement changes to the code-base for this software or replace this software with internally developed or commercially licensed software.

***System failures, including failures due to natural disasters or other catastrophic events, could prevent access to our websites, which could reduce our net sales and harm our reputation.***

Our sales would decline and we could lose existing or potential customers if they are not able to access our websites or if our websites, transactions processing systems or network infrastructure do not perform to our customers’ satisfaction. Any Internet network interruptions or problems with our websites could:

- prevent customers from accessing our websites;
- reduce our ability to fulfill orders or bill customers;
- reduce the number of products that we sell;
- cause customer dissatisfaction;  
or
- damage our brand and reputation.

We have experienced brief computer system interruptions in the past, and we believe they may continue to occur from time to time in the future. Our systems and operations are also vulnerable to damage or interruption from a number of sources, including a natural disaster or other catastrophic event such as an earthquake, typhoon, volcanic eruption, fire, flood, terrorist attack, computer viruses, power loss, telecommunications failure, physical and electronic break-ins and other similar events. For example, our headquarters and the majority of our infrastructure, including some of our servers, are located in Southern California, a seismically active region. We also maintain offshore and outsourced operations in the Philippines, an area that has been subjected to a typhoon and a volcanic eruption in the past. In addition, California has in the past experienced power outages as a result of limited electrical power supplies and due to recent fires in the southern part of the state. Such outages, natural disasters and similar events may recur in the future and could disrupt the operation of our business. Our technology infrastructure is also vulnerable to computer viruses, physical or electronic break-ins and similar disruptions. Although the critical portions of our systems are redundant and backup copies are maintained offsite, not all of our systems and data are fully redundant. We do not presently have a formal disaster recovery plan in effect and may not have sufficient insurance for losses that may occur from natural disasters or catastrophic events. Any substantial disruption of our technology infrastructure could cause interruptions or delays in our business and loss of data or render us unable to accept and fulfill customer orders or operate our websites in a timely manner, or at all.

#### **Risks Related To Our Capital Stock**

***Our common stock price has been and may continue to be volatile, which may result in losses to our stockholders.***

The market prices of technology and e-commerce companies generally have been extremely volatile and have recently experienced sharp share price and trading volume changes. The trading price of our common stock is likely to be volatile and



could fluctuate widely in response to, among other things, the risk factors described in this report and other factors beyond our control such as fluctuations in the operations or valuations of companies perceived by investors to be comparable to us, our ability to meet analysts' expectations, our trading volume, activities of activist investors, the impact of any stock repurchase program or conditions or trends in the Internet or auto parts industries.

Since the completion of our initial public offering in February 2007 through December 31, 2016, the trading price of our common stock has been volatile, ranging from a high of \$12.61 per share to a low per share of \$0.91. We have also experienced significant fluctuations in the trading volume of our common stock. General economic and political conditions unrelated to our performance may also adversely affect the price of our common stock. In the past, following periods of volatility in the market price of a public company's securities, securities class action litigation has often been initiated. Due to the inherent uncertainties of litigation, we cannot predict the ultimate outcome of any such litigation if it were initiated. The initiation of any such litigation or an unfavorable result could have a material adverse effect on our financial condition and results of operations.

***Our executive officers, directors and certain related parties and entities that are affiliated with them have registered the resale of a significant portion of our total outstanding shares of common stock, and any sale of such shares into the market in the future could cause the market price of our common stock to drop significantly, even if our business is doing well.***

Our executive officers, directors and certain related parties and entities that are affiliated with them have registered the resale of up to 12,023,656 shares of our common stock that they currently hold, which represents approximately 35.2% of our total outstanding shares of common stock as of December 31, 2016. Sales of a substantial number of shares of our common stock in the public market by these selling stockholders, or the perception that these sales might occur, could depress the market price of our common stock and could impair our ability to raise capital through the sale of additional equity securities. We are unable to predict the effect that sales or perceived sales by these stockholders may have on the prevailing market price of our common stock.

***Our common stock may be delisted from the NASDAQ Global Market ("NASDAQ") if we are unable to maintain compliance with Nasdaq's continued listing standards.***

NASDAQ imposes, among other requirements, continued listing standards including minimum bid and public float requirements. The price of our common stock must trade at or above \$1.00 to comply with NASDAQ's minimum bid requirement for continued listing on the NASDAQ. If our stock trades at bid prices of less than \$1.00 for a period in excess of 30 consecutive business days, the NASDAQ could send a deficiency notice to us for not remaining in compliance with the minimum bid listing standards. During the fiscal 2016 and fiscal 2015, our common stock never traded below \$1.00. However, if the closing bid price of our common stock fails to meet NASDAQ's minimum closing bid price requirement, or if we otherwise fail to meet any other applicable requirements of the NASDAQ and we are unable to regain compliance, NASDAQ may make a determination to delist our common stock.

Any delisting of our common stock could adversely affect the market liquidity of our common stock and the market price of our common stock could decrease. Furthermore, if our common stock were delisted it could adversely affect our ability to obtain financing for the continuation of our operations and/or result in the loss of confidence by investors, customers, suppliers and employees.

***Our executive officers and directors and certain related parties own a significant percentage of our stock.***

As of December 31, 2016, our executive officers and directors and certain related parties and entities that are affiliated with them beneficially owned in the aggregate approximately 43% of our outstanding shares of stock. This significant concentration of share ownership may adversely affect the trading price for our common stock because investors often perceive disadvantages in owning stock in companies with controlling stockholders. In addition, the significant concentration of share ownership may provide for less trading volume of our common stock. These stockholders, acting together, also will be able to significantly influence our management and affairs and control matters requiring stockholder approval including the election of our entire Board of Directors and certain significant corporate actions such as mergers, consolidations or the sale of substantially all of our assets. As a result, this concentration of ownership could delay, defer or prevent others from initiating a potential merger, takeover or other change in our control, even if these actions would benefit our other stockholders and us.

***The rights, preferences and privileges of our existing preferred stock may restrict our financial and operational flexibility and may dilute our common stockholders.***

In March 2013, our Board of Directors, under the authority granted by our Certificate of Incorporation, established a series of preferred stock, our Series A Convertible Preferred, which has various rights, preferences and privileges senior to the shares of our common stock. Dividends on the Series A Convertible Preferred are payable quarterly, subject to the satisfaction of certain conditions, at a rate of \$0.058 per share per annum in cash, in shares of common stock or in any combination of cash and common stock as determined by our Board of Directors. While we may, at our election, subject to the satisfaction of certain

conditions, pay any accrued but unpaid dividends on the Series A Convertible Preferred in either cash or in common stock, we may be unable to satisfy the requisite conditions for paying dividends in common stock and, under such circumstances, we will be required to pay such accrued but unpaid dividends in cash. In such circumstances, we will be required to use cash that would otherwise be used to fund our ongoing operations to pay such accrued but unpaid dividends. To the extent we do pay dividends in common stock as we have done in certain prior periods, the ownership percentage of our common stockholders who are not holders of the Series A Convertible Preferred will be diluted. Our Series A Convertible Preferred is initially convertible for 4,149,997 shares of common stock, and to the extent that the Series A Convertible Preferred is converted, the common stock ownership percentage of our common stockholders who are not converting holders of the Series A Convertible Preferred will be diluted.

***Our future operating results may fluctuate and may fail to meet market expectations.***

We expect that our revenue and operating results will continue to fluctuate from quarter to quarter due to various factors, many of which are beyond our control. If our quarterly revenue or operating results fall below the expectations of investors or securities analysts, the price of our common stock could significantly decline. The factors that could cause our operating results to continue to fluctuate include, but are not limited to:

- fluctuations in the demand for aftermarket auto parts;
- price competition on the Internet or among offline retailers for auto parts;
- our ability to attract visitors to our websites and convert those visitors into customers, including to the extent based on our ability to successfully work with different search engines to drive visitors to our websites;
- our ability to successfully sell our products through third-party online marketplaces or the effects of any price increases in those marketplaces;
- competition from companies that have longer operating histories, larger customer bases, greater brand recognition, access to merchandise at lower costs and significantly greater resources than we do, like third-party online market places and our suppliers;
- our ability to maintain and expand our supplier and distribution relationships without significant price increases or reduced service levels;
- our ability to borrow funds under our credit facility;
- the effects of seasonality on the demand for our products;
- our ability to accurately forecast demand for our products, price our products at market rates and maintain appropriate inventory levels;
- our ability to build and maintain customer loyalty;
- our ability to successfully integrate our acquisitions;
- infringement actions that could impact the viability of the auto parts aftermarket or portions thereof;
- the success of our brand-building and marketing campaigns;
- our ability to accurately project our future revenues, earnings, and results of operations;
- government regulations related to use of the Internet for commerce, including the application of existing tax regulations to Internet commerce and changes in tax regulations;
- technical difficulties, system downtime or Internet brownouts;
- the amount and timing of operating costs and capital expenditures relating to expansion of our business, operations and infrastructure; and
- macroeconomic conditions that adversely impact the general and automotive retail sales environment.

***If we fail to maintain an effective system of internal control over financial reporting or comply with Section 404 of the Sarbanes-Oxley Act of 2002, we may not be able to accurately report our financial results or prevent fraud, and our stock price could decline.***

While management has concluded that our internal controls over financial reporting were effective as of December 31, 2016, we have in the past, and could in the future, have a significant deficiency or material weakness in internal control over financial reporting or fail to comply with Section 404 of the Sarbanes-Oxley Act of 2002. If we fail to properly maintain an effective system of internal control over financial reporting, it could impact our ability to prevent fraud or to issue our financial

statements in a timely manner that presents fairly our financial condition and results of operations. The existence of any such deficiencies or weaknesses, even if remediated, may also lead to the loss of investor confidence in the reliability of our financial statements, could harm our business and negatively impact the trading price of our common stock. Such deficiencies or material weaknesses may also subject us to lawsuits, regulatory investigations and other penalties.

***Our charter documents could deter a takeover effort, which could inhibit your ability to receive an acquisition premium for your shares.***

Provisions in our certificate of incorporation and bylaws could make it more difficult for a third party to acquire us, even if doing so would be beneficial to our stockholders. Such provisions include the following:

- our Board of Directors are authorized, without prior stockholder approval, to create and issue preferred stock which could be used to implement anti-takeover devices;
- advance notice is required for director nominations or for proposals that can be acted upon at stockholder meetings;
- our Board of Directors is classified such that not all members of our board are elected at one time, which may make it more difficult for a person who acquires control of a majority of our outstanding voting stock to replace all or a majority of our directors;
- stockholder action by written consent is prohibited except with regards to an action that has been approved by the Board;
- special meetings of the stockholders are permitted to be called only by the chairman of our Board of Directors, our chief executive officer or by a majority of our Board of Directors;
- stockholders are not permitted to cumulate their votes for the election of directors; and
- stockholders are permitted to amend certain provisions of our bylaws only upon receiving at least 66 2/3% of the votes entitled to be cast by holders of all outstanding shares then entitled to vote generally in the election of directors, voting together as a single class.

***We do not intend to pay dividends on our common stock.***

We currently do not expect to pay any cash dividends on our common stock for the foreseeable future.

**General Market and Industry Risk**

***Economic conditions have had, and may continue to have an adverse effect on the demand for aftermarket auto parts and could adversely affect our sales and operating results.***

We sell aftermarket auto parts consisting of collision and engine parts used for repair and maintenance, performance parts used to enhance performance or improve aesthetics and accessories that increase functionality or enhance a vehicle's features. Demand for our products has been and may continue to be adversely affected by general economic conditions. In declining economies, consumers often defer regular vehicle maintenance and may forego purchases of nonessential performance and accessories products, which can result in a decrease in demand for auto parts in general. Consumers also defer purchases of new vehicles, which immediately impacts performance parts and accessories, which are generally purchased in the first six months of a vehicle's lifespan. In addition, during economic downturns some competitors may become more aggressive in their pricing practices, which would adversely impact our gross margin and could cause large fluctuations in our stock price. Certain suppliers may exit the industry which may impact our ability to procure parts and may adversely impact gross margin as the remaining suppliers increase prices to take advantage of limited competition.

***The seasonality of our business places increased strain on our operations.***

We have historically experienced higher sales of collision parts in winter months when inclement weather and hazardous road conditions typically result in more automobile collisions. Engine parts and performance parts and accessories have historically experienced higher sales in the summer months when consumers have more time to undertake elective projects to maintain and enhance the performance of their automobiles and the warmer weather during that time is conducive for such projects. We also have experienced increased demand following the issuance of tax rebates by the government. If we do not stock or restock popular products in sufficient amounts such that we fail to meet increased customer demand, it could significantly affect our revenue and our future growth. Likewise, if we overstock products in anticipation of increased demand, we may be required to take significant inventory markdowns or write-offs and incur commitment costs, which could reduce profitability.

***Vehicle miles driven, vehicle accident rates and insurance companies' willingness to accept a variety of types of replacement parts in the repair process have fluctuated and may decrease, which could result in a decline of our revenues and negatively affect our results of operations.***

We and our industry depend on the number of vehicle miles driven, vehicle accident rates and insurance companies' willingness to accept a variety of types of replacement parts in the repair process. Decreased miles driven reduce the number of accidents and corresponding demand for crash parts, and reduce the wear and tear on vehicles with a corresponding reduction in demand for vehicle repairs and replacement or engine parts. If consumers were to drive less in the future and/or accident rates were to decline, as a result of higher gas prices, increased use of ride-shares, the advancement of driver assistance technologies, or otherwise, our sales may decline and our business and financial results may suffer.

***We may become liable for collecting and paying more sales taxes, and other fees and penalties, which could have an adverse effect on our business.***

We currently collect sales or other similar taxes only on the shipment of goods to customers in the states of California, Virginia, Illinois, and Ohio. Other states or jurisdictions could seek to impose or enforce sales tax collection or other tax obligations on us because we engage in and facilitate online commerce.

To the extent we are not subject to certain tax obligations, we enjoy a competitive advantage to the extent our competitors are subject to those obligations. Several states have enacted, and a number of states and the U.S. Congress have been considering, various initiatives that could impose broad sales and use tax collection obligations on Internet retailers. Federal, state and local governments could accelerate efforts to pass Internet sales tax initiatives in response to pressure to make up budgetary shortfalls resulting from recessionary economic conditions and the failure to collect sales and use taxes on Internet purchases under current self-assessment regimes. Any of these initiatives would increase total costs to our customers, which could adversely affect our sales.

We are closely monitoring developments in this area. The imposition by national, state and local governments of various tax obligations upon Internet commerce could create significant administrative burdens for us as well as substantially impair the growth of our e-commerce business, which could adversely affect our sales and profitability. Because our consumer websites and product deliveries are available in all 50 states, some or all of those jurisdictions may require us to register or qualify to do business in their jurisdictions. If we fail to collect and remit or pay required sales or other taxes in a jurisdiction, or qualify or register to do business in a jurisdiction that requires us to do so or if we have failed to do so in the past, we could face material liabilities for taxes, fees, interest and penalties. If various jurisdictions impose new tax obligations on our business activities, our sales and net income in those jurisdictions could decrease significantly, which could harm our business.

***If we do not respond to technological change, our websites could become obsolete and our financial results and conditions could be adversely affected.***

We maintain a network of websites which requires substantial development and maintenance efforts, and entails significant technical and business risks. To remain competitive, we must continue to enhance and improve the responsiveness, functionality and features of our websites. The Internet and the e-commerce industry are characterized by rapid technological change, the emergence of new industry standards and practices and changes in customer requirements and preferences. Therefore, we may be required to license emerging technologies, enhance our existing websites, develop new services and technology that address the increasingly sophisticated and varied needs of our current and prospective customers, and adapt to technological advances and emerging industry and regulatory standards and practices in a cost-effective and timely manner. Our ability to remain technologically competitive may require substantial expenditures and lead time and our failure to do so may harm our business and results of operations.

***Existing or future government regulation could expose us to liabilities and costly changes in our business operations and could reduce customer demand for our products and services.***

We are subject to federal and state consumer protection laws and regulations, including laws protecting the privacy of customer non-public information and regulations prohibiting unfair and deceptive trade practices, as well as laws and regulations governing businesses in general and the Internet and e-commerce and certain environmental laws. Additional laws and regulations may be adopted with respect to the Internet, the effect of which on e-commerce is uncertain. These laws may cover issues such as user privacy, spyware and the tracking of consumer activities, marketing e-mails and communications, other advertising and promotional practices, money transfers, pricing, content and quality of products and services, taxation, electronic contracts and other communications, intellectual property rights, and information security. Furthermore, it is not clear how existing laws such as those governing issues such as property ownership, sales and other taxes, trespass, data mining and collection, and personal privacy apply to the Internet and e-commerce. To the extent we expand into international markets, we will be faced with complying with local laws and regulations, some of which may be materially different than U.S. laws and

regulations. Any such foreign law or regulation, any new U.S. law or regulation, or the interpretation or application of existing laws and regulations to the Internet or other online services or our business in general, may have a material adverse effect on our business, prospects, financial condition and results of operations by, among other things, impeding the growth of the Internet, subjecting us to fines, penalties, damages or other liabilities, requiring costly changes in our business operations and practices, and reducing customer demand for our products and services. We may not maintain sufficient insurance coverage to cover the types of claims or liabilities that could arise as a result of such regulation.

***We may be affected by global climate change or by legal, regulatory, or market responses to such change.***

The growing political and scientific sentiment is that global weather patterns are being influenced by increased levels of greenhouse gases in the earth's atmosphere. This growing sentiment and the concern over climate change have led to legislative and regulatory initiatives aimed at reducing greenhouse gas emissions which warm the earth's atmosphere. These warmer weather conditions could result in a decrease in demand for auto parts in general. Moreover, proposals that would impose mandatory requirements on greenhouse gas emissions continue to be considered by policy makers in the United States. Laws enacted that directly or indirectly affect our suppliers (through an increase in the cost of production or their ability to produce satisfactory products) or our business (through an impact on our inventory availability, cost of sales, operations or demand for the products we sell) could adversely affect our business, financial condition, results of operations and cash flows. Significant increases in fuel economy requirements or new federal or state restrictions on emissions of carbon dioxide that may be imposed on vehicles and automobile fuels could adversely affect demand for vehicles, annual miles driven or the products we sell or lead to changes in automotive technology. Compliance with any new or more stringent laws or regulations, or stricter interpretations of existing laws, could require additional expenditures by us or our suppliers. Our inability to respond to such changes could adversely impact the demand for our products and our business, financial condition, results of operations or cash flows.

***The United States government may substantially increase border controls and impose restrictions on cross-border commerce that may substantially harm our business.***

We purchase a substantial portion of our products from foreign manufacturers and other suppliers who source products internationally. Restrictions on shipping goods into the United States from other countries pose a substantial risk to our business. Particularly since the terrorist attacks on September 11, 2001, the United States government has substantially increased border surveillance and controls. In addition, President Trump has indicated he supports the implementation of tariffs on goods exported from overseas and it is possible he will introduce legislation supporting his position. If the United States were to impose further border controls and restrictions, impose quotas, tariffs or import duties, increase the documentation requirements applicable to cross border shipments or take other actions that have the effect of restricting the flow of goods from other countries to the United States, we may have greater difficulty acquiring our inventory in a timely manner, experience shipping delays, or incur increased costs and expenses, all of which would substantially harm our business and results of operations.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

As of December 31, 2016, the total square footage of our leased office and distribution centers was 574,000 square feet. This includes approximately 531,000 square feet for our corporate headquarters located in Carson, California and distribution centers in LaSalle, Illinois and Chesapeake, Virginia; and approximately 43,000 square feet of office space in the Philippines. For additional information regarding our obligations under property leases, see “*Note 10-Commitments and Contingencies*” of the Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report.

**ITEM 3. LEGAL PROCEEDINGS**

The information set forth under the caption “*Legal Matters*” in “*Note 10-Commitments and Contingencies*” of the Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, and is incorporated herein by reference. For an additional discussion of certain risks associated with legal proceedings, see the section entitled “*Risk Factors*” in Item 1A of this report.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## PART II

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

#### Market Information

Our common stock is being trading on the Nasdaq under the symbol "PRTS." The table below sets forth the high and low sales prices of our common stock for the periods indicated:

	High	Low
<b>2016:</b>		
Quarter ended April 2, 2016	\$ 3.28	\$ 2.35
Quarter ended July 2, 2016	4.39	2.58
Quarter ended October 1, 2016	4.49	3.21
Quarter ended December 31, 2016	3.66	2.40
<b>2015:</b>		
Quarter ended April 4, 2015	\$ 3.34	\$ 2.07
Quarter ended July 4, 2015	2.71	1.50
Quarter ended October 3, 2015	2.43	1.87
Quarter ended January 2, 2016	2.99	1.92

On March 2, 2017, the last reported sale price of our common stock on the Nasdaq was \$3.40 per share.

#### Holders

As of March 2, 2017, there were approximately 2,020 holders of record of our common stock.

#### Stock Performance Graph

*The material in this section is not "soliciting material," is not deemed "filed" with the SEC, and shall not be deemed to be incorporated by reference into any of our filings under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.*

The following graph shows a quarterly comparison of the total cumulative returns of an investment of \$100 in cash on December 31, 2011, in (i) our common stock, (ii) the Morgan Stanley Technology Index, (iii) the S&P 500 Retail Index and (iv) NASDAQ Composite Index, in each case through December 31, 2016. The performance of our stock, the Morgan Stanley Technology Index, the S&P 500 Retail Index and the NASDAQ Composite Index have been obtained from online data available. We have used the available prices at the end of the week closest to the end of the period for the purposes of the graph. The comparisons in the graph are required by the SEC and are not intended to forecast or be indicative of the possible future performance of our common stock. The graph assumes that all common stock dividends have been reinvested (to date, we have not declared dividends on our common stock).





**Dividend Policy**

No dividends on common stock were paid during the fiscal year ended December 31, 2016. We issued approximately \$241,000 in common stock to our Series A Preferred shareholders during each of the fiscal years ended December 31, 2016 and January 2, 2016. We do not anticipate that we will declare or pay any cash dividends on our common stock in the foreseeable future; however, we will have to pay dividends to our preferred shareholders until such shares are redeemed or converted. We maintain an asset-based revolving credit facility with JPMorgan Chase Bank (the "Credit Agreement") that provides for, among other things, a revolving commitment in an aggregate principal amount of up to \$30 million subject to a borrowing base derived from certain of our receivables, inventory and property and equipment. The Credit Agreement requires us to obtain a prior written consent from JPMorgan Chase Bank when we determine to pay any dividends on or make any distribution with respect to our common stock. Under the Second Amendment to Credit Agreement dated March 25, 2013, we obtained written consent from JPMorgan Chase Bank to pay dividends on our Series A Preferred Shares. See "Liquidity and Capital Resources" in Item 7 of Part II included in this report for further information on the covenants under the secured Credit Agreement. Any future determination to pay cash dividends on our common stock will be subject to the above restriction, as well as restrictions under any other existing indebtedness, at the discretion of our Board of Directors and will be dependent upon our financial condition, results of operations, capital requirements, and other factors the Board of Directors deems relevant.

**Recent Sales of Unregistered Securities**

None.

**Use of Proceeds from Sales of Registered Securities**

None.

### Purchases of Equity Securities by the Issuer and Affiliated Purchasers

We purchased the following shares of common stock for the fourth quarter of fiscal 2016, all of which were made as part of publicly announced plans or programs:

<b>Period</b>	<b>Total Number of Shares Purchased <sup>(1)</sup></b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Number (or Approximate Dollar Value) of Shares that May Yet be Purchased Under the Plans or Programs</b>
Oct 2 - Oct 29, 2016	—	—	—	—
Oct 30 - Nov 26, 2016	87,820	\$ 2.89	87,820	—
Nov 27 - Dec 31, 2016	357,259	\$ 3.14	357,259	—

<sup>(1)</sup> Stock repurchases were made pursuant to a stock repurchase program authorized by our Board of Directors on November 15, 2016. The program allows for the repurchase of up to \$5.0 million of its common stock. All repurchases were made using cash resources. Stock repurchases may occur through open market purchases or pursuant to a 10b5-1 trading plan.

## ITEM 6. SELECTED FINANCIAL DATA

The following selected financial information as of and for the dates and periods indicated have been derived from our audited consolidated financial statements. The information set forth below is not necessarily indicative of results of future operations, and should be read in conjunction with “*Management’s Discussion and Analysis of Financial Condition and Results of Operations*” in Part II, Item 7 of this report and our consolidated financial statements and related notes included elsewhere in this report (in thousands, except per share data).

	52 Weeks Ended December 31, 2016 ("fiscal year 2016")	52 Weeks Ended January 2, 2016 ("fiscal year 2015")	53 Weeks Ended January 3, 2015 ("fiscal year 2014") (1)	52 Weeks Ended December 28, 2013 ("fiscal year 2013") (2)	52 Weeks Ended December 29, 2012 ("fiscal year 2012") (3)
<b>(In thousands, except per share data)</b>					
<b>Consolidated Statements of Operations</b>					
<b>Data:</b>					
Net sales	\$ 303,571	\$ 291,091	\$ 283,508	\$ 254,753	\$ 304,017
Cost of sales	211,289	207,657	205,058	180,620	212,379
Gross profit	92,282	83,434	78,450	74,133	91,638
Operating expenses:					
Marketing	43,555	43,279	42,008	41,045	51,416
General and administrative	17,907	16,509	16,701	17,567	19,857
Fulfillment	22,975	20,237	20,368	18,702	22,265
Technology	5,843	5,000	4,863	5,128	6,274
Amortization of intangible assets	482	464	422	381	1,189
Impairment loss on goodwill	—	—	—	—	18,854
Impairment loss on property and equipment	—	—	—	4,832	1,960
Impairment loss on intangible assets	1,130	—	—	1,245	5,613
Total operating expenses	91,892	85,489	84,362	88,900	127,428
Income (loss) from operations	390	(2,055)	(5,912)	(14,767)	(35,790)
Other expense, net	(1,192)	(1,180)	(1,036)	(824)	(1,125)
Income (loss) before income taxes	(802)	(3,235)	(6,948)	(15,591)	(36,915)
Income tax (benefit) provision	(199)	(811)	138	43	(937)
Net income (loss)	(603)	(2,424)	(7,086)	(15,634)	(35,978)
Net loss attributable to noncontrolling interests	(1,334)	(1,143)	(207)	—	—
Net income (loss) attributable to U.S. Auto Parts	\$ 731	\$ (1,281)	\$ (6,879)	\$ (15,634)	\$ (35,978)
Basic net income (loss) per share	\$ 0.01	(0.04)	(0.21)	(0.48)	(1.17)
Diluted net income (loss) per share	\$ 0.01	(0.04)	(0.21)	(0.48)	(1.17)
Shares used in computation of basic net loss per share	34,765	33,946	33,489	32,697	30,818
Shares used in computation of diluted net loss per share	36,207	33,946	33,489	32,697	30,818

- (1) Fiscal year 2014 included restructuring charges of \$1.1 million and inventory write-downs of \$0.9 million incurred due to the closure of our warehouse in Carson, California.
- (2) Fiscal year 2013 included severance charges of \$0.7 million incurred due to a reduction in workforce during the first half of 2013.
- (3) Fiscal year 2012 included restructuring costs of \$0.6 million related to severance charges incurred due to a reduction in workforce from the closure of our call center in La Salle, Illinois.

	December 31, 2016	January 2, 2016	January 3, 2015	December 28, 2013	December 29, 2012
<b>(In thousands, except per share data)</b>					
<b>Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 6,643	\$ 5,537	\$ 7,653	\$ 818	\$ 1,030
Working capital	16,869	13,605	14,645	9,761	(4,027)
Total assets	82,134	83,756	82,907	69,182	88,877
Revolving loan payable	—	11,759	11,022	6,774	16,222
Current portion of long-term debt and capital leases	542	521	269	269	70
Long-term debt including capital leases, net of current portion	9,770	10,168	9,270	9,502	70
U.S. Auto Parts stockholders' equity	22,853	20,340	19,277	20,866	27,644
Noncontrolling interests	469	1,803	2,946	—	—

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS** *(Dollar Amounts in Thousands, Except Per Share Data, or as Otherwise Noted)*

**Cautionary Statement**

You should read the following discussion and analysis in conjunction with our consolidated financial statements and the related notes thereto contained in Part IV, Item 15 of this report. Certain statements in this report, including statements regarding our business strategies, operations, financial condition, and prospects are forward-looking statements. Use of the words "anticipates," "believes," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects," "should," "will," "would," "will likely continue," "will likely result" and similar expressions that contemplate future events may identify forward-looking statements.

The information contained in this section is not a complete description of our business or the risks associated with an investment in our common stock. We urge you to carefully review and consider the various disclosures made by us in this report and in our other reports filed with the SEC, which are available on the SEC's website at <http://www.sec.gov>. The section entitled "Risk Factors" set forth in *Part I, Item 1A* of this report, and similar discussions in our other SEC filings, describe some of the important factors, risks and uncertainties that may affect our business, results of operations and financial condition and could cause actual results to differ materially from those expressed or implied by these or any other forward-looking statements made by us or on our behalf. You are cautioned not to place undue reliance on these forward-looking statements, which are based on current expectations and reflect management's opinions only as of the date thereof. We do not assume any obligation to revise or update forward-looking statements. Finally, our historic results should not be viewed as indicative of future performance.

**Overview**

We are a leading online provider of aftermarket auto parts, including collision parts, engine parts, and performance parts and accessories. Our user-friendly websites provide customers with a broad selection of SKUs, with detailed product descriptions and photographs. Our proprietary product database maps our SKUs to product applications based on vehicle makes, models and years. We principally sell our products to individual consumers through our network of websites and online marketplaces. Through AutoMD.com, the Company also educates consumers on the maintenance and service of their vehicles. Our flagship consumer websites are located at [www.autopartswarehouse.com](http://www.autopartswarehouse.com), [www.carparts.com](http://www.carparts.com), [www.jcwhitney.com](http://www.jcwhitney.com) and [www.AutoMD.com](http://www.AutoMD.com) and our corporate website is located at [www.usautoparts.net](http://www.usautoparts.net).

We believe our strategy of disintermediating the traditional auto parts supply chain and selling products directly to customers over the Internet allows us to efficiently deliver products to our customers. Industry-wide trends that support our strategy include:

1. *Number of SKUs required to serve the market.* The number of automotive SKUs has grown dramatically over the last several years. In today's market, unless the consumer is driving a high volume produced vehicle and needs a simple maintenance item, the part they need is not typically on the shelf at a brick-and-mortar store. We believe our user-friendly websites provide customers with a favorable alternative to the brick-and-mortar shopping experience by

offering a comprehensive selection of over 1.0 million SKUs with detailed product descriptions, attributes and photographs combined with the flexibility of fulfilling orders using both drop-ship and stock-and-ship methods.

2. *U.S. vehicle fleet expanding and aging.* The average age of U.S. vehicles, an indicator of auto parts demand, rose to a record-high 11.5 years as of January 2016, according to IHS Automotive, a market analytics firm that expects the average age to remain at, or near record-highs through 2020. IHS expects the number of vehicles that are 12 years or older to increase by 15% by 2020. IHS found that the total number of light vehicles in operation in the U.S. has increased to record levels, with new vehicle registrations outpacing scrappage rates. We believe an increasing vehicle base and rising average age of vehicles will have a positive impact on overall aftermarket parts demand because older vehicles generally require more repairs. In many cases we believe these older vehicles are driven by do-it-yourself ("DIY") car owners who are more likely to handle any necessary repairs themselves rather than taking their car to the professional repair shop.

3. *Growth of online sales.* Management estimates that overall revenue from online sales of auto parts and accessories is projected to increase from approximately \$5.5 billion in 2015 to \$9.7 billion in 2018. Improved product availability, lower prices and consumers' growing comfort with digital platforms are driving the shift to online sales. We believe that we are well positioned for the shift to online sales due to our history of being a leading source for aftermarket automotive parts through online marketplaces and our network of websites.

*Our History.* We were formed in California in 1995 as a distributor of aftermarket auto parts and launched our first website in 2000. We reincorporated in Delaware in 2006 and expanded our online operations, increasing the number of SKUs sold through our e-commerce network, adding additional websites, improving our Internet marketing proficiency and commencing sales in online marketplaces. Additionally, in August 2010, through our acquisition of Whitney Automotive Group, Inc. (referred to herein as "WAG"), we expanded our product-lines and increased our customer reach in the DIY automobile and off-road accessories market.

*International Operations.* In April 2007, we established offshore operations in the Philippines. Our offshore operations allow us to access a workforce with the necessary technical skills at a significantly lower cost than comparably experienced U.S.-based professionals. Our offshore operations are responsible for a majority of our website development, catalog management, and back office support. Our offshore operations also house our main call center. We had 768 employees in the Philippines as of January 2, 2016. We had 748 employees in the Philippines as of December 31, 2016. We believe that the cost advantages of our offshore operations provide us with the ability to grow our business in a cost-effective manner.

*AutoMD.* In October 2008, we acquired AutoMD for the purpose of developing content and a user community to educate consumers on maintenance and service of their vehicles. The AutoMD.com site provides auto information, with tools for diagnosing car troubles, locating repair shops, estimating the cost of repairs, accessing recalls and technical service bulletins, reading do-it-yourself ("DIY") repair guides, and getting questions answered in the automotive enthusiast community forum. In 2013, AutoMD launched its *Insta-Quotes!* program which used real time data to estimate auto repair costs for consumers, and in 2014, we sold a non-controlling interest in AutoMD to outside investors and certain of our existing shareholders. In the first quarter of 2017, AutoMD repurchased the non-controlling interests and closed down the *Insta-Quotes!* program. Following the redemptions, AutoMD filed for dissolution and all of the remaining assets of AutoMD will be distributed to the Company except for certain cash reserved for creditors of AutoMD. We intend to utilize the AutoMD assets as part our media business going forward.

*Key Metrics.* To understand revenue generation through our network of e-commerce websites and online marketplaces, we monitor several key business metrics, including the following:

	52 Weeks Ended December 31, 2016	52 Weeks Ended January 2, 2016	53 Weeks Ended January 3, 2015
Unique Visitors (millions) <sup>1</sup>	117.9	116.7	119.8
E-commerce Orders (thousands)	2,161	2,043	2,010
Online Marketplace Orders (thousands)	1,265	1,061	1,049
Total Online Orders (thousands)	3,426	3,104	3,059
E-commerce Average Order Value	\$ 104	\$ 109	\$ 111
Online Marketplace Average Order Value	\$ 69	\$ 71	\$ 66
Total Online Average Order Value	\$ 91	\$ 96	\$ 96
Revenue Capture <sup>1</sup>	84.8 %	85.6 %	85.0 %
Conversion <sup>1</sup>	1.83 %	1.75 %	1.68 %

<sup>1</sup> Excludes online marketplaces and media properties (e.g. AutoMD).

*Unique Visitors:* A unique visitor to a particular website represents a user with a distinct IP address that visits that particular website. We define the total number of unique visitors in a given month as the sum of unique visitors to each of our websites during that month. We measure unique visitors to understand the volume of traffic to our websites and to track the effectiveness of our online marketing efforts. The number of unique visitors has historically varied based on a number of factors, including our marketing activities and seasonality. Included in the unique visitors are mobile device based customers, who are becoming an increasing part of our business. Shifting consumer behavior and technology enhancements indicates that customers are becoming more inclined to purchase auto parts through their mobile devices. User sophistication and technological advances have increased consumer expectations around the user experience on mobile devices, including speed of response, functionality, product availability, security, and ease of use. We believe enhancements to online solutions specifically catering to mobile based shopping can result in an increase in the number of orders and revenues. We believe an increase in unique visitors to our websites will result in an increase in the number of orders. We seek to increase the number of unique visitors to our websites by attracting repeat customers and improving search engine marketing and other internet marketing activities. During fiscal year 2016, our unique visitors increased by 1.0% compared to the fiscal year 2015 primarily due to an increase in paid traffic, partially offset by a decrease in organic traffic, as described in further detail under “—Executive Summary” below.

*Total Number of Orders:* We monitor the total number of orders as an indicator of future revenue trends. During the fiscal year 2016, the total number of orders was up by 10.4% compared to the fiscal year 2015, with e-commerce and online marketplace orders up by 5.8% and 19.2%, respectively. We believe e-commerce and online marketplace orders improved through an enhanced customer experience, greater product selection and certain strategic pricing initiatives. We recognize revenue associated with an order when the products have been delivered, consistent with our revenue recognition policy.

*Average Order Value:* Average order value represents our net sales on a placed orders basis for a given period of time divided by the total number of orders recorded during the same period of time. During the fiscal year 2016, our average order value decreased by 5.2% when compared to the fiscal year 2015 primarily due to a mix shift towards more private label sales. We seek to increase the average order value as a means of increasing net sales. Average order values vary depending upon a number of factors, including the components of our product offering, the order volume in certain online sales channels, mix changes between private label and branded, macro-economic conditions, and the competition online.

*Revenue Capture:* Revenue capture is the amount of actual dollars retained after taking into consideration returns, credit card declines and product fulfillment. During the fiscal year 2016, our revenue capture decreased by 0.9% to 84.8% compared to 85.6% in fiscal year 2015.

*Conversion:* Conversion is the number of orders as a rate to the total number of unique visitors. This rate indicates how well we convert a visitor to a customer sales order. During fiscal year 2016, our conversion improved by 4.6% to 1.83% in fiscal year 2016 compared to 1.75% in fiscal year 2015.

## **Executive Summary**

For fiscal 2016, Base USAP (which excludes AutoMD) generated net sales of \$303,324, compared with \$290,833 for fiscal year 2015, representing an increase of 4.3%. Base USAP net income for fiscal 2016 was \$2,973, compared to a net loss of \$136 for fiscal 2015. We generated Adjusted EBITDA, or net income before net interest expense, income tax provision, depreciation and amortization expense and amortization of intangible assets, plus share-based compensation expense, impairment loss and restructuring costs ("Adjusted EBITDA"), of \$14,024 in fiscal 2016 compared to \$10,029 in fiscal 2015. Adjusted EBITDA, which is not a Generally Accepted Accounting Principle (GAAP) measure, is presented because management uses it as one measure of the Company's operating performance, as it assists in comparing the Company's operating performance on a consistent basis by removing the impact of stock compensation expense, as well as items that are not expected to be recurring. Internally, this non-GAAP measure is also used by management for planning purposes, including the preparation of internal budgets; for allocating resources to enhance financial performance; and for evaluating the effectiveness of operational strategies. The Company also believes that such measure is used by rating agencies, securities analysts, investors and other parties in evaluating the Company. It should not be considered, however, as an alternative to operating income, or as an alternative to cash flows as a measure of the Company's overall liquidity, as presented in the Company's consolidated financial statements. Further, the Adjusted EBITDA measure shown may not be comparable to similarly titled measures used by other companies. Refer to the table presented below for reconciliation of net loss to Adjusted EBITDA.

For fiscal 2016, AutoMD generated net sales of \$247 compared to \$258 in fiscal 2015. AutoMD's net loss was \$3,576 for fiscal 2016, which included a non-cash impairment charge of \$1,130 relating to the impairment of certain AutoMD

software, compared to a net loss of \$2,288 for fiscal 2015. AutoMD's Adjusted EBITDA was negative \$1,354 in fiscal 2016 compared to negative \$1,663 in fiscal 2015.

Total revenues increased in fiscal 2016 compared to fiscal 2015 primarily due to growth in our online sales. Our online sales, which include our e-commerce, online marketplace sales channels and online advertising, contributed 91.0% of total revenues, and our offline sales, which consist of our Kool-View™ and wholesale operations, contributed 9.0% of total revenues. Our online sales for fiscal year 2016 increased by \$11,395, or 4.3%, to \$276,116 compared to \$264,721 in fiscal 2015 primarily due to an increase in unique visitors as well as conversion, resulting in a 10.4% increase in the total number of orders. Our offline sales increased by \$1,080, or 4.1%, to \$27,451 compared to the same period last year due to an expanded drop ship customer base.

Like most e-commerce retailers, our success depends on our ability to attract online consumers to our websites and convert them into customers in a cost-effective manner. Historically, marketing through search engines provided the most efficient opportunity to reach millions of online auto part buyers. We are included in search results through paid search listings, where we purchase specific search terms that will result in the inclusion of our listing, and algorithmic searches that depend upon the searchable content on our websites. Algorithmic listings cannot be purchased and instead are determined and displayed solely by a set of formulas utilized by the search engine. We have had a history of success with our search engine marketing techniques, which gave our different websites preferred positions in search results. Search engines, like Google, revise their algorithms from time to time in an attempt to optimize their search results. During the last few years, Google has changed its search results ranking algorithm. In some cases our unique visitor count, and therefore our financial results, were negatively impacted by these changes. We continue to address the ongoing changes to the Google methodology, and during the fiscal year 2016, our unique visitor count increased by 1.2 million, or 1.0%, to 117.9 million unique visitors compared to 116.7 million unique visitors in fiscal 2015 primarily due to an increase in paid traffic, partially offset by lower organic traffic. As in the past we expect Google will continue to make changes in their search engine algorithms to improve their user experience. As we are significantly dependent upon search engines for our website traffic, if we are unable to address these ongoing changes and attract unique visitors, our business and results of operations will be harmed.

Total expenses, which primarily consisted of cost of sales and operating costs, increased in fiscal year 2016 compared to the same period in 2015. Components of our cost of sales and operating costs are described in further detail under — “*Basis of Presentation*” below.

In 2016, we made positive strides towards achieving our strategic goals and in 2017 we will continue to pursue these strategies to continue our positive sales growth, improve gross profit while reducing operating costs as percent of sales:

- We expect to continue positive e-commerce growth by providing unique catalog content and providing better content on our websites with the goal of improving our ranking on the search results. In addition, we intend to improve mobile enabled websites to take advantage of shifting consumer behaviors. We expect revenue trends to remain positive in 2017.
- We continue to work to improve the website purchase experience for our customers by (1) helping our customers find the parts they want to buy by reducing failed searches and increasing user purchase confidence; (2) implementing guided navigation and custom buying experiences specific to strategic part names; and (3) increasing order size across our sites through improved recommendation engines. In addition, we intend to build mobile enabled features to take advantage of shifting consumer behaviors. These efforts may increase the conversion rate of our visitors to customers, the total number of orders and average order value, and the number of repeat purchases, as well as contribute to our revenue growth.
- We continue to work towards becoming one of the preferred low price options in the market for aftermarket auto parts and accessories. We also continue to offer lower prices by increasing foreign sourced private label products as they are generally less expensive and we believe provide better value for the consumer. We believe our product offering can improve the conversion rate of visitors to our websites, grow our revenues and improve our margins.
- We continue to increase product selection by being the first to market with many new SKUs. We currently have over 55,000 private label SKUs and over 1.0 million branded SKUs in our product selection. We will continue to seek to add new categories and expand our existing specialty categories. We believe continued product expansion will increase the total number of orders and contribute to our revenue growth. Additionally, we plan to continue to maintain certain in-stock inventory throughout the year to provide consistent service levels and improve customer experience.
- We continue to implement cost saving measures.

Overall, we expect revenue growth and increased net income in 2017 compared to 2016, due to the above initiatives we expect to continue to follow in 2017.

We have redesigned our approach to attracting customers through search engines with increased paid advertising which has helped us offset some of the decline in organic traffic to our e-commerce sites. We have also continued to pursue revenue opportunities in third-party online marketplaces, a number of which continue to grow each year. Auto parts buyers are finding third-party online marketplaces to be a very attractive environment, for many reasons, the top five being: (1) the security of their personal information; (2) the ability to easily compare product offerings from multiple sellers; (3) transparency (consumers can leave positive or negative feedback about their experience); (4) favorable pricing; and (5) the availability of products not found in stock at brick-and-mortar stores. Successful selling in these third-party online marketplaces depends on product innovation, and strong relationships with suppliers, both of which we believe to be our core competencies.

Adjusted EBITDA, which is not a Generally Accepted Accounting Principle measure, is presented because management uses it as one measure of the Company's operating performance, as it assists in comparing the Company's operating performance on a consistent basis by removing the impact of stock compensation expense, as well as items that are not expected to be recurring. Internally, this non-GAAP measure is also used by management for planning purposes, including the preparation of internal budgets; for allocating resources to enhance financial performance; and for evaluating the effectiveness of operational strategies. The Company also believes that analysts and investors use Adjusted EBITDA as a supplemental measure to evaluate the ongoing operations of companies in our industry. It should not be considered, however, as an alternative to operating income, or as an alternative to cash flows as a measure of the Company's overall liquidity. Further, the Adjusted EBITDA measure shown may not be comparable to similarly titled measures used by other companies. The table below reconciles net



income loss to Adjusted EBITDA for the periods presented (in thousands):

	<b>Fifty-two weeks ended December 31, 2016</b>		
	<b>Base USAP</b>	<b>AMD</b>	<b>Consolidated</b>
	<b>(In thousands)</b>		
Net sales	\$ 303,324	\$ 247	\$ 303,571
Cost of sales	211,277	12	211,289
Gross profit	92,047	235	92,282
Operating expenses:			
Marketing	41,104	2,451	43,555
General and administrative	17,629	278	17,907
Fulfillment	22,975	—	22,975
Technology	5,625	218	5,843
Amortization of intangible assets	449	33	482
Impairment loss on intangible assets	—	1,130	1,130
Total operating expenses	87,782	4,110	91,892
Income (loss) from operations	4,265	(3,875)	390
Other income (expense):			
Other income, net	46	—	46
Interest expense	(1,238)	—	(1,238)
Total other expense	(1,192)	—	(1,192)
Income (loss) before income taxes	3,073	(3,875)	(802)
Income tax (benefit) provision	100	(299)	(199)
Net income (loss)	\$ 2,973	\$ (3,576)	\$ (603)
Net income (loss)	\$ 2,973	\$ (3,576)	\$ (603)
Depreciation & amortization	6,351	1,159	7,510
Amortization of intangible assets	449	33	482
Interest expense, net	1,219	—	1,219
Taxes	100	(299)	(199)
EBITDA	\$ 11,092	\$ (2,683)	\$ 8,409
Stock comp expense	\$ 2,932	\$ 199	\$ 3,131
Impairment loss on intangible assets	—	1,130	1,130
Adjusted EBITDA	\$ 14,024	\$ (1,354)	\$ 12,670
Capital expenditures	5,414	939	6,353
Total assets, net of accumulated depreciation	78,094	4,040	82,134

**Fifty-two weeks ended January 2, 2016**

	<b>Base USAP</b>	<b>AMD</b>	<b>Consolidated</b>
	<b>(In thousands)</b>		
Net sales	\$ 290,833	\$ 258	\$ 291,091
Cost of sales	207,657	—	207,657
Gross profit	83,176	258	83,434
Operating expenses:			
Marketing	40,218	3,061	43,279
General and administrative	16,325	184	16,509
Fulfillment	20,237	—	20,237
Technology	4,833	167	5,000
Amortization of intangible assets	431	33	464
Total operating expenses	82,044	3,445	85,489
Income (loss) from operations	1,132	(3,187)	(2,055)
Other income (expense):			
Other income, net	36	—	36
Interest expense	(1,216)	—	(1,216)
Total other expense	(1,180)	—	(1,180)
Loss before income taxes	(48)	(3,187)	(3,235)
Income tax provision (benefit)	88	(899)	(811)
Net loss	\$ (136)	\$ (2,288)	\$ (2,424)
Net loss	\$ (136)	\$ (2,288)	\$ (2,424)
Depreciation & amortization	6,141	1,369	7,510
Amortization of intangible assets	431	33	464
Interest expense, net	1,208	—	1,208
Taxes	88	(899)	(811)
EBITDA	\$ 7,732	\$ (1,785)	\$ 5,947
Stock comp expense	\$ 2,297	\$ 122	\$ 2,419
Adjusted EBITDA	10,029	(1,663)	8,366
Capital expenditures	6,701	1,079	7,780
Total assets, net of accumulated depreciation	78,092	5,664	83,756

**Fifty-three weeks ended January 3, 2015**

	Base USAP	AMD	Consolidated
	(In thousands)		
Net sales	\$ 283,211	\$ 297	\$ 283,508
Cost of sales	205,058	—	205,058
Gross profit	78,153	297	78,450
Operating expenses:			
Marketing	39,574	2,434	42,008
General and administrative	16,697	4	16,701
Fulfillment	20,368	—	20,368
Technology	4,826	37	4,863
Amortization of intangible assets	422	—	422
Total operating expenses	81,887	2,475	84,362
Loss from operations	(3,734)	(2,178)	(5,912)
Other income (expense):			
Other income, net	65	—	65
Interest expense	(1,101)	—	(1,101)
Total other expense	(1,036)	—	(1,036)
Loss before income taxes	(4,770)	(2,178)	(6,948)
Income tax provision	137	1	138
Net loss	\$ (4,907)	\$ (2,179)	\$ (7,086)
Net loss	\$ (4,907)	\$ (2,179)	\$ (7,086)
Depreciation & amortization	7,230	1,693	8,923
Amortization of intangible assets	422	—	422
Interest expense, net	1,101	—	1,101
Taxes	137	1	138
EBITDA	\$ 3,983	\$ (485)	\$ 3,498
Stock comp expense	\$ 2,367	\$ 4	\$ 2,371
Inventory write-down related to Carson closure <sup>(1)</sup>	897	—	897
Restructuring costs <sup>(2)</sup>	1,137	—	1,137
Adjusted EBITDA	\$ 8,384	\$ (481)	\$ 7,903
Capital expenditures	4,237	1,319	5,556
Total assets, net of accumulated depreciation	74,414	8,493	82,907

- (1) As a result of the closure of the Carson warehouse, the Company reduced the sales price of certain inventory in an effort to reduce inventory levels. Additional charges were incurred related to inventory that was not deemed economical to transfer to the remaining warehouses. Refer to “*Note 12 – Restructuring Costs*” of our Notes to Consolidated Financial Statements for additional details.
- (2) We incurred restructuring costs related to our initiatives to reduce labor costs and improve operating efficiencies in response to the challenges in the marketplace and general market conditions. Refer to “*Note 12 – Restructuring Costs*” of our Notes to Consolidated Financial Statements for additional details.

## **Basis of Presentation**

*Net Sales.* Online and offline sales represent two different sales channels for our products. We generate online net sales primarily through the sale of auto parts to individual consumers through our network of e-commerce websites, online marketplace sales channels and online advertising. E-commerce sales are derived from our network of websites, which we own and operate. E-commerce and online marketplace sales also include inbound telephone sales through our call center that supports these sales channels. Online marketplaces consist primarily of sales of our products on online auction websites, where we sell through auctions as well as through storefronts that we maintain on third-party owned websites. We sell advertising and sponsorship positions on our e-commerce websites to highlight vendor brands and offer complementary products and services that benefit our customers. Advertising is targeted to specific sections of the websites and can also be targeted to specific users based on the vehicles they drive. Advertising partners primarily include part vendors, national automotive aftermarket brands and automobile manufacturers. Our offline sales channel represents our distribution of products directly to commercial customers by selling auto parts to collision repair shops. Our offline sales channel also includes both stock ship distribution as well as drop ship programs for automotive warehouse distributors and other online resellers. The product mix includes the majority of our private labeled stock ship items, which include the replacement collision parts and our Kool-Vue™ mirror line. We also serve consumers by operating a retail outlet store in LaSalle, Illinois.

*Cost of Sales.* Cost of sales consists of the direct costs associated with procuring parts from suppliers and delivering products to customers. These costs include direct product costs, outbound freight and shipping costs, warehouse supplies and warranty costs, partially offset by purchase discounts and cooperative advertising. Depreciation and amortization expenses are excluded from cost of sales and included in marketing, general and administrative and fulfillment expenses as noted below.

*Marketing Expense.* Marketing expense consists of online advertising spend, internet commerce facilitator fees and other advertising costs, as well as payroll and related expenses associated with our marketing catalog, customer service and sales personnel. These costs are generally variable and are typically a function of net sales. Marketing expense also includes depreciation and amortization expense and share-based compensation expense.

*General and Administrative Expense.* General and administrative expense consists primarily of administrative payroll and related expenses, merchant processing fees, legal and professional fees and other administrative costs. General and administrative expense also includes depreciation and amortization expense and share-based compensation expense.

*Fulfillment Expense.* Fulfillment expense consists primarily of payroll and related costs associated with our warehouse employees and our purchasing group, facilities rent, building maintenance, depreciation and other costs associated with inventory management and our wholesale operations. Fulfillment expense also includes share-based compensation expense.

*Technology Expense.* Technology expense consists primarily of payroll and related expenses of our information technology personnel, the cost of hosting our servers, communications expenses and Internet connectivity costs, computer support and software development amortization expense. Technology expense also includes share-based compensation expense.

*Amortization of Intangible Assets.* Amortization of intangibles consists of the amortization expense associated with our definite-lived intangible assets.

*Impairment Loss.* Impairment loss is recorded as a result of impairment testing performed for goodwill and indefinite-lived intangible assets in accordance with ASC 350 *Intangibles – Goodwill and Other, and long-lived assets*, including intangible assets subject to amortization, in accordance with ASC 360 *Property, Plant and Equipment*.

*Other Income, Net.* Other income, net consists of miscellaneous income or expense such as gains/losses from disposition of assets, and interest income comprised primarily of interest income on investments.

*Interest Expense.* Interest expense consists primarily of interest expense on our outstanding loan balance, deferred financing cost amortization and capital lease interest.

## **Segment Data**

The Company operates in two reportable segments identified as Base USAP, which is the core auto parts business, and AutoMD, an online automotive repair source which has closed down its *Insta-Quotes!* program subsequent to year end. Segment information is prepared on the same basis that our chief executive officer, who is our chief operating decision maker, manages the segments, evaluates financial results, and makes key operating decisions. Management evaluates the performance of its operating segments based on net sales, gross profit and loss from operations. The accounting policies of the operating segments are the same as those described in “*Note 1 - Summary of Significant Accounting Policies*” of our Notes to

Consolidated Financial Statements. Operating income represents earnings before other income, interest expense and income taxes. The identifiable assets by segment disclosed in this note are those assets specifically identifiable within each segment.

## Results of Operations

The following table sets forth selected statement of operations data for the periods indicated, expressed as a percentage of net sales:

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
Net sales	100.0 %	100.0 %	100.0 %
Cost of sales	69.6	71.3	72.3
Gross profit	30.4	28.7	27.7
Operating expenses:			
Marketing	14.3	14.9	14.8
General and administrative	5.9	5.7	5.9
Fulfillment	7.6	7.0	7.2
Technology	1.9	1.7	1.7
Amortization of intangible assets	0.2	0.2	0.1
Impairment loss on intangible assets	0.4	—	—
Total operating expenses	30.3	29.5	29.7
Income (loss) from operations	0.1	(0.8)	(2.0)
Other income (expense):			
Interest expense	(0.4)	(0.4)	(0.4)
Total other expense	(0.4)	(0.4)	(0.4)
Loss before income taxes	(0.3)	(1.2)	(2.4)
Income tax (benefit) provision	(0.1)	(0.3)	—
Net loss	(0.2)%	(0.9)%	(2.4)%

### *Fifty-Two Weeks Ended December 31, 2016 Compared to the Fifty-Two Weeks Ended January 2, 2016*

#### *Net Sales and Gross Margin*

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Net sales	\$ 303,571	\$ 291,091	\$ 12,480	4.3%
Cost of sales	211,289	207,657	3,632	1.7%
Gross profit	\$ 92,282	\$ 83,434	\$ 8,848	10.6%
Gross margin	30.4%	28.7%		1.7%

Net sales increased \$12,480, or 4.3%, for fiscal year 2016 compared to fiscal year 2015. Our net sales consisted of online sales, which include our e-commerce sites, online marketplace sales channels and online advertising, representing 91.0% of the total for fiscal year 2016 (compared to 90.9% in fiscal year 2015), and offline sales, representing 9.0% of the total for fiscal year 2016 (compared to 9.1% in fiscal year 2015). The net sales increase was due to an increase of \$11,395, or 4.3%, in online sales and a \$1,080, or 4.1%, increase in offline sales. Online sales increased primarily due to an increase in unique visitors, resulting in an increase in the number of orders.

Gross profit increased \$8,848, or 10.6%, in fiscal year 2016 compared to fiscal year 2015. Gross margin increased 1.7% to 30.4% in fiscal year 2016 compared to 28.7% in fiscal year 2015. Gross margin increased in fiscal year 2016 compared to fiscal year 2015 primarily due to a favorable mix shift of private label sales compared to last year as well as strategic pricing initiatives, freight efficiencies and lower shipping supply costs.

### Marketing Expense

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Marketing expense	\$ 43,555	\$ 43,279	\$ 276	0.6 %
Percent of net sales	14.3%	14.9%		(0.6)%

Total marketing expense increased \$276, or 0.6%, for fiscal year 2016 compared to fiscal year 2015. As a percent to net sales, total marketing expense was 14.3% for fiscal 2016 compared to 14.9% for fiscal year 2015. Online advertising expense, which includes catalog costs, was \$22,616, or 8.2%, of online sales for fiscal year 2016, compared to \$20,251, or 7.7%, of online sales for fiscal year 2015. Online advertising expense increased primarily due to increases in our non-catalog online advertising costs to \$21,198 or 7.0% of net sales for fiscal 2016 compared to \$18,524, or 6.4% of net sales for fiscal 2015. This increase relates primarily to the increase in the proportion of paid traffic compared to organic traffic. Marketing expense, excluding online advertising, was \$20,935, or 6.9%, of net sales for fiscal year 2016, compared to \$23,028, or 7.9%, of net sales for fiscal year 2015. The decrease was primarily due to a decrease in depreciation and amortization, overhead and labor cost.

### General and Administrative Expense

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
General and administrative expense	\$ 17,907	\$ 16,509	\$ 1,398	8.5%
Percent of net sales	5.9%	5.7%		0.2%

General and administrative expense increased \$1,398, or 8.5%, for fiscal year 2016 compared to fiscal year 2015. The increase for fiscal year 2016 as compared to fiscal year 2015 was primarily due to increased depreciation and amortization.

### Fulfillment Expense

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Fulfillment expense	\$ 22,975	\$ 20,237	\$ 2,738	13.5%
Percent of net sales	7.6%	7.0%		0.6

Fulfillment expense increased \$2,738, or 13.5%, for fiscal year 2016 compared to fiscal year 2015 and increased as a percent of sales primarily due to increased fixed and variable wages as well as increased depreciation and amortization.

### Technology Expense

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Technology expense	\$ 5,843	\$ 5,000	\$ 843	16.9%
Percent of net sales	1.9%	1.7%		0.2%

Technology expense increased \$843, or 16.9%, for fiscal year 2016 compared to fiscal year 2015. The increase was primarily due to higher computer support costs to support increased sales, as well as increased overhead.

### Amortization of Intangible Assets

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Amortization of intangible assets	\$ 482	\$ 464	\$ 18	3.9%
Percent of net sales	0.2%	0.2%		—%

Amortization of intangibles increased \$18, or 3.9% for fiscal 2016 compared to fiscal 2015. Amortization of intangible assets remained flat as a percent of net sales during fiscal 2016.

#### Impairment loss on Intangible Assets

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Impairment loss on intangible assets	\$ 1,130	\$ —	\$ 1,130	100.0%
Percent of net sales	0.4%	—%		0.4%

Impairment loss on intangible assets consists of a non-cash impairment charge during fiscal year 2016 in the amount of \$1,130, related to AutoMD Software. During fiscal 2015 there was no impairment loss on intangible assets. See further detail in "Note 1- Summary of Significant Accounting Policies and Nature of Operations", "Note 3 – Fair Value Measurements" and "Note 5- Intangible Assets, net" of the Notes to Consolidated Financial Statements included in Part IV, Item 15 of this report and under "Critical Accounting Policies and Estimates" section below.

#### Total Other Expense, Net

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Other expense, net	\$ (1,192)	\$ (1,180)	\$ 12	1.0%
Percent of net sales	(0.4)%	(0.4)%		—

Total other expense, net increased \$12, or 1.0%, for fiscal year 2016 compared to fiscal year 2015. Total other expense increased during fiscal year 2016 compared to fiscal year 2015 primarily due to increased costs due to a higher letters of credit balance. (See further detail in "Note 6 – Borrowings" of the Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report).

#### Income Tax Provision

	Fiscal Year Ended		\$ Change	% Change
	December 31, 2016	January 2, 2016		
	(in thousands)			
Income tax provision	\$ (199)	\$ (811)	\$ 612	(75.5)%
Percent of net sales	(0.1)%	(0.3)%		0.2 %

We have a full valuation allowance against our net deferred income tax assets due to our past history of operating losses. In fiscal years 2016 and 2015, we recorded an addition of \$579 and \$329, respectively, to our valuation allowance. Income tax benefit in 2016 and 2015 relate primarily to the change in the outside basis difference of the Company's investment in AutoMD (see below).

Income tax (benefit) provision differs from the amount that would result from applying the federal statutory rate as follows (in thousands):

	Fiscal Year Ended	
	December 31, 2016	January 2, 2016
Income tax at U.S. federal statutory rate	\$ (273)	\$ (1,100)
Share-based compensation	316	50
State income tax, net of federal tax effect	(559)	672
Foreign tax	20	(18)
Basis difference in subsidiary equity	(267)	(820)
Other	(15)	76
Change in valuation allowance	579	329
Effective income tax provision	\$ (199)	\$ (811)

Prior to 2012, the Company treated earnings of the foreign subsidiaries as permanently invested in that jurisdiction. As a result, no additional income tax withholding was provided on the possible future repatriation of these earnings to the parent company in prior years. During fiscal year 2012, based on current year operating and future cash flow needs the Company decided that it could no longer represent that these funds would be indefinitely reinvested in the foreign jurisdictions but that such funds may be needed for general corporate purposes. As a result, the Company recorded future withholding taxes which would be due if the funds are required to be repatriated. The Company intends to continue to pursue all reasonable means to increase its investment in the foreign jurisdictions as dictated by future growth in general business activities or as allowed by the foreign jurisdictions to avoid incurring the income tax withholding expense.

As of December 31, 2016, the Company had no material unrecognized tax benefits, interest or penalties related to federal and state income tax matters. At December 31, 2016, federal and state net operating loss ("NOL") carryforwards were \$75,261 and \$83,027, respectively. Federal NOL carryforwards of \$2,690 were acquired in the acquisition of WAG which are subject to Internal Revenue Code section 382 and limited to an annual usage limitation of \$135. Additionally, the tax benefit of \$41 of the federal and state NOL carryforwards which was created by the exercise of stock options will be credited to additional paid-in-capital once recognized. Federal NOL carryforwards began to expire in 2029, while state NOL carryforwards begin to expire in 2016. The amounts of State NOL's expiring in the next five years and thereafter are disclosed under *Income Taxes* in the *Critical Accounting Policies and Estimates* section below.

As a result of the October 8, 2014 sale of equity, AutoMD was not included in the consolidated state and federal tax filings of the Company for fiscal year 2016. For the fiscal year ended December 31, 2016, the effective tax rate for AutoMD was (7.7%). AutoMD's effective tax rate differs from the U.S. federal statutory rate primarily as a result of the recording of a \$1,183 valuation allowance against the Company's net deferred tax assets. At December 31, 2016, AutoMD had NOLs of approximately \$7,506 for federal tax purposes that begin to expire in 2031. These amounts are included in the consolidated figures presented above. AutoMD state NOLs were not material as of December 31, 2016.

#### ***Fifty-Two Weeks Ended January 2, 2016 Compared to the Fifty-Three Weeks Ended January 3, 2015***

##### *Net Sales and Gross Margin*

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
Net sales	\$ 291,091	\$ 283,508	\$ 7,583	2.7%
Cost of sales	207,657	205,058	2,599	1.3%
Gross profit	\$ 83,434	\$ 78,450	\$ 4,984	6.4%
Gross margin	28.7%	27.7%		1.0%

Net sales increased \$7,583, or 2.7%, for fiscal year 2015 compared to fiscal year 2014. Our net sales consisted of online sales, representing 90.9% of the total for fiscal year 2015 (compared to 90.7% in fiscal year 2014), and offline sales, representing 9.1% of the total for fiscal year 2015 (compared to 9.3% in fiscal year 2014). The net sales increase was due to an increase of \$7,561, or 2.9%, in online sales, and a \$21, or 0.1%, increase in offline sales. Online sales increased primarily due to improvement in conversion, resulting in a 1.5% increase in number of orders.

Gross profit increased \$4,984, or 6.4%, in fiscal year 2015 compared to fiscal year 2014. Gross margin increased 1.0% to 28.7% in fiscal year 2015 compared to 27.7% in fiscal year 2014. Gross margin primarily increased in fiscal year 2015



compared to fiscal year 2014 due a favorable mix shift of private label sales compared to last year as well as strategic pricing initiatives, freight efficiencies and lower shipping supply costs, partially offset by lower margin in our offline revenue. In addition, gross margin improved due to the unfavorable impact to fiscal 2014's margin as a result of the restructuring charges related to the distribution facility closure in Carson, California.

#### Marketing Expense

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
Marketing expense	\$ 43,279	\$ 42,008	\$ 1,271	3.0%
Percent of net sales	14.9%	14.8%		0.1%

Total marketing expense increased \$1,271, or 3.0%, for fiscal year 2015 compared to fiscal year 2014. As a percent to net sales, total marketing expense was 14.9% for fiscal 2015 compared to 14.8% for fiscal year 2014. Online advertising expense, which includes catalog costs, was \$20,251, or 7.7%, of online sales for fiscal year 2015, compared to \$18,485, or 7.2%, of online sales for fiscal year 2014. Online advertising expense increased primarily due to increases in our non-catalog online advertising costs to \$18,524 or 6.4% of net sales for fiscal 2015 compared to \$16,327, or 5.8% of net sales for fiscal 2014. This increase relates primarily to the increase in the proportion of paid traffic compared to organic traffic. Marketing expense, excluding online advertising, was \$23,028, or 7.9%, of net sales for fiscal year 2015, compared to \$23,523, or 8.3%, of net sales for fiscal year 2014. The decrease was primarily due to a decrease in depreciation and amortization, partially offset by increased overhead and labor cost.

#### General and Administrative Expense

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
General and administrative expense	\$ 16,509	\$ 16,701	\$ (192)	(1.1)%
Percent of net sales	5.7%	5.9%		(0.2)%

General and administrative expense decreased \$192, or 1.1%, for fiscal year 2015 compared to fiscal year 2014. The decrease for fiscal year 2015 as compared to fiscal year 2014 was primarily due to lower overhead costs.

#### Fulfillment Expense

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
Fulfillment expense	\$ 20,237	\$ 20,368	\$ (131)	(0.6)%
Percent of net sales	7.0%	7.2%		(0.2)%

Fulfillment expense decreased \$131, or 0.6%, for fiscal year 2015 compared to fiscal year 2014 and declined as a percent of sales primarily because 2014 included severance costs of \$414 and labor related and other restructuring charges of approximately \$145 associated with the closure of our Carson warehouse in 2014.

#### Technology Expense

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
Technology expense	\$ 5,000	\$ 4,863	\$ 137	2.8%
Percent of net sales	1.7%	1.7%		—%

Technology expense increased \$137, or 2.8%, for fiscal year 2015 compared to fiscal year 2014. The increase was primarily due to higher computer support costs to support increased sales, while technology expense remained flat to last year as a percent of sales.

#### *Amortization of Intangible Assets*

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
Amortization of intangible assets	\$ 464	\$ 422	\$ 42	10.0%
Percent of net sales	0.2%	0.1%		0.1%

Amortization of intangible assets increased by \$42, or 10.0%, for fiscal 2015 compared to fiscal 2014. The increase was primarily due to the purchase of intangible assets during fiscal 2015.

#### *Total Other Expense, Net*

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
Other expense, net	\$ (1,180)	\$ (1,036)	\$ 144	13.9%
Percent of net sales	(0.4)%	(0.4)%		—%

Total other expense, net increased \$144, or 13.9%, for fiscal year 2015 compared to fiscal year 2014. Total other expense increased during fiscal year 2015 compared to fiscal year 2014 primarily due to increased interest expense in respect of the borrowings under our credit facility. (See further detail in “*Note 6 – Borrowings*” of the Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report).

#### *Income Tax Provision*

	Fiscal Year Ended		\$ Change	% Change
	January 2, 2016	January 3, 2015		
	(in thousands)			
Income tax provision	\$ (811)	\$ 138	\$ (949)	(687.7)%
Percent of net sales	(0.3)%	—%		(0.3)%

We have a full valuation allowance against our net deferred income tax assets. In fiscal year 2015 and fiscal 2014, we recorded an addition of \$329 and \$2,366, respectively, to our income valuation allowance. Income tax benefit in 2015 is primarily due to federal statutory rate basis difference in subsidiary equity, partially offset by state income tax and change in valuation allowance.

## **Liquidity and Capital Resources**

#### *Sources of Liquidity*

During the fifty-two weeks ended December 31, 2016, we primarily funded our Base USAP operations with cash and cash equivalents generated from operations as well as through borrowing under our credit facility, and primarily funded our AutoMD operating segment using the cash investment from third-party investors. We had cash and cash equivalents of \$6,643 as of December 31, 2016, representing a \$1,106 increase from \$5,537 of cash and cash equivalents as of January 2, 2016. The cash increase was primarily due to cash provided by operating activities.

As of December 31, 2016, the Company had \$6,643 of cash and cash equivalents, including \$3,972 that was restricted to be used only for general operating purposes of AutoMD unless otherwise approved by AutoMD’s Board of Directors. Based on our current operating plan, we believe that our existing cash and cash equivalents, investments, cash flows from operations and available funds under our credit facility will be sufficient to finance both our Base USAP and AutoMD operating segments through at least the next twelve months (see “*Debt and Available Borrowing Resources*” and “*Funding Requirements*” below).

As of December 31, 2016, our credit facility provided for a revolving commitment of up to \$30,000 subject to a borrowing base derived from certain of our receivables, inventory and property and equipment. (see “*Debt and Available Borrowing Resources*” below).

In August 2014, we filed a shelf registration statement covering the offer and sale of up to \$100,000 of common stock with the SEC. The shelf registration was declared effective by the SEC on August 20, 2014. The terms of any offering under our shelf registration statement will be determined at the time of the offering and disclosed in a prospectus supplement filed with the SEC. The shelf registration expires on August 20, 2017. Refer to “*Note 7 – Stockholders’ Equity and Share-Based Compensation*” of our Notes to Consolidated Financial Statements included in Part I, Item 1 of this report for additional details.

On October 8, 2014, AutoMD entered into a common stock purchase agreement to sell seven million shares of AutoMD common stock at a purchase price of \$1.00 per share to third party investors. On October 19, 2016, the Company purchased two million shares of AutoMD common stock at a purchase price of \$1.00 per share pursuant to its funding milestone obligation under the common stock purchase agreement. In addition, on January 26, 2017, AutoMD entered into a redemption agreement with third-party investors to redeem an aggregate of 5.0 million shares of AutoMD common stock for a purchase price of \$1,292. On March 6, 2017, following a review of various business and strategic options, AutoMD entered into a dissolution agreement with its two remaining minority stockholders pursuant to which the Company repurchased the remaining shares of common stock from minority stockholders for a purchase price of \$1,194 in consideration for terminating the prior investor agreements. Following the redemptions, AutoMD filed for dissolution and all of the remaining assets of AutoMD will be distributed to the Company, except for certain cash reserved for creditors of AutoMD. The Company estimates that AutoMD will incur approximately \$2.1 million in charges related to severance and other contractual obligations that could impact cash during the first quarter of fiscal 2017.

#### *Working Capital*

As of December 31, 2016 and January 2, 2016, our working capital was \$16,869 and \$13,605, respectively. Our revolving loan does not require principal payments, however it is classified as current due to certain U.S. GAAP requirements (see “*Debt and Available Borrowing Resources*” below for further details). The historical seasonality in our business during the year can cause cash and cash equivalents, inventory and accounts payable to fluctuate, resulting in changes in our working capital.

#### *Cash Flows*

The following table summarizes the key cash flow metrics from our consolidated statements of cash flows for fiscal year 2016, 2015 and 2014, respectively (in thousands):

	<b>Fiscal Year Ended</b>		
	<b>December 31, 2016</b>	<b>January 2, 2016</b>	<b>January 3, 2015</b>
Net cash provided by operating activities	\$ 21,571	\$ 5,745	\$ 1,243
Net cash used in investing activities	(6,477)	(7,792)	(5,730)
Net cash (used in) provided by financing activities	(13,954)	(105)	11,311
Effect of exchange rate changes on cash	(34)	36	11
Net increase (decrease) in cash and cash equivalents	<u>\$ 1,106</u>	<u>\$ (2,116)</u>	<u>\$ 6,835</u>

#### *Operating Activities*

Cash provided by operating activities is primarily comprised of net loss, adjusted for non-cash activities such as depreciation and amortization expense, amortization of intangible assets, impairment losses and share-based compensation expense. These non-cash adjustments represent charges reflected in net income and, therefore, to the extent that non-cash items increase or decrease our operating results, there will be no corresponding impact on our cash flows. Net loss adjusted for non-cash adjustments to operating activities was \$10,891 (adjusted for non-cash charges primarily consisting of depreciation and amortization expense of \$7,510) for the period ended December 31, 2016 compared to \$7,134 (adjusted for non-cash charges primarily consisting of depreciation and amortization expense of \$7,510) for the period ended January 2, 2016. After excluding the effects of the non-cash charges, the primary changes in cash flows relating to operating activities resulted from changes in operating assets and liabilities.

- Accounts receivable increased to \$3,266 at December 31, 2016 from \$3,236 at January 2, 2016, resulting in an increase in operating assets and reflecting a cash outflow of \$30 for the fiscal year ended December 31, 2016. Accounts receivable increased primarily due to decreases in trade and credit card receivables due related to timing of collections during the year end holiday season. Accounts receivable decreased to \$3,236 at January 2, 2016 from \$3,804 at January 3, 2015, resulting in a decrease in operating assets and reflecting a cash inflow of \$568 for the fiscal year ended January 2, 2016. Accounts receivable decreased primarily due to decreases in trade and credit card receivables due related to timing of collections during the year end holiday season.
- Inventory decreased to \$50,904 at December 31, 2016 from \$51,216 at January 2, 2016, resulting in a decrease in operating assets and reflecting a cash inflow of \$312 for the fiscal year ended December 31, 2016. Inventory increased to \$51,216 at January 2, 2016 from \$48,362 at January 3, 2015, resulting in an increase in operating assets and reflecting a cash outflow of \$2,854 for the fiscal year ended January 2, 2016.
- Accounts payable and accrued expenses increased to \$40,557 at December 31, 2016 compared to \$32,790 at January 2, 2016 resulting in an increase in operating liabilities and reflecting a cash inflow of \$7,767 for the fiscal year ended December 31, 2016. Accounts payable and accrued expenses increased primarily due to an increase in accounts payable of \$8,174, partially offset by a decrease in accrued expenses of \$407. Accounts payable and accrued expenses decreased to \$32,790 at January 2, 2016 compared to \$33,109 at January 3, 2015 resulting in a decrease in operating liabilities and reflecting a cash outflow of \$319 for the fiscal year ended January 2, 2016. Accounts payable and accrued expenses decreased primarily due to the decrease in accrued expenses of \$480, partially offset by an increase in accounts payable of \$161.
- Other current liabilities increased to \$1,972 at December 31, 2016 compared to \$1,276 at January 2, 2016, resulting in an increase in operating liabilities and reflecting a cash inflow of \$696 for the fiscal year ended December 31, 2016. Other current liabilities increased primarily due to an increase in deferred warranty revenues. Other current liabilities increased to \$1,276 at January 2, 2016 compared to \$3,505 at January 3, 2015, resulting in an increase in operating liabilities and reflecting a cash inflow of \$349 for the fiscal year ended January 2, 2016. Other current liabilities increased due to an increase in customer deposits.

#### *Investing Activities*

For the fiscal years ended December 31, 2016, January 2, 2016 and January 3, 2015, net cash used in investing activities was primarily the result of increases in property and equipment (\$6,353, \$7,780 and \$5,556 respectively). Property and equipment is primarily internally developed software. Capitalized costs include amounts directly related to website and software development, primarily payroll and payroll related costs for employees and outside contractors who are directly associated with and devote time to the internal use software project. We expect our capital expenditures to be flat or slightly higher in fiscal 2017 compared to fiscal 2016.

#### *Financing Activities*

For the fiscal year ended December 31, 2016, net cash used in financing activities was primarily due to the net payments made on debt, totaling \$11,758. For the fiscal year ended January 2, 2016, net cash used in financing activities was primarily due to primarily due to the payments made on debt, totaling \$14,900. (see further discussion in "*Debt and Available Borrowing Resources*" below).

For the fiscal year ended January 3, 2015, net cash provided by financing activities was primarily due to gross proceeds of \$7,000 received from the sale of 35.9% of AutoMD's outstanding common stock and the net draws made on debt, totaling \$4,248.

#### *Debt and Available Borrowing Resources*

Total debt was \$10,312 as of December 31, 2016 (comprised of capital lease payable), compared to \$22,448 (comprised of capital lease payable and revolving loan payable) as of January 2, 2016. The decrease was primarily due to a reduction in the amount outstanding under our credit facility from January 2, 2016 to December 31, 2016, as further described below.

The Company maintains an asset-based revolving credit facility ("Credit Facility") that provides for, among other things, a revolving commitment in an aggregate principal amount of up to \$30,000, which is subject to a borrowing base derived from certain receivables, inventory and property and equipment. At December 31, 2016, our outstanding revolving loan balance was \$0. The customary events of default under the Credit Facility (discussed below) include certain subjective acceleration clauses. Management has determined the likelihood of an acceleration is more than remote, considering the recurring losses experienced by the Company. As a result, any outstanding borrowings under the Credit Facility would be classified as a current liability.

On November 15, 2016, the Company and JPMorgan Chase Bank, N.A. (“JPMorgan”) entered into the Tenth Amendment to Credit Agreement and Third Amendment to Pledge and Security Agreement (the “Amendment”), which amended the Credit Agreement previously entered into by the Company, certain of its domestic subsidiaries and JPMorgan on April 26, 2012 (as amended, the “Credit Agreement”) and the Pledge and Security Agreement previously entered into by the Company, certain of its domestic subsidiaries and JPMorgan on April 26, 2012. Pursuant to the Amendment, letters of credit can be issued if after giving effect to such issuance, the letters of credit exposure shall not exceed \$20,000, which was an increase from the previously agreed upon \$15,000. As of December 31, 2016, our outstanding letters of credit balance was \$11,658.

The following amendments to the Credit Agreement and Security Agreement were also made under the Tenth Amendment:

- The aggregate principal amount of indebtedness that is permitted related to capital leases was increased from \$2,000 to \$3,500.
- The Company’s letters of credit exposure was increased from \$15,000 to \$20,000.
- Under the terms of the Security Agreement, cash receipts are deposited into a lock-box, which are at the Company’s discretion unless the “cash dominion period” is in effect, during which cash receipts will be used to reduce amounts owing under the Credit Agreement. The cash dominion period is triggered in an event of default or if excess availability is less than the \$3,600 for three consecutive business days, and will continue until, during the preceding 60 consecutive days, no event of default existed and excess availability has been greater than \$3,600 at all times (with the trigger subject to adjustment based on the Company’s revolving commitment).
- The Company’s required excess availability related to the “Covenant Testing Trigger Period” (as defined under the Credit Agreement) under the revolving commitment under the Credit Agreement is less than \$2,400 for the period commencing on any day that excess availability is less than \$2,400 for three consecutive business days, and continuing until excess availability has been greater than or equal to \$2,400 at all times for 45 consecutive days (with the trigger subject to adjustment based on the Company’s revolving commitment).
- The trigger, requiring the Company to provide certain reports under the Credit Agreement, relating to excess availability under the revolving commitment under the Credit Agreement is less than \$3,600 for the period commencing on any day that excess availability is less than \$3,600 for three consecutive business days, and continuing until excess availability has been greater than or equal to \$3,600 at all times for 45 consecutive days (with the trigger subject to adjustment based on the Company’s revolving commitment).

Loans drawn under the credit facility bear interest at a per annum rate equal to either (a) LIBOR plus an applicable margin of 1.25%, or (b) a “base rate” subject to an increase or reduction by up to 0.25% per annum based on the Company’s fixed charge coverage ratio. At December 31, 2016, the Company’s LIBOR based interest rate was 2.06% (on \$0 principal) and the Company’s prime based rate was 3.50% (on \$0 principal). A commitment fee, based upon undrawn availability under the Credit Facility bearing interest at a rate of 0.25% per annum, is payable monthly.

Certain of the Company’s domestic subsidiaries are co-borrowers (together with the Company, the “Borrowers”) under the Credit Agreement, and certain other domestic subsidiaries are guarantors (the “Guarantors” and, together with the Borrowers, the “Loan Parties”) under the Credit Agreement. The Borrowers and the Guarantors are jointly and severally liable for the Borrowers’ obligations under the Credit Agreement. The Loan Parties’ obligations under the Credit Agreement are secured, subject to customary permitted liens and certain exclusions, by a perfected security interest in (a) all tangible and intangible assets and (b) all of the capital stock owned by the Loan Parties (limited, in the case of foreign subsidiaries, to 65% of the capital stock of such foreign subsidiaries). The Borrowers may voluntarily prepay the loans at any time. The Borrowers are required to make mandatory prepayments of the loans (without payment of a premium) with net cash proceeds received upon the occurrence of certain “prepayment events,” which include certain sales or other dispositions of collateral, certain casualty or condemnation events, certain equity issuances or capital contributions, and the incurrence of certain debt.

The Credit Agreement contains customary representations and warranties and customary affirmative and negative covenants applicable to the Company and its subsidiaries, including, among other things, restrictions on indebtedness, liens, fundamental changes, investments, dispositions, prepayment of other indebtedness, mergers, and dividends and other distributions.

Events of default under the Credit Agreement include: failure to timely make payments due under the Credit Agreement; material misrepresentations or misstatements under the Credit Agreement and other related agreements; failure to comply with covenants under the Credit Agreement and other related agreements; certain defaults in respect of other material indebtedness; insolvency or other related events; certain defaulted judgments; certain ERISA-related events; certain security interests or liens under the loan documents cease to be, or are challenged by the Company or any of its subsidiaries as not being, in full force and

effect; any loan document or any material provision of the same ceases to be in full force and effect; and certain criminal indictments or convictions of any Loan Party. As of December 31, 2016, the Company was in compliance with all covenants under the Credit Agreement.

Our Credit Facility requires us to satisfy certain financial covenants which could limit our ability to react to market conditions or satisfy extraordinary capital needs and could otherwise restrict our financing and operations. If we are unable to satisfy the financial covenants and tests at any time, we may as a result cease being able to borrow under the Credit Facility or be required to immediately repay loans under the Credit Facility, and our liquidity and capital resources and ability to operate our business could be severely impacted, which would have a material adverse effect on our financial condition and results of operations. In those events, we may need to sell additional assets or seek additional equity or additional debt financing or attempt to modify our existing Credit Agreement. There can be no assurance that we would be able to raise such additional financing or engage in such asset sales on acceptable terms, or at all, or that we would be able to modify our existing Credit Agreement.

As of December 31, 2016, the Company had total capital leases payable of \$10,312. The present value of the net minimum payments on capital leases as of December 31, 2016 is as follows:

Total minimum lease payments	\$ 17,947
Less amount representing interest	(7,635)
Present value of net minimum lease payments	<u>10,312</u>
Current portion of capital leases payable	542
Capital leases payable, net of current portion	<u>\$ 9,770</u>

See additional information in “*Note 6 – Borrowings*” of the Notes to Consolidated Financial Statements included in Part IV, Item 15 of this report.

#### *Funding Requirements*

Based on our current operating plan, we believe that our existing cash, cash equivalents, investments, cash flows from operations and available debt financing will be sufficient to finance our operational cash needs through at least the next twelve months. Our future capital requirements may, however, vary materially from those now planned or anticipated. Changes in our operating plans, lower than anticipated net sales or gross margins, increased expenses, continued or worsened economic conditions, worsening operating performance by us, or other events, including those described in “*Risk Factors*” included in Part II, Item 1A may force us to sell additional assets and seek additional debt or equity financing in the future. We may need to issue additional common stock under our shelf registration, discussed above. There can be no assurance that we would be able to raise such additional financing or engage in such additional asset sales on acceptable terms, or at all. If we are not able to raise adequate additional financing or proceeds from additional asset sales, we will need to defer, reduce or eliminate significant planned expenditures, restructure or significantly curtail our operations.

#### **Off-Balance Sheet Arrangements**

We have no significant off-balance sheet arrangements.

#### **Contractual Obligations**

The following table sets forth our contractual cash obligations and commercial commitments as of December 31, 2016:

<u>Contractual Obligations:</u>	<u>Payment Due By Period (in thousands)</u>				
	<u>Total</u>	<u>Less than 1 year</u>	<u>1-3 years</u>	<u>3-5 years</u>	<u>More than 5 years</u>
Operating lease obligations <sup>(1)</sup>	4,696	1,453	2,693	550	—
Capital lease obligations <sup>(2)</sup>	17,947	1,285	2,623	2,091	11,948

- (1) Commitments under operating leases relate primarily to our leases on our principal facility in Carson, California, our distribution centers in Chesapeake, Virginia and La Salle, Illinois, and our call center in the Philippines.
- (2) Commitments under capital leases include the lease for our LaSalle distribution facility and equipment lease agreements which include interest.

## Seasonality

We believe our business is subject to seasonal fluctuations. We have historically experienced higher sales of collision parts in winter months when inclement weather and hazardous road conditions typically result in more automobile collisions. Engine parts and performance parts and accessories have historically experienced higher sales in the summer months when consumers have more time to undertake elective projects to maintain and enhance the performance of their automobiles and the warmer weather during that time is conducive for such projects. We expect the historical seasonality trends to continue to have a material impact on our financial condition and results of operations during the reporting periods in any given year.

## Inflation

Inflation has not had a material impact upon our operating results, and we do not expect it to have such an impact in the near future. We cannot assure you that our business will not be affected by inflation in the future.

## Recent Accounting Pronouncements

See “*Note 1 – Summary of Significant Accounting Policies and Nature of Operations*” of the Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report.

## Critical Accounting Policies and Estimates

Our consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of our financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, net sales, costs and expenses, as well as the disclosure of contingent assets and liabilities and other related disclosures. On an ongoing basis, we evaluate our estimates, including, but not limited to, those related to revenue recognition, uncollectible receivables, inventory, valuation of deferred tax assets and liabilities, intangible and other long-lived assets and contingencies. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about carrying values of our assets and liabilities that are not readily apparent from other sources. Actual results could differ from those estimates, and we include any revisions to our estimates in our results for the period in which the actual amounts become known.

We believe the critical accounting policies described below affect the more significant judgments and estimates used in the preparation of our consolidated financial statements. Accordingly, these are the policies we believe are the most critical to aid in fully understanding and evaluating our historical consolidated financial condition and results of operations:

*Revenue Recognition.* We recognize revenue from product sales and shipping revenues, net of promotional discounts and return allowances, when the following four revenue recognition criteria are met: persuasive evidence of an arrangement exists, both title and risk of loss or damage have transferred, the selling price is fixed or determinable, and collectability is reasonably assured. The Company retains the risk of loss or damage during transit, therefore, revenue from product sales is recognized at the delivery date to the customer. Return allowances, which reduce product revenue by the Company’s best estimate of expected product returns, are estimated using historical experience.

Revenue from sales of advertising is recorded when performance requirements of the related advertising program agreement are met.

We evaluate the criteria of ASC 605-45 *Revenue Recognition Principal Agent Considerations* in determining whether it is appropriate to record the gross amount of product sales and related costs or the net amount earned as commissions. Generally, when the Company is the primary party obligated in a transaction, the Company is subject to inventory risk, has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, revenue is recorded at gross.

Payments received prior to the delivery of goods to customers are recorded as deferred revenue.

We periodically provide incentive offers to our customers to encourage purchases. Such offers include current discount offers, such as percentage discounts off of current purchases and other similar offers. Current discount offers, when accepted by our customers, are treated as a reduction to the sales price of the related transaction.

Sales discounts are recorded in the period in which the related sale is recognized. Sales return allowances are estimated based on historical amounts and are recorded upon recognizing the related sales. Credits are issued to customers for returned products.

*Fair Value Measurements.* We account for fair value measurements in accordance with ASC Topic 820 - *Fair Value Measurements and Disclosures* (“ASC 820”), which defines fair value, provides a framework for measuring fair value and provides the disclosure requirements for fair value measurements. ASC 820 also establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1 - defined as observable inputs such as quoted prices in active markets; Level 2 - defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3 - defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

*Inventory.* Inventory consists of finished goods available-for-sale. We purchase inventory from suppliers both domestically and internationally, primarily in Taiwan and China. We believe that our products are generally available from more than one supplier, and we maintain multiple sources for many of our products, both internationally and domestically. We offer a broad line of auto parts for automobiles, trucks, motorcycles and recreational vehicles from model years 1965 to 2016. Because of the continued demand for our products, we primarily purchase products in bulk quantities to take advantage of quantity discounts and to ensure inventory availability.

Inventory is accounted for using the first-in first-out (“FIFO”) method and valued at the lower of cost or market value. During this valuation, we are required to make judgments about expected disposition of inventory, generally, through sales, returns to product vendors, or liquidations of obsolete or scrap products, and expected recoverable values of each disposition category based on currently-available information. If actual market conditions are less favorable than those anticipated by management, additional write-down of the value of our inventory may be required.

*Website and Software Development Costs.* We capitalize certain costs associated with software developed for internal use according to ASC Topic 350-40- *Intangibles – Goodwill and Other – Internal-Use Software* (“ASC 350-40”), and ASC Topic 350-50- *Intangibles – Goodwill and Other – Website Development Costs* (“ASC 350-50”). Under these provisions, we capitalize costs associated with website development and software developed for internal use when both the preliminary project design and testing stage are completed and management has authorized further funding for the project, which it deems probable of completion and to be used for the function intended. Capitalized costs include amounts directly related to website development and software development such as payroll and payroll-related costs for employees who are directly associated with, and who devote time to, the internal-use software project. Capitalization of these costs ceases when the project is substantially complete and ready for its intended use. These amounts are amortized on a straight-line basis over two to three years once the software is placed into service.

*Long-Lived Assets and Intangibles.* We acquire tangible and intangible assets in the normal course of business. We evaluate the recoverability of the carrying amount of these long-lived assets whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable in accordance with ASC Topic 360- *Property, Plant, and Equipment* (“ASC 360”). Management assesses potential impairments whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. An impairment loss will result when the carrying value exceeds the undiscounted cash flows estimated to result from the use and eventual disposition of the asset. We continually use judgment when applying these impairment rules to determine the timing of the impairment tests, undiscounted cash flows used to assess impairments, and the fair value of a potentially impaired asset. The reasonableness of our judgments could significantly affect the carrying value of our long-lived assets. During the fourth quarter of 2016, the Company recognized an impairment loss on intangible assets of \$1,130 related to the impairment of AutoMD Software. During fiscal years 2015 and 2014 no adverse events related to the Company's financial performance were identified which would have indicated property and equipment and intangibles subject to amortization may not be recoverable.

*Income Taxes.* The Company accounts for income taxes in accordance with ASC Topic 740 - *Income Taxes* (“ASC 740”). Under ASC 740, deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. When appropriate, a valuation reserve is established to reduce deferred tax assets, which include tax credits and loss carry forwards, to the amount that is more likely than not to be realized. The ability to realize deferred tax assets depends on the ability to generate sufficient taxable income within the carryback or carryforward periods provided for in the tax law for each applicable tax jurisdiction. We consider the following possible sources of taxable income when assessing the realization of our deferred tax assets:

- Future reversals of existing taxable temporary differences;
- Future taxable income exclusive of reversing temporary differences and carryforwards;
- Taxable income in prior carryback years; and
- Tax-planning strategies.



The assessment regarding whether a valuation allowance is required or should be adjusted also considers, among other matters, the nature, frequency and severity of recent losses, forecasts of future profitability, the duration of statutory carryforward periods, our experience with tax attributes expiring unused and tax planning alternatives. In making such judgments, significant weight is given to evidence that can be objectively verified.

Concluding that a valuation allowance is not required is difficult when there is significant negative evidence that is objective and verifiable, such as cumulative losses in recent years. We utilized a three-year analysis of actual results as the primary measure of cumulative losses in recent years. However, because a substantial portion of those cumulative losses relate to impairment of intangible assets and goodwill, those three-year cumulative results are adjusted for the effect of these items. In addition, the near- and medium-term financial outlook is considered when assessing the need for a valuation allowance.

The valuation of deferred tax assets requires judgment and assessment of the future tax consequences of events that have been recorded in the financial statements or in the tax returns, and our future profitability represents our best estimate of those future events. Changes in our current estimates, due to unanticipated events or otherwise, could have a material effect on our financial condition and results of operations. Due to our combined cumulative three-year adjusted loss position, it was determined that it was not more likely than not that we would realize our net deferred tax assets. As of January 3, 2015, the valuation allowance was \$45,867, after recording an additional valuation allowance of \$2,358 in fiscal year 2014. As of January 2, 2016, the valuation allowance was \$46,196, after recording an additional valuation allowance of \$329 in fiscal year 2015. As of December 31, 2016, the valuation allowance was \$46,775, after recording an additional valuation allowance of \$579 in fiscal year 2016.

Over the past twelve quarters the Company has been in a position of overall cumulative losses however, there is a possibility that sometime next year we will be able to demonstrate overall cumulative income in the trailing twelve quarters. While this factor does not in and of itself indicate that the valuation allowance or a portion of the allowance should be removed, it is an indicator that needs to be considered in the evaluation of the valuation allowance. Other factors will also need to be assessed including the future projections of taxable income and the Company's ability to accurately project such taxable income. As such, the Company will be continuously reassessing the appropriateness of releasing the valuation allowance.

As of December 31, 2016, federal and state NOL carryforwards were \$75,261 and \$83,027, respectively. Federal NOL carryforwards of \$2,690 were acquired in the acquisition of WAG which are subject to Internal Revenue Code section 382 and limited to an annual usage limitation of \$135. Federal NOL carryforwards begin to expire in 2029, while state NOL carryforwards begin to expire in 2017. The state NOL carryforwards expire in the respective tax years as follows (in thousands):

	2017	\$	6,930
	2018		1,132
	2019		7,646
	2020		2,121
	2021		4,050
Thereafter			61,148
		\$	<u>83,027</u>

We utilize a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount which is more than 50% likely of being realized upon ultimate settlement. We consider many factors when evaluating and estimating our tax positions and tax benefits, which may require periodic adjustments and which may not accurately forecast actual outcomes. As of December 31, 2016, we had no material unrecognized tax benefits, interest or penalties related to federal and state income tax matters. The Company's policy is to record interest and penalties as income tax expense.

We are subject to U.S. federal income tax as well as income tax of foreign and state tax jurisdictions. The tax years 2012-2015 remain open to examination by the major taxing jurisdictions to which the Company is subject, except the Internal Revenue Service for which the tax years 2013-2015 remain open. The Company does not anticipate a significant change to the amount of unrecognized tax benefits within the next twelve months.

*Share-Based Compensation.* We account for share-based compensation in accordance with ASC Topic 718- *Compensation – Stock Compensation* ("ASC 718"). ASC 718 requires that all share-based compensation to employees, including grants of employee stock options, be recognized in our financial statements based on their respective grant date fair

values. Under this standard, the fair value of each share-based payment award is estimated on the date of grant using an option pricing model that meets certain requirements. We currently use the Black-Scholes option pricing model to estimate the fair value of our share-based payment awards. The Black-Scholes valuation models require extensive use of accounting judgment and financial estimates, including estimates of the expected term participants will retain their vested stock options before exercising them, the estimated volatility of our common stock price over the expected term and the number of options that will be forfeited prior to the completion of their vesting requirements. Application of alternative assumptions could produce significantly different estimates of the fair value of share-based compensation and, consequently, the related amount of share-based compensation expense recognized in the Consolidated Statements of Comprehensive Operations could have been significantly different than the amounts recorded.

The Company has incorporated its own historical volatility into the grant-date fair value calculations. The Company's historical volatility was not materially different than the estimates applied to past award fair value calculations. The expected term of an award is based on combining historical exercise data with expected weighted time outstanding. Expected weighted time outstanding is calculated by assuming the settlement of outstanding awards is at the midpoint between the remaining weighted average vesting date and the expiration date. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures significantly differ from those estimates. The Company considers many factors when estimating expected forfeitures, including employee class, economic environment, and historical experience.

The Company accounts for equity instruments issued in exchange for the receipt of services from non-employee directors in accordance with the provisions of ASC 718. The Company accounts for equity instruments issued in exchange for the receipt of goods or services from other than employees in accordance with ASC 505-50 - *Equity-Based Payments to Non-Employees*. Costs are measured at the estimated fair market value of the consideration received or the estimated fair value of the equity instruments issued, whichever is more reliably measurable. The value of equity instruments issued for consideration other than employee services is determined on the earlier of a performance commitment or completion of performance by the provider of goods or services. Equity instruments awarded to non-employees are periodically re-measured as the underlying awards vest unless the instruments are fully vested, immediately exercisable and non-forfeitable on the date of grant.

#### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

*Market Risk.* Market risk represents the risk of loss that may impact our financial position, results of operations or cash flows due to adverse changes in financial commodity market prices and rates. We are exposed to market risk primarily in the area of changes in U.S. interest rates and conditions in the credit markets. We also have some exposure related to foreign currency fluctuations. Under our current policies, we do not use interest rate derivative instruments to manage exposure to interest rate changes. We do not have any derivative financial instruments as of December 31, 2016. We attempt to increase the safety and preservation of our invested principal funds by limiting default risk, market risk and reinvestment risk. We mitigate default risk by investing in investment grade securities and mutual funds that hold debt securities.

*Interest Rate Risk.* Our investment securities generally consist of mutual funds. As of December 31, 2016, our investments were comprised of \$30 of investments in mutual funds that primarily hold debt securities.

As of December 31, 2016, we had a \$0 outstanding balance under a revolving loan under our credit facility. The interest rate on this loan is computed based on a LIBOR and Prime loan rate, adjusted by features specified in our loan agreement. At our debt level as of December 31, 2016, a 100 basis point increase in interest rates would not materially affect our earnings and cash flows. If, however, we are unable to meet the covenants in our loan agreement, we would be required to renegotiate the terms of credit under the loan agreement, including the interest rate. There can be no assurance that any renegotiated terms of credit would not materially impact our earnings. At December 31, 2016, our LIBOR based interest rate was 2.06% per annum (on \$0 principal) and our Prime based rate was 3.50% per annum (on \$0 principal). Refer to additional discussion in Item 7, under the caption "*Liquidity and Capital Resources – Debt and Available Borrowing Resources*" and in "*Note 6 – Borrowings*" of the Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report.

*Foreign Currency Risk.* Our purchases of auto parts from our Asian suppliers are denominated in U.S. dollars; however, a change in the foreign currency exchange rates could impact our product costs over time. Our financial reporting currency is the U.S. dollar and changes in exchange rates significantly affect our reported results and consolidated trends. For example, if the U.S. dollar weakens year-over-year relative to currencies in our international locations, our consolidated gross profit would be lower and operating expenses would be higher than if currencies had remained constant. Likewise, if the U.S. dollar strengthens year-over-year relative to currencies in our international locations, our consolidated gross profit would be higher and operating expenses would be lower than if currencies had remained constant. Our operating expenses in the Philippines are generally paid in Philippine Pesos, and as the exchange rate fluctuates, it adversely or favorably impacts our operating results. In light of the above, a fluctuation of 10% in the Peso/U.S. dollar exchange rate would have approximately a \$1.0 million impact on our Philippine operating expenses for the fifty-two weeks ended December 31, 2016. During fiscal 2014 we hedged

a portion of our forecasted foreign currency exposure associated with operating expenses incurred in the Philippines. The use of such hedging activities may not offset any or more than a portion of the adverse financial effects of unfavorable movements in foreign exchange rates over the limited time the hedges are in place. As of December 31, 2016, we had no hedges in place. We are evaluating our options on how to manage this risk and considering various methods to mitigate such risk. Our Canadian website sales are denominated in Canadian dollars; however, fluctuations in exchange rates from these operations are only expected to have a nominal impact on our operating results due to the relatively small number of sales generated in Canada. We believe it is important to evaluate our operating results and growth rates before and after the effect of currency changes.

## **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The financial statements required by this Item 8 are set forth in Part IV, Item 15 of this report and are hereby incorporated into this Item 8 by reference.

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

None.

## **ITEM 9A. CONTROLS AND PROCEDURES**

### **Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures designed to provide reasonable assurance that information required to be disclosed in reports filed with the SEC under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the specified time periods, and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2016 pursuant to Rule 13a-15 and 15d-15 of the Exchange Act. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of such date, our disclosure controls and procedures were effective to meet the objectives for which they were designed and operated at the reasonable assurance level.

### **Management's Report on Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). We assessed the effectiveness of our internal control over financial reporting as of December 31, 2016, based on the "Internal Control — Integrated Framework (2013)" issued by the Committee of Sponsoring Organizations of the Treadway Commission. This assessment was conducted utilizing our documentation of policies and procedures, risk control matrices, gap analysis, key process walk-throughs and management's knowledge of and interaction with its controls and testing of our key controls.

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

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. Based on such assessment and criteria, management has concluded that the internal controls over financial reporting were effective, and were operating at the reasonable assurance level as of December 31, 2016.

### **Changes in Internal Control Over Financial Reporting**

The Company monitors and evaluates on an ongoing basis its internal control over financial reporting in order to improve its overall effectiveness. In the course of these evaluations, the Company modifies and refines its internal processes as conditions warrant. As required by Rule 13a-15(d), the Company's management, including the Chief Executive Officer and the Chief Financial Officer, also conducted an evaluation of the Company's internal control over financial reporting to determine whether any changes occurred during the quarter ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Based on that evaluation, there has been no such change during the period covered by this report.

**ITEM 9B. OTHER INFORMATION**

On March 6, 2017, AutoMD entered into a dissolution agreement with each of Oak Investment Partners XI, Limited Partnership (“Oak”) and the Sol Khazani Living Trust (the “Trust”), pursuant to which AutoMD redeemed 1.5 million and 0.5 million shares of its common stock, respectively, for a purchase price of \$895 and \$299, respectively. In connection with the dissolution agreement, each of the prior investor agreements entered into between AutoMD, on the one hand, and Oak and the Trust, on the other, were terminated. Fredric W. Harman and Sol Khazani, each a current director of the Company and AutoMD, are affiliated with Oak and the Trust, respectively. The foregoing description of the terms of the dissolution agreement are qualified in their entirety by reference to the dissolution agreement, which is attached hereto as Exhibit 10.55.

## PART III

### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

- (a) *Identification of Directors.* The information under the caption “Election of Directors,” appearing in the Proxy Statement (“Proxy Statement”), is hereby incorporated by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.
- (b) *Identification of Executive Officers and Certain Significant Employees.* The information under the caption “Executive Compensation and Other Information—Executive Officers,” appearing in the Proxy Statement, is hereby incorporated by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.
- (c) *Compliance with Section 16(a) of the Exchange Act.* The information under the caption “Section 16(a) Beneficial Ownership Reporting Compliance,” appearing in the Proxy Statement, is hereby incorporated by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.
- (d) *Code of Ethics.* The information under the caption “Corporate Governance – Code of Ethics and Business Conduct,” appearing in the Proxy Statement, is hereby incorporated by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.
- (e) *Board Committees.* The information under the caption “Corporate Governance — Board Committees and Meetings,” appearing in the Proxy Statement, is hereby incorporated by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.

### **ITEM 11. EXECUTIVE COMPENSATION**

The information under the caption “Executive Compensation and Other Information”, appearing in the Proxy Statement, is incorporated herein by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.

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

The information under the captions “Securities Authorized for Issuance Under Equity Compensation Plans” and “Ownership of Securities by Certain Beneficial Owners and Management,” appearing in the Proxy Statement, is incorporated herein by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.

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

The information under the captions “Corporate Governance — Director Independence” and “Certain Relationships and Related Transactions,” appearing in the Proxy Statement, is incorporated herein by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.

### **ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information under the caption “Fees Paid to Independent Registered Public Accounting Firm,” appearing in the Proxy Statement, is incorporated herein by reference. The Proxy Statement will be filed with the SEC within 120 days from the end of fiscal year 2016.

## PART IV

### ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) Documents filed as part of this report:

(1) *Financial Statements*. The following financial statements of U.S. Auto Parts Network, Inc. are included in a separate section of this Annual Report on Form 10-K commencing on the pages referenced below:

	<u>Page</u>
<a href="#"><u>Report of RSM US LLP, independent registered public accounting firm</u></a>	<a href="#"><u>F- 1</u></a>
<a href="#"><u>Report of Deloitte &amp; Touche LLP, independent registered public accounting firm</u></a>	<a href="#"><u>F- 2</u></a>
<a href="#"><u>Consolidated Balance Sheets as of December 31, 2016 and January 2, 2016</u></a>	<a href="#"><u>F- 3</u></a>
<a href="#"><u>Consolidated Statements of Operations and Comprehensive Operations for each of the three years in the period ended December 31, 2016</u></a>	<a href="#"><u>F- 4</u></a>
<a href="#"><u>Consolidated Statements of Stockholders' Equity for each of the three years in the period ended December 31, 2016</u></a>	<a href="#"><u>F- 5</u></a>
<a href="#"><u>Consolidated Statements of Cash Flows for each of the three years in the period ended December 31, 2016</u></a>	<a href="#"><u>F- 7</u></a>
<a href="#"><u>Notes to Consolidated Financial Statements</u></a>	<a href="#"><u>F- 8</u></a>

(2) *Financial Statement Schedules*.

All schedules have been omitted because they are not required or the required information is included in our consolidated financial statements and notes thereto.

(3) *Exhibits*.

The following exhibits are filed herewith or incorporated by reference to the location indicated below:

## EXHIBIT INDEX

<u>Exhibit No.</u>	<u>Description</u>
2.1	Stock Purchase Agreement executed August 2, 2010 among the Acquisition Sub, WAG, Riverside and the other stockholders of WAG (incorporated by reference to Exhibit 10.57 to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on August 4, 2010)
3.1	Second Amended and Restated Certificate of Incorporation of U.S. Auto Parts Network, Inc. as filed with the Delaware Secretary of State on February 14, 2007 (incorporated by reference to Exhibit 3.1 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on April 2, 2007)
3.2	Amended and Restated Bylaws of U.S. Auto Parts Network, Inc. (incorporated by reference to Exhibit 3.2 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on April 2, 2007)
3.3	Certificate of Designation, Preferences and Rights of the Series A Convertible Preferred Stock of U.S. Auto Parts Network, Inc. (incorporated by reference to the Current Report on Form 8-K filed on March 25, 2013)
3.4	Amendment to Amended and Restated Bylaws of U.S. Auto Parts Network, Inc. (incorporated by reference to Exhibit 3.4 to the Annual Report on Form 10-K file with the Securities and Exchange Commission on March 11, 2016)
4.1*	Specimen common stock certificate
10.1+*	U.S. Auto Parts Network, Inc. 2006 Equity Incentive Plan
10.2+*	Form of Stock Option Agreement under the U.S. Auto Parts Network, Inc. 2006 Equity Incentive Plan.
10.3+*	Form of Notice of Grant of Stock Option under the U.S. Auto Parts Network, Inc. 2006 Equity Incentive Plan.
10.4+*	Form of Acceleration Addendum to Stock Option Agreement under the U.S. Auto Parts Network, Inc. 2006 Equity Incentive Plan.
10.5+*	U.S. Auto Parts Network, Inc. 2007 Omnibus Plan and Form of Award Agreements
10.6+	2016 Independent Director Compensation Plan
10.7+	Form of Indemnification Agreement for Officers and Directors (incorporated by reference to Exhibit 10.7 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2016)
10.8+	Employment Agreement dated March 23, 2015 between U.S. Auto Parts Network, Inc. and Neil Watanabe (incorporated by reference to Exhibit 99.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on March 24, 2015).
10.9+	Employment Agreement dated May 20, 2015 between U.S. Auto Parts Network, Inc. and David Eisler (incorporated by reference to Exhibit 10.9 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2016)
10.10+	Employment Agreement dated February 14, 2014 between U.S. Auto Parts Network, Inc. and Shane Evangelist (incorporated by reference to Exhibit 99.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on February 18, 2014)
10.11+	Non-Qualified Stock Option Agreement dated October 15, 2007 between U.S. Auto Parts Network, Inc. and Shane Evangelist (incorporated by reference to Exhibit 99.3 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on October 17, 2007)
10.12+	Non-Qualified Stock Option Agreement dated October 15, 2007 (performance grant) between U.S. Auto Parts Network, Inc. and Shane Evangelist (incorporated by reference to Exhibit 99.4 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on October 17, 2007)
10.13+	2007 New Employee Incentive Plan (incorporated by reference to Exhibit 99.5 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on October 17, 2007)
10.14+	Employment Agreement dated February 14, 2014, between the Company and Aaron Coleman (incorporated by reference to Exhibit 99.5 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on February 18, 2014)
10.15+	Non-Qualified Stock Option Agreement, dated May 15, 2008, by and between the Company and Shane Evangelist (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on May 15, 2008)

<u>Exhibit No.</u>	<u>Description</u>
10.16	Contract of Lease dated January 7, 2010 by and between U.S. Autoparts Network Philippines Corporation and Robinsons Land Corporation (incorporated by reference to Exhibit 10.56 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 15, 2010)
10.17	Agreement of Sublease dated September 22, 2011 by and between the Company and Timec Company Inc. ((incorporated by reference to Exhibit 10.61 to the Company's Quarterly Report on Form 10-Q filed with the Securities Exchange and Commission on November 9, 2011)
10.18	First Amendment to Agreement of Sublease, dated June 1, 2016, between the Company and Broadspectrum Downstream Services, Inc. (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on June 2, 2016)
10.19+	U.S. Auto Parts Network Inc. Director Payment Election Plan (incorporated by reference to Exhibit 10.68 to the Company's Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 9, 2011)
10.20	Credit Agreement, dated April 26, 2012, by and between U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JP Morgan Chase Bank, N.A. (incorporated by reference to Exhibit 99.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on April 30, 2012)
10.21	First Amended Credit Agreement, effective as of March 12, 2013, by and between U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A. (incorporated by reference to Exhibit 10.78 to the Annual Report on Form 10-K for the fiscal year ended December 29, 2012 filed with the Securities Exchange Commission on March 25, 2013)
10.22	Second Amended Credit Agreement, effective as of March 25, 2013, by and between U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A. (incorporated by reference to exhibit 10.79 to the Current Report on Form 8-k filed with the Securities and Exchange Commission on March 25, 2013)
10.23	Purchase and Sale Agreement dated April 17, 2013 by and among Whitney Automotive Group, Inc. and STORE Capital Acquisitions, LLC (incorporated by reference to the Current Report on Form 8-K filed on April 23, 2013)
10.24	Lease Agreement dated April 17, 2013 by and among U.S. Auto Parts Network, Inc. and STORE Master Funding III, LLC (incorporated by reference to the Current Report on Form 8-K filed on April 23, 2013)
10.25+	Form of Stock Unit Award Agreement (incorporated by reference to Exhibit 99.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on February 18, 2014)
10.26+	Form of Stock Unit Award Agreement under the U.S. Auto Parts Network, Inc. 2007 Omnibus Incentive Plan (incorporated by reference to Exhibit 99.3 to the Current Report on Form 8-k filed with the Securities and Exchange Commission on February 18, 2014)
10.27	Third Amendment to Credit Agreement dated as of August 2, 2013 by and between U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A. (incorporated by reference to the Quarterly Report on Form 10-Q for the quarterly period ended June 29, 2013)
10.28	Fourth Amendment to Credit Agreement dated August 4, 2014 by and between U.S. Auto Parts Network, Inc., certain of its wholly-owned domestic subsidiaries and JPMorgan Chase Bank, N.A. (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on August 5, 2014)
10.29	Common Stock Purchase Agreement, dated October 8, 2014, by and among AutoMD, Inc., U.S. Auto Parts Network, Inc., Muzzy-Lyon Auto Parts, Inc., Manheim Investments, Inc., Oak Investment Partners XI, L.P. and the Sol Khazani Living Trust (incorporated by reference to the Current Report on Form 8-K filed on October 9, 2014)
10.30	Investor Rights Agreement, dated October 8, 2014, by and among AutoMD, Inc., U.S. Auto Parts Network, Inc., Muzzy-Lyon Auto Parts, Inc., Manheim Investments, Inc., Oak Investment Partners XI, L.P. and the Sol Khazani Living Trust (incorporated by reference to the Current Report on Form 8-K filed on October 9, 2014)
10.31	Voting Agreement, dated October 8, 2014, by and among AutoMD, Inc., U.S. Auto Parts Network, Inc., Muzzy-Lyon Auto Parts, Inc., Manheim Investments, Inc., Oak Investment Partners XI, L.P. and the Sol Khazani Living Trust (incorporated by reference to the Current Report on Form 8-K filed on October 9, 2014)
10.32	Right of First Refusal and Co-Sale Agreement, dated October 8, 2014, by and among AutoMD, Inc., U.S. Auto Parts Network, Inc., Muzzy-Lyon Auto Parts, Inc., Manheim Investments, Inc., Oak Investment Partners XI, L.P. and the Sol Khazani Living Trust (incorporated by reference to the Current Report on Form 8-K filed on October 9, 2014)



<b>Exhibit No.</b>	<b>Description</b>
10.33	Fifth Amendment to Credit Agreement and First Amendment to Pledge and Security Agreement, dated October 8, 2014, by and among U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A (incorporated by reference to the Current Report on Form 8-K filed on October 9, 2014)
10.34	Sixth Amendment to Credit Agreement and First Amendment to Pledge and Security Agreement, dated January 2, 2015, by and among U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A (incorporated by reference to the Current Report on Form 8-K filed on January 5, 2015)
10.35	Seventh Amendment to Credit Agreement and Second Amendment to Pledge and Security Agreement, dated March 24, 2015, by and among U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q filed on May 13, 2015)
10.36	Eighth Amendment to Credit Agreement and Third Amendment to Pledge and Security Agreement, dated February 5, 2016, by and among U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A (incorporated by reference to Exhibit 10.38 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2016)
10.37	Ninth Amendment to Credit Agreement, dated May 6, 2016, by and among U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A (incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q filed on May 10, 2016)
10.38	Tenth Amendment to Credit Agreement and Fourth Amendment to Pledge and Security Agreement, dated November 15, 2016, by and among U.S. Auto Parts Network, Inc., certain of its domestic subsidiaries and JPMorgan Chase Bank, N.A (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed on November 15, 2016)
10.39+	Form of Performance Restricted Stock Unit Award Agreement under the U.S. Auto Parts Network, Inc. 2007 Omnibus Incentive Plan (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 26, 2016)
10.40+	Form of Performance Cash Bonus Award Agreement under the U.S. Auto Parts Network, Inc. 2007 Omnibus Incentive Plan (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 26, 2016)
10.41+	AutoMD, Inc. 2014 Equity Incentive Plan (incorporated by reference to Exhibit 10.41 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2016)
10.42+	AutoMD, Inc. Stock Option Grant Notice and Option Agreement, dated January 29, 2015, between AutoMD, Inc. and Shane Evangelist (incorporated by reference to Exhibit 10.42 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2016)
10.43	Deed of Lease dated February 4, 2016 by and between U.S. Auto Parts Network, Inc. and Liberty Property Limited Partnership (incorporated by reference to Exhibit 10.43 to the Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 11, 2016)
10.44+	U.S. Auto Parts Network, Inc. 2016 Equity Incentive Plan (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on June 2, 2016)
10.45+	Form of Employee Option Agreement under the U.S. Auto Parts Network, Inc. 2016 Equity Incentive Plan (incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on June 2, 2016)
10.46+	Form of Director Option Agreement under the U.S. Auto Parts Network, Inc. 2016 Equity Incentive Plan (incorporated by reference to Exhibit 10.4 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on June 2, 2016)
10.47+	Form of Restricted Stock Unit Agreement under the U.S. Auto Parts Network, Inc. 2016 Equity Incentive Plan (incorporated by reference to Exhibit 10.5 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on June 2, 2016)
10.48+	Form of Performance Restricted Stock Unit Award Agreement under the U.S. Auto Parts Network, Inc. 2016 Equity Incentive Plan (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 26, 2017)
10.49+	Form of Performance Cash Bonus Award Agreement under the U.S. Auto Parts Network, Inc. 2016 Equity Incentive Plan (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 26, 2017)

<b>Exhibit No.</b>	<b>Description</b>
10.50+	Form of Director and Section 16 Officer Restricted Stock Unit Agreement under the U.S. Auto Parts Network, Inc. 2016 Equity Incentive Plan (incorporated by reference to Exhibit 10.4 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 26, 2017)
10.51+	Redemption Agreement, dated January 26, 2017 by and among AutoMD, Inc., Federal-Mogul Motorparts Corporation, and Muzzy-Lyon Auto Parts, Inc. (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 30, 2017)
10.52+	Redemption Agreement, dated January 26, 2017 by and among AutoMD, Inc. and Manheim Investments, Inc. (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 30, 2017)
10.53+	Release Agreement, dated January 26, 2017 by and among AutoMD, Inc., U.S. Auto Parts Network, Inc., Muzzy-Lyon Auto Parts, Inc., Federal-Mogul Motorparts Corporation, Manheim Investments, Inc., Oak Investment Partners XI, L.P. and the Sol Khazani Living Trust (incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 30, 2017)
10.54+	Deferred Compensation Plan
10.55	Dissolution Agreement, dated March 6, 2017, by and among AutoMD, Inc., Oak Investment Partners XI, L.P. and the Sol Khazani Living Trust.
21.1	Subsidiaries of U.S. Auto Parts Network, Inc.
23.1	Consent of Independent Registered Public Accounting Firm
23.2	Consent of Independent Registered Public Accounting Firm
31.1	Certification of the Principal Executive Officer required by Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934, as amended
31.2	Certification of the Principal Financial Officer required by Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934, as amended
32.1	Certification of the Chief Executive Officer required by 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer required by 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
*	Incorporated by reference to the exhibit of the same number from the registration statement on Form S-1 of U.S. Auto Parts Network, Inc. (File No. 333-138379) initially filed with the Securities and Exchange Commission on November 2, 2006, as amended.
+	Indicates a management contract or compensatory plan or arrangement.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: March 7, 2017

**U.S. AUTO PARTS NETWORK, INC.**

By: /s/ Shane Evangelist  
Shane Evangelist  
Chief Executive Officer

## POWER OF ATTORNEY

We, the undersigned officers and directors of U.S. Auto Parts Network, Inc., do hereby constitute and appoint Shane Evangelist and Neil Watanabe, and each of them, our true and lawful attorneys-in-fact and agents, each with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this report, and to file the same, with exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby, ratifying and confirming all that each of said attorneys-in-fact and agents, or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report on Form 10-K has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated:

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Shane Evangelist</u> Shane Evangelist	Chief Executive Officer and Director (principal executive officer)	March 7, 2017
<u>/s/ Neil Watanabe</u> Neil Watanabe	Chief Financial Officer (principal financial and accounting officer)	March 7, 2017
<u>/s/ Robert J. Majteles</u> Robert J. Majteles	Chairman of the Board	March 7, 2017
<u>/s/ Joshua L. Berman</u> Joshua L. Berman	Director	March 7, 2017
<u>/s/ Fredric W. Harman</u> Fredric W. Harman	Director	March 7, 2017
<u>/s/ Jay K. Greyson</u> Jay K. Greyson	Director	March 7, 2017
<u>/s/ Sol Khazani</u> Sol Khazani	Director	March 7, 2017
<u>/s/ Warren B. Phelps III</u> Warren B. Phelps III	Director	March 7, 2017
<u>/s/ Barbara Palmer</u> Barbara Palmer	Director	March 7, 2017
<u>/s/ Bradley E. Wilson</u> Bradley E. Wilson	Director	March 7, 2017

## INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

<a href="#"><u>Report of RSM US LLP, independent registered public accounting firm</u></a>	<a href="#"><u>F- 1</u></a>
<a href="#"><u>Report of Deloitte &amp; Touche LLP, independent registered public accounting firm</u></a>	<a href="#"><u>F- 2</u></a>
<a href="#"><u>Consolidated Balance Sheets as of December 31, 2016 and January 2, 2016</u></a>	<a href="#"><u>F- 3</u></a>
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<a href="#"><u>Consolidated Statements of Cash Flows for each of the three years in the period ended December 31, 2016</u></a>	<a href="#"><u>F- 7</u></a>
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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders  
U.S. Auto Parts Network, Inc.

We have audited the accompanying consolidated balance sheets of U.S. Auto Parts Network, Inc. and subsidiaries (the Company) as of December 31, 2016 and January 2, 2016, and the related consolidated statements of operations and other comprehensive operations, stockholders' equity and cash flows for each of the two fiscal years in the period ended December 31, 2016. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of U.S. Auto Parts Network, Inc. and subsidiaries as of December 31, 2016 and January 2, 2016, and the results of their operations and their cash flows each of the two fiscal years in the period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

*/s/ RSM US LLP*

Los Angeles, CA  
March 6, 2017

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of  
U.S. Auto Parts Network, Inc.  
Carson, CA

We have audited the accompanying consolidated statements of operations and comprehensive operations, stockholders' equity, and cash flows for the year ended January 3, 2015 of U.S. Auto Parts Network, Inc. and subsidiaries (the Company). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the results of U.S. Auto Parts Network, Inc. and subsidiaries operations and cash flows for the year ended January 3, 2015, in conformity with accounting principles generally accepted in the United States of America.

*/s/ DELOITTE & TOUCHE LLP*

Los Angeles, CA

March 19, 2015 (March 9, 2016, as to the disclosure of the approximate distribution of Base USAP online revenue by product type for fiscal year 2014 included in Note 15 - Segment Information)

**U.S. AUTO PARTS NETWORK, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
*(In Thousands, Except Par and Per Share Liquidation Value)*

	December 31, 2016	January 2, 2016
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 6,643	\$ 5,537
Short-term investments	30	65
Accounts receivable, net of allowances of \$36 and \$17 at December 31, 2016 and January 2, 2016, respectively	3,266	3,236
Inventory	50,904	51,216
Other current assets	2,815	2,475
Total current assets	63,658	62,529
Property and equipment, net	16,478	18,431
Intangible assets, net	969	1,476
Other non-current assets	1,029	1,320
Total assets	\$ 82,134	\$ 83,756
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 33,697	\$ 25,523
Accrued expenses	6,860	7,267
Revolving loan payable	—	11,759
Current portion of capital leases payable	542	521
Customer deposits	3,718	2,578
Other current liabilities	1,972	1,276
Total current liabilities	46,789	48,924
Capital leases payable, net of current portion	9,770	10,168
Deferred income taxes	156	944
Other non-current liabilities	2,097	1,577
Total liabilities	58,812	61,613
Commitments and contingencies		
Stockholders' equity:		
Series A convertible preferred stock, \$0.001 par value; \$1.45 per share liquidation value or aggregate of \$6,017; 4,150 shares authorized; 4,150 and 4,150 shares issued and outstanding at December 31, 2016 and January 2, 2016, respectively	4	4
Common stock, \$0.001 par value; 100,000 shares authorized; 35,068 and 34,137 shares issued and outstanding at December 31, 2016 and January 2, 2016, respectively (445 of which are treasury stock)	35	34
Treasury stock	(1,376)	—
Additional paid-in-capital	180,153	176,873
Accumulated other comprehensive income	557	440
Accumulated deficit	(156,520)	(157,011)
Total stockholders' equity	22,853	20,340
Noncontrolling interest	469	1,803
Total equity	23,322	22,143
Total liabilities and equity	\$ 82,134	\$ 83,756

*See accompanying notes to consolidated financial statements.*

**U.S. AUTO PARTS NETWORK, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE OPERATIONS**  
*(In Thousands, Except Per Share Data)*

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
Net sales	\$ 303,571	\$ 291,091	\$ 283,508
Cost of sales <sup>(1)</sup>	211,289	207,657	205,058
Gross profit	92,282	83,434	78,450
Operating expenses:			
Marketing	43,555	43,279	42,008
General and administrative	17,907	16,509	16,701
Fulfillment	22,975	20,237	20,368
Technology	5,843	5,000	4,863
Amortization of intangible assets	482	464	422
Impairment loss on intangibles	1,130	—	—
Total operating expenses	91,892	85,489	84,362
Income (loss) from operations	390	(2,055)	(5,912)
Other income (expense):			
Other income, net	46	36	65
Interest expense	(1,238)	(1,216)	(1,101)
Total other expense, net	(1,192)	(1,180)	(1,036)
Loss before income taxes	(802)	(3,235)	(6,948)
Income tax (benefit) provision	(199)	(811)	138
Net loss including noncontrolling interests	(603)	(2,424)	(7,086)
Net loss attributable to noncontrolling interests	(1,334)	(1,143)	(207)
Net income (loss) attributable to U.S. Auto Parts	731	(1,281)	(6,879)
Other comprehensive income attributable to U.S. Auto Parts, net of tax:			
Foreign currency translation adjustments	9	36	20
Actuarial gain (loss) on defined benefit plan	110	44	(106)
Unrealized loss on investments	(2)	—	—
Total other comprehensive income (loss) attributable to U.S. Auto Parts	117	80	(86)
Comprehensive income (loss) attributable to U.S. Auto Parts	\$ 848	\$ (1,201)	\$ (6,965)
Basic net income (loss) per share	\$ 0.01	\$ (0.04)	\$ (0.21)
Diluted net income (loss) per share	0.01	(0.04)	(0.21)
Shares used in computation of basic net income (loss) per share	34,765	33,946	33,489
Shares used in computation of diluted net income (loss) per share	36,207	33,946	33,489

(1) Excludes depreciation and amortization expense which is included in marketing, general and administrative and fulfillment expense as described in “*Note 1 – Summary of Significant Accounting Policies and Nature of Operations*”.

*See accompanying notes to consolidated financial statements.*



**U.S AUTO PARTS NETWORK, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
*(In Thousands)*

	Preferred Stock		Common Stock		Additional Paid-in- Capital	Treasury Stock	Preferred Stock Dividend Distributable	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders' Equity	Noncontrolling Interest	Total
	Shares	Amount	Shares	Amount								
<b>Balance, December 28, 2013</b>	4,150	4	33,352	\$ 33	\$168,693	\$ —	60	\$ 446	(148,370)	\$ 20,866	—	20,866
Issuance of shares of Auto MD common stock	—	—	—	—	2,512	—	—	—	—	2,512	3,153	5,665
Net loss	—	—	—	—	—	—	—	—	(6,879)	(6,879)	(207)	(7,086)
Issuance of common stock in connection with preferred stock dividends	—	—	107	—	300	—	(300)	—	—	—	—	—
Issuance of shares in connection with stock option exercises	—	—	144	—	295	—	—	—	—	295	—	295
Issuance of shares in connection with restricted stock units vesting	—	—	21	—	—	—	—	—	—	—	—	—
Share-based compensation	—	—	—	—	2,569	—	—	—	—	2,569	—	2,569
Common stock dividend distributable on Series A Preferred Stock	—	—	—	—	—	—	240	—	(240)	—	—	—
Actuarial loss on defined benefit plan	—	—	—	—	—	—	—	(106)	—	(106)	—	(106)
Effect of changes in foreign currencies	—	—	—	—	—	—	—	20	—	20	—	20
<b>Balance, January 3, 2015</b>	4,150	4	33,624	33	174,369	—	—	360	(155,489)	19,277	2,946	22,223
Net loss	—	—	—	—	—	—	—	—	(1,281)	(1,281)	(1,143)	(2,424)
Issuance of common stock in connection with preferred stock dividends	—	—	103	—	241	—	(241)	—	—	—	—	—
Issuance of shares in connection with stock option exercises	—	—	301	—	135	—	—	—	—	135	—	135
Issuance of shares in connection with restricted stock units vesting	—	—	397	—	(809)	—	—	—	—	(809)	—	(809)

Minimum tax withholding on RSU's	—	—	(151)	1	450	—	—	—	—	451	—	451
Minimum tax withholdings on Options exercised	—	—	(139)	—	(80)	—	—	—	—	(80)	—	(80)
Share-based compensation	—	—	—	—	2,565	—	—	—	—	2,565	—	2,565
Issuance of shares in connection with BOD fees	—	—	2	—	2	—	—	—	—	2	—	2
Common stock dividend distributable on Series A Preferred Stock	—	—	—	—	—	—	241		(241)	—	—	—

Actuarial loss on defined benefit plan	—	—	—	—	—	—	—	44	—	44	—	44
Effect of changes in foreign currencies	—	—	—	—	—	—	—	36	—	36	—	36
<b>Balance, January 2, 2016</b>	<b>4,150</b>	<b>4</b>	<b>34,137</b>	<b>34</b>	<b>176,873</b>	<b>—</b>	<b>—</b>	<b>440</b>	<b>(157,011)</b>	<b>20,340</b>	<b>1,803</b>	<b>22,143</b>
Net income (loss)	—	—	—	—	—	—	—	—	731	731	(1,334)	(603)
Issuance of common stock in connection with preferred stock dividends	—	—	37	—	120	—	(120)	—	—	—	—	—
Issuance of shares in connection with stock option exercises	—	—	442	—	908	—	—	—	—	908	—	908
Issuance of shares in connection with restricted stock units vesting	—	—	774	1	(1,897)	—	—	—	—	(1,896)	—	(1,896)
Minimum tax withholding on RSU's	—	—	(335)	—	927	—	—	—	—	927	—	927
Issuance of shares in connection with BOD Fees	—	—	3	—	9	—	—	—	—	9	—	9
Issuance of stock awards	—	—	10	—	—	—	—	—	—	—	—	—
Share-based compensation	—	—	—	—	3,213	—	—	—	—	3,213	—	3,213
Cash Dividend on preferred stock	—	—	—	—	—	—	—	—	(120)	(120)	—	(120)
Treasury Stock	—	—	—	—	—	(1,376)	—	—	—	(1,376)	—	(1,376)
Common stock dividend distributable on Series A Preferred Stock	—	—	—	—	—	—	120	—	(120)	—	—	—
Actuarial gain on defined benefit plan	—	—	—	—	—	—	—	110	—	110	—	110
Unrealized (loss) gain on investments, net of tax	—	—	—	—	—	—	—	(2)	—	(2)	—	(2)
Effect of changes in foreign currencies	—	—	—	—	—	—	—	9	—	9	—	9
<b>Balance, December 31, 2016</b>	<b>4,150</b>	<b>\$ 4</b>	<b>35,068</b>	<b>\$ 35</b>	<b>\$180,153</b>	<b>\$(1,376)</b>	<b>\$ —</b>	<b>\$ 557</b>	<b>\$(156,520)</b>	<b>\$ 22,853</b>	<b>\$ 469</b>	<b>\$23,322</b>

*See accompanying notes to consolidated financial statements.*

**U.S. AUTO PARTS NETWORK, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In Thousands)

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
<b>Operating activities</b>			
Net loss including noncontrolling interests	\$ (603)	\$ (2,424)	\$ (7,086)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:			
Depreciation and amortization expense	7,510	7,510	8,923
Amortization of intangible assets	482	464	422
Deferred income taxes	(838)	(906)	74
Share-based compensation expense	3,131	2,419	2,371
Stock awards issued for non-employee director service	9	2	—
Impairment loss on intangible assets	1,130	—	—
Amortization of deferred financing costs	70	82	81
Gain from disposition of assets	—	(13)	(96)
Changes in operating assets and liabilities:			
Accounts receivable	(30)	568	1,105
Inventory	312	(2,854)	(11,412)
Other current assets	(255)	262	471
Other non-current assets	203	225	(39)
Accounts payable and accrued expenses	7,906	119	6,992
Other current liabilities	1,775	475	(302)
Other non-current liabilities	769	(184)	(261)
Net cash provided by operating activities	<u>21,571</u>	<u>5,745</u>	<u>1,243</u>
<b>Investing activities</b>			
Additions to property and equipment	(6,353)	(7,780)	(5,556)
Proceeds from sale of property and equipment	—	13	27
Cash paid for intangibles	(125)	(25)	(200)
Proceeds from sale of marketable securities and investments	1	—	745
Purchases of marketable securities and investments	—	—	(746)
Net cash used in investing activities	<u>(6,477)</u>	<u>(7,792)</u>	<u>(5,730)</u>
<b>Financing activities</b>			
Proceeds from revolving loan payable	13,727	15,637	19,506
Payments made on revolving loan payable	(25,485)	(14,900)	(15,258)
Proceeds from sale of equity in subsidiary	—	—	7,000
Payments on capital leases	(587)	(438)	(232)
Treasury stock purchases	(1,387)	—	—
Statutory tax withholding payment for share-based compensation	(969)	(438)	—
Proceeds from exercise of stock options	908	134	295
Payment of liabilities related to financing activities	(100)	(100)	—
Preferred stock dividends paid	(61)	—	—
Net cash (used in) provided by financing activities	<u>(13,954)</u>	<u>(105)</u>	<u>11,311</u>
Effect of exchange rate changes on cash	(34)	36	11
Net change in cash and cash equivalents	1,106	(2,116)	6,835
Cash and cash equivalents, beginning of period	5,537	7,653	818
Cash and cash equivalents, end of period	<u>\$ 6,643</u>	<u>\$ 5,537</u>	<u>\$ 7,653</u>
Supplemental disclosure of non-cash investing and financing activities:			
Accrued asset purchases	\$ 744	\$ 708	\$ 1,232
Accrued intangible asset purchases	—	125	—
Property acquired under capital lease	211	1,588	—
Preferred stock dividends declared and not paid	60	—	—
Unrealized loss on investments	(2)	—	—
Supplemental disclosure of cash flow information:			
Cash paid during the period for income taxes	\$ 89	\$ 104	\$ 60
Cash paid during the period for interest	1,077	1,145	1,029

*See accompanying notes to consolidated financial statements.*

**U.S. AUTO PARTS NETWORK, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
*(In Thousands, Except Per Share Data)*

**Note 1 – Summary of Significant Accounting Policies and Nature of Operations**

U.S. Auto Parts Network, Inc. (including its subsidiaries) is a leading online provider of aftermarket auto parts and accessories and was established in 1995. The Company entered the e-commerce sector by launching its first website in 2000 and currently derives the majority of its revenues from online sales channels. The Company sells its products to individual consumers through a network of websites and online marketplaces. Through AutoMD.com, the Company educates consumers on maintenance and service of their vehicles. The site provides auto information, with tools for diagnosing car troubles, locating repair shops and do-it-yourself (“DIY”) repair guides. Our flagship websites are located at [www.autopartswarehouse.com](http://www.autopartswarehouse.com), [www.carparts.com](http://www.carparts.com), [www.jcwhitney.com](http://www.jcwhitney.com) and [www.AutoMD.com](http://www.AutoMD.com) and our corporate website is located at [www.usautoparts.net](http://www.usautoparts.net). References to the “Company,” “we,” “us,” or “our” refer to U.S. Auto Parts Network, Inc. and its consolidated subsidiaries.

The Company’s products consist of collision parts serving the body repair market, engine parts to serve the replacement parts market, and performance parts and accessories. The collision parts category is primarily comprised of body parts for the exterior of an automobile. Our parts in this category are typically replacement parts for original body parts that have been damaged as a result of a collision or through general wear and tear. The majority of these products are sold through our websites. In addition, we sell an extensive line of mirror products, including our own private-label brand called Kool-Vue™, which are marketed and sold as aftermarket replacement parts and as upgrades to existing parts. The engine parts category is comprised of engine components and other mechanical and electrical parts. These parts serve as replacement parts for existing engine parts and are generally used by professionals and do-it-yourselfers for engine and mechanical maintenance and repair. We offer performance versions of many parts sold in each of the above categories. Performance parts and accessories generally consist of parts that enhance the performance of the automobile, upgrade existing functionality of a specific part or improve the physical appearance or comfort of the automobile.

The Company is a Delaware C corporation and is headquartered in Carson, California. The Company has employees located in both the United States and the Philippines.

***Fiscal Year***

The Company’s fiscal year is based on a 52/53 week fiscal year ending on the Saturday closest to December 31. The fiscal years ended December 31, 2016 (fiscal year 2016) and January 2, 2016 (fiscal year 2015) are both 52 week periods. The fiscal year ended January 3, 2015 (fiscal year 2014) is a 53 week period.

***Principles of Consolidation***

The consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries and its subsidiaries in which it has a controlling interest. On October 8, 2014, AutoMD, Inc. (“AutoMD”) sold seven million shares of its common stock to third-party investors, reducing the Company’s ownership interest in AutoMD to 64.1%. In October 2016, the Company purchased an additional two million shares of AutoMD common stock pursuant to its funding milestone obligations under the common stock purchase agreement, increasing the Company’s ownership interest in AutoMD to 67.4%. On January 26, 2017, AutoMD entered into redemption agreements with certain third-party investors to redeem an aggregate of five million shares of AutoMD common stock for a purchase price of \$1,292. The redemption agreements increased the Company’s ownership interest in AutoMD to 87.9% of AutoMD’s outstanding common stock. The remaining 12.1% of AutoMD controlled by third-party investors was repurchased on March 6, 2017. The Company reports noncontrolling interests in consolidated entities as a component of equity separate from the Company’s equity. All inter-company transactions between and among the Company and its consolidated subsidiaries have been eliminated in consolidation.

***Basis of Presentation***

During fiscal year 2016, the Company’s revenues increased 4.3% from fiscal 2015 after having increased in fiscal year 2015 by 2.7% from fiscal year 2014. In fiscal year 2016, the Company generated net income of \$731, after incurring net losses of \$1,281 and \$6,879 in fiscal years 2015 and 2014, respectively. Based on our current operating plan, we believe that our existing cash, cash equivalents, short-term investments, cash flows from operations and available debt financing will be sufficient to finance our operational cash needs through at least the next twelve months. Should the Company’s operating results not meet expectations in 2017, it could negatively impact our liquidity as we may not be able to provide positive cash flows from operations in order to meet our working capital requirements. We may need to borrow additional funds from our credit facility, which under certain circumstances may not be available, sell assets or seek additional equity or additional debt

financing in the future. There can be no assurance that we would be able to raise such additional financing or engage in such additional asset sales on acceptable terms, or at all. If revenues were to decline and we incur net losses because our strategies to return to consistent profitability are not successful or otherwise, and if we are not able to raise adequate additional financing or proceeds from asset sales to continue to fund our ongoing operations, we will need to defer, reduce or eliminate significant planned expenditures, restructure or significantly curtail our operations.

#### ***Use of Estimates***

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates made by management include, but are not limited to, those related to revenue recognition, uncollectible receivables, the valuation of short-term investments, valuation of inventory, valuation of deferred tax assets and liabilities, valuation of intangible and other long-lived assets, recoverability of software development costs, contingencies and share-based compensation expense that results from estimated grant date fair values and vesting of issued equity awards. Actual results could differ from these estimates.

#### ***Statement of Cash Flows***

The net change in the Company's book overdraft is presented as an operating activity in the consolidated statement of cash flows. The book overdraft represents a credit balance in the Company's general ledger but the Company has a positive bank account balance.

#### ***Cash and Cash Equivalents***

The Company considers all money market funds and short-term investments purchased with original maturities of ninety days or less to be cash equivalents.

#### ***Fair Value of Financial Instruments***

Financial instruments that are not measured at fair value include accounts receivable, accounts payable and debt. Refer to "Note 3 – Fair Value Measurements" for additional fair value information. If the Company's revolving loan payable (see "Note 6 – Borrowings") had been measured at fair value, it would be categorized in Level 2 of the fair value hierarchy, as the estimated value would be based on the quoted market prices for the same or similar issues or on the current rates available to the Company for debt of the same or similar terms. The carrying values of cash and cash equivalents, accounts receivable and accounts payable approximate fair value due to their short-term maturities. Short-term investments are carried at fair value. Based on the borrowing rates currently available to the Company for bank loans with similar terms and average maturities, the fair value of our revolving loan payable, classified as current liability in our consolidated balance sheet, approximates its carrying amount because the interest rate is variable.

#### ***Accounts Receivable and Concentration of Credit Risk***

Accounts receivable are stated net of allowance for doubtful accounts. The allowance for doubtful accounts is determined primarily on the basis of past collection experience and general economic conditions. The Company determines terms and conditions for its customers primarily based on the volume purchased by the customer, customer creditworthiness and past transaction history.

Concentrations of credit risk are limited to the customer base to which the Company's products are sold. The Company does not believe significant concentrations of credit risk exist.

#### ***Investments***

Short-term investments are comprised of closed-end funds primarily invested in mutual funds that hold government bonds and stock and short-term money market funds. Mutual funds are classified as short-term investments available-for-sale and recorded at fair market value, based on quoted prices of identical assets that are trading in active markets as of the end of the period for which the values are determined. All of the Company's marketable securities and investments are subject to a periodic impairment review. The Company recognizes an impairment charge when a decline in the fair value of its investments below the cost basis is judged to be other-than-temporary. The Company considers various factors in determining whether to recognize an impairment charge, including the length of time and extent to which the fair value has been less than the Company's cost basis, the financial condition and near-term prospects of the investee, and the Company's intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in the market value. No other-than-temporary impairment charges were recorded on any investments during fiscal years presented.

### ***Inventory***

Inventories consist of finished goods available-for-sale and are stated at the lower of cost or market value, determined using the first-in first-out (“FIFO”) method. The Company purchases inventory from suppliers both domestically and internationally, and routinely enters into supply agreements with Asia-Pacific based suppliers of private label products and U.S.-based suppliers who are primarily drop-ship vendors. The Company believes that its products are generally available from more than one supplier and seeks to maintain multiple sources for its products, both internationally and domestically. The Company primarily purchases products in bulk quantities to take advantage of quantity discounts and to ensure inventory availability. Inventory is reported at the lower of cost or market, adjusted for slow moving, obsolete or scrap product. Inventory at December 31, 2016 and January 2, 2016 included items in-transit to our warehouses, in the amount of \$9,767 and \$12,241, respectively.

### ***Website and Software Development Costs***

The Company capitalizes certain costs associated with website and software developed for internal use according to ASC 350-50 - *Intangibles – Goodwill and Other – Website Development Costs* and ASC 350-40 *Intangibles – Goodwill and Other – Internal-Use Software*, when both the preliminary project design and testing stage are completed and management has authorized further funding for the project, which it deems probable of completion and to be used for the function intended. Capitalized costs include amounts directly related to website and software development such as payroll and payroll-related costs for employees who are directly associated with, and who devote time to, the internal-use software project. Capitalization of such costs ceases when the project is substantially complete and ready for its intended use. These amounts are amortized on a straight-line basis over two to three years once the software is placed into service. The Company capitalized website and software development costs of \$4,977 and \$5,664 during fiscal year 2016 and 2015, respectively. At December 31, 2016 and January 2, 2016, our internally developed website and software costs amounted to \$22,366 and \$22,745, respectively, and the related accumulated amortization and impairment amounted to \$18,520 and \$17,669, respectively.

### ***Long-Lived Assets and Intangibles Subject to Amortization***

The Company accounts for the impairment and disposition of long-lived assets, including intangibles subject to amortization, in accordance with ASC - 360 *Property, Plant and Equipment* (“ASC 360”). Management assesses potential impairments whenever events or changes in circumstances indicate that the carrying value of an asset or asset group may not be recoverable. An impairment loss will result when the carrying value exceeds the undiscounted cash flows estimated to result from the use and eventual disposition of the asset or asset group. Impairment losses will be recognized in operating results to the extent that the carrying value exceeds the discounted future cash flows estimated to result from the use and eventual disposition of the asset or asset group. The Company continually uses judgment when applying these impairment rules to determine the timing of the impairment tests, undiscounted cash flows used to assess impairments, and the fair value of a potentially impaired asset or asset group. The reasonableness of our judgments could significantly affect the carrying value of our long-lived assets. During the fourth quarter of 2016, the Company recognized an impairment loss on intangible assets of \$1,130 related to the impairment of AutoMD software. As of January 2, 2016 and January 3, 2015, the Company’s long-lived assets did not indicate a potential impairment under the provisions of ASC 360, therefore no impairment charges were recorded for either fiscal 2015 or fiscal 2014.

### ***Deferred Catalog Expenses***

Deferred catalog expenses consist of third-party direct costs including primarily creative design, paper, printing, postage and mailing costs for all Company direct response catalogs. Such costs are capitalized as deferred catalog expenses and are amortized over their expected future benefit period. Each catalog is fully amortized within nine months. Deferred catalog expenses are included in other current assets and amounted to \$160 and \$256 at December 31, 2016 and January 2, 2016, respectively.

### ***Deferred Financing Costs***

Deferred financing costs are being amortized over the life of the loan using the straight-line method as it is not significantly different from the effective interest method.

### ***Revenue Recognition***

The Company recognizes revenue from product sales and shipping revenues, net of promotional discounts and return allowances, when the following revenue recognition criteria are met: persuasive evidence of an arrangement exists, both title and risk of loss or damage have transferred, delivery has occurred, the selling price is fixed or determinable, and collectability is reasonably assured. The Company retains the risk of loss or damage during transit, therefore, revenue from product sales is

recognized at the delivery date to customers. Return allowances, which reduce product revenue by the Company's best estimate of expected product returns, are estimated using historical experience.

Revenue from sales of advertising is recorded when performance requirements of the related advertising program agreement are met. For each of the fiscal years ended 2016, 2015 and 2014, the advertising revenue represented approximately 1%, of our total revenue.

The Company evaluates the criteria of ASC 605-45 - *Revenue Recognition Principal Agent Considerations* in determining whether it is appropriate to record the gross amount of product sales and related costs or the net amount earned as commissions. Generally, when the Company is the primary party obligated in a transaction, the Company is subject to inventory risk, has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, revenue is recorded at gross.

Payments received prior to the delivery of goods to customers are recorded as deferred revenue.

The Company periodically provides incentive offers to its customers to encourage purchases. Such offers include current discount offers, such as percentage discounts off current purchases and other similar offers. Current discount offers, when accepted by the Company's customers, are treated as a reduction to the purchase price of the related transaction.

Sales discounts are recorded in the period in which the related sale is recognized. Sales return allowances are estimated based on historical amounts and are recorded upon recognizing the related sales. Credits are issued to customers for returned products. Credits for returned products amounted to \$23,876, \$23,543, and \$24,903 for fiscal year 2016, 2015 and 2014, respectively.

No customer accounted for more than 10% of the Company's net sales.

The following table provides an analysis of the allowance for sales returns and the allowance for doubtful accounts (in thousands):

	Balance at Beginning of Period	Charged to Revenue, Cost or Expenses	Deductions	Balance at End of Period
<b>Fifty-Two Weeks Ended December 31, 2016</b>				
Allowance for sales returns	\$ 1,009	\$ 23,804	\$ (23,876)	\$ 937
Allowance for doubtful accounts	17	254	(235)	36
<b>Fifty-Two Weeks Ended January 2, 2016</b>				
Allowance for sales returns	\$ 897	\$ 23,655	\$ (23,543)	\$ 1,009
Allowance for doubtful accounts	41	29	(53)	17
<b>Fifty-Three Weeks Ended January 3, 2015</b>				
Allowance for sales returns	\$ 893	\$ 24,907	\$ (24,903)	\$ 897
Allowance for doubtful accounts	213	64	(236)	41

#### ***Cost of Sales***

Cost of sales consists of the direct costs associated with procuring parts from suppliers and delivering products to customers. These costs include direct product costs, outbound freight and shipping costs, warehouse supplies and warranty costs, partially offset by purchase discounts and cooperative advertising. Total freight and shipping expense included in cost of sales for fiscal year 2016, 2015 and 2014 was \$41,937, \$41,250, and \$40,428, respectively. Depreciation and amortization expenses are excluded from cost of sales and included in marketing, general and administrative and fulfillment expenses.

#### ***Warranty Costs***

The Company or the vendors supplying its products provide the Company's customers limited warranties on certain products that range from 30 days to lifetime. Historically, the Company's vendors have been the party primarily responsible for warranty claims. Standard product warranties sold separately by the Company are recorded as deferred revenue and recognized ratably over the life of the warranty, ranging from one to five years. The Company also offers extended warranties that are imbedded in the price of selected private label products sold. The product brands that include the extended warranty coverage are offered at three different service levels: (a) a five year unlimited product replacement, (b) a five year one-time product



replacement, and (c) a three year one-time product replacement. Warranty costs relating to merchandise sold under warranty not covered by vendors are estimated and recorded as warranty obligations at the time of sale based on each product's historical return rate and historical warranty cost. The standard and extended warranty obligations are recorded as warranty liabilities and included in other current liabilities in the consolidated balance sheets. For the fiscal year 2016 and 2015, the activity in the aggregate warranty liabilities was as follows (in thousands):

	December 31, 2016	January 2, 2016
Warranty liabilities, beginning of period	\$ 110	\$ 218
Adjustments to preexisting warranty liabilities	—	(109)
Additions to warranty liabilities	918	53
Reductions to warranty liabilities	(139)	(52)
Warranty liabilities, end of period	<u>\$ 889</u>	<u>\$ 110</u>

#### ***Marketing Expense***

Marketing costs, including advertising, are expensed as incurred. The majority of advertising expense is paid to internet search engine service providers and internet commerce facilitators. For fiscal year 2016, 2015 and 2014, the Company recognized advertising costs of \$22,616, \$20,251 and \$18,485, respectively. Marketing costs also include depreciation and amortization expense and share-based compensation expense.

#### ***General and Administrative Expense***

General and administrative expense consists primarily of administrative payroll and related expenses, merchant processing fees, legal and professional fees and other administrative costs. General and administrative expense also includes depreciation and amortization expense and share-based compensation expense.

#### ***Fulfillment Expense***

Fulfillment expense consists primarily of payroll and related costs associated with warehouse employees and the Company's purchasing group, facilities rent, building maintenance, depreciation and other costs associated with inventory management and wholesale operations. Fulfillment expense also includes share-based compensation expense.

#### ***Technology Expense***

Technology expense consists primarily of payroll and related expenses of our information technology personnel, the cost of hosting the Company's servers, communications expenses and Internet connectivity costs, computer support and software development amortization expense. Technology expense also includes share-based compensation expense.

#### ***Share-Based Compensation***

The Company accounts for share-based compensation in accordance with ASC 718 - *Compensation – Stock Compensation* ("ASC 718"). All share-based payment awards issued to employees are recognized as share-based compensation expense in the financial statements based on their respective grant date fair values, and are recognized within the statement of comprehensive income or loss as marketing, general and administrative, fulfillment or technology expense, based on employee departmental classifications. Under this standard, compensation expense for both time-based and performance-based restricted stock units is based on the closing stock price of our common shares on the date of grant, and is recognized on a straight-line basis over the requisite service period. Compensation expense for performance-based awards is measured based on the amount of shares ultimately expected to vest, estimated at each reporting date based on management's expectations regarding the relevant performance criteria. Compensation expense for stock options is based on the fair value estimated on the date of grant using an option pricing model, and is recognized over the vesting period of three to four years. The Company currently uses the Black-Scholes option pricing model to estimate the fair value of share-based payment awards for such stock options, which is affected by the Company's stock price and a number of assumptions, including expected volatility, expected life, risk-free interest rate and expected dividends.

The Company incorporates its own historical volatility into the grant-date fair value calculations for the stock options. The expected term of an award is based on combining historical exercise data with expected weighted time outstanding. Expected weighted time outstanding is calculated by assuming the settlement of outstanding awards is at the midpoint between the remaining weighted average vesting date and the expiration date. The risk-free interest rate assumption is based on observed interest rates appropriate for the expected life of awards. The dividend yield assumption is based on the Company's

expectation of paying no dividends on its common stock. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures significantly differ from those estimates. The Company considers many factors when estimating expected forfeitures, including employee class, economic environment, and historical experience.

The Company accounts for equity instruments issued in exchange for the receipt of services from non-employee directors in accordance with the provisions of ASC 718. The Company accounts for equity instruments issued in exchange for the receipt of goods or services from other than employees in accordance with ASC 505-50 - *Equity-Based Payments to Non-Employees*. Costs are measured at the estimated fair market value of the consideration received or the estimated fair value of the equity instruments issued, whichever is more reliably measurable. The value of equity instruments issued for consideration other than employee services is determined on the earlier of a performance commitment or completion of performance by the provider of goods or services. Equity instruments awarded to non-employees are periodically re-measured as the underlying awards vest unless the instruments are fully vested, immediately exercisable and non-forfeitable on the date of grant.

The Company accounts for modifications to its share-based payment awards in accordance with the provisions of ASC 718. Incremental compensation cost is measured as the excess, if any, of the fair value of the modified award over the fair value of the original award immediately before its terms are modified, measured based on the share price and other pertinent factors at that date, and is recognized as compensation cost on the date of modification (for vested awards) or over the remaining service (vesting) period (for unvested awards). Any unrecognized compensation cost remaining from the original award is recognized over the vesting period of the modified award.

#### ***Other Income, net***

Other income, net consists of miscellaneous income or expense such as gains/losses from disposition of assets, and interest income comprised primarily of interest income on investments.

#### ***Interest Expense***

Interest expense consists primarily of interest expense on our outstanding loan balance, deferred financing cost amortization, and capital lease interest.

#### ***Income Taxes***

The Company accounts for income taxes in accordance with ASC 740 - *Income Taxes* ("ASC 740"). Under ASC 740, deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. When appropriate, a valuation allowance is established to reduce deferred tax assets, which include tax credits and loss carry forwards, to the amount that is more likely than not to be realized. In making such determination, the Company considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, future taxable income exclusive of reversing temporary differences and carryforwards, taxable income in prior carryback years, tax planning strategies and recent financial operations.

The Company utilizes a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount which is more than 50% likely of being realized upon ultimate settlement. The Company considers many factors when evaluating and estimating our tax positions and tax benefits, which may require periodic adjustments and which may not accurately forecast actual outcomes. As of December 31, 2016, the Company had no material unrecognized tax benefits, interest or penalties related to federal and state income tax matters. The Company's policy is to record interest and penalties as income tax expense.

#### ***Taxes Collected from Customers and Remitted to Governmental Authorities***

We present taxes collected from customers and remitted to governmental authorities on a net basis in accordance with the guidance on ASC 605-45-50-3 - *Taxes Collected from Customers and Remitted to Governmental Authorities*.

#### ***Leases***

The Company analyzes lease agreements for operating versus capital lease treatment in accordance with ASC 840 *Leases*. Rent expense for leases designated as operating leases is expensed on a straight-line basis over the term of the lease. For capital leases, the present value of future minimum lease payments at the inception of the lease is reflected as a capital lease asset and

a capital lease payable in the consolidated balance sheets. Amounts due within one year are classified as current liabilities and the remaining balance as non-current liabilities.

### ***Foreign Currency Translation***

For each of the Company's foreign subsidiaries, the functional currency is its local currency. Assets and liabilities of foreign operations are translated into U.S. dollars using the current exchange rates, and revenues and expenses are translated into U.S. dollars using average exchange rates. The effects of the foreign currency translation adjustments are included as a component of accumulated other comprehensive income or loss in the Company's consolidated balance sheets.

### ***Comprehensive Income***

The Company reports comprehensive income or loss in accordance with ASC 220 - *Comprehensive Income*. Accumulated other comprehensive income or loss, included in the Company's consolidated balance sheets, includes foreign currency translation adjustments related to the Company's foreign operations, actuarial gains and losses on the Company's defined benefit plan and unrealized holding gains and losses from available-for-sale marketable securities and investments. The Company presents the components of net income or loss and other comprehensive income or loss in its consolidated statements of comprehensive operations.

### ***Segment Data***

The Company operates in two reportable operating segments. The criteria we use to identify operating segments are primarily the nature of the products we sell or services we provide and the consolidated operating results that are regularly reviewed by our chief operating decision maker to assess performance and make operating decisions. We identified two reportable operating segments, Base USAP, which is the core auto parts business, and AutoMD, an online automotive repair source, in accordance with ASC 280 - *Segment Reporting* ("ASC 280").

### ***Recently Adopted Accounting Pronouncements***

In July 2015, the FASB issued Accounting Standards Update No. 2015-11, "*Simplifying the Measurement of Inventory*," ("ASU 2015-11") which requires an entity to measure inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable cost of completion, disposal, and transportation. The new standard is effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017. The amendments in ASU 2015-11 should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period. This guidance was adopted by us in the fourth quarter of 2016, and it did not have a material impact on our consolidated financial statements.

In November 2014, the FASB issued Accounting Standards Update No. 2014-16 "*Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity*". The objective of this Update is to eliminate the use of different methods in practice and thereby reduce existing diversity under GAAP in the accounting for hybrid financial instruments issued in the form of a share. The new standard is effective for fiscal years beginning after December 15, 2015. Early adoption is permitted. The Company has adopted ASU 2014-16 and it did not have a material impact on our financial statements.

### ***Recent Accounting Pronouncements***

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2016-09, "*Compensation - Stock Compensation*" ("ASU 2016-09"). The objective of this update is to simplify accounting related to stock compensation. The new standard is effective for fiscal years beginning after December 15, 2016, and interim periods within those annual periods. The Company is evaluating the financial impacts that ASU 2016-09 will have on the consolidated financial statements and related disclosures, and it is not expected to have a material impact.

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2016-02, "*Leases*" ("ASU 2016-02"). The objective of this update is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The new standard is effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early adoption is permitted. The Company is evaluating the effect that ASU 2016-02 will have on the consolidated financial statements and related disclosures. The Company has not yet selected a transition method, however, due to the limited nature of our lease activity, it is not expected to have a material impact.

In May 2014, the FASB issued Accounting Standards Update No. 2014-9, “Revenue from Contracts with Customers,” (“ASU 2014-9”) which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. This guidance will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for fiscal years beginning after December 15, 2017. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-9 will have on the consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has the effect of the standard on ongoing financial reporting been determined, however, due to the nature of our revenue streams it is not expected to have a material impact.

## Note 2 – Short-term investments

As of December 31, 2016, the Company held the following short-term investments, recorded at fair value:

	Amortized Cost	Unrealized		Fair Value
		Gains	Losses	
Mutual funds <sup>(1)</sup>	\$ 32	\$ —	\$ (2)	\$ 30

As of January 2, 2016, the Company held the following short-term investments, recorded at fair value:

	Amortized Cost	Unrealized		Fair Value
		Gains	Losses	
Mutual funds <sup>(1)</sup>	\$ 65	\$ —	\$ —	\$ 65

- (1) Mutual funds are classified as short-term investments available-for-sale and recorded at fair market value, based on quoted prices of identical assets that are trading in active markets as of the end of the period for which the values are determined.

Proceeds from the sale of available-for-sale securities are disclosed separately in the accompanying consolidated statements of cash flow. For fiscal years 2016 and 2015, the Company recognized no realized gain or loss of from the sale of mutual funds.

## Note 3 – Fair Value Measurements

Fair value is defined as an exit price representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability.

Provisions of ASC 820 establish a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include:

- Level 1** – Observable inputs such as quoted prices in active markets;
- Level 2** – Inputs other than quoted prices in active markets that are either directly or indirectly observable; and
- Level 3** – Unobservable inputs in which little or no market data exists, therefore, requiring an entity to develop its own assumptions.

We measure our financial assets and liabilities at fair value on a recurring basis using the following valuation techniques:

- (a) Market Approach – uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.
- (b) Income Approach – uses valuation techniques to convert future estimated cash flows to a single present amount based on current market expectations about those future amounts, using present value techniques.

### *Financial Assets Valued on a Recurring Basis*

As of December 31, 2016 and January 2, 2016, the Company held certain assets that are required to be measured at fair value on a recurring basis. These included the Company’s financial instruments, including cash and cash equivalents and short-term investments. The following table represents our fair value hierarchy and the valuation techniques used for financial assets measured at fair value on a recurring basis:

December 31, 2016

	Total	Level 1	Level 2	Level 3	Valuation Techniques
<b>Assets:</b>					
Cash and cash equivalents <sup>(1)</sup>	\$ 6,643	\$ 6,643	\$ —	\$ —	(a)
Short-term investments – mutual funds <sup>(2)</sup>	30	30	—	—	(a)
	<u>\$ 6,673</u>	<u>\$ 6,673</u>	<u>\$ —</u>	<u>\$ —</u>	

January 2, 2016

	Total	Level 1	Level 2	Level 3	Valuation Techniques
<b>Assets:</b>					
Cash and cash equivalents <sup>(1)</sup>	\$ 5,537	\$ 5,537	\$ —	\$ —	(a)
Short-term investments – mutual funds <sup>(2)</sup>	65	65	—	—	(a)
	<u>\$ 5,602</u>	<u>\$ 5,602</u>	<u>\$ —</u>	<u>\$ —</u>	

- (1) Cash equivalents consist primarily of money market funds and short-term investments with original maturity dates of three months or less at the date of purchase, for which the Company determines fair value through quoted market prices.
- (2) Short-term investments consist of mutual funds, classified as available-for-sale and recorded at fair market value, based on quoted prices of identical assets that are trading in active markets as of the end of the period for which the values are determined.

During fiscal year 2016 and 2015, there were no transfers into or out of Level 1 and Level 2 assets.

***Non-Financial Assets Valued on a Non-Recurring Basis***

The Company's long-lived assets, including intangible assets subject to amortization, are measured at fair value on a non-recurring basis. These assets are measured at cost but are written-down to fair value, if necessary, as a result of impairment. During the fourth quarter of fiscal 2016 the Company identified a triggering event related to AutoMD, which indicated certain AutoMD long-lived assets may not be recoverable. As a result, the Company recorded an impairment loss on AutoMD intangible assets of \$1,130. The fair value measurements are categorized as Level 3 of the fair value hierarchy, as the Company developed its own assumptions and analysis to determine if such assets were impaired.

**Note 4 – Property and Equipment, Net**

The Company's fixed assets are stated at cost less accumulated depreciation, amortization and impairment. Depreciation and amortization expense are provided for in amounts sufficient to relate the cost of depreciable and amortizable assets to operations over their estimated service lives. Depreciation and amortization expense for fiscal year 2016, 2015 and 2014 was \$7,510, \$7,510 and \$8,923, respectively, which included amortization expense of \$475 in each year for capital leased assets. The cost and related accumulated depreciation of assets retired or otherwise disposed of are removed from the accounts and the resultant gain or loss is reflected in earnings.

Property and equipment consisted of the following at December 31, 2016 and January 2, 2016:

	December 31, 2016	January 2, 2016
Land	\$ 630	\$ 630
Building	8,877	8,877
Machinery and equipment	12,368	12,334
Computer software (purchased and developed) and equipment	26,717	27,083
Vehicles	98	136
Leasehold improvements	1,007	1,474
Furniture and fixtures	1,030	1,039
Construction in process	1,539	1,588
	<u>52,266</u>	<u>53,161</u>
Less accumulated depreciation and amortization	(35,788)	(34,730)
Property and equipment, net	<u>\$ 16,478</u>	<u>\$ 18,431</u>

On April 17, 2013, the Company's wholly-owned subsidiary, Whitney Automotive Group, Inc. ("WAG") entered into a sales leaseback for its facility in LaSalle, Illinois, receiving \$9,750 pursuant to a purchase and sale agreement dated April 17, 2013 between WAG and STORE Capital Acquisitions, LLC. The Company used the net proceeds of \$9,507 from this sale to reduce its revolving loan payable. Simultaneously with the execution of the purchase and sale agreement and the closing of the sale of the property, the Company entered into a lease agreement with STORE Master Funding III, LLC ("STORE") whereby we leased back the property for our continued use as an office, retail and warehouse facility for storage, sale and distribution of automotive parts, accessories and related items for 20 years, terminating on April 30, 2033. The related assets represent the amounts included in land and building in the summary above. The Company's initial base annual rent is \$853 for the first year ("Base Rent Amount"), after which the rental amount will increase annually on May 1 by the lesser of 1.5% or 1.25 times the change in the Consumer Price Index as published by the U.S. Department of Labor's Bureau of Labor Statistics, except that in no event will the adjusted annual rental amount fall below the Base Rent Amount. We were not required to pay any security deposit. Under the terms of the lease, we are required to pay all taxes associated with the lease, pay for any required maintenance on the property, maintain certain levels of insurance and indemnify STORE for losses incurred that are related to our use or occupancy of the property. The lease was accounted for as a capital lease and the \$376 excess of the net proceeds over the net carrying amount of the property is amortized in interest expense on a straight-line basis over the lease term of 20 years. As of December 31, 2016, the gross carrying value, the accumulated depreciation and the net carrying value of all capital leased assets included in property and equipment were \$11,306, \$2,273 and \$9,033, respectively. As of January 2, 2016, the gross carrying value, the accumulated depreciation and the net carrying value of all capital leased assets included in property and equipment were \$11,543, \$1,839 and \$9,704, respectively.

Construction in process primarily relates to the Company's internally developed software. Certain of the Company's net property and equipment were located in the Philippines as of December 31, 2016 and January 2, 2016, in the amount of \$367 and \$302, respectively.

Depreciation of property and equipment is provided using the straight-line method for financial reporting purposes, at rates based on the following estimated useful lives:

	Years
Machinery and equipment	2 - 5
Computer software (purchased and developed)	2 - 3
Computer equipment	2 - 5
Vehicles	3 - 5
Leasehold improvements*	3 - 5
Furniture and fixtures	3 - 7
Facility subject to capital lease	20

\* The estimated useful life is the lesser of 3-5 years or the lease term, whichever is shorter.

## Note 5 – Intangible Assets, Net

Intangible assets consisted of the following at December 31, 2016 and January 2, 2016:

	Useful Life	December 31, 2016			January 2, 2016		
		Gross Carrying Amount	Accumulated Amort. and Impairment	Net Carrying Amount	Gross Carrying Amount	Accum. Amort. and Impairment	Net Carrying Amount
Intangible assets subject to amortization:							
Product design intellectual property	4 years	2,750	(2,620)	130	2,750	(2,361)	389
Patent license agreements	3 - 5 years	562	(368)	194	562	(219)	343
Domain and trade names	10 years	1,407	(762)	645	1,407	(663)	744
Total		\$ 4,719	\$ (3,750)	\$ 969	\$ 4,719	\$ (3,243)	\$ 1,476

Intangible assets subject to amortization are amortized on a straight-line basis. Amortization expense relating to intangibles totaled \$507, \$464 and \$422 for fiscal year 2016, 2015 and 2014, respectively.

The following table summarizes the future estimated annual amortization expense for these assets over the next five years and thereafter:

2017	\$	319
2018		185
2019		100
2020		100
2021		100
Thereafter		165
Total	\$	969

## Note 6 – Borrowings

The Company maintains an asset-based revolving credit facility that provides for, among other things a revolving commitment in an aggregate principal amount of up to \$30,000, which is subject to a borrowing base derived from certain receivables, inventory and property and equipment. At December 31, 2016, our outstanding revolving loan balance was \$0. The customary events of default under the credit facility (discussed below) include certain subjective acceleration clauses, which management has determined the likelihood of such acceleration is more than remote, considering the recurring losses experienced by the Company, therefore a current classification of our revolving loan payable was required.

On November 15, 2016, the Company and JPMorgan Chase Bank, N.A. (“JPMorgan”) entered into the Tenth Amendment to Credit Agreement and Third Amendment to Pledge and Security Agreement (the “Amendment”), which amended the Credit Agreement previously entered into by the Company, certain of its domestic subsidiaries and JPMorgan on April 26, 2012 (as amended, the “Credit Agreement”) and the Pledge and Security Agreement previously entered into by the Company, certain of its domestic subsidiaries and JPMorgan on April 26, 2012. Pursuant to the Amendment, letters of credit can be issued if after giving effect to such issuance, the letters of credit exposure shall not exceed \$20,000, which was an increase from the previously agreed upon \$15,000. As of December 31, 2016, our outstanding letters of credit balance was \$11,658.

The following amendments to the Credit Agreement and Security Agreement were also made under the Tenth Amendment:

- The aggregate additional principal amount of indebtedness that is permitted related to capital leases was increased from \$2,000 to \$3,500.

- The Company's letters of credit exposure was increased from \$15,000 to \$20,000.
- Under the terms of the Security Agreement, cash receipts are deposited into a lock-box, which are at the Company's discretion unless the "cash dominion period" is in effect, during which cash receipts will be used to reduce amounts owing under the Credit Agreement. The cash dominion period is triggered in an event of default or if excess availability is less than the \$3,600 for three consecutive business days, and will continue until, during the preceding 60 consecutive days, no event of default existed and excess availability has been greater than \$3,600 at all times (with the trigger subject to adjustment based on the Company's revolving commitment).
- The Company's required excess availability related to the "Covenant Testing Trigger Period" (as defined under the Credit Agreement) under the revolving commitment under the Credit Agreement is less than \$2,400 for the period commencing on any day that excess availability is less than \$2,400 for three consecutive business days, and continuing until excess availability has been greater than or equal to \$2,400 at all times for 45 consecutive days (with the trigger subject to adjustment based on the Company's revolving commitment).
- The trigger, requiring the Company to provide certain reports under the Credit Agreement, relating to excess availability under the revolving commitment under the Credit Agreement is less than \$3,600 for the period commencing on any day that excess availability is less than \$3,600 for three consecutive business days, and continuing until excess availability has been greater than or equal to \$3,600 at all times for 45 consecutive days (with the trigger subject to adjustment based on the Company's revolving commitment).

Loans drawn under the credit facility bear interest at a per annum rate equal to either (a) LIBOR plus an applicable margin of 1.25%, or (b) a "base rate" subject to an increase or reduction by up to 0.25% per annum based on the Company's fixed charge coverage ratio. At December 31, 2016, the Company's LIBOR based interest rate was 2.06% (on \$0 principal) and the Company's prime based rate was 3.50% (on \$0 principal). A commitment fee, based upon undrawn availability under the Credit Facility bearing interest at a rate of 0.25% per annum, is payable monthly.

Certain of the Company's domestic subsidiaries are co-borrowers (together with the Company, the "Borrowers") under the Credit Agreement, and certain other domestic subsidiaries are guarantors (the "Guarantors" and, together with the Borrowers, the "Loan Parties") under the Credit Agreement. The Borrowers and the Guarantors are jointly and severally liable for the Borrowers' obligations under the Credit Agreement. The Loan Parties' obligations under the Credit Agreement are secured, subject to customary permitted liens and certain exclusions, by a perfected security interest in (a) all tangible and intangible assets and (b) all of the capital stock owned by the Loan Parties (limited, in the case of foreign subsidiaries, to 65% of the capital stock of such foreign subsidiaries). The Borrowers may voluntarily prepay the loans at any time. The Borrowers are required to make mandatory prepayments of the loans (without payment of a premium) with net cash proceeds received upon the occurrence of certain "prepayment events," which include certain sales or other dispositions of collateral, certain casualty or condemnation events, certain equity issuances or capital contributions, and the incurrence of certain debt.

The Credit Agreement contains customary representations and warranties and customary affirmative and negative covenants applicable to the Company and its subsidiaries, including, among other things, restrictions on indebtedness, liens, fundamental changes, investments, dispositions, prepayment of other indebtedness, mergers, and dividends and other distributions.

Events of default under the Credit Agreement include: failure to timely make payments due under the Credit Agreement; material misrepresentations or misstatements under the Credit Agreement and other related agreements; failure to comply with covenants under the Credit Agreement and other related agreements; certain defaults in respect of other material indebtedness; insolvency or other related events; certain defaulted judgments; certain ERISA-related events; certain security interests or liens under the loan documents cease to be, or are challenged by the Company or any of its subsidiaries as not being, in full force and effect; any loan document or any material provision of the same ceases to be in full force and effect; and certain criminal indictments or convictions of any Loan Party.

As of December 31, 2016, the Company had capital leases payable of \$10,312. The present value of the net minimum payments on capital leases as of December 31, 2016 is as follows:

Total minimum lease payments	\$ 17,947
Less amount representing interest	\$ (7,635)
Present value of net minimum lease payments	<u>10,312</u>
Current portion of capital leases payable	(542)
Capital leases payable, net of current portion	<u>\$ 9,770</u>



## Note 7 – Stockholders' Equity and Share-Based Compensation

### *Non-Controlling Interest*

Non-controlling interests represent equity interests in consolidated subsidiaries that are not attributable, either directly or indirectly, to the Company (i.e., minority interests). Non-controlling interests include the minority equity holders' proportionate share of the equity of AutoMD. As of March 6, 2017, all of the non-controlling interests of AutoMD were repurchased by the Company.

Ownership interests in subsidiaries held by parties other than the Company are presented as non-controlling interests within stockholders' equity, separately from the equity held by the Company. Revenues, expenses, net loss and other comprehensive income are reported in the consolidated financial statements at the consolidated amounts, which includes amounts attributable to both the Company's interest and the non-controlling interests in AutoMD. Net loss and other comprehensive income is then attributed to the Company's interest and the non-controlling interests. Net loss to non-controlling interests is deducted from net loss in the consolidated statements of comprehensive operations to determine net loss attributable to the Company's common stockholders.

The table below presents the changes in the Company's ownership interest in AutoMD on the Company's equity as of the dates indicated:

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
Net income (loss) attributable to U.S. Auto Parts stockholders'	\$ 731	\$ (1,281)	\$ (6,879)
Transfers (to) from the noncontrolling interest:			
Increase in U.S. Auto Parts paid-in-capital from sale of AutoMD common stock	—	—	2,512
Changes from net income (loss) attributable to U.S. Auto Parts stockholders' and transfers to noncontrolling interest	\$ 731	\$ (1,281)	\$ (4,367)

### *Common Stock*

The Company has 100,000 shares of common stock authorized. We have never paid cash dividends on our common stock. The following issuances of common stock were made during the fiscal year ended December 31, 2016:

- The Company issued 442 shares of common stock from option exercises under its various share-based compensation plans.
- The Company issued 439 shares of common stock from restricted stock units that vested during the period.
- The Company issued 10 shares of common stock for advisory services previously provided by a consultant.
- 37 shares of common stock were issued as stock dividends on the Series A Preferred.
- The Company issued 3 shares of common stock to one non-employee member of the Board of Directors for service fees earned during the period.

### *Treasury Stock*

On November 15, 2016, our Board of Directors approved a share repurchase program which authorizes the Company to purchase up to \$5,000 of its outstanding shares of common stock. Purchases under the Company's repurchase program may be made from time to time in the open market, in negotiated transactions off the market, or in such other manner as determined by the Company, including through plans complying with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended. The share repurchase program will expire on March 4, 2017, unless extended or shortened by the Board of Directors.

As of December 31, 2016, the Company repurchased 445 shares of common stock at an average price of \$3.09, for an aggregate purchase price of approximately \$1,376, net of costs.

### *Series A Convertible Preferred Stock*

On March 25, 2013, the Company authorized the issuance of 4,150 shares of Series A Preferred and entered into a Securities Purchase Agreement pursuant to which the Company agreed to sell up to an aggregate of 4,150 shares of our Series A Preferred, \$0.001 par value per share at a purchase price per share of \$1.45 for aggregate proceeds to the Company of approximately \$6,017. On March 25, 2013, we sold 4,000 shares of Series A Preferred for aggregate proceeds of \$5,800. On April 5, 2013, we sold the remaining 150 shares of Series A Preferred for aggregate proceeds of \$217. The Company incurred issuance costs of \$847 and used the net proceeds from the sale of the Series A Preferred to reduce its revolving loan payable.

Each share of Series A Preferred is convertible into shares of our common stock at the initial conversion rate of one share of common stock for each share of Series A Preferred. The conversion will be adjusted for certain non-price based events, such as dividends and distributions on the common stock, stock splits, combinations, recapitalizations, reclassifications, mergers, or consolidations. If not previously converted by the holder, the Series A Preferred will automatically convert to common stock if the volume weighted average price for the common stock for any 30 consecutive trading days is equal to or exceeds \$4.35 per share. The shares that would be issued if the contingently convertible Series A Preferred were converted are not excluded from the calculation of diluted earnings per share for the fiscal year ended December 31, 2016 (refer to "Note 8 – Net Loss Per Share" for anti-dilutive securities).

In the event of any liquidation event, which includes changes of control of the Company and sales or other dispositions by the Company of more than 50% of its assets, the Series A Preferred is entitled to receive, prior and in preference to any distribution to the common stock, an amount per share equal to \$1.45 per share of Series A Preferred, plus all then accrued but unpaid dividends on such Series A Preferred. Following this distribution, if assets or surplus funds remain, the holders of the common stock shall share ratably in all remaining assets of the Company, based on the number of shares of common stock then outstanding. Notwithstanding the foregoing, if, in connection with any liquidation event, a holder of Series A Preferred would receive an amount greater than \$1.45 per share of Series A Preferred by converting such shares held by such holder into shares of common stock, then such holder shall be treated as though such holder had converted such shares of Series A Preferred into shares of common stock immediately prior to such liquidation event, whether or not such holder had elected to so convert.

Dividends on the Series A Preferred are payable quarterly at a rate of \$0.058 per share per annum in cash, in shares of common stock or in any combination of cash and common stock as determined by the Company's Board of Directors. Certain conditions are required to be satisfied in order for the Company to pay dividends on the Series A Preferred in shares of common stock, including (i) the common stock being registered pursuant to Section 12(b) or (g) of the Securities Exchange Act of 1934, as amended, (ii) the common stock being issued having been approved for listing on a trading market and (iii) the common stock being issued either being covered by an effective registration statement or being freely tradable without restriction under Rule 144 (subject to certain exceptions). The Series A Preferred shall each be entitled to one vote per share for each share of common stock issuable upon conversion thereof (excluding from any such calculation any dividends accrued on such shares) and shall vote together with the holders of common stock as a single class on any matter on which the holders of common stock are entitled to vote. In addition, the Company must obtain the consent of holders of at least a majority of the then outstanding Series A Preferred in connection with (a) any amendment, alteration or repeal of any provision of the certificate of incorporation or bylaws of the Company as to adversely affect the preferences, rights or voting power of the Series A Preferred, or (b) the creation, authorization or issuance of any additional Series A Preferred or any other class or series of capital stock of the Company ranking senior to or on parity with the Series A Preferred or any security convertible into, or exchangeable or exercisable for Series A Preferred or any other class or series of capital stock of the Company ranking senior to or on parity with the Series A Preferred. Concurrent with the Company's issuance of Series A Preferred, the Company, certain of its domestic subsidiaries and JPMorgan entered into a Second Amended Credit Agreement to allow the Company to pay cash dividends on the Series A Preferred in an aggregate amount of up to \$400 per year and pay cash in lieu of issuing fractional shares upon conversion of or in payment of dividends on the Series A Preferred (refer to "Note 6 – Borrowings" of our Notes to Consolidated Financial Statements for additional details). For the fiscal year ended January 3, 2015, the Company recorded dividends of \$240. The Company issued 83 shares of common stock in payment of the fiscal 2014 dividends. There were no accrued dividends outstanding as of January 3, 2015. For the fiscal year ended January 2, 2016, the Company recorded dividends of \$241. The Company issued 103 shares of common stock in payment of the fiscal 2015 dividends. There were no accrued dividends outstanding as of January 2, 2016. For the fiscal year ended December 31, 2016, the Company recorded dividends of \$241. The Company issued 37 shares of common stock in payment of the fiscal 2016 dividends. There were \$61 dividends accrued as of December 31, 2016.

### ***Share-Based Compensation Plan Information***

The Company adopted the 2016 Equity Incentive Plan ("2016 Equity Plan") on March 9, 2016, which became effective on May 31, 2016, following stockholder approval. Subject to adjustment for certain changes in the Company's capitalization, the aggregate number of shares of the Company's common stock that may be issued under the 2016 Equity Plan will not exceed the sum of (i) two million five hundred thousand (2,500) new shares, (ii) the number of unallocated shares remaining available for the grant of new awards under the Company's prior equity plans described below (the "Prior Equity Plans") as of the effective date of the 2016 Plan (which was equal to 3,894 shares as of May 31, 2016) and (iii) any shares subject to a stock award under the Prior Equity Plans that are not issued because such stock award expires or otherwise terminates without all of the shares covered by such stock award having been issued, that are not issued because such stock award is settled in cash, that are forfeited back to or repurchased by the Company because of the failure to meet a contingency or condition required for the vesting of such shares, or that are reacquired, withheld (or not issued) to satisfy a tax withholding obligation in connection with an award or to satisfy the purchase price or exercise price of a stock award. In addition, the share reserve will automatically

increase on January 1st of each year, for a period of nine years, commencing on January 1, 2017 and ending on (and including) January 1, 2026, in an amount equal to one million five hundred thousand (1,500) shares per year; however the Board of Directors of the Company may act prior to January 1st of a given year to provide that there will be no January 1st increase in the share reserve for such year or that the increase in the share reserve for such year will be a lesser number of shares of common stock than would otherwise occur pursuant the automatic increase. Options granted under the 2016 Equity Plan generally expire no later than ten years from the date of grant and generally vest over a period of four years. The exercise price of all option grants must be equal to 100% of the fair market value on the date of grant. As of December 31, 2016, 6,307 shares were available for future grants under the 2016 Equity Plan.

The Company adopted the 2007 Omnibus Incentive Plan (the “2007 Omnibus Plan”) in January 2007, which became effective on February 8, 2007, the effective date of the registration statement filed in connection with the Company’s initial public offering. Under the 2007 Omnibus Plan, the Company was previously authorized to issue 2,400 shares of common stock, under various instruments to eligible employees and non-employees of the Company, plus an automatic annual increase on the first day of each of the Company’s fiscal years beginning on January 1, 2008 and ending on January 1, 2017 equal to (i) the lesser of (A) 1,500 shares of common stock or (B) five percent (5)% of the number of shares of common stock outstanding on the last day of the immediately preceding fiscal year or (ii) such lesser number of shares of common stock as determined by the Company’s Board of Directors. Options granted under the 2007 Omnibus Plan generally expire no later than ten years from the date of grant and generally vest over a period of four years. The exercise price of all option grants must be equal to 100% of the fair market value on the date of grant. The 2007 Omnibus Plan also allows for the grant of options to purchase common stock and common stock awards to non-employee directors. As of December 31, 2016, 0 shares were available for future grants under the 2007 Omnibus Plan.

The Company adopted the 2007 New Employee Incentive Plan (the “2007 New Employee Plan”) in October 2007. Under the 2007 New Employee Plan, the Company was authorized to issue 2,000 shares of common stock under various instruments solely to new employees. Options granted under the 2007 New Employee Plan generally expire no later than ten years from the date of grant and generally vest over a period of four years. The exercise price of all option grants must not be less than 100% of the fair market value on the date of grant. As of December 31, 2016, 0 shares were available for future grants under the 2007 New Employee Plan.

The Company adopted the U.S. Auto Parts Network, Inc. 2006 Equity Incentive Plan (the “2006 Plan”) in March 2006. All stock options to purchase common stock granted to employees in 2006 were granted under the 2006 Plan and had exercise prices equal to the fair value of the underlying stock, as determined by the Company’s Board of Directors on the applicable option grant date. After fiscal year 2008, no shares have been available for future grants under the 2006 Plan.

The following tables summarizes the Company’s stock option activity for the fiscal years ended, and details regarding the options outstanding and exercisable at December 31, 2016, and January 2, 2016:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value <sup>(1)</sup>
Options outstanding, January 2, 2016	5,841	\$ 2.80		
Granted	1,000	\$ 3.03		
Exercised	(442)	\$ 2.06		
Cancelled:				
Forfeited	(149)	\$ 2.47		
Expired	(122)	\$ 7.66		
Options outstanding, December 31, 2016	6,128	\$ 2.81	5.74	\$ 6,561
Vested and expected to vest at December 31, 2016	5,658	\$ 2.82	5.49	\$ 6,111
Options exercisable, December 31, 2016	4,220	\$ 2.92	4.49	\$ 4,618

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value <sup>(1)</sup>
Options outstanding, January 3, 2015	5,281	\$ 2.85		
Granted	1,315	\$ 2.24		
Exercised	(301)	\$ 1.45		
Cancelled:				
Forfeited	(256)	\$ 2.06		
Expired	(198)	\$ 3.31		
Options outstanding, January 2, 2016	5,841	\$ 2.80	6.03	\$ 4,333
Vested and expected to vest at January 2, 2016	5,285	\$ 2.88	5.74	\$ 3,853
Options exercisable, January 2, 2016	3,735	\$ 3.21	4.54	\$ 2,479

- (1) These amounts represent the difference between the exercise price and the closing price of U.S. Auto Parts Network, Inc. common stock on December 31, 2016 as reported on the NASDAQ Stock Market, for all options outstanding that have an exercise price currently below the closing price.

The weighted-average fair value of options granted during fiscal year 2016, 2015 and 2014 was \$1.65, \$1.19 and \$1.34, respectively. The intrinsic value of stock options at the date of the exercise is the difference between the fair value of the stock at the date of exercise and the exercise price. During fiscal year 2016, 2015 and 2014, the total intrinsic value of the exercised options was \$599, \$346 and \$153, respectively. The Company had \$1,344 of unrecognized share-based compensation expense related to stock options outstanding as of December 31, 2016, which expense is expected to be recognized over a weighted-average period of 2.34 years.

The following tables summarize the Company's stock option activity under the AutoMD 2014 Equity Incentive Plan (the "AMD Plan") for the fiscal years ended, and details regarding the options outstanding and exercisable at December 31, 2016 and January 2, 2016:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Options outstanding, January 2, 2016	1,430	\$ 1.00		
Granted	10	\$ 1.00		
Exercised	—	\$ —		
Cancelled:				
Forfeited	(35)	\$ 1.00		
Expired	—	\$ —		
Options outstanding, December 31, 2016	1,405	\$ 1.00	8.20	
Vested and expected to vest at December 31, 2016	1,044	\$ 1.00	8.19	
Options exercisable, December 31, 2016	632	\$ 1.00	8.14	

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Options outstanding, January 3, 2015	180	\$ 1.00		
Granted	1,250	\$ 1.00		
Exercised	—	\$ —		
Cancelled:				
Forfeited	—	\$ —		
Expired	—	\$ —		
Options outstanding, January 2, 2016	1,430	\$ 1.00	9.19	\$ —
Vested and expected to vest at January 2, 2016	1,061	\$ 1.00	9.19	\$ —
Options exercisable, January 2, 2016	49	\$ 1.00	8.92	\$ —

At December 31, 2016 520 shares were available for future grants under the AMD Plan.

The weighted-average fair value of options granted during fiscal year 2016, 2015 and 2014 was \$0.55, \$0.55 and \$0.56, respectively. The intrinsic value of stock options at the date of the exercise is the difference between the fair value of the stock at the date of exercise and the exercise price. The Company had \$224 of unrecognized share-based compensation expense related to stock options outstanding as of December 31, 2016, which expense is expected to be recognized over a weighted-average period of 2.20 years.

Options exercised under all share-based compensation plans are granted net of the minimum statutory withholding requirements that we pay in cash to the appropriate taxing authorities on behalf of our employees. For those employees who elect not to receive shares net of the minimum statutory withholding requirements, the appropriate taxes are paid directly by the employee. During fiscal 2016, we withheld 0 shares to satisfy \$0 of employees' tax obligations and 0 shares related to the net settlement of the stock options. During fiscal 2015, we withheld 27 shares to satisfy \$80 of employees' tax obligations and 112 shares related to the net settlement of the stock options.

#### ***Restricted Stock Units***

During 2016 and 2015 the Company granted an aggregate of 954 and 435 RSUs, respectively, to certain employees of the Company. The RSUs were granted under the 2007 Omnibus Plan, and reduced the pool of equity instruments available under that plan.

During 2016 there were 382 RSUs granted that were time-based and 572 were performance-based. All of the RSUs granted during 2015 were time-based. As of March 3, 2017, 525 of the performance-based RSUs met the maximum performance criteria upon certification by the Compensation Committee and 47 PSUs were forfeited. Of the RSUs granted during 2015, 348 vested, 30 remain unvested, and 57 were forfeited during 2016. The vesting of each RSU is subject to the employee's continued employment through applicable vesting dates. Some RSUs granted to certain executives may vest on an accelerated basis in part or in full upon the occurrence of certain events. The RSUs are accounted for as equity awards and are measured at fair value based upon the grant date price of the Company's common stock. The closing price of the Company's common stock on January 21, 2016 and February 29, 2016, the date of each grant was \$2.64 and \$2.75, respectively. The closing price of the Company's common stock on January 29, 2015, March 23, 2015, May 20, 2015, June 23, 2015 and July 28, 2015, the date of each grant, was \$2.29, \$2.18, \$2.33, \$2.23, and \$2.18 per share, respectively. Compensation expense is recognized on a straight-line basis over the requisite service period of one-to-three years. Compensation expense for performance-based awards is measured based on the amount of shares ultimately expected to vest, estimated at each reporting date based on management's expectations regarding the relevant performance criteria.

For the fiscal year ended December 31, 2016, we recorded compensation expense of \$1,626 related to RSU's. As of December 31, 2016, there was unrecognized compensation expense of \$ 600 related to unvested RSUs based on awards that are expected to vest. The unrecognized compensation expense is expected to be recognized over a weighted-average period of 0.63 years.

#### ***Stock Option Exchange Program***

On July 9, 2013, the Company's stockholders approved a proposed stock option exchange program for the exchange of certain outstanding stock options held by eligible employees for new options to purchase fewer shares. On August 12, 2013, the Company commenced an offering to eligible employees to voluntarily exchange certain vested and unvested stock options with exercise prices above \$4.00 per share at an exchange ratio of 3.5 to 1 to be granted following the expiration of the tender offer with exercise prices equal to the fair market value of one share of the Company's common stock on the day the new options were issued. Stock options to purchase an aggregate of 3,733 shares with exercise prices ranging from \$4.01 to \$11.68 were eligible for tender at the commencement of the program. The Company's non-employee directors were not eligible to participate in the program. The terms and conditions of the new options are subject to an entirely new four year vesting schedule where 25% will vest on the first anniversary, and the remaining 75% will vest monthly over the following 36 months. All new options have a ten year contractual term. The offer period for the stock option exchange ended on September 9, 2013. There were no modifications or exchanges to share based payment awards in fiscal 2015 or 2016.

On September 10, 2013, the Company accepted for exchange 3,475 eligible options to purchase common stock, with a weighted average exercise price of \$6.65 for 45 eligible employees, and issued 993 unvested options to purchase shares of the Company's common stock with an exercise price of \$0.9866, the closing price of the Company's common stock on that day. Using the Black-Scholes option pricing model, the Company determined that the fair value of the surrendered stock options on a grant-by-grant basis was lower than the fair value of the new stock options, as of the date of the exchange, resulting in incremental fair value of \$422. The incremental fair value as a result of the stock option exchange and the remaining compensation expense associated with the surrendered stock options will be recorded as compensation expense over the four year vesting period of the new options.

The fair value of the surrendered stock options and the new stock options was estimated on the date of the exchange using the Black-Scholes option pricing model with the following assumptions:

	Surrendered Stock Options	New Stock Options
Expected life	1.93 – 6.87 years	5.84 years
Risk-free interest rate	0.5% – 2.4%	2.0%
Expected volatility	55% – 73%	72%
Expected dividend yield	—%	—%

#### ***Warrants***

On May 5, 2009, the Company issued warrants to purchase up to 30 shares of common stock at an exercise price of \$2.14 per share. On April 27, 2010, the Company issued additional warrants to purchase up to 20 shares of common stock at an exercise price of \$8.32 per share. Both issuances of warrants terminate seven years after their grant date. The warrants were issued in connection with the financial advisory services provided by a consultant to the Company. On August 8, 2016 10 shares of common stock were issued in settlement of the May 5, 2009 warrants. As of December 31, 2016, warrants to purchase 20 shares of common stock were outstanding and exercisable. The aggregate intrinsic value of outstanding and exercisable warrants was \$0 as of December 31, 2016, which was calculated as the difference between the exercise price of underlying awards and the closing price of the Company's common stock for warrants that were in-the-money. No warrants share-based compensation expense was recognized during the fiscal years 2016, 2015 and 2014. The Company had no unrecognized share-based compensation expense related to warrants outstanding as of December 31, 2016.

#### ***Share-Based Compensation Expense***

The fair value of each option grant, excluding those options issued from the stock option exchange program as discussed above, was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions for each of the periods ended:

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
Expected life	5.57 - 5.61 years	5.34 - 5.52 years	5.30 - 5.37 years
Risk-free interest rate	1% - 2%	1% - 2%	2% - 2%
Expected volatility	60% - 61%	59% - 60%	62% - 68%
Expected dividend yield	—%	—%	—%

Share-based compensation from options and RSUs, is included in our consolidated statements of comprehensive operations, as follows:

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
Marketing expense	\$ 433	\$ 518	\$ 540
General and administrative expense	2,111	1,614	1,476
Fulfillment expense	450	241	220
Technology expense	137	46	135
Total share-based compensation expense	\$ 3,131	\$ 2,419	\$ 2,371

The share-based compensation expense is net of amounts capitalized to internally-developed software of \$83, \$146 and \$196 during the fiscal year 2016, 2015, and 2014, respectively. No tax benefit was recognized for fiscal years 2016, 2015, and 2014 due to the valuation allowance position.

Under ASC 718, forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures significantly differ from those estimates. The Company's estimated forfeiture rates are calculated based on actual historical forfeitures experienced under our equity plans. The Company's forfeiture rates were 10%-34% for fiscal years 2016, 2015, and 2014.

#### Note 8 – Net Income (Loss) Per Share

The following table sets forth the computation of basic and diluted net income (loss) per share:

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
<b>Net income (loss) per share:</b>			
Numerator:			
Net income (loss) attributable to U.S. Auto Parts	\$ 731	\$ (1,281)	\$ (6,879)
Dividends on Series A Convertible Preferred Stock	(241)	(241)	(240)
Net income (loss) available to common shares	\$ 490	\$ (1,522)	\$ (7,119)
Denominator:			
Weighted-average common shares outstanding (basic)	34,765	33,946	33,489
Common equivalent shares from common stock options, preferred stock and warrants	1,442	—	—
Weighted-average common shares outstanding (diluted)	36,207	33,946	33,489
Basic net income (loss) per share	\$ 0.01	\$ (0.04)	\$ (0.21)
Diluted net income (loss) per share	\$ 0.01	\$ (0.04)	\$ (0.21)

The anti-dilutive securities, which are excluded from the calculation of diluted earnings per share due to the Company's net loss position for the periods then ended (including securities that would otherwise be excluded from the calculation of diluted earnings per share due the Company's stock price), are as follows (in thousands):

	Fiscal Year		
	December 31, 2016	January 2, 2016	January 3, 2015
Common stock warrants	20	50	50
Series A Convertible Preferred Stock	4,150	4,150	4,150
Options to purchase common stock	2,142	5,941	5,467
Restricted Stock Units	—	839	796
Total	6,312	10,980	10,463

#### Note 9 – Income Taxes

The components of loss before income tax provision consist of the following:

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
Domestic operations	\$ (1,305)	\$ (3,718)	\$ (7,424)
Foreign operations	503	483	476
Total loss before income taxes	<u>\$ (802)</u>	<u>\$ (3,235)</u>	<u>\$ (6,948)</u>

Income tax (benefit) provision for fiscal year 2016, 2015 and 2014 consists of the following:

	Fiscal Year Ended		
	December 31, 2016	January 2, 2016	January 3, 2015
Current:			
Federal tax	\$ —	\$ —	\$ —
State tax	7	7	(15)
Foreign tax	162	88	78
Total current taxes	<u>169</u>	<u>95</u>	<u>63</u>
Deferred:			
Federal tax	(331)	(1,887)	(2,232)
State tax	(616)	591	(125)
Foreign tax	—	61	74
Total deferred taxes	<u>(947)</u>	<u>(1,235)</u>	<u>(2,283)</u>
Valuation allowance	579	329	2,358
Income tax (benefit) provision	<u>\$ (199)</u>	<u>\$ (811)</u>	<u>\$ 138</u>

Income tax (benefit) provision differs from the amount that would result from applying the federal statutory rate as follows:

	December 31, 2016	January 2, 2016	January 3, 2015
Income tax at U.S. federal statutory rate	\$ (273)	\$ (1,100)	\$ (2,362)
Share-based compensation	316	50	33
State income tax, net of federal tax effect	(559)	672	(143)
Foreign tax	20	(18)	117
Basis difference in subsidiary equity	(267)	(820)	—
Other	(15)	76	127
Change in valuation allowance	579	329	2,366
Effective tax (benefit) provision	<u>\$ (199)</u>	<u>\$ (811)</u>	<u>\$ 138</u>

For fiscal year 2016, 2015 and 2014, the effective tax rate for the Company was 24.8%, 25.1% and (2.0)%, respectively. The Company's effective tax rate for fiscal years 2016 and 2015 differs from the U.S. federal rate primarily as a result of the recording of the basis difference in the Company's subsidiary and the recording of valuation allowances against the Company's deferred tax assets. The Company's effective tax rate for fiscal year 2014 differs from the U.S. federal rate primarily as a result of the recording of valuation allowances against the Company's deferred tax assets.



Deferred tax assets and deferred tax liabilities consisted of the following:

	December 31, 2016	January 2, 2016
Deferred tax assets:		
Inventory and inventory related allowance	\$ 839	\$ 976
Share-based compensation	5,083	4,924
Amortization	7,636	9,244
Sales and bad debt allowances	749	443
Vacation accrual	224	220
Book over tax amortization	—	31
Net operating loss and AMT credit carry-forwards	33,026	30,254
Other	800	843
Total deferred tax assets	48,357	46,935
Valuation Allowance	(46,775)	(46,196)
Net deferred tax assets	1,582	739
Deferred tax liabilities:		
Investment in subsidiary	—	368
Tax over book depreciation	1,518	639
Foreign tax withholdings	—	470
Prepaid catalog expenses	64	100
Total deferred tax liabilities	1,582	1,577
Net deferred tax liabilities	\$ —	\$ (838)

At December 31, 2016, federal and state net operating loss (“NOL”) carryforwards were \$75,261 and \$83,027, respectively. Federal NOL carryforwards of \$2,690 were acquired in the acquisition of WAG which are subject to Internal Revenue Code section 382 and limited to an annual usage limitation of \$135. Federal NOL carryforwards begin to expire in 2029, while state NOL carryforwards begin to expire in 2017. The state NOL carryforwards expire in the respective tax years as follows:

	2017	\$ 6,930
	2018	1,132
	2019	7,646
	2020	2,121
	2021	4,050
Thereafter		61,148
		\$ 83,027

On October 8, 2014, AutoMD sold seven million shares of its common stock to third-party investors, reducing the Company’s ownership interest in AutoMD to 64.1%. As a result, AutoMD was excluded from the consolidated state and federal tax filings of the Company for fiscal year 2016. As a result of the investment a deferred tax liability of \$1,335 was created which reduced the increase in additional paid-in-capital which was created as a result of the investment. At December 31, 2016, AutoMD had net operating loss carryforwards (NOLs) of approximately \$7,506 for federal tax purposes that begin to expire in 2031. AutoMD state NOLs were not material as of December 31, 2016.

Under the provisions of ASC 740, management is required to evaluate whether a valuation allowance should be established against its deferred tax assets based on the consideration of all available evidence using a “more likely than not” standard. Realization of deferred tax assets is dependent upon taxable income in prior carryback years, estimates of future taxable income, tax planning strategies, and reversal of existing taxable temporary differences. ASC 740 provides that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years or losses expected in early future years. Based on this evaluation, as of December 31, 2016, a valuation allowance of \$46,775 has been recorded against our deferred tax assets.

We are subject to U.S. federal income tax as well as income tax of foreign and state tax jurisdictions. During fiscal 2010, the Company was audited by the Internal Revenue Service for the year ended December 31, 2008. The audit was concluded with no change. The tax years 2012-2015 remain open to examination by the major taxing jurisdictions to which the Company is subject, except the Internal Revenue Service for which the tax years 2013-2015 remain open. The Company does not anticipate a significant change to the amount of unrecognized tax benefits within the next twelve months.

Included in accrued expenses are income taxes payable of \$35 and \$12 for the fiscal year 2016 and 2015 respectively, consisting primarily of current foreign taxes. Included in other non-current liabilities are income taxes payable of \$525, \$470 and \$409 for the fiscal year 2016, 2015 and 2014 respectively relating to future foreign withholding taxes.

**Note 10 – Commitments and Contingencies**

***Facilities Leases***

The Company’s corporate headquarters is located in Carson, California. The Company’s corporate headquarters has a lease term through October 2020, which was renewed in June 2016. The Company also leases warehouse space in LaSalle, Illinois and in Chesapeake, Virginia. The Company’s Philippines subsidiary leases office space under an agreement through April 2020.

Facility rent expense for fiscal year ended 2016, 2015 and 2014 was \$1,670, \$1,555 and \$1,895, respectively. The Company’s facility rent expense did not include any amounts charged from a related party during fiscal years 2016 and 2015, and was inclusive of amounts charged from a related party of \$378 for fiscal 2014.

On February 4, 2016, the Company entered into a new lease for its distribution center located in Chesapeake, Virginia. The Lease between the Company and Liberty Property Limited Partnership is for approximately 159,294 square feet. The initial three-year term of the Lease commenced on July 1, 2016. The Company is obligated to pay approximately \$640 in annual base rent, which shall increase by approximately 2.5% each year. The Company is also obligated to pay certain operating expenses set forth in the Lease. Pursuant to the Lease, the Company has the option to extend the Lease for an additional three-year term, with certain increases in base rent. The monthly base rent commitment was \$53 as of December 31, 2016.

In January 2010, the Company’s Philippines subsidiary entered into a new lease agreement that accommodates the Company’s Philippines workforce into one office building. Under the terms of the lease agreement, effective March 1, 2010, the monthly rent was approximately \$25, and became subject to 5% annual escalation beginning on the 3rd year of the lease term. The lease renewed for a sixty month term upon mutual agreement of both parties during 2015.

As described in detail under “*Note 4 – Property and Equipment Net*”, on April 17, 2013, the Company entered into a sale lease-back agreement with STORE Master Funding III, LLC (“STORE”) whereby we leased back our facility located in LaSalle, Illinois for our continued use as an office, retail and warehouse facility for storage, sale and distribution of automotive parts, accessories and related items for 20 years commencing upon the execution of the lease and terminating on April 30, 2033. The related assets for the sale lease-back land and building is represented by the amount included in leased facility in the summary above. The Company’s initial base annual rent is \$853 for the first year (“Base Rent Amount”), after which the rental amount will increase annually on May 1 by the lesser of 1.5% or 1.25 times the change in the Consumer Price Index as published by the U.S. Department of Labor’s Bureau of Labor Statistics, except that in no event will the adjusted annual rental amount fall below the Base Rent Amount. We were not required to pay any security deposit. Under the terms of the lease, we are required to pay all taxes associated with the lease, pay for any required maintenance on the property, maintain certain levels of insurance and indemnify STORE for losses incurred that are related to our use or occupancy of the property. The lease was accounted for as a capital lease and the \$376 excess of the net proceeds over the net carrying amount of the property is amortized in interest expense on a straight-line basis over the lease term of 20 years. As of December 31, 2016, the net carrying value of all capital leased assets included in property and equipment was \$9,033.

Minimum lease commitments under non-cancelable operating leases as of December 31, 2016 are as follows:

2017	\$	1,453
2018		1,493
2019		1,200
2020		550
2021		—
Total		<u>4,696</u>

Capital lease commitments as of December 31, 2016 were as follows:

	Capital Lease Commitments	Less: Interest Payments	Principal Obligations
2017	\$ 1,285	\$ 743	\$ 542
2018	1,319	721	598
2019	1,304	690	614
2020	1,129	657	472
2021	962	630	332
2022 onwards	11,948	4,194	7,754
<b>Total</b>	<b>\$ 17,947</b>	<b>\$ 7,635</b>	<b>\$ 10,312</b>

### **Legal Matters**

**Asbestos.** A wholly-owned subsidiary of the Company, Automotive Specialty Accessories and Parts, Inc. and its wholly-owned subsidiary WAG, are named defendants in several lawsuits involving claims for damages caused by installation of brakes during the late 1960's and early 1970's that contained asbestos. WAG marketed certain brakes, but did not manufacture any brakes. WAG maintains liability insurance coverage to protect its and the Company's assets from losses arising from the litigation and coverage is provided on an occurrence rather than a claims made basis, and the Company is not expected to incur significant out-of-pocket costs in connection with this matter that would be material to its consolidated financial statements.

The Company is subject to legal proceedings and claims which arise in the ordinary course of its business. As of the date hereof, the Company believes that the final disposition of such matters will not have a material adverse effect on the financial position, results of operations or cash flow of the Company. The Company maintains liability insurance coverage to protect the Company's assets from losses arising out of or involving activities associated with ongoing and normal business operations.

### **Note 11 – Employee Retirement Plan and Deferred Compensation Plan**

Effective February 17, 2006, the Company adopted a 401(k) defined contribution retirement plan covering all full time employees who have completed one month of service. The Company may, at its sole discretion, match fifty cents per dollar up to 6% of each participating employee's salary. The Company's contributions vest in annual installments over three years. Discretionary contributions made by the Company totaled \$289, \$280 and \$256 for fiscal year 2016, 2015 and 2014, respectively.

In January 2010, the Company adopted the U.S. Auto Parts Network, Inc. Management Deferred Compensation Plan (the "Deferred Compensation Plan"), for the purpose of providing highly compensated employees a program to meet their financial planning needs. The Deferred Compensation Plan provides participants with the opportunity to defer up to 90% of their base salary and up to 100% of their annual earned bonus, all of which, together with the associated investment returns, are 100% vested from the outset. The Deferred Compensation Plan, which is designed to be exempt from most provisions of the Employee Retirement Security Act of 1974, is informally funded by the Company through the purchase of Company-owned life insurance policies with the Company (employer) as the owner and beneficiary, in order to preserve the tax-deferred savings advantages of a non-qualified plan. The plan assets are the cash surrender value of the Company-owned life insurance policies and not associated with the deferred compensation liability. The deferred compensation liabilities (consisting of employer contributions, employee deferrals and associated earnings and losses) are general unsecured obligations of the Company. Liabilities under the Deferred Compensation Plan are recorded at amounts due to participants, based on the fair value of participants' selected investments. The Company may at its discretion contribute certain amounts to eligible employee accounts. In January 2010, the Company began to contribute 50% of the first 2% of participants' eligible contributions into their Deferred Compensation Plan accounts. In September 2010, the Company established and transferred its ownership to a rabbi trust to hold the Company-owned life insurance policies. As of December 31, 2016, the assets and associated liabilities of the Deferred Compensation Plan were \$676 and \$688, respectively, and were \$781 and \$558, respectively, as of January 2, 2016 and are included in other non-current assets, other current liabilities and other non-current liabilities in our consolidated balance sheets. For fiscal year 2016, the change in the associated liabilities include the employee contributions of \$156, the Company contributions of \$69, offset by unrealized earnings of \$41 and distributions of \$23. For fiscal year 2015, the associated liabilities primarily include the employee contributions of \$102 and the Company contributions of \$27 offset by unrealized losses of \$13 and distributions of \$307. For fiscal year 2016, included in other income, the Company recorded a net loss of \$2 for the change in the cash surrender value of the Company-owned life insurance policies. For fiscal year 2015, included in other income, the Company recorded a net loss of \$73 for the change in the cash surrender value of the Company-owned life insurance policies.

## Note 12 – Restructuring Costs

### *Fiscal 2014*

On June 25, 2014, the Company committed to a plan to permanently close its distribution facility located in Carson, California (the “Carson Distribution Facility”) effective July 25, 2014. The Company consolidated the Carson Distribution Facility’s distribution and warehousing operations into the Company’s existing distribution facilities located in LaSalle, Illinois and Chesapeake, Virginia. This consolidation was part of the Company’s continued efforts for simplification and improved efficiencies. The closure of the Carson Distribution Facility resulted in a head count reduction of approximately 77 employees.

The following table summarizes the charges related to the restructure recognized during the fiscal year ended January 3, 2015:

Employee severance	\$	526
Accounts receivable allowance		73
Relocation costs (employee and equipment)		127
Inventory transfers		411
Total restructuring costs	\$	<u>1,137</u>

Substantially all of the unsold inventory in the Carson Distribution Facility on the date of closure was moved to the remaining two warehouses. Costs related to inventory transfers were recorded to cost of sales. A charge for \$130 was taken for inventory that was not deemed economical to transfer. Additionally, due to expected future capacity constraints, the Company reduced the sales price of certain inventory resulting in a charge of \$767. The aggregate charge of \$897 was recorded to cost of sales. The severance charges and relocation costs were included in fulfillment expense. Severance charges were reduced by \$26 in the fourth quarter of 2014 as certain employees were able to find employment before they became eligible for severance benefits. As of January 3, 2015, there was no severance payable.

## Note 13 – Related-Party Transactions

The Company leased its Carson warehouse from Nia Chloe, LLC (“Nia Chloe”), a member of which, Sol Khazani, is one of our board of directors. Lease payments and expenses associated with this related party arrangement totaled \$378 for fiscal year 2014. The lease expired during fiscal 2014 and was not renewed.

On October 8, 2014, Oak Investment Partners XI, L.P. (“Oak”) and the Sol Khazani Living Trust (“Trust”) purchased 1.5 million and 0.5 million shares of AutoMD common stock, respectively, at a purchase price of \$1.00 per share. Fredric W. Harman and Sol Khazani, each a current director of the Company, are affiliated with Oak and the Trust, respectively.

On March 6, 2017, AutoMD entered into a dissolution agreement with each of Oak Investment Partners XI, Limited Partnership (“Oak”) and the Sol Khazani Living Trust (the “Trust”), pursuant to which AutoMD redeemed 1.5 million and 0.5 million shares of its common stock, respectively, for a purchase price of \$895 and \$299, respectively. In connection with the dissolution agreement, each of the prior investor agreements entered into between AutoMD, on the one hand, and Oak and the Trust, on the other, were terminated. Fredric W. Harman and Sol Khazani, each a current director of the Company and AutoMD, are affiliated with Oak and the Trust, respectively.

The Company has entered into indemnification agreements with the Company’s directors and executive officers. These agreements require the Company to indemnify these individuals to the fullest extent permitted under law against liabilities that may arise by reason of their service to the Company, and to advance expenses incurred as a result of any proceeding against them as to which they could be indemnified.

**Note 14 – Quarterly Information (Unaudited)**

The following quarterly information (in thousands, except per share data) includes all adjustments which management considers necessary for a fair presentation of such information. For interim quarterly financial statements, the provision for income taxes is estimated using the best available information for projected results for the entire year.

	Quarter Ended				Quarter Ended			
	April 2, 2016	July 2, 2016	Oct. 1, 2016	Dec. 31, 2016	April 4, 2015	July 4, 2015	Oct. 3, 2015	Jan. 2, 2016
<b>Consolidated Statement of Income Data:</b>								
Net sales	\$ 80,806	\$ 78,055	\$ 73,515	\$ 71,195	\$ 76,388	\$ 76,462	\$ 70,648	\$ 67,593
Gross profit	24,592	23,754	22,414	21,522	21,478	20,868	21,042	20,046
Income (loss) from operations	1,182	865	(84)	(1,573)	(18)	(1,107)	(222)	(708)
Income (loss) before income taxes	841	625	(367)	(1,901)	(368)	(1,369)	(491)	(1,007)
Net income (loss)	990	681	(360)	(1,914)	(316)	(1,022)	(288)	(798)
Net loss attributable to noncontrolling interests	(262)	(253)	(258)	(561)	(256)	(247)	(296)	(344)
Net income (loss) attributable to U.S. Auto Parts	\$ 1,252	\$ 934	\$ (102)	\$ (1,353)	\$ (60)	\$ (775)	\$ 8	\$ (454)
Basic net income (loss) per share as reported and adjusted	\$ 0.03	\$ 0.03	\$ 0.00	\$ (0.04)	\$ 0.00	\$ (0.02)	\$ 0.00	\$ (0.01)
Diluted net income (loss) per share as reported and adjusted	\$ 0.03	\$ 0.02	\$ 0.00	\$ (0.04)	\$ 0.00	\$ (0.02)	\$ 0.00	\$ (0.01)
Shares used in computation of basic net income (loss) per share as reported and adjusted	34,497	34,753	34,932	34,878	33,720	33,963	34,018	34,084
Shares used in computation of diluted net income (loss) per share as reported and adjusted	39,359	40,007	34,932	34,878	33,720	33,963	34,018	34,084

**Note 15 – Segment Information**

As described in Note 1 above, the Company operates in two reportable segments identified as Base USAP, which is the core auto parts business, and AutoMD, an online automotive repair source. Segment information is prepared on the same basis that our chief executive officer, who is our chief operating decision maker, manages the segments, evaluates financial results, and makes key operating decisions. Management evaluates the performance of its operating segments based on net sales, gross profit and loss from operations. The accounting policies of the operating segments are the same as those described in Note 1. Operating income represents earnings before other income, interest expense and income taxes. The identifiable assets by segment disclosed in this note are those assets specifically identifiable within each segment.

Summarized segment information for our continuing operations from the two reportable segments for the periods presented is as follows (in thousands):

	<b>Base USAP</b>	<b>AutoMD</b>	<b>Consolidated</b>
<b><u>Fiscal year ended December 31, 2016</u></b>			
Net sales	\$ 303,324	\$ 247	\$ 303,571
Gross profit	92,047	235	92,282
Operating costs (1)	87,782	4,110	91,892
Income (loss) from operations	4,265	(3,875)	390
Capital expenditures	5,414	939	6,353
Depreciation and amortization	6,351	1,159	7,510
Total assets, net of accumulated depreciation	78,094	4,040	82,134
<b><u>Fiscal year ended January 2, 2016</u></b>			
Net sales	\$ 290,833	\$ 258	\$ 291,091
Gross profit	83,176	258	83,434
Operating costs (1)	82,044	3,445	85,489
Loss from operations	1,132	(3,187)	(2,055)
Capital expenditures	6,701	1,079	7,780
Depreciation and amortization	6,141	1,369	7,510
Total assets, net of accumulated depreciation	78,092	5,664	83,756
<b><u>Fiscal year ended January 3, 2015</u></b>			
Net sales	\$ 283,211	\$ 297	\$ 283,508
Gross profit	78,153	297	78,450
Operating costs (1)	81,887	2,475	84,362
Loss from operations	(3,734)	(2,178)	(5,912)
Capital expenditures	4,237	1,319	5,556
Depreciation and amortization	7,230	1,693	8,923
Total assets, net of accumulated depreciation	74,414	8,493	82,907

(1) Operating costs for AutoMD primarily consist of depreciation on fixed assets and personnel costs.

The following table summarizes the approximate distribution of Base USAP revenue by product type.

	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Private Label</b>			
Collision	51%	48%	43%
Engine	15%	14%	13%
Performance	1%	1%	1%
<b>Branded</b>			
Collision	2%	2%	2%
Engine	12%	14%	16%
Performance	19%	21%	25%
<b>Total</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

**Note 16 – AutoMD**

On October 8, 2014, AutoMD entered into a Common Stock Purchase Agreement ("Purchase Agreement") to sell an aggregate of seven million shares of AutoMD common stock at a purchase price of \$1.00 per share to third-party investors and investors that are affiliated with two of our board members. On October 19, 2016, the Company purchased two million shares of AutoMD common stock at a purchase price of \$1.00 per share pursuant to its funding milestone obligation under the Purchase Agreement. On January 26, 2017, AutoMD entered into a redemption agreement with third-party investors to redeem an aggregate of five million shares of AutoMD common stock for a purchase price of \$1,292. On March 6, 2017, following a review of various business and strategic options, AutoMD entered into a dissolution agreement with its two remaining minority stockholders pursuant to which the Company repurchased the remaining shares of common stock from minority stockholders for a purchase price of \$1,194 in consideration for terminating the prior investor agreements. Following the redemptions, AutoMD filed for dissolution and all of the remaining assets of AutoMD will be distributed to the Company, except for certain cash reserved for creditors of AutoMD. These actions will likely result in the Company presenting AutoMD as discontinued operations.

The Company estimates that we will incur charges related to severance, other contractual obligations and premium charges related to repurchasing shares from minority stockholders that will impact cash during the first quarter of fiscal 2017. AutoMD intends to continue to operate its media business, and accordingly, the Company anticipates continued revenue associated with the media business.

## **2016 Independent Director Compensation Policy**

The compensation and benefits for service as a member of the Board of Directors is determined by our Board of Directors. Directors employed by us or one of our subsidiaries are not compensated for service on the Board or on any committee of the Board; however, we reimburse each of our directors for any out-of-pocket expenses in connection with attending meetings of our Board of Directors and committees of the Board of Directors. Each of our independent directors, which include our non-employee directors other than Fred Harman and Sol Khazani, are entitled to a fee of \$30,000 per year for his or her service as a director. Members of the Audit Committee, the Compensation Committee, and the Nominating and Corporate Governance Committee each receive an additional \$7,500, \$5,000 and \$2,500, respectively, per year for his or her service on such committee. The chairpersons of the Board, the Audit Committee, the Compensation Committee, and the Nominating and Corporate Governance Committee receive an additional \$25,000, \$22,000, \$7,500, and \$5,000, respectively, per year for his or her service as chairperson for such committee.

Any independent director who is first elected to the Board of Directors will be granted an option to purchase 45,000 shares of our common stock on the date of his or her initial election to the Board of Directors. In addition, on the date of each annual stockholders meeting, each person who has served as an independent member of the Board of Directors for at least six months before the date of the stockholder meeting will be granted a stock option to purchase 30,000 shares of our common stock and our Chairman of the Board will be granted an additional stock option to purchase 20,000 shares of our common stock for his service.. These options will have an exercise price per share equal to the fair market value of our common stock on the date of grant and will vest over a three year period, subject to the director's continuing service on our Board of Directors. These options will also immediately vest in full upon a change in control of the Company. The term of each option granted to an independent director shall be ten years. These options are currently granted under our 2016 Equity Incentive Plan.



**FORM OF ADOPTION AGREEMENT DEFERRED COMPENSATION PLAN**

The undersigned Company, having been duly advised by its own counsel as to the legal and tax consequences of adopting this Deferred Compensation Plan, and having determined that adoption of this Plan as an unfunded, nonqualified deferred compensation plan (intending that the same comply with the applicable requirements of Section 409A of the Internal Revenue Code of 1986, as amended) would better enable the Company to attract and retain key personnel, **HEREBY ADOPTS** the attached Deferred Compensation Plan, subject to the following terms, conditions and elections, all of which are integral parts of the Plan adopted hereby:

Company Name: US Auto Parts

Plan Name: US Auto Parts Deferred Compensation

Capitalized terms used in this Adoption Agreement that are defined in the Plan document attached hereto and not separately defined herein shall have the respective defined meanings set forth in the attached Plan document.

The Company hereby elects, for purposes of this Plan, as follows *(insert check mark or "X" for each desired election and fill in appropriate blanks)*:

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I. **Pay Types** from which **Annual Deferral Amounts** may be deferred by Participants are as follows:

Pay Type (check to allow inclusion for Annual Deferrals by Participants)	Maximum Deferral Percentage	Minimum Deferral
<input checked="" type="checkbox"/> Annual Base Salary	90	\$5,000
<input checked="" type="checkbox"/> Annual Bonuses	100	
<input checked="" type="checkbox"/> Annual Commissions	90	
<input checked="" type="checkbox"/> Discretionary Bonus	100	
<input checked="" type="checkbox"/> Other Pay Type 1*		
<input type="checkbox"/> Other Pay Type 2**		

\* Other Pay Type 1 consists of (*insert description*): Equity Grants \_\_\_\_\_

\*\* Other Pay Type 2 consists of (*insert description*): \_\_\_\_\_

**II. Company Matching Amounts:** The Company will credit Company Matching Amounts under this Plan for Participants who are employees of the Company or participating Affiliates:

Yes  No

(if yes, select and complete matching contribution formula and credit date below)

a. **Matching Contribution Formula:** If Yes, the following matching contribution formulas apply (Select (i) or (ii)):

- (i)  **Percent of Participant deferrals formula**, subject to a specified limit, as follows:
- (a)  **Matching Contribution Rate:**   % of each Participant's Annual Deferral Amount
- (b)  **Matching Contribution Limit:**   o/o of each Participant's Pay Type that is used to calculate his or her Annual Deferral Amount, which will be applied separately to each Pay Type (*if none selected, no limit applies, other than as required by Section 409A Requirements and applicable law*); or

- (ii)  **Other matching formula** (insert formula and any applicable Contribution Limits below):

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- b. **Match Crediting Date** - For each Pay Type selected for Company Matching Amounts above, the applicable Company Matching Amount, if any, will be credited in each instance as of the following date (*select one*):
- (i)  Simultaneously with each deferral of the applicable Pay Type
  - (ii)  Monthly
  - (iii)  Quarterly
  - (iv)  Other

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**III. Discretionary Contributions.** Without limiting the discretion of the Company at any time to make, amend, add or remove discretionary benefits under Section 3.5 of the Plan with respect to any one or more Participants or groups of Participants, the Company initially elects to credit Annual Company Discretionary Amounts on the last day of each Calendar Year for Participants then employed by the Company or any Affiliate and entitled thereto under the Plan, the amounts to be calculated in one of the following manners (*select one*):

- a.  None
- b.  A fixed annual dollar amount per Calendar Year, to be designated by the Committee for each Participant it elects, acting in the Committee's discretion, which amounts need not be the same among different Participants or groups of Participants

- c.  Subject to any applicable Contribution Limit set forth below, the following percentage amounts of the Pay Types selected below:

Pay Type (check to include for calculation of Company Contributions)	Contribution Limit (insert dollar limit, if applicable)*	Discretionary Contribution Percentage for All Participants
<input type="checkbox"/> Annual Base Salary		
<input type="checkbox"/> Annual Bonus		
<input type="checkbox"/> Annual Commissions		
<input type="checkbox"/> Other Pay Type 1**		
<input type="checkbox"/> Other Pay Type 2***		

\* Company Contribution Limits will be applied separately to each Pay Type in each Calendar Year. If blank in any selected row, no limit applies to that row's Pay Type, other than as required by applicable law and Section 409A Requirements.

\*\* Other Pay Type 1 consists of *(insert description)*: \_\_\_\_\_

\*\*\* Other Pay Type 2 consists of *(insert description)*: \_\_\_\_\_

- d.  **Other discretionary formula** *(insert formula and, if any, the applicable Company Contribution Limits and Annual Adjustments, below)*:

Discretionary match of employee deferrals (from all pay types, excluding equity grants) to make up for lost 401(k) match (50% of the first 2% of compensation). Credited on the last day of the year.

I. **Vesting.**

- a. The following **Vesting Schedule** shall apply to all Annual Company Discretionary Amounts and to all Annual Company Matching Amounts, as follows *(select one)*:

- (i)  Immediate vesting (100%) as amounts are credited to a Participant's Account;
- (ii)  Cliff vesting, 100% at the end of *(insert no. of years)* Plan Years *(five years if no number of years is indicated)* following the Plan Year containing the Vesting Commencement Date (as defined in Part IV.B. below); or
- (iii)  Incremental annual vesting, as of the last day of each Plan Year, starting with the Plan Year containing the Vesting Commencement Date, as follows *(complete chart below)*:

Vesting Date	% of Contribution Vested
Year 0 (Plan Year in which Vesting Commencement Date occurs)	0%
Year 1	33%
Year 2	66%
Year 3	100%
Year 4	-%
Year 5	-%
Year 6	%
Year 7	%
Year 8	%
Year 9	%
Year 10	%

b. The **Vesting Commencement Date** shall be determined as follows *(select one)*:

- (i)  Class year basis: The last day of each Plan Year for which any Annual Company Discretionary Amounts or any Annual Company Matching Amounts are credited to a Participant's Account.
- (ii)  Participation date basis: The date an individual becomes a Participant in this Plan.
- (iii)  Years of service basis: The Participant's date of hire by the Company or any Affiliate.

c. A Participant **will** be 100% vested at his or her Retirement Date *(if not already fully vested under the Vesting Schedule) (select one)*:

Yes  No

d. Vesting shall accelerate upon a Participant's Disability *(select one)*:

Yes  No

e. Vesting shall accelerate upon a Change in Control *(select one)*:

Yes  No

f. A former Participant who is rehired following a Termination of Employment, and who is selected for participation in accordance with the terms of the Plan, shall be treated as a new employee and new participant for purposes of determining such individual's Vesting Commencement Date, without regard to earlier dates of hire or enrollment prior to such Termination of Employment.

**V. Retirement Date** (select only one):

Age 65 or  Age \_

(select one of the above, and insert age if not 65)

Age 55 with 10 years of cumulative service as an employee of the Company and/or any Affiliate

**VI. In-Service Distributions** will be allowed under this Plan prior to retirement: (class year elections paid in a lump Sum)

Yes  No

If "yes", the Minimum Deferral Period for scheduling an In-Service Distribution for each Plan Year is as follows:

Other (specify, but not less than three years): (but in no event for any amount not yet fully vested).  
Three  
Years

**VII. Distributions.**

- a. **Distribution Payment Options:** Participants may select any of the Distribution Payment Options designated below for payment of their Retirement Benefit and Disability Benefit distributions. Any payments made other than by a single lump sum payment to be payable as a series of installments *over* the following whole number(s) of years (select ALL that will be allowed under the Plan):

Lump Sum  3 Years  5 Years  10 Years  15 Years

Any whole no. yrs., up to 10  Any whole no. yrs., up to 15

- b. **Default Distribution Method:** The Default Distribution Method will be deemed to be (select method to be used in the absence of an election by a Participant; if none selected, the Default Distribution Method will be a single lump sum payment):

Lump sum  5 annual installments  10 annual installments

15  \_\_ (insert number) annual installments, but in no event more than fifteen.  
annual  
installments

Termination Benefits (i.e., amounts paid due to Termination of Employment other than on account of death, Retirement or Disability) are paid in a single lump sum payment under Section 6.6 of the Plan.

- c. **Change in Control Event:** Participants may elect upon initial enrollment to have accounts distributed in a lump sum upon a Change in Control Event.

Yes  No

VIII. Pre-retirement Death Benefit (DBO): *(in addition to account balance distribution)*

Yes  No

Fixed dollar amount of 3X Salary

Discretionary amount designated by the Committee for each participant it elects

IX. Cause: For purposes of the Plan, "Cause" shall mean as follows *(if blank, as defined in the Plan)*:

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X. **Rabbi Trust:** The Sponsor elects to establish a grantor trust (rabbi trust) under the Plan:

Yes  No

If yes, the initial Trustee's Name: Wilmington Trust

Trustee's Address: \_\_\_\_\_

Trustee's Contact Name and Number: \_\_\_\_\_

Trustee Contact Email Address: \_\_\_\_\_

(or such other address and contact as the Trustee may designate from time to time)

XI. **Governing Law:** The Governing Law for the Plan, to the extent not preempted by federal law, and in any case subject to the choice of law rules of any court before which any suit or proceeding affecting this Plan may be heard, shall be the laws of the following state (*specify state*):

Delaware

IN WITNESS WHEREOF, the Company has caused its duly authorized representative to execute this Adoption Agreement, under seal, as of the Effective Date set forth above, intending that the Company shall be bound hereby, and that each Participant, Committee Member and Record Keeper may rely hereon.

ATTEST:

ATTEST:

COMPANY:

\_\_\_\_\_  
(insert Company name above)

By:

Print Name:

Title:

\_\_\_\_\_  
Duly authorized

\_\_\_\_\_

Secretary/Clerk

Date Executed:

\_\_\_\_\_



## FORM OF DEFERRED COMPENSATION PLAN

### Preamble

This Plan is adopted as of the date and by the Company set forth in the attached Adoption Agreement, which is an integral part of this plan as it pertains to the Company. The Company, having been duly advised by its own counsel as to the legal and tax consequences of adopting this Plan, intends that the Plan shall at all times be administered and interpreted in such a manner as to constitute an unfunded plan for a select group of management or highly compensated employees who contribute materially to the management of the Company, so as to qualify for all available exemptions from the provisions of Title I of ERISA and to fulfill the applicable requirements of Section 409A of the Internal Revenue Code of 1986, as amended.

### ARTICLE 1 DEFINITIONS

1.1 DEFINED TERMS. Certain words and phrases are defined when first used in later paragraphs of this Plan or in the Adoption Agreement pursuant to which this Plan was adopted. In addition, the following words and phrases when used herein, unless the context clearly requires otherwise, shall have the following respective meanings:

**"Account"** means, with respect to any Participant, a bookkeeping entry used as a measurement and determination of the amounts to be paid to a Participant, or his or her designated Beneficiary, pursuant to this Plan and subject to such limits, rules and procedures as the Committee from time to time may adopt under this Plan. The Committee and the Record Keeper may establish and use sub-accounts and other record keeping entries with respect to any Participant's Account, including without limitation any Deferral Account, Company Contribution Account and Company Discretionary Account applicable to such Participant.

**"Account Balance"** means, with respect to any Participant at any particular time, the sum at such time of such Participant's (i) Deferral Account balance, (ii) Company Matching Account balance and (iii) Company Discretionary Account balance. The Account Balance shall be a bookkeeping entry only and shall be utilized solely as a measurement and determination of the amounts to be paid to a Participant, or his or her designated Beneficiary, pursuant to this Plan.

**"Advisor "** shall have the meaning set forth in Section 6.10.

**"Adoption Agreement"** means the agreement pursuant to which the Company has adopted this Plan, which Adoption Agreement is incorporated herein by reference, including without limitation any terms defined therein. Adoption Agreements may be completed and/or signed using such online systems and other electronic means as the Committee or Record Keeper from time to time may designate for such purpose.

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**"Affiliate"** means a corporation, partnership, limited liability company or other entity that is required to be considered, together with the Company, as a single employer under Section 414(b) of the Code (employees of controlled group of Companies) or Section 414(c) of the Code (employees of partnerships or limited liability companies under common control). For purposes of determining a controlled group of Companies under Section 414(b), the language "at least 50 percent" shall be used instead of "at least 80 percent" each place it appears in Section 1563(a)(1), (2), and (3) of the Code. For purposes of determining trades or businesses that are under common control for purposes of Section 414(c) of the Code, "at least 50 percent" shall be used instead of "at least 80 percent" each place it appears in Treas. Reg. §1.414(c)-2. An entity shall not be considered an "Affiliate" for any period of time prior to satisfying the controlled group or common control tests described above.

**"Annual Company Discretionary Amount"** means the benefit amount, if any, for any one Plan Year that is determined for a Participant in accordance with Section 3.5.

**"Annual Company Matching Amount"** means the benefit amount, if any, for any one Plan Year that is determined for a Participant in accordance with Section 3.4.

**"Annual Deferral Amount"** means that portion of a Participant's Pay Type(s) that a Participant elects to have deferred, and is deferred, in accordance with [Article 3](#), for any one Plan Year. In the event of a Participant's Retirement, Disability, death or a Termination of Employment prior to the end of a Plan Year, such year's Annual Deferral Amount shall be the actual amount deferred in such Plan Year prior to such event.

**"Base Salary"** means base salary earned with respect to services performed and payable in cash (before reductions for, contributions to or deferrals under this Plan or any other profit sharing, 401 (k), pension, deferred compensation or benefit plan sponsored by the Company or any Affiliate), exclusive of any of the following: Bonuses, Commissions, overtime, incentive payments and other performance-based forms of compensation, director and other special fees, expense allowances and reimbursements, and any other forms of compensation, earnings or payments that are not regular in frequency and form.

**"Beneficiary"** means one or more persons, trusts, estates, or other entities, designated in accordance with Article 8 that are entitled to receive benefits under this Plan upon the death of a Participant.

**"Beneficiary Designation Form"** means the form attached as Exhibit D hereto or such other form established from time to time by the Committee that a Participant completes, signs and returns to the Company to designate one or more Beneficiaries. Beneficiary Designation Forms may be completed and/or signed using such online systems and other electronic means as the Committee or Record Keeper from time to time may designate for such purpose.

**"Bonus"** means any compensation relating to services performed that is granted or awarded apart from Base Salary and Commissions and that is identified by the applicable Company or Affiliate as a "bonus" (before reductions for, contributions to or deferrals under this Plan or any other profit sharing, 401 (k), pension, deferred compensation or benefit plan sponsored by the Company or any Affiliate).

**"Calendar Year"** means the annual period measured from January 1 to December 31.

**"Cause"**, unless otherwise defined in the Adoption Agreement, means: (a) with respect to each Participant who has an employment agreement containing a definition of "cause" or "for cause", said definition as set forth in his or her employment agreement; and (b) with respect to all other Participants, willfully engaging in misconduct which is demonstrably and materially injurious to the Company or any Affiliate, unless the act or omission giving rise to such misconduct is done, or omitted to be done, by a Participant in good faith and with a reasonable reason to believe that such action or omission was in the best interest of the Company and its Affiliates.

**"Change in Control"** means, with respect to the employer of any particular Participant, the first to occur of any event constituting a change in the ownership or effective control of such employer, or in the ownership of a substantial portion of such employer's assets, determined objectively by the Committee in accordance with Section 409A Requirements. It is the Company's responsibility to determine whether a Change in Control has occurred to advise the Committee and the Record Keeper accordingly.

**"Change in Control Payment"** shall have the meaning set forth in Section 6.10.

**"Claimant"** shall have the same meaning set forth in Section 10.1.

**"Code"** means the Internal Revenue Code of 1986, as the same may be amended from time to time.

**"Commission"** means compensation, or portions of compensation, earned by a Participant for services that consist in substantial part in the direct sale of a product or service to a customer of the Company or of an Affiliate, which compensation consists of either a portion of the purchase price for the product or service or an amount calculated solely by reference to the volume of sales, and payment of which compensation is contingent upon the Company or applicable Affiliate's receipt of payment for the product or services from an unrelated customer (the determination of whether such customer is related to be made in accordance with applicable Section 409A Requirements). For purposes of this Plan, a Commission shall be deemed to have been earned, and a Participant's services for Commission compensation shall be deemed to have been performed, in the year in which the customer remits payment to the Company or applicable Affiliate for the product or services with respect to which the Commission is paid.

**"Committee"** means the person(s) designated as Committee members in the Adoption Agreement or such other persons as the Company's Board of Directors from time to time may designate to serve as members of the Committee hereunder. In the absence of any Committee, or should the Committee be unable or unwilling to serve, the Company shall perform the duties of the Committee under this Plan.

**"Company"** means the entity identified as the "Company" in the Adoption Agreement pursuant to which this Plan has been adopted.

**"Company Discretionary Account"** means, with respect to any Participant (but subject in the case of each Participant to Section 3.7), an Account consisting of the sum of (i) all of the Participant's Annual Company Discretionary Amounts, plus (ii) Notional Investment Adjustments in value credited or debited thereon in accordance with Article 4 of this Plan, less (iii) all distributions from such account.

**"Company Matching Account"** means, with respect to any Participant (but subject in the case of each Participant to Section 3.7), an Account consisting of the sum of (i) all of the Participant's

Annual Company Matching Amounts, plus (ii) Notional Investment Adjustments in value credited or debited thereon in accordance with Article 4 of this Plan, less (iii) all distributions from such account.

**"Day"** means a calendar day or any part thereof.

**"Deferral Account"** means an Account consisting of the sum of (i) all of a Participant's Annual Deferral Amounts, plus (ii) Notional Investment Adjustments in value credited or debited thereon in accordance with Article 4 of this Plan, less (iii) all distributions from such account.

**"Deferral Election Form"** means a written notice filed by a Participant with the Record Keeper in substantially the form of the sample attached hereto as Exhibit B (conformed to be consistent with elections made under the Adoption Agreement and as the same may be amended from time to time by the Committee), specifying the amount of the Participant's Pay Type(s) to be deferred, and the time and form of distribution payments. Deferral Election Forms may be completed and/or signed using such online systems and other electronic means as the Committee or Record Keeper from time to time may designate for such purpose.

**"Disability"** means an inability to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, or the receipt of income replacement benefits for a period of not less than 3 months under an accident and health plan covering employees of the Participant's employer by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, all as determined by the Committee in accordance with Section 409A, or a determination by the Social Security Administration that the applicable Participant has become totally disabled. A Participant shall also be deemed Disabled if determined to be disabled in accordance with the applicable disability insurance program of such Participant's employer, provided that the definition of "disability" applied under such disability insurance program complies with the requirements of this paragraph.

**"Disability Benefit"** means the benefit set forth in Section 6.2.

**"Eligible Employee"** means any employee of the Company or an Affiliate who is selected to participate herein in accordance with the provisions of Article 2 hereof, and is one of a select group of management or highly compensated employees.

**"ERISA"** means the Employee Retirement Income Security Act of 1974, as the same may be amended from time to time.

**"First Plan Year"** means the period beginning on the Effective Date set forth in the Adoption Agreement and ending on December 31 immediately following the Effective Date.

**"Hardship Distribution"** means any distribution or waiver of deferral granted by the Committee pursuant to Article 7.

**"In-Service Distribution"** means a distribution made pursuant to Section 6.7.

**"Matching Contribution Limit"** means, with respect to each Pay Type, the Maximum Contribution Limit set forth for such Pay Type in the Adoption Agreement, to be used and calculated as a limit on Annual Company Matching Amounts pursuant to Section 3.4.

**"Matching Contribution Rate"** means, with respect to each Pay Type, the respective percentage rate, if any, set forth in the Adoption Agreement for such Pay Type, which rate shall be used to calculate Annual Company Matching Amounts pursuant to Section 3.4, subject to the Matching Contribution Limit, if any, applicable to such Pay Type.

**"Notional Investment"** means any security, fund, account, sub-account, index, formula or other instrument, asset, measure or method from time to time designated by the Committee as a means to calculate the amount of any Notional Investment Adjustment.

**"Notional Investment Adjustment"** means earnings, gains, losses and any other adjustments made with respect to any Annual Deferral Amount, Annual Company Matching Amount or Annual Company Discretionary Amount, which adjustments are made based on the performance of a Notional Investment pursuant to Article 4.

**"Notional Investment Election Form"** means a written notice filed with the Record Keeper by or on behalf of a Participant (or his or her Beneficiaries, as provided below) in substantially the form attached hereto as Exhibit C (conformed to be consistent with elections made under the Adoption Agreement and as the same may be amended from time to time by the Committee), specifying the allocation of the Participant's Annual Deferral Amount and how the Participant's Annual Deferral Amount, Annual Company Matching Amount and Annual Company Discretionary Amount, if any, are to be allocated under the Plan among the Notional Investments provided under the Plan. Notional Investment Election Forms may be completed and/or signed using such online systems and other electronic means as the Committee or Record Keeper from time to time may designate for such purpose. Upon the death of a Participant, for so long as such Participant's Beneficiaries retain an interest in such Participant's Account hereunder, such Beneficiaries may file Notional Investment Election Forms with respect to such Account in accordance with such policies and procedures as the Committee from time to time may specify for such purpose.

**"Participant"** means any Eligible Employee (i) who is selected to participate in the Plan, (ii) who elects to participate in the Plan, (iii) who signs a Participation Agreement, a Deferral Election Form, a Notional Investment Election Form, (iv) whose signed Participation Agreement, Deferral Election Form, and Notional Investment Election Form are accepted by the Committee, and (v) who commences participation in the Plan. A spouse or former spouse (or beneficiary) of a Participant shall not be treated as a Participant in the Plan, even if he or she has an interest in the Participant's benefits under the Plan as a result of applicable law or property settlements resulting from legal separation or divorce.

**"Participation Agreement"** means the form attached as Exhibit A hereto, or such other form established from time to time by the Committee, that a Participant completes, signs and returns to the Company to become a Participant in this Plan. Participation Agreements may be completed and/or signed using such online systems and other electronic means as the Committee or Record Keeper from time to time may designate for such purpose.

**"Pay Type"** means the forms of compensation selected in the Adoption Agreement for inclusion in the calculation of Annual Deferral Amounts under the Plan. References to one or more "Pay Types" with respect to any particular Calendar Year mean said forms of compensation relating

to services performed during such Calendar Year, whether or not paid in such Calendar Year or included on a Federal Income Tax Form W-2 for such Calendar Year (except and to the extent otherwise required under any applicable Section 409A Requirements). The Committee from time to time may adopt and amend such rules and procedures as it deems appropriate to more particularly define or classify any particular Pay Type for further clarification in the administration of this Plan.

**"Permissible Change Election"** means an election to change the time or form of payment of any benefit under the Plan that:

- a) does not take effect until at least 12 months after the date on which such election to delay or change is made;
- b) is made at least 12 months prior to the date previously scheduled for the payment affected thereby;
- c) postpones the payment affected thereby for a period of not less than 5 years from the date when such payment otherwise would have been made; provided, however, that this restriction shall not apply in the case of a payment on account of a Disability, death or an Unforeseeable Emergency; and
- d) does not accelerate the scheduled time for payment of any distribution, except as permitted under Section 409A Requirements.

For purposes of the foregoing, unless otherwise provided in the Adoption Agreement or otherwise required under applicable Section 409A Requirements, any distribution that a Participant elects to receive in a series of equal installments (subject to Notional Investment Adjustments) shall be treated as being a single payment on the date of the first installment of such series.

**"Plan"** means this Plan, as adopted by the Adoption Agreement.

**"Plan Year"** means each Calendar Year.

**"Pre-Retirement Death Benefit"** means the death benefit payable under Section 6.5. No Participant or Beneficiary of any participant shall be entitled to receive a Pre-Retirement Death Benefit if such Participant, or any of his or her Beneficiaries, already have received or are receiving a Termination Benefit, Retirement Benefit or Disability Benefit under this Plan.

**"Record Keeper"** means the party designated as the Record Keeper in the Adoption Agreement, as such designation may be amended from time to time in the discretion of the Committee. In the absence of any such designation, or should the Record Keeper be unable or unwilling to serve, the Company shall perform the duties of the Record Keeper under this Plan.

**"Retirement"** means the Termination of Employment of a Participant by retiring on or after such Participant's Retirement Date.

**"Retirement Benefit"** means the benefit set forth in Section 6.1.

**"Retirement Date"** means the date when the Participant attains the years of age and, if applicable, completes the necessary years of service, as designated in the Adoption Agreement.

**"Section 409A"** means Section 409A of the Code, as the same may be amended from time to time, and any successor statute thereto. References to Section 409A or any requirement under Section 409A, as the same may be interpreted, construed or applied to this Plan at any particular time, shall be deemed to mean and include, to the extent then applicable and then in force and effect (but not to the extent overruled, limited or superseded), published guidance, regulations, notices, rulings and similar announcements issued by the Internal Revenue Service or by the Secretary of the Treasury under or interpreting Section 409A, decisions by any court of competent jurisdiction involving a Participant or a beneficiary and any closing agreement made under section 7121 of the Code that is approved by the Internal Revenue Service and involves a Participant, all as determined by the Committee in good faith, which determination may (but shall not be required to) be made in reliance on the advice of such tax counsel or other tax professional(s) with whom the Committee from time to time may elect to consult with respect to any such matter.

**"Section 409A Requirement"** means any requirement under Section 409A, the failure of which would result in the imposition or accrual of interest or additional taxes under Section 409A on or with respect to any income intended to be deferred under the Plan.

**"Section 4999 Excise Tax", "Section 4999 Limit", "Section 4999 Determination" and "Section 4999 Dispute"** shall have the respective meanings set forth in Section 6.10 of this Plan.

**"Specified Employee"** means, at any time when stock of the Company is publicly traded on an established securities market or otherwise (as determined in accordance with Section 409A Requirements), those employees who are "specified employees" within the meaning of Section 409A. It is the Company's responsibility to elect which rules under Section 409A shall apply when determining who is a Specified Employee, to annually determine who are the Specified Employees, and to timely provide a list of Specified Employees to the Record Keeper.

**"Termination Benefit"** means the benefit set forth in Section 6.6.

**"Termination of Employment" or "Terminates Employment"** means a separation from service with the Company or any Affiliate, whether voluntary or involuntary, for any reason other than an authorized leave of absence or for a transfer in employment from the Company or an Affiliate to another Affiliate or the Company, as the case may be. If a Participant is on a bona fide leave of absence, as defined in the final regulations under Section 409A, of more than six months in duration, then such Participant shall be deemed to have terminated employment on the first day immediately following the expiration of such six month period (or, if such Participant has a contractual or statutory right of reemployment that extends beyond six months, upon the first day following expiration of such statutory or contractual period, whichever is longer if both shall be applicable). It is the Company's responsibility to determine whether there is a Termination of Employment in accordance with Section 409A with respect to any Participant and to advise the Record Keeper accordingly.

**"Unforeseeable Emergency"** means, with respect to any particular Participant, (i) a severe financial hardship of such Participant resulting from an illness or accident suffered by such Participant, by such Participant's spouse or by a dependent (within the meaning of Section 152

of the Code without regard to Section 152(b)(1), (b)(2) and (d)(1)(B) of the Code) of such Participant; (ii) a Participant's loss of property due to casualty; or (iii) other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the Participant. It is the Company's responsibility to determine whether there is an Unforeseeable Emergency in accordance with Section 409A with respect to any Participant and to advise the Record Keeper accordingly.

It is intended that the Plan shall conform with all applicable Section 409A Requirements. Accordingly, in interpreting, construing or applying any of the foregoing definitions or any of the terms, conditions or provisions of the Plan, the same shall be construed in such manner as shall meet and comply with Section 409A Requirements then applicable thereto, and in the event of any inconsistency with any Section 409A Requirements, the same shall be reformed so as to meet such Section 409A Requirements to the fullest extent then permitted without penalty (and without imposition or accrual of interest or additional taxes) under Section 409A.

## ARTICLE 2 ELIGIBILITY AND PARTICIPATION

2.1 SELECTION. Participation in the Plan shall be limited to any Eligible Employee, as determined by the Committee in its sole discretion. Any action so taken with respect to any particular Participant or group of Participants shall not imply a right on the part of any other Participant or group of Participants to enroll for or receive additional benefits or amounts of benefits. The Committee may terminate the right of any existing Participant to file additional Deferral Election Forms under this Plan, and shall terminate any such right for a Participant who ceases to be one of a select group of management or highly compensated employees, or otherwise ceases to meet any of the requirements applicable to participation in this Plan.

2.2 ENROLLMENT. As a condition to participate, each Eligible Employee shall complete, execute and return to the Record Keeper a Participation Agreement, a Deferral Election Form and a Notional Investment Election Form within 30 days after he or she is selected to participate in the Plan. The Committee may establish from time to time such other enrollment requirements as it determines in its sole discretion are necessary, convenient or appropriate to carry out any of the purposes or intent of the Plan or to better assure the Plan's compliance with Section 409A Requirements. Eligible Employees also shall submit to the Record Keeper a Beneficiary Designation Form, but receipt of the Beneficiary Designation Form within 30 days of eligibility shall not be a condition to enrollment in this Plan.

2.3 ELIGIBILITY. An Eligible Employee shall commence participation in the Plan on the first day of the month following the month in which the Eligible Employee completes all enrollment requirements, including timely submission of all required enrollment documents to the Record Keeper; provided, however, that if an Eligible Employee is a former employee that has been rehired following a Termination of Employment, such employee may not commence participation in the Plan until the first day of the following Plan Year. If an Eligible Employee fails to meet all such requirements within the period required in accordance with Section 2.2, that Eligible Employee shall not be eligible to participate in the Plan until the first day of the Plan Year following the delivery to and acceptance by the Committee (or its designee) of the required documents.

2.4 REHIRED EMPLOYEES. Except as otherwise required under Section 409A Requirements (or as otherwise approved by the Committee if permitted under Section 409A Requirements), a Participant who is rehired following a Termination of Employment will be



treated as a new employee, without affecting any benefit payment resulting from any previous participation in this Plan or previous Termination of Employment, and without implying any right to participate further in this Plan as a result of his or her reemployment. If such former Participant is selected to become an Eligible Employee under the Plan following his or her rehiring, such Participant may not commence participation in the Plan until the first day of the Plan Year following his or her submission of all required enrollment documents to the Record Keeper, and for purposes of any applicable vesting, he or she shall be treated as a new employee and new enrollee based on his or her most recent date of hire and participation as a new Participant in this Plan.

### ARTICLE 3 CONTRIBUTIONS AND CREDITS

3.1 DEFERRAL AMOUNT. For each Plan Year, a Participant may elect to defer amounts of those Pay Type(s) designated in the Adoption Agreement, using a Deferral Election Form. Any deferral election shall be subject to such limits, rules and procedures from time to time established by the Committee. The Committee, among other matters, may establish one or more minimum and/or maximum limits on how much of any particular Pay Type that a Participant may elect to defer for such Participant's Annual Deferral Amount in any Plan Year. In no event will the Annual Deferral Amount or the Matching Contribution Amount (if any) for any Pay Type, or for all Pay Types combined, for any particular Participant exceed the maximum amounts permitted under any applicable law.

#### 3.2 ELECTION TO DEFER.

3.2.1 FIRST PLAN YEAR. When a Participant first enrolls to participate in the Plan, except as otherwise provided in Section 2.4 above, the Participant shall make an irrevocable deferral election by completing a Deferral Election Form for the remainder of the Plan Year in which the Participant first enrolls, along with such other elections as the Committee deems necessary or desirable under the Plan. For these elections to be valid, the Election Form must be completed and signed by the Participant, timely delivered to the Record Keeper in accordance with Section 2.2 above and accepted by the Committee or its designee. To the extent that Bonus is included within the Pay Types available for deferrals under this Plan, such elections may include a pro-rata portion of the then-current Plan Year's Bonus, based on the number of days remaining in the applicable Bonus performance period after such election irrevocably takes effect, divided by the total number of days in said performance period. Any election under this paragraph shall apply only on a prospective basis, and only with respect to compensation for services to be performed after the date when the election is made and final. Despite the foregoing, if a Participant already is a participant under any other nonqualified account balance plan of the same employer, or if such Participant is subject to the terms of Section 2.4 above, then such Participant's first Deferral Election Form under this Plan shall contain elections only with respect to Plan Years after the date when such Deferral Election Form is filed, in the same manner as contemplated for subsequent Plan Years in Section 3.2.2 below.

3.2.2 SUBSEQUENT PLAN YEARS. For each succeeding Plan Year, an irrevocable deferral election shall be made by completing a new Deferral Election Form for that Plan Year, and such other elections as the Committee deems necessary or desirable under the Plan, which elections shall be made by timely filing with the Committee or its designee, in accordance with its and the Committee's rules and procedures, before the end of the Plan Year preceding the Plan Year for which the election is made.

**3.2.3 PERFORMANCE-BASED COMPENSATION.** Despite the foregoing, in the case of any Performance-Based Compensation based on services performed over a period of at least 12 consecutive months, such election may be made no later than 6 months before the end of such period. Amounts to be treated as "Performance-Based Compensation" under Section 3.2.3 of this Plan must meet the following criteria:

- (i) the Pay Type must be based on services performed over a period of at least 12 months;
- (ii) the Pay Type must be contingent on the satisfaction of pre-established organizational or individual performance criteria (established no later than 90 days after the beginning of the Service Period); and
- (iii) the Pay Type cannot include any amount or portion of any amount that will be paid either regardless of performance or based on a level of performance that is substantially certain to be met at the time the performance criteria are established.

The term Performance-Based Compensation includes payments based upon subjective performance criteria, provided that the subjective performance criteria are bona fide and relate to the performance of the Eligible Employee, a group of employees that includes the Eligible Employee, or a business unit for which the Eligible Employee provides services (which may include the entire organization), and the determination that any subjective performance criteria have been met is not made by the Eligible Employee or a family member of the Eligible Employee (as defined in Section 267(c)(4) of the Code applied as if the family of an individual includes the spouse or any member of the family), or a person under the effective control of the Eligible Employee or such a family member, and no amount of the compensation of the person making such determination is effectively controlled in whole or in part by the Eligible Employee or such a family member.

It is the Company's responsibility to determine whether a Pay Type qualifies as Performance Based Compensation in accordance with the foregoing requirements with respect to any Participant and to advise the Record Keeper accordingly.

**3.2.4 CHANGES.** Deferral Election Forms filed prior to their applicable filing deadline hereunder may be changed, until such filing deadline occurs, by filing an updated or amended Deferral Election Form in accordance with the foregoing requirements.

**3.3 WITHHOLDING OF ANNUAL DEFERRAL AMOUNTS.** For each Plan Year, the Base Salary portion of the Annual Deferral Amount shall be withheld from each regularly scheduled Base Salary payroll in equal amounts, as adjusted from time to time for increases and decreases in Base Salary. Deferrals of all other Pay Types that are included in the Annual Deferral Amount shall be withheld at the time each such Pay Type is or otherwise would be paid to the Participant, whether or not this occurs during the Plan Year itself (except as otherwise required under applicable Section 409A Requirements).

**3.4 ANNUAL COMPANY MATCHING AMOUNT.** If the Company shall elect in the Adoption Agreement to make Annual Company Matching Amounts, then in each Plan Year, for so long as a Participant remains actively employed by the Company or any Affiliate and continues to be a Participant in this Plan, the Company shall credit to such Participant's Account an Annual Company Matching Amount, such amount to be calculated in the manner and on the Match Crediting Dates set forth in the Adoption Agreement, up to (and not exceeding) in each Plan

Year the Company Contribution Limit, if any, applicable thereto. Annual Company Matching Amounts shall be credited in each instance as of the applicable Match Crediting Date designated in the Adoption Agreement, such amounts to be determined by the Record Keeper as soon as practicable, but not later than 60 days after each applicable Match Crediting Date.

3.5 ANNUAL COMPANY DISCRETIONARY AMOUNTS. The Company, in its discretion, may credit additional amounts to the Company Discretionary Account of any Participant or group of Participants. No such contribution to a Participant or group of Participants shall imply any right on the part of other Participants to receive a similar contribution, nor are such contributions required to be uniform with respect to the Participants for whom they are made.

3.6 FICA/FUTA AND OTHER TAXES. For each Plan Year in which a Participant elects an Annual Deferral Amount, the Participant's employer(s) shall ratably withhold, from that portion of the Participant's wages, salary, bonus or other compensation that is not being deferred, the Participant's share of taxes under the Federal Insurance Contributions Act and the Federal Unemployment Tax Act ("FICA/FUTA Taxes") and any other taxes on deferred amounts which may be required or appropriate. If necessary, the Committee shall reduce the Annual Deferral Amount in order to comply with this paragraph. In addition, as balances with Company Matching Accounts and Company Discretionary Accounts, if any, become vested pursuant to Article 5, to the extent that such amounts are subject to FICA/FUTA Taxes or any other taxes, the Participant's employer(s) shall withhold from the Participant's wages, salary, bonus or other compensation for the year in which such vesting occurs the Participant's share of FICA/FUTA taxes and such other taxes on the amounts that have vested in such year, all to the extent necessary and appropriate to satisfy such tax obligations. If necessary, the Committee shall reduce the Annual Deferral Amount for the year in which FICA/FUTA or other taxes must be paid in order to comply with this paragraph.

3.7 FOR CAUSE TERMINATIONS. Despite anything to the contrary in this Plan, if the Committee in good faith determines that a Participant has caused or incurred a Termination of Employment for Cause, then such Participant's Company Discretionary Account and such Participant's Company Matching Account (including both vested and unvested balances thereof) automatically shall be forfeited in their entirety.

#### ARTICLE 4 ALLOCATION OF FUNDS

4.1 CREDITING/DEBITING OF ACCOUNT BALANCES. In accordance with, and subject to, the rules and procedures that are established from time to time by the Committee, in its sole discretion, amounts shall be credited or debited to a Participant's Account in accordance with the following:

4.2 NOTIONAL INVESTMENT CALCULATIONS. The Committee shall designate in its sole discretion one or more Notional Investments to be used to calculate Notional Investment Adjustments to be credited or debited to Participants' Accounts, as if each Participant were making an actual investment in Notional Investments with his or her Account Balance. Notional Investments shall be used to calculate bookkeeping entries in each Participant's respective Account, and shall be utilized solely as a means to calculate and adjust Account Balances pursuant to this Plan. The Committee from time to time may delete, modify, substitute or otherwise change any Notional Investment under the Plan for any reason with respect to any future Account Balance calculations, and the Committee may impose such limits, rules and procedures governing the frequency, timing, methods and other matters pertaining to the

calculation of Notional Investment Adjustments, and the use, effectiveness and application thereof, as the Committee from time to time may deem to be necessary, convenient or appropriate for purposes of administering the Plan.

4.3 ELECTION OF NOTIONAL INVESTMENTS. If the Committee shall approve more than one Notional Investment to be used with respect to any Plan Year, then each Participant shall elect, on a Notional Investment Election Form duly filed with the Record Keeper for such Plan Year, one or more Notional Investment(s) to be used to calculate the Notional Investment Adjustments to be credited or debited, as the case may be, to his or her Account under this Article 4. Each Participant shall specify, on each Notional Investment Election Form, the portions of his or her Account to be allocated to one or more Notional Investments, as if the Participant was making an actual investment in that Notional Investment with that portion of his or her Account Balance. The Committee may impose such limits, rules and procedures governing the frequency of permitted changes, timing of effectiveness, minimum and maximum amounts (if any) and other matters pertaining to Notional Investment Election Forms, and the use, effectiveness and application thereof, as the Committee from time to time may deem to be necessary, convenient or appropriate for purposes of administering the Plan.

4.4 CREDITING OR DEBITING METHOD. The Participant's Account will be credited or debited, as the case may be, with the increase or decrease in the performance of each Notional Investment selected by the Participant, as though the portion of the Participant's Account Balance then was actually invested in the Notional Investments selected by the Participant, in the percentages (if more than one Notional Investment is available under this Plan) then applicable to each portion of the Participant's Account. The value of each Notional Investment shall be calculated under the Plan as of the close of business on the business day when the published or calculated value of such Notional Investment becomes effective generally, but not more frequently than once per business day. The Committee from time to time may specify such times, frequencies, methods, rules and procedures for calculating the value of any particular Notional Investment (for example, specifying that interest on money market funds shall be calculated and credited on a monthly basis).

4.5 NO ACTUAL INVESTMENT. Notwithstanding any other provision of this Plan that may be interpreted to the contrary, each Notional Investment is to be used for measurement purposes only. A Participant's election of any Notional Investment(s), the allocation of any portion of his or her Account thereto and the use of any Notional Investment(s) to calculate any Notional Investment Adjustment in value to be credited or debited to his or her Account shall not be considered or construed in any manner as an actual investment of his or her Account in any such Notional Investment. In the event that the Company, in its own discretion, decides to invest funds in any or all of the Notional Investments, no Participant shall have any rights or interests in or to any such investment. Without limiting the foregoing, a Participant's Account Balance shall at all times be a bookkeeping entry only, and shall not represent any investment made on his or her behalf by the Company. The Participant at all times shall remain an unsecured creditor of the Company.

#### ARTICLE 5 VESTING

5.1 VESTING OF BENEFITS. The Participant's Account Balance attributable to his or her Deferral Accounts, and Notional Investment Adjustments thereto, will always be 100% vested. Subject to Section 3.7, credits to each Participant's Company Matching Accounts, and Notional Investment Adjustments thereto, and credits to each Participant's Company Discretionary

Accounts, and Notional Investment Adjustments thereto, will be vested in accordance with the Vesting Schedule set forth in the Adoption Agreement. Except as otherwise provided in the Adoption Agreement, Annual Company Discretionary Amounts and Annual Company Matching Amounts that are made in a particular Plan Year (together with Notional Investment Adjustments in value credited or debited thereon in accordance with Article 4 of this Plan, net of distributions) shall vest in annual increments as measured from the end of the last day of the Plan Year in which such contributions occurred and each applicable anniversary thereof.

Despite the foregoing, but subject to Section 3.7, unless a Participant shall have previously had a Termination of Employment (without subsequently having been rehired, re-designated as an Eligible Employee and re-enrolled as a Participant in this Plan), upon the death of a Participant, such Participant's Company Matching Account and Company Discretionary Account shall be fully vested. Subject to the foregoing, all portions of a Participant's Account that are unvested when his or her Termination of Employment occurs shall be forfeited.

## ARTICLE 6 DISTRIBUTION OF BENEFITS

6.1 RETIREMENT BENEFIT. If a Participant shall remain (other than for intervening authorized leaves of absence) an active employee of the Company or any Affiliate until such Participant's Retirement Date, then upon such Participant's Retirement, the Company shall pay to such Participant a Retirement Benefit in an amount equal to such Participant's Account Balance, to be calculated and paid as more particularly provided in Section 6.4 below, subject to the terms and conditions of this Plan.

6.2 DISABILITY BENEFIT. If a Participant shall remain (other than for intervening authorized leaves of absence) an active employee of the Company or any Affiliate until such Participant's Disability, then upon such Participant's Disability, the Company shall pay to such Participant a Disability Benefit in an amount equal to such Participant's Account Balance, to be paid as more particularly provided in Section 6.4 below, subject to the terms and conditions of this Plan. In the event of a Participant's Disability, to the extent permitted under applicable Section 409A Requirements, all deferrals following the date of Disability will be waived. The Committee may require, as a condition to any waiver or benefit under this paragraph, that the Participant be examined by a duly licensed physician selected by the Company to determine or confirm the existence of such Participant's Disability.

6.3 CONTINUATION OF DISABILITY OR RETIREMENT BENEFITS AFTER DEATH. If a Participant dies after his or her Termination of Employment, the Company shall make (or, if payment of any Retirement Benefit or Disability Benefit shall have commenced for such Participant prior to his or her death, the Company shall continue to make) payments of any remaining Retirement Benefit or Disability Benefit for such Participant, as the case may be, to the Participant's Beneficiary, such payments to be made and continued in accordance with Section 6.4, subject to the terms and conditions of this Plan.

6.4 PAYMENTS. A Participant's Retirement Benefit or Disability Benefit, as the case may be, shall be distributed in one or more annual installments as set forth in the Participant's applicable Deferral Election Form, subject to any applicable limitations set forth in the Adoption Agreement. The amount of the first such installment shall be calculated by taking the amount of the Participant's Account Balance as of the end of the day (the "Valuation Date") that is the last day of the calendar month in which such Participant's Retirement or Disability first occurred; provided, however, that in the case of a Specified Employee's Retirement, then the Valuation Date shall be extended to be the end of the sixth month following the month in which such

Participant's Retirement occurred. The amount so determined shall be divided by the total number of installments (in the case of a lump sum distribution, divided by one). Such payment shall be made as soon as practicable, but, in any event, within 60 days after the Valuation Date (extended, in the case of Disability, by such reasonable period of time as the Committee may require to confirm the existence of such Disability). If there shall be more than one installment to be paid, then each subsequent installment shall be calculated on the anniversary of the Valuation Date, by taking the Participant's Account Balance as of the close of business on such anniversary, and dividing such amount by the number of installments then remaining, with payment to be made as soon as practical, but in any event within 60 days of said anniversary. The final installment payment shall be equal to the remaining Account Balance of the Participant. In no event shall the amount of any lump sum or installment payment to a Participant exceed the remaining vested Account Balance of such Participant.

6.5 PRE-RETIREMENT DEATH BENEFIT. If a Participant dies prior to Retirement while actively employed by the Company or an Affiliate, then the Company shall pay a Pre Retirement Death Benefit to such Participant's Beneficiary in a lump sum amount equal to the Account Balance as of the close of business on the last day of the calendar month of such Participant's death. In addition, if the Pre-retirement Death Benefit option is chosen in the Adoption Agreement, in the event of the death of an Employee designated by the Employer ("Designated Employee"), the Employer shall thereafter pay the sum referenced in the Adoption Agreement or other supporting Exhibits or Schedules, to the Employee's designed beneficiary. Upon payment, the Employer shall not be obligated to make any further payments hereunder; thereafter, neither the Employee's personal representative, [his/her] heirs or any other beneficiary shall have any claim to any such further payments. A "Designated Employee" is defined as all employees who are eligible to participate in the Plan and have signed notice and consent form.

The Employee's beneficiary shall be the person, persons, entity or entities designated by the Employee on the beneficiary designation form provided by and filed with the Committee or its designee. If the Employee does not designate a beneficiary, the beneficiary shall be his/her Surviving Spouse. If the Employee does not designate a beneficiary and has no Surviving Spouse, the beneficiary shall be the Employee's estate. The designation of a beneficiary may be changed or revoked only by filing a new beneficiary designation form with the Committee or its designee. If a beneficiary dies before receiving all of the payments due him/her, the balance to which he/she is entitled shall be paid to the contingent beneficiary, if any, named in the Employee's current beneficiary designation form. If there is no contingent beneficiary, the balance shall be paid to the estate of the primary beneficiary. Any beneficiary may disclaim all or any part of any benefit to which such beneficiary shall be entitled hereunder by filing a written disclaimer with the Committee before payment of such benefit is to be made. Such a disclaimer shall be made in a form satisfactory to the Committee and shall be irrevocable when filed.

In the event that the employment of the Employee is terminated by the Employer for any reason other than [his/her] death, the death benefit shall thereupon terminate, and the Employer shall have no further obligation hereunder. Nothing contained herein shall be construed to be a contract of employment for any term of years, nor as conferring upon the Employee the right to continue to be employed by the Employer, in any capacity.

The payments to the Employee's designated beneficiary hereunder shall be made from assets which shall continue, for all purposes, to be a part of the general, unrestricted assets of the Employer; no such person, shall have nor acquire any interest in any such assets by virtue of the provisions of this Agreement. The Employer's obligation hereunder shall be unfunded and

unsecured promise to pay money in the future. To the extent that any person acquires a right to receive payments from the Employer under the provisions hereof, such right shall be no greater than the right of any unsecured general creditor of the Employer under the provisions hereof, such right shall be no greater than the right of any unsecured general creditor of the Employer; no such person shall have nor require any legal or equitable right, interest or claim in or to any property or assets of the Employer.

In the event that, in its discretion, the Employer purchases an insurance policy or policies insuring the life of the Employee (or any other property) to allow the Employer to recover, in whole, or in part, the cost of providing the benefits hereunder, neither the Employee nor any of his/her designated beneficiary shall have or acquire any right whatsoever therein or in the proceeds therefrom. The Employer shall be the sole owner and beneficiary of any such policy or policies, and, as such, shall possess and may exercise all incidents of ownership therein.

6.6 TERMINATION BENEFITS. In the event of the Participant's Termination of Employment, either voluntarily or involuntarily, for any reason other than Disability, Retirement or death, the Company shall pay to the Participant a Termination Benefit in a lump sum. The amount payable shall be equal to the portion of the Account Balance attributable to the Participant's Deferral Account, and subject to Section 3.7, the vested portion, if any, of the Participant's Company Matching Account and the vested portion, if any, of the Participant's Company Discretionary Account. Such payment shall be valued as of the last day of the calendar month in which such Participant's Termination of Employment occurs; provided, however, that in the case of Specified Employees, then the date for such valuation shall be extended to be the end of the sixth month following the month in which such Participant's Termination of Employment occurred. The Termination Benefit shall be paid as soon as practicable, but in any event within 60 days after the date of said valuation.

6.7 IN-SERVICE DISTRIBUTIONS. If the Adoption Agreement allows for In-Service Distributions under this Plan, then in each Deferral Election Form, a Participant may specify an amount to be paid as a scheduled lump sum In-Service Distribution, such payment to be made at a date designated on the form pursuant to this paragraph and subject to the terms and conditions of this Plan. The amount specified for an In-Service Distribution shall not exceed the Annual Deferral Amounts, Annual Company Contribution Amounts and Annual Company Matching Amounts that are covered by such Deferral Election Form, and the date designated for an In-Service Distribution shall occur on or after expiration of the Minimum Deferral Period set forth in the Adoption Agreement, as measured from the close of business of the last day of the Plan Year covered by such Deferral Election Form. The amount of each such payment shall equal the Participant's Account Balance that is attributable to the amount originally specified in the Deferral Election Form (including any Notional Investment Adjustments thereon, net of distributions), and shall be paid as soon as practicable after the calculation thereof, in any event within 60 days after the date designated for payment on such form. Despite the foregoing, if an event occurs that would result in the payment of any Termination Benefit, Disability Benefit, Retirement Benefit or Pre-Retirement Death Benefit prior to an In-Service Distribution, then such other form of benefit shall be paid in lieu of such In-Service Distribution. A Participant may elect to delay the scheduled time for payment of an In-Service Distribution under this paragraph, but only if such election constitutes a Permissible Change Election. If any amount of the Account Balance that has been designated for an In-Service Distribution shall be unvested at the time such In-Service Distribution was scheduled to occur, such unvested amount instead shall remain in such Participant's Account, to be included within such Participant's Termination Benefit, Disability Benefit, Retirement Benefit or Pre-Retirement Death Benefit, as the case may be.

6.8 NO ACCELERATION; CHANGES; CERTAIN DELAYS. The time or schedule for payment of any distribution under the Plan may not be accelerated, except as set forth in this Plan and as permitted under applicable Section 409A Requirements. No election may be made to change the time or form of payment of any distribution under this Plan, or any installment thereof, except for a Permissible Change Election. Despite the foregoing, to the extent consistent with applicable Section 409A Requirements, the Committee may elect to delay payment of any benefit hereunder if such benefit would be fully or partially non-deductible under Section 162(m) of the Code, would violate securities laws, or if there is a bona fide payment dispute (but only if the applicable Participant or Beneficiary is diligently attempting to collect the applicable benefit and does not control the Company or the Committee, or control the Company's or the Committee's decisions with respect thereto); and to the extent permitted under Section 409A Requirements, the time or schedule of payment of a benefit hereunder may be accelerated:

6.8.1 to the extent that such benefit (or this Plan as it pertains thereto in the case of any particular Participant) fails to meet Section 409A Requirements, but only in an amount equal to the amount required to be included in income as a result of the failure to comply with Section 409A Requirements;

6.8.2 for payment to an individual other than a Participant, to the extent necessary to fulfill a domestic relations order as defined in Section 414(p)(1)(B) of the Code;

6.8.3 to pay Federal Insurance Contributions Act tax imposed under Section 3101, 3121(a) and 3121(v)(2) of the Code, where applicable, on compensation deferred under this Plan (hereinafter, the "FICA Amount"), or to pay the income tax at source on wages imposed under Section 3401 of the Code or the corresponding withholding provisions of applicable state, local or foreign tax laws as a result of the payment of the FICA Amount, and to pay additional income tax at source on wages attributable to the pyramiding Section 3401 wages and taxes, but not in excess of the FICA Amount and the income tax withholding related to such FICA Amount; or

6.8.4 as more particularly provided in Section 6.9, Section 6.10, Article 7 or Section 11.10.

6.9 SMALL ACCOUNT BALANCE. Notwithstanding any other provisions of this Plan to the contrary, if the Account Balance of a Participant is not greater than the then current applicable limit under Section 402(g) of the Code (\$16,500 for 2009) at the time payment of any distribution first becomes due hereunder, then the Committee shall pay the vested portion of the Account Balance in a single lump sum, payable on the date on which such benefits would otherwise have become payable (or such other date as may be required under applicable Section 409A Requirements), and no additional benefit shall be payable under this Plan with respect to such Participant.

6.10 CHANGE IN CONTROL. The Committee, acting in its discretion, may elect to terminate the Plan within 30 days prior to or 12 months following a Change in Control, in which case any payments made on or after the effective date of such termination (but within said 12 month period) shall be deemed to have been made by reason of such Change in Control. Despite anything to the contrary in this Plan, if any payment or benefit to a Participant or Beneficiary pursuant to the terms of this Plan or otherwise in connection with, or arising out of, a Change of Control, or in connection with, or arising out of, any other event which constitutes a "change in



control" within the meaning of Section 280G of the Code (a "Change in Control Payment"), would be subject to the excise tax imposed by Section 4999 of the Code (the "Section 4999 Excise Tax"), then the benefits payable under this Plan shall be reduced (but not below zero), but only to the extent necessary so that no portion of the Change in Control Payments shall be subject to the Section 4999 Excise Tax (the "Section 4999 Limit"); provided, however, that an amount shall be payable to a Participant in excess of the Section 4999 Limit if required under any separate employment agreement, plan, program or other arrangement extended by the employer to that Participant. Unless otherwise determined by the Committee in its discretion, the Company shall reduce or eliminate the benefits payable under this Plan by first reducing or eliminating those benefits beginning with benefits which are to be paid the farthest in time from the Section 4999 Determination (as defined below). All determinations required to be made under this section (each, a "Section 4999 Determination") shall be made by the Committee. The calculations shall be provided to the Participant upon request (provided that the Company or the Participant believe in good faith that any of the Payments may be subject to the Section 4999 Excise Tax); provided, however, that if the Committee determines that no Section 4999 Excise Tax is payable by the Participant with respect to one or more Payments, the Participant may request that the independent certified public accountants of the Company or, in the absence of such independent accountants, a nationally recognized accounting firm, law firm or compensation consultant designated by the Company and reasonably acceptable to the Participant (the "Advisor") furnish the Participant with an opinion reasonably acceptable to the Participant that no Excise Tax will be imposed with respect to any such Payment(s). Within ten (10) calendar days of delivery of the Section 4999 Determination to the Participant, the Participant shall have the right to dispute the Section 4999 Determination (the "Section 4999 Dispute"). The existence of any Section 4999 Dispute shall not in any way affect the Participant's right to receive the benefits under this Plan in accordance with the Section 4999 Determination. If there is no Section 4999 Dispute, the Section 4999 Determination by the Advisor shall be final, binding and conclusive upon the Company and the Participant, subject to Section 9.5 of this Plan.

6.11 NO DUPLICATION OF BENEFITS. This Plan is intended to provide benefits based on a Participant's Account Balance, subject to the terms and conditions hereof. Nothing in this Plan shall be construed to express or imply the right of any Participant to receive, or to have his or her Beneficiary(ies) receive, benefits in amounts exceeding in the aggregate his or her vested Account Balance.

#### ARTICLE 7 HARDSHIP DISTRIBUTIONS

7.1 APPLICATION FOR HARDSHIP DISTRIBUTION OR DEFERRAL ELECTION TERMINATION. In the event that any Participant incurs an Unforeseeable Emergency, if consistent with applicable Section 409A Requirements, such Participant may apply to the Committee for a Hardship Distribution in the form of (i) cancellation of existing Annual Deferral Amount elections for Pay Types not yet earned by such Participant, and (ii) to the extent cancellation of all such elections is insufficient to satisfy the needs resulting from such Unforeseeable Emergency, a payment. In the event that any Participant receives a distribution from a plan due to an unforeseeable emergency or a hardship pursuant to Treasury Regulation § 1.401(k)-1(d)(3) (or successor regulation thereto, to the extent recognized for these purposes under Section 409A Requirements), such Participant's existing Annual Deferral Amount elections for Pay Types not yet earned by such Participant shall be cancelled for the remainder of the Calendar Year. The Committee shall consider the circumstances of each such case, and the best interests of the Participant and his or her family, and shall have the right, in its sole

discretion, to allow such application, in full or in part, or to refuse to make a Hardship Distribution.

7.2 AMOUNT OF DISTRIBUTION. In no event shall the amount of any Hardship Distribution payment exceed the lesser of: (a) the Participant's vested Account Balance, or (b) the amount determined by the Committee to be necessary to alleviate the hardship, including any taxes payable by the Participant as a result of receiving such Hardship Distribution, and which is not reasonably available from other resources of the Participant, including reimbursement or compensation from insurance or otherwise, by liquidation of the Participant's assets (unless liquidation of such assets would cause severe financial hardship) or by cessation of deferrals under this Plan or other nonqualified plans in which such Participant participates, all in a manner consistent with any applicable Section 409A Requirements.

7.3 RULES ADOPTED BY COMMITTEE. The Committee shall have the authority to adopt additional rules relating to Hardship Distributions. In adopting and administering these rules, the Committee shall act in accordance with the principle that the primary purpose of this Plan is to provide additional retirement income, not additional funds for current consumption, and that the intent of the Plan is to comply with all applicable Section 409A Requirements.

7.4 LIMIT ON NUMBER OF HARDSHIP DISTRIBUTIONS; EFFECT ON DEFERRALS. No Participant may receive more than one Hardship Distribution in any Calendar Year. If a Participant shall receive a Hardship Distribution (whether by payment or by termination of any Annual Deferral Amount election), then such Participant may not make any further Annual Deferral Amount elections for any Plan Year until the second Plan Year immediately following the Plan Year in which such Hardship Distribution was made.

## ARTICLE 8 BENEFICIARY DESIGNATION

8.1 BENEFICIARY. Each Participant shall have the right, at any time, to designate his or her Beneficiary(ies) (both primary as well as contingent) to receive any benefit under this Plan after the Participant's death. The Beneficiary designated under this Plan may be the same as or different from the Beneficiary designation under any other plan of the Company in which the Participant participates.

8.2 BENEFICIARY DESIGNATION; CHANGE; SPOUSAL CONSENT. A Participant shall designate his or her Beneficiary by completing and signing the Beneficiary Designation Form and returning it to the Record Keeper. A Participant shall have the right to change a Beneficiary by completing, signing and otherwise complying with the terms of the Beneficiary Designation Form and the Committee's rules and procedures, as in effect from time to time. If the Participant names someone other than his or her spouse as a Beneficiary, then to the extent required by applicable law, a spousal consent, in the form designated by the Committee, must be signed by that Participant's spouse and returned to the Record Keeper. The Committee and the Record Keeper shall be entitled to rely on the last Beneficiary Designation Form filed by the Participant and accepted by the Committee prior to his or her death.

8.3 ACKNOWLEDGEMENT. No designation or change in designation of a Beneficiary shall be effective until received and acknowledged in writing by the Committee.

8.4 NO BENEFICIARY DESIGNATION. If a Participant fails to designate a Beneficiary as provided above, or if all designated Beneficiaries predecease the Participant or die prior to

complete distribution of the Participant's benefits, then the Participant's designated Beneficiary shall be deemed to be his or her surviving spouse. If the Participant has no surviving spouse, the benefits remaining under the Plan to be paid to a Beneficiary shall be payable to the executor or personal representative of the Participant's estate.

8.5 DOUBT AS TO BENEFICIARY. If the Record Keeper has any doubt as to the proper Beneficiary to receive payments pursuant to this Plan, the Committee shall have the right, exercisable in its discretion, to cause the Company to withhold such payments until this matter is resolved to the Committee's satisfaction.

8.6 DISCHARGE OF OBLIGATION. The payment of benefits under the Plan to a Beneficiary shall fully and completely discharge the Company and the Committee from all further obligations under the Plan with respect to the Participant, and that Participant's Participation Agreement shall terminate upon such full payment of benefits.

## ARTICLE 9 MANAGEMENT AND ADMINISTRATION OF THIS PLAN

9.1 THE COMMITTEE. The Committee shall be responsible for the management, operation and administration of the Plan, and for processing claims under Article 10 of this Plan. The Committee shall administer the Plan in accordance with its terms and shall have the discretion, power and authority to determine all questions arising in connection with the administration, interpretation and application of the Plan. Any such determination shall be conclusive and binding upon all persons. The Committee shall have all powers necessary or appropriate to accomplish its duties under the Plan. The Committee from time to time may employ others to render advice with regard to its responsibilities under this Plan and to perform services under this Plan, including the services contemplated to be performed by the Record Keeper. It may also allocate its responsibilities to others and may exercise any other powers necessary for the discharge of its duties.

9.2 THE RECORD KEEPER. Except to the extent provided to the contrary in a separate written agreement, the Record Keeper shall solely be responsible for keeping records of Account Balances, and for receiving and processing data pertaining to elections and transactions affecting Account Balances pursuant to the Plan.

9.3 INFORMATION FROM COMPANY. The Company and each Affiliate shall supply full and timely information to the Committee and the Record Keeper on all matters as may be required properly to administer the Plan. The Committee and the Record Keeper may rely upon the correctness of all such information as is so supplied and shall have no duty or responsibility to verify such information. The Committee and the Record Keeper shall also be entitled to rely conclusively upon all tables, valuations, certifications, opinions and reports furnished by any actuary, accountant, controller, counsel or other person employed or engaged by or on behalf of the Company or the Committee with respect to the Plan.

9.4 FIDUCIARY DUTIES; INDEMNIFICATION. The Company, acting by and through the Committee, if the Company so elects, is the named fiduciary under this Plan. The named fiduciary is authorized to control and manage the operation and administration of this Plan, and shall be responsible for establishing and carrying out a funding policy and method consistent with the objectives of this Plan. The Company, to the fullest extent permitted by applicable law, shall indemnify and hold harmless the members of the Committee, the Record Keeper and their respective employees, officers, directors, partners, agents, affiliates and representatives, from

and against any and all claims, losses, liabilities, costs, damages and expenses (including without limitation reasonable attorneys' fees) arising from any action or failure to act with respect to this Plan on account of such party's services hereunder, except in the case of gross negligence or willful misconduct.

9.5 SECTION 409A COMPLIANCE. The Company intends that this Plan will be established, construed, administered and applied in compliance with all Section 409A Requirements, but in light of uncertainty with respect to such requirements and limits, the Company reserves the right to unilaterally amend the Plan without the consent of the Participants and to take any actions that may be appropriate to comply with the Section 409A Requirements.

## ARTICLE 10 CLAIMS PROCEDURES

10.1 PRESENTATION OF CLAIM. A Participant or a Participant's Beneficiary after a Participant's death (such Participant or Beneficiary being referred to below as a "Claimant") may deliver to the Company a written claim for a determination under this Article with respect to the amounts distributable to such Claimant. If such a claim relates to the contents of a notice received by the Claimant, the claim must be made within sixty (60) days after such notice was received by the Claimant. All other claims must be made within 180 days of the date on which the event that caused the claim to arise occurred. The claim must state with particularity the determination desired by the Claimant.

10.2 NOTIFICATION OF DECISION. The Company shall consider a Claimant's claim within a reasonable time, but no later than ninety (90) days after receiving the claim. If the Company determines that special circumstances require an extension of time for processing the claim, written notice of the extension shall be furnished to the Claimant prior to the termination of the initial ninety (90) day period. In no event shall such extension exceed a period of ninety (90) days from the end of the initial period. The extension notice shall indicate the special circumstances requiring an extension of time and the date by which the Company expects to render the benefit determination. The Company shall notify the Claimant in writing:

10.2.1 that the Claimant's requested determination has been made, and that the claim has been allowed in full; or

10.2.1 that the Company has reached a conclusion contrary, in whole or in part, to the Claimant's requested determination, and such notice must set forth in a manner calculated to be understood by the Claimant:

- (i) the specific reason(s) for the denial of the claim, or any part of it;
- (ii) specific reference(s) to pertinent provisions of this Plan upon which such denial was based;
- (iii) a description of any additional material or information necessary for the Claimant to perfect the claim, and an explanation of why such material or information is necessary;
- ( iv ) an explanation of the claim review procedure set forth in Section 10.3 below; and

- (v) a statement of the Claimant's right to bring a civil action under ERISA Section 502(a) following an adverse benefit determination on review.

10.3 REVIEW OF A DENIED CLAIM. On or before sixty (60) days after receiving a notice from the Company that a claim has been denied, in whole or in part, a Claimant (or the Claimant's duly authorized representative) may file with the Company a written request for a review of the denial of the claim. The Claimant (or the Claimant's duly authorized representative):

10.3.1 may, upon request and free of charge, have reasonable access to, and copies of, all documents, records and other information relevant to the claim for benefits;

10.3.2 may submit written comments or other documents; and/or

10.3.3 may request a hearing, which the Company, in its sole discretion, may grant.

10.4 DECISION ON REVIEW. The Company shall render its decision on review promptly, and no later than sixty (60) days after the Company receives the Claimant's written request for a review of the denial of the claim. If the Company determines that special circumstances require an extension of time for processing the claim, written notice of the extension shall be furnished to the Claimant prior to the termination of the initial sixty (60) day period. In no event shall such extension exceed a period of sixty (60) days from the end of the initial period. The extension notice shall indicate the special circumstances requiring an extension of time and the date by which the Company expects to render the benefit determination. In rendering its decision, the Company shall take into account all comments, documents, records and other information submitted by the Claimant relating to the claim, without regard to whether such information was submitted or considered in the initial benefit determination. The decision must be written in a manner calculated to be understood by the Claimant, and it must contain:

10.4.1 specific reasons for the decision;

10.4.2 specific reference(s) to the pertinent provisions of this Plan upon which the decision was based;

10.4.3 a statement that the Claimant is entitled to receive, upon request and free of charge, reasonable access to and copies of, all documents, records and other information relevant (as defined in applicable ERISA regulations) to the Claimant's claim for benefits; and

10.4.4 a statement of the Claimant's right to bring a civil action under ERISA Section 502(a).

#### ARTICLE 11 MISCELLANEOUS

1. TRUST. Except as set forth below, nothing contained in this Plan, nor any action taken pursuant to its provisions by any person, shall create, or be construed to create, a trust of any kind, or a fiduciary relationship between the Company and any other person. Despite the foregoing, if the Company, pursuant to the Adoption Agreement or otherwise, elects to establish a grantor trust for the purpose of holding any assets intended to fund the payment of any

benefits under this Plan, the Company shall have no obligation to make any contributions or deposits into such trust and all assets of such trust shall remain subject to the claims of the Company's creditors generally in the event of any insolvency or bankruptcy of the Company, and except as permitted under applicable Section 409A Requirements, no such assets shall be located outside of the United States of America. No trust or restriction shall be imposed on any assets intended to fund the payment of any benefits under this Plan as a result of any change in Company's financial health. The creation of any trust shall not relieve the Company of its obligations under this Plan.

**11.2 BENEFITS PAYABLE ONLY FROM GENERAL CORPORATE ASSETS (UNSECURED GENERAL CREDITOR STATUS OF PARTICIPANT).**

11.2.1 Payments to any Participant or Beneficiary hereunder shall be made from assets which shall continue, for all purposes, to be part of the general, unrestricted assets of the Company. No person shall have any interest in any such asset by virtue of any provision of this Plan. The Company's obligation hereunder shall be an unfunded and unsecured promise to pay money in the future. To the extent that any person acquires a right to receive payments from the Company under the provisions hereof, such right shall be no greater than the right of any unsecured general creditor of the Company; no such person shall have or acquire any legal or equitable right, interest or claim in or to any property or assets of the Company.

11.2.2 In the event that, in its discretion, the Company purchases an insurance policy or policies insuring the life of a Participant or any other property, to allow the Company to recover or meet the cost of providing benefits, in whole or in part, hereunder, no Participant or Beneficiary shall have any rights whatsoever therein or in the proceeds therefrom. The Company shall be the sole owner and beneficiary of any such insurance policy or property and shall possess and may exercise all incidents of ownership therein.

11.3 CAPTIONS. The captions of the articles, sections and paragraphs of this Plan are for convenience only and shall not control or affect the meaning or construction of any of its provisions.

11.4 FURNISHING INFORMATION. Each Participant and his or her Beneficiary(ies) will cooperate with the Committee and the Record Keeper by furnishing any and all information requested by the Committee or the Record Keeper and take such other actions as may be requested in order to facilitate the administration of the Plan and the payments of benefits hereunder, including but not limited to taking such physical examinations as the Committee may deem necessary.

11.5 NO CONTRACT OF EMPLOYMENT. Nothing contained herein shall be construed to be a contract of employment for any term of years, nor as conferring upon any Participant the right to continue to be employed by the Company or any Affiliate in his or her present capacity or in any capacity. It is expressly understood that this Plan relates to the payment of deferred compensation for each Participant's services, and is not intended to be an employment contract.

11.6 BENEFITS NOT TRANSFERABLE. No Participant or beneficiary under this Plan shall have any power or right to transfer, assign, anticipate, hypothecate or otherwise encumber any part or all of the amounts payable hereunder. No such amounts shall be subject to seizure by any creditor of any such Participant or Beneficiary, by a proceeding at law or in equity, nor shall such amounts be transferable by operation of law in the event of bankruptcy, insolvency or death of the Participant or Beneficiary. Any such attempted assignment shall be void.

11.7 SUCCESSORS. The provisions of this Plan shall bind and inure to the benefit of the Participant's employer and its successors and assigns and the Participant and the Participant's designated Beneficiaries.

11.8 SPOUSE'S INTEREST. The interest in the benefits hereunder of a spouse of a Participant who predeceases the Participant shall automatically pass to the Participant and shall not be transferable by such spouse in any manner, including but not limited to such spouse's will, nor shall such interest pass under the laws of intestate succession.

11.10 AMENDMENT AND TERMINATION. To the extent permitted under Section 409A Requirements, this Plan may be amended or terminated by the Company at any time, without notice to or consent of any person, pursuant to resolutions adopted by the Company. Any such amendment or termination shall take effect as of the date specified therein and, to the extent permitted by law and Section 409A Requirements, may have retroactive effect. However, no such amendment or termination shall reduce the amount then credited to the Participant's Account Balance under Section 4. Upon termination of this Plan, no further Deferral Election Forms may be filed hereunder, and to the extent permitted under Section 409A Requirements, all Account Balances shall be distributed and paid in full in a lump sum, and otherwise in accordance with the applicable terms of this Plan as in effect at the time of termination. Any other provision of this Plan to the contrary notwithstanding, the Plan may be amended by the Company at any time, and retroactively if required to the extent that, in the opinion of the Company, such amendment shall be necessary in order to conform the Plan to the requirements of any applicable law, including without limitation ERISA, any Section 409A Requirement and any other provision of the Code. No such amendment shall be considered prejudicial to any interest of a Participant or Beneficiary hereunder.

11.11 NOTICE. **Either the Committee or the Record Keeper may specify that any election, form, designation, agreement or communication by a Participant under the Plan shall be made or submitted online at a site on the World Wide Web designated for such purpose, or by other reasonable electronic means.** Subject to the foregoing, any notice, consent or demand required or permitted to be given under the provisions of this Plan shall be in writing, and shall be signed by the party giving or making the same. If such notice, consent or demand is mailed, it shall be sent by United States certified mail, postage prepaid, addressed, if to the Company or the Committee, to the Company Address set forth in the Adoption Agreement, and if to the Record Keeper, to the Record Keeper Address set forth in the Adoption Agreement, and if to any Participant, to such Participant's address most recently submitted by him or her to the Record Keeper (and in the absence of such submission, as most recently appearing on the records of the Company). The date of such mailing shall be deemed the date of notice, consent or demand. Any person may change the address to which notice is to be sent by giving notice of the change of address in the manner aforesaid.

11.12 FACILITY OF PAYMENT. If a distribution is to be made to a minor, or to a person who is otherwise incompetent, then the Committee may, in its discretion, make such distribution (i) to the legal guardian, or if none, to a parent of a minor payee with whom the payee maintains his or her residence, or (ii) to the conservator or committee or, if none, to the person having custody of an incompetent payee. Any such distribution shall fully discharge the Committee, the Record Keeper, the Company and the Plan from further liability on account thereof.

11.13 TAX WITHHOLDING AND REPORTING. The Company shall have the right to deduct any required withholding taxes from any payment made under this Plan.

11.14 GOVERNING LAW. The Plan and the right and obligations of all persons hereunder shall be governed by and construed in accordance with the laws of the state set forth in the Adoption Agreement, other than its laws regarding choice of law, to the extent that such state law is not preempted by federal law.



## DISSOLUTION AGREEMENT

This Dissolution Agreement (this “**Agreement**”) is entered into as of March 6, 2017 (the “**Effective Date**”), by and between AutoMD, Inc., a Delaware corporation (“**AutoMD**”), with an address of 16941 Keegan Avenue, Carson, California 90746, Oak Investment Partners XI, Limited Partnership (“**Oak**”), with an address of 525 University Avenue, Suite 1300, Palo Alto, CA 94301, and Sol Khazani Living Trust (the “**Khazani Trust**” and together with USAP and Oak, the “**AutoMD Stockholders**”), with an address of 578 Washington Blvd., #854, Marina Del Rey, CA 90292. AutoMD and the AutoMD Stockholders shall together be referred to herein as the “**Parties**”, and each may be referred to herein as a “**Party**”.

WHEREAS, the Board of Directors of AutoMD and the AutoMD Stockholders have evaluated various business and strategic options with respect to AutoMD, and following such evaluation, have determined that it is in the best interests of the AutoMD Stockholders to dissolve AutoMD.

WHEREAS, Oak and the Khazani Trust (the together, the “**Sellers**”) would have certain preferential stockholder rights upon a dissolution of the Company as set forth under the AutoMD Financing Documents (as defined below), and in consideration of the Redemptions (as defined below), the Parties agree to terminate the AutoMD Financing Documents pursuant to the terms of this Agreement.

WHEREAS, prior to a dissolution of AutoMD, the Board of Directors of AutoMD and the AutoMD Stockholders deem it to be in the best interests of AutoMD to effect a redemption of the 1,500,000 shares of AutoMD common stock owned by Oak (the “**Oak Shares**”) and the 500,000 shares of AutoMD common stock owned by the Khazani Trust (the “**Khazani Trust Shares**”, and together with the Oak Shares, the “**Shares**”) and to settle and compromise fully and finally any and all disputes, controversies, entitlements, and claims that the Sellers may have against AutoMD and its parent company, U.S. Auto Parts Network, Inc. (“**USAP**”), and their respective directors and officers, on the terms and conditions set forth herein.

NOW, THEREFORE, in consideration of the promises, covenants, and agreements contained herein, the Parties agree as follows:

### 1. **Redemption.**

1.1 Redemptions. Subject to the terms and conditions set forth in this Agreement, the Sellers agree to sell to AutoMD, and AutoMD agrees to purchase and redeem from the Sellers all of their respective shares (the “**Shares**”) of AutoMD common stock (the “**Redemptions**”):

#### 1.2 Closing.

- (a) The closing of the Redemptions (the “**Closing**”) shall be effective as of the Effective Date.
- (b) At Closing, each Seller shall deliver to AutoMD their respective share certificate evidencing the Shares, together with a stock power executed in blank; and
- (c) At Closing, AutoMD shall deliver to Oak the sum of \$895,500 by wire transfer of immediately available funds to an account or accounts designated by Oak.
- (d) At Closing, AutoMD shall deliver to the Khazani Trust the sum of \$298,500 by wire transfer of immediately available funds to an account or accounts designated by the Khazani Trust.

1.3 Termination of Obligations under Existing Agreements. From and after the Closing, except as otherwise set forth in this Agreement or any agreement, instrument, or document executed in connection herewith or delivered at Closing, all of the Parties’ obligations (whether accrued or contingent) to each other under all agreements between each Seller, on the one hand, and USAP and/or AutoMD, on the other hand, shall cease and be of no further force and effect and such agreements shall be deemed terminated and of no further force or effect, including without limitation, the following agreements and the Parties’ obligations thereunder: (a) the Investor Rights Agreement, dated October 8, 2014, by and among AutoMD and the investors named therein, (b) the Voting Agreement, dated October 8, 2014, by and among AutoMD and the investors named therein, (c) the Right of First Refusal Agreement and Co-Sale Agreement, dated October 8, 2014, by and among AutoMD and the investors named therein, and (d) the Common Stock Purchase Agreement, dated October 8, 2014, by and among AutoMD and the investors named therein (collectively, the “**AutoMD Financing Documents**”).

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## 2. Release.

### 2.1 Seller Release.

(a) Each Seller hereby acknowledges that, in consideration for its respective Redemption and other valuable consideration, the receipt and sufficiency of which are hereby acknowledged, from and after the Closing, such Seller, on behalf of itself and its respective subsidiaries, parents, affiliates, agents, legal representatives, predecessors, successors and assigns (collectively, the “**Other Releasing Parties**”) hereby fully, finally, and completely releases each of AutoMD, USAP and their respective subsidiaries, affiliates, stockholders, officers, directors, employees, agents, attorneys, representatives and representatives of each of them (the “**Released Parties**”), of and from any and all claims, actions, demands, and/or causes of action, of whatever kind or character, whether now known or unknown, arising from, relating to, or in any way connected with such Seller’s investment in AutoMD, Seller’s rights as a stockholder of AutoMD, Seller’s rights under the AutoMD Financing Documents, and/or any other facts or events occurring on or before the Closing; provided, however, that such Seller is not releasing any claims for (a) breach of any representation, warranty, covenant or agreement of this Agreement or any agreement, instrument, or document executed or delivered in connection with the Closing by any Released Parties, or (b) any director indemnification obligations owed by any Released Party pursuant to AutoMD’s or USAP’s certificate of incorporation or bylaws or any director indemnification agreement. Each Seller, on behalf of itself and the Other Releasing Parties, agree that this Agreement includes a release of any negligence claims, contractual claims for breach or default, and any claims for any alleged breach of fiduciary duties owed by AutoMD, USAP, or any of the other Released Parties in any capacity, and any related attorneys’ fees and costs, if any, that such Seller or any of the Other Releasing Parties may have against AutoMD, USAP, or any of the other Released Parties. Each Seller, on behalf of itself and the Other Releasing Parties, waives and releases the Released Parties from each and every claim that this Agreement was procured by fraud or signed under duress or coercion so as to make this release not binding. Each Seller, on behalf of itself and the Other Releasing Parties, understands and agrees that by signing this Agreement it is giving up the right to pursue legal claims that it may have against any of the Released Parties.

(b) The release set forth in this Section 2.1 is intended as a release of all claims against the Released Parties, whether now known or unknown. In furtherance thereof, each Seller, on behalf of itself and the Other Releasing Parties, expressly waives any right or claim of right to assert hereafter that any claim, demand, obligation and/or cause of action has, through ignorance, oversight, error or otherwise, been omitted from the terms of this Agreement. Each Seller, on behalf of itself and the Other Releasing Parties, make this waiver with full knowledge of its rights, after consulting with legal counsel, and with specific intent to release both their known and unknown claims.

(c) Each Seller hereby represents and warrants that neither it nor any Other Releasing Party has assigned or otherwise transferred to any other person or entity any interest in any claim, action, demand and/or cause of action it has, or may have, or may claim to have in connection with the matters released hereby and/or the persons and entities released herein, and hereby agrees to indemnify and hold harmless the Released Parties from any and all injuries, harm, damages, penalties, costs, losses, expenses and/or liability or other detriment including all reasonable attorneys’ fees incurred as a result of any and all claims, actions, demands, and/or causes of action of whatever nature or character that may hereafter be asserted against any of the Released Parties by any person or entity claiming by, through or under such Seller or any Other Releasing Party by virtue of such an assignment or other transfer.

(d) In furtherance of such Seller’s intent to waive and release any and all claims against the Released Parties, on behalf of itself and the Other Releasing Parties, *whether or not now known* to such Seller, each Seller also expressly waives and releases, on behalf of itself and the Other Releasing Parties, any and all rights and benefits under Section 1542 of the *Civil Code of the State of California*, which reads as follows:

**A general release does not extend to claims which the creditor does not know or suspect to exist in his favor at the time of executing the release, which if known by him, must have materially affected his settlement with the debtor.**

Each Seller, on behalf of itself and the Other Releasing Parties, acknowledge that it understands that this provision means that, if it later discover facts different from, or facts in addition to, those facts currently known by them, or believed by them to be true, the waivers and releases of this Agreement will remain effective in all respects-despite such different or additional facts and such Seller’s or any Other Releasing Party’s later discovery of such facts, and even if they would not have agreed to these waivers and releases if they had prior knowledge of such facts.

### 3. Representations and Warranties of Seller. Each Seller represents and warrants to AutoMD as follows:

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3.1 Ownership. Such Seller owns the Shares beneficially and of record free and clear of all liens, claims, encumbrances, proxies and restrictions of any kind or nature whatsoever and will convey to AutoMD valid and marketable title to its respective Shares. There are no outstanding options, warrants, subscriptions or other rights or obligations to purchase or acquire any of its respective Shares issued, created or otherwise made effective by such Seller, nor any outstanding securities convertible into or exchangeable for any of its respective Shares issued, created or otherwise made effective by such Seller.

3.2 Authority. Upon the execution and delivery by such Seller of this Agreement and the other agreements contemplated hereby, this Agreement and the other agreements contemplated hereby will constitute the legal, valid, and binding obligations of such Seller. Such Seller has the right, power, and authority to execute and deliver this Agreement and to perform its obligations under this Agreement and the other agreements contemplated hereby. Such Seller is not, nor will it be, required to obtain any consent from any person in connection with the execution and delivery of this Agreement and the other agreements contemplated hereby, the consummation or performance of any of the transactions contemplated hereby or thereby, or the sale and delivery of its respective Shares (other than consents obtained prior to, and in full force and effect as of, the Effective Date).

3.3 Investment Representations.

(a) Such Seller is capable of evaluating and bearing the risks and merits of selling its respective Shares for the respective redemption price set forth above and pursuant to the terms of this Agreement.

(b) Such Seller has had, during the course of this transaction and prior hereto, the opportunity to ask questions of, and receive answers from, AutoMD and its management concerning AutoMD, its operations and prospects, and the terms and conditions of this Agreement.

(c) Such Seller believes that it has received all such information as it considers necessary for evaluating the risks and merits of selling the Shares for the redemption price and pursuant to the terms of this Agreement and for verifying the accuracy of any information furnished to it or to which it had access.

(d) Neither AutoMD, nor USAP, nor any of the other Released Parties has made any representations or warranties, express or implied, regarding AutoMD, its management, operations and prospects, the value of the Shares or otherwise regarding any aspect of the transaction except as set forth in Section 4 of this Agreement, and such Seller is not relying on any such representation or warranty not contained in Section 4 of this Agreement, and shall have no claim or right against either AutoMD or USAP or any of their respective Released Parties with respect to any information, documents or materials furnished by either AutoMD or USAP or any of their respective Released Parties to such Seller or any of its respective affiliates, employees, attorneys, advisors or representatives in any data room, presentation, interview or in any other form or manner relating to the transactions contemplated hereby.

3.4 Acceptance of Risk. Each Seller, on behalf of itself and the Other Releasing Parties, is entering into this Agreement freely and understand and expressly accept and assume the economic and market risk associated with such Seller selling its respective Shares for the respective redemption price set forth above (including that such redemption price may be less than the fair market value of the Shares or less than the price that the Shares might have been sold for in an alternative transaction), agree that this Agreement shall be in all respects effective and not subject to termination or rescission under any circumstances, and agree, on behalf of themselves and the other Releasing Parties, that they shall have no claim or right against AutoMD, USAP or any of the other Released Parties based on such redemption price being less than the fair market value of the Shares or less than the price that the Shares might have been sold for in an alternative transaction.

3.5 Tax Consequences. Each Seller acknowledges that AutoMD is making no representation or warranty as to the tax consequences for such Seller in selling its respective Shares for the respective redemption price pursuant to this Agreement. Each Seller further acknowledges that it has had an opportunity to seek independent counsel and advisors with respect to tax and other matters relating to this Agreement, that it shall bear the full tax consequences, if any, of selling its respective Shares for the redemption price set forth above and pursuant to the terms of this Agreement in all circumstances.

3.6 Indemnification Covenant. Each Seller is aware that AutoMD is relying upon the truth of the foregoing representations, warranties and covenants in this Section 3 in connection with entering into this Agreement and the transactions contemplated by this Agreement. Each Seller shall indemnify, protect, defend and hold free and harmless AutoMD and USAP from and against all losses resulting from the defense, settlement or compromise of a claim or demand or assessment incurred by them as a result of any breach by such Seller of any of its representations, warranties or covenants contained in this Agreement.

**4. Representations and Warranties of the Company.** AutoMD represents and warrants to Seller as follows:

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4.1 **Capital Structure.** AutoMD's authorized capital stock (immediately prior to Closing) is 23,450,000 shares of common stock, of which 16,500,000 shares are currently issued and outstanding. In addition, there are 1,405,000 options to purchase shares of common stock outstanding. The 16,500,000 outstanding shares of common stock together with the 1,405,000 options represent all of the outstanding equity interests in AutoMD. There are no outstanding or authorized options, warrants, purchase rights, subscription rights, conversion rights, exchange rights or other contracts or commitments that require AutoMD to issue, sell or otherwise cause to become outstanding any of its capital stock, other than those set forth in the AutoMD Financing Documents. There are no outstanding stock appreciation, phantom stock or similar rights with respect to AutoMD. AutoMD has no obligation of any kind to issue any additional equity interests in AutoMD to any person.

4.2 **Authority.** Upon the execution and delivery by AutoMD of this Agreement and the other agreements contemplated hereby, this Agreement and the other agreements contemplated hereby will constitute the legal, valid, and binding obligations of AutoMD. AutoMD has the right, power, and authority to execute and deliver this Agreement and the other agreements contemplated hereby and to perform its obligations under this Agreement and the other agreements contemplated hereby. Other than consents obtained prior to, and in full force and effect as of, the Effective Date, AutoMD is not, nor will be, required to obtain any consent from any person in connection with the execution and delivery of this Agreement and the other agreements contemplated hereby, the consummation or performance of any of the transactions contemplated hereby or thereby, or the Redemptions.

5. **Choice of Law.** This Agreement shall be governed by and construed under the laws of the State of Delaware in all respects as such laws are applied to agreements among Delaware residents entered into and performed entirely within Delaware, without giving effect to conflict of law principles thereof. The parties agree that any action brought by any Party under or in relation to this Agreement, including without limitation to interpret or enforce any provision of this Agreement, shall be brought in, and each Party agrees to and does hereby submit to the jurisdiction and venue of, any state or federal court located in the State of Delaware.

6. **Terms Confidential.** The Parties shall keep the terms, amounts and facts of this Agreement completely confidential to avoid disclosure hereafter of any information concerning this Agreement to anyone except their respective attorneys, accountants, or other professional advisors. Notwithstanding the foregoing prohibition, (a) the Parties shall not be prohibited from disclosing the terms, amounts and facts of this Agreement or this Agreement itself as may be requested by governmental entities or as may be required by law, including any Federal or state securities laws or regulations, (b) AutoMD shall not be prohibited from disclosing the terms, amounts and facts of this Agreement or this Agreement itself as may be requested by any person or entity with whom AutoMD is engaged in discussions with concerning any investment in AutoMD or any financing, recapitalization, reorganization, or sale of the capital stock of AutoMD (or any rights thereto) or all or substantially all of the assets of AutoMD and (c) USAP shall not be prohibited from disclosing the terms, amounts and facts of this Agreement or this Agreement itself as may be requested by any person or entity with whom USAP is engaged in discussions with concerning any investment in USAP or any financing, recapitalization, reorganization, or sale of the capital stock of AutoMD (or any rights thereto) or all or substantially all of the assets of USAP.

7. **Entire Agreement.** This Agreement, and the other agreements, instruments, or documents executed in connection herewith or delivered at Closing, constitute the entire agreement among the parties with respect to the subject matter hereof and thereof, and supersede any other agreement with respect hereto and thereto, and there are no other or continuing agreements or understandings between each Seller, on one hand, and AutoMD and/or USAP, on the other hand, except as expressly recited herein or therein.

8. **Execution in Counterparts.** This Agreement may be executed in any number of counterparts, each of which when so executed and delivered shall constitute an original, but such counterparts together shall constitute but one and the same Agreement. The exchange of copies of this Agreement and of signature pages by facsimile transmission or PDF shall constitute effective execution and delivery of this Agreement as to the Parties and may be used in lieu of the original Agreement for all purposes. Signatures of the Parties transmitted by facsimile or PDF shall be deemed to be their original signatures for all purposes.

9. **Legal Advice.** Each Party hereto acknowledges that such Party has had the advice of independent counsel selected by such Party in connection with the terms of this Agreement and the other agreements executed in connection herewith, and that no offer, promise, inducement or consideration of any kind or degree, except as expressly stated in this Agreement, has been provided or promised to such Party by any other Party or person in connection with such Party's entry into this Agreement and the other agreements executed in connection herewith.

10. **Severability.** Should any provision of this Agreement be declared and/or be determined by any court to be illegal or invalid, the validity of the remaining parts, terms or provisions shall not be affected thereby.

11. **Expenses.** Except as otherwise provided in this Agreement, each Party to this Agreement will bear its respective fees and expenses incurred in connection with the preparation, negotiation, execution and performance of this Agreement and the transactions

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contemplated by this Agreement, including all fees and expenses of its agents and representatives. If any Party hereto institutes a proceeding to enforce such Party's rights in accordance with the provisions of this Agreement, the prevailing Party shall be entitled to recover its reasonable expenses, including attorneys' fees, in connection with any such action.

12. **Further Assurances.** At any time and from time to time, upon the reasonable request of a Party hereto, each other Party hereto shall promptly execute and deliver all such further agreements, documents, and instruments and take such further action as may be necessary or appropriate to carry out the provisions and purposes of this Agreement or any other agreement executed in connection herewith.

13. **Miscellaneous.** This Agreement shall be binding upon, and inure to the benefit of the Parties hereto and their respective heirs, successors and assigns. A modification or waiver of any of the provisions of this Agreement shall be effective only if made in writing and signed by each of the Parties hereto. The failure of any Party to insist upon the strict performance of any of the provisions of this Agreement shall not be construed as a waiver of any subsequent default of the same or any other provision.

14. **Notices.** Any notices required to be given pursuant to the provisions hereof shall be given in writing to the parties below by certified mail, return receipt requested, as follows:

If to AutoMD:

AutoMD, Inc.  
16941 Keegan Avenue  
Carson, California 90746  
Attention: General Counsel

If to Oak:

Oak Investment Partners XI, Limited Partnership  
525 University Avenue, Suite 1300  
Palo Alto, CA 94301  
Attention: Fred Harman and Craig Lang

If to the Khazani Trust:

Sol Khazani Living Trust  
578 Washington Blvd., #854  
Marina Del Rey, CA 90292  
Attention: Sol Khazani

15. **Third Party Beneficiary.** For avoidance of doubt, USAP and the other Released Parties are third party beneficiaries under this Agreement and shall be entitled to the rights and benefits hereunder and may enforce the provisions hereof as if they were parties hereto.

**[SIGNATURE PAGE FOLLOWS]**

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IN WITNESS WHEREOF, the undersigned have caused this Agreement to be executed and entered into as of the day and year first above written.

**AutoMD, Inc.**

By: /s/ Shane Evangelist  
Name: Shane Evangelist  
Title: Chief Executive Officer

**Oak Investment Partners XI, Limited Partnership**

By: Oak Associates XI, LLC, its General Partner

By: /s/ Fred Harman  
Name: Fred Harman  
Title: Managing Member

**Sol Khazani Living Trust**

By: /s/ Sol Khazani  
Name: Sol Khazani  
Titles: Authorized Signatory

## SUBSIDIARIES OF THE REGISTRANT

<b>Name</b>	<b>Jurisdiction</b>	<b>DBA</b>
PartsBin, Inc.	Delaware	
U.S. Auto Parts Network (Philippines) Corporation	Philippines	
Lobo Marketing, Inc.	Texas	
Go Fido, Inc.	Delaware	
Private Label Parts, Inc.	Delaware	Kool-Vue
Pacific 3PL, Inc.	Delaware	
AutoMD, Inc.	Delaware	
Local Body Shops, Inc.	Delaware	Perfect Fit
Automotive Specialty Accessories and Parts, Inc. (1)	Delaware	
Whitney Automotive Group, Inc. (2)	Delaware	

(1) Subsidiary of Go Fido, Inc.

(2) Subsidiary of Automotive Specialty Accessories and Parts, Inc.

**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We consent to the incorporation by reference in Registration Statement Nos. 333-143179, 333-149973, 333-158224, 333-165493, 333-173851, 333-204096, 333-212256 and 333-210093 on Form S-8 and Registration Statement Nos. 333-163811, 333-188492, 333-197903 and 333-213223 on Form S-3 of U.S. Auto Parts Network, Inc. and subsidiaries of our report dated March 6, 2017 relating to our audit of the consolidated financial statements, which appears in this Annual Report on Form 10-K of U.S. Auto Parts Network, Inc. and subsidiaries for the fiscal year ended December 31, 2016.

/s/ RSM US LLP

Los Angeles, CA

March 6, 2017



## **CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We consent to the incorporation by reference in Registration Statement Nos. 333-212256, 333-143179, 333-149973, 333-158224, 333-165493, 333-173851 and 333-204096 on Form S-8 and Registration Statement Nos. 333-213223, 333-163811, 333-188492 and 333-197903 on Form S-3 of our report dated March 19, 2015 (March 9, 2016, as to the disclosure of the approximate distribution of Base USAP online revenue by product type for fiscal year 2014 included in Note 15 - Segment Information), relating to the consolidated financial statements of U.S. Auto Parts Network, Inc. for the fiscal year ended January 3, 2015, appearing in this Annual Report on Form 10-K of U.S. Auto Parts Network, Inc. for the fiscal year ended December 31, 2016.

/s/ Deloitte & Touche LLP

Los Angeles, CA  
March 7, 2017

**CERTIFICATION PURSUANT TO EXCHANGE ACT  
RULE 13a-14(a)/15d-14(a), AS ADOPTED PURSUANT TO  
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Shane Evangelist, certify that:

1. I have reviewed this annual report on Form 10-K of U.S. Auto Parts Network, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f), for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 7, 2017

/s/ SHANE EVANGELIST

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Shane Evangelist  
Chief Executive Officer  
(principal executive officer)

**CERTIFICATION PURSUANT TO EXCHANGE ACT  
RULE 13a-14(a)/15d-14(a), AS ADOPTED PURSUANT TO  
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Neil Watanabe, certify that:

1. I have reviewed this annual report on Form 10-K of U.S. Auto Parts Network, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f), for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 7, 2017

/s/ NEIL WATANABE

Neil Watanabe

Chief Financial Officer

(principal financial officer)

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

In connection with the Annual Report of U.S. Auto Parts Network, Inc. (the "Company") on Form 10-K for the fiscal year ended December 31, 2016, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Shane Evangelist, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 7, 2017

/s/ SHANE EVANGELIST

Shane Evangelist

Chief Executive Officer

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

In connection with the Annual Report of U.S. Auto Parts Network, Inc. (the "Company") on Form 10-K for the fiscal year ended December 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Neil Watanabe, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 7, 2017

/s/ NEIL WATANABE

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Neil Watanabe

Chief Financial Officer