AMERICAN AIRLINES INC
Form 10-Q
April 18, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

ý Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the Quarterly Period Ended March 31, 2013.

¨ 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 1-2691.

American Airlines, Inc.
(Exact name of registrant as specified in its charter)

Delaware	13-1502798
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
4333 Amon Carter Blvd. Fort Worth, Texas	76155
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (817) 963-1234
Not Applicable
(Former name, former address and former fiscal year , if changed since last report)

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. ý Yes ¨ No
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act.
¨ Large Accelerated Filer ¨ Accelerated Filer ý Non-accelerated Filer
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ý Yes ¨ No
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). ¨ Yes ý No
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
Common Stock, $1 par value – 1,000 shares as of April 10, 2013.

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Forward-Looking Information

Statements in this report contain various forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which represent the Company's expectations or beliefs concerning future events. When used in this document and in documents incorporated herein by reference, the words “expects,” “estimates,” “plans,” “anticipates,” “indicates,” “believes,” “projects,” “forecast,” “guidance,” “outlook,” “may,” “will,” “could,” “should,” “seeks,” "intends," “targets” and similar expre intended to identify forward-looking statements. Similarly, statements that describe the Company's objectives, plans or goals, or actions the Company may take in the future, are forward-looking statements. Forward-looking statements include, without limitation, the Company's expectations concerning its anticipated merger with US Airways Group, Inc., the Chapter 11 Cases and the Company's business plan; the Company's operations and financial conditions, including changes in capacity, revenues, and costs; future financing plans and needs; the amounts of its unencumbered assets and other sources of liquidity; fleet plans; overall economic and industry conditions; plans and objectives for future operations; regulatory approvals and actions; and the impact on the Company of its results of operations in recent years and the sufficiency of its financial resources to absorb that impact. Other forward-looking statements include statements which do not relate solely to historical facts, such as, without limitation, statements which discuss the possible future effects of current known trends or uncertainties, or which indicate that the future effects of known trends or uncertainties cannot be predicted, guaranteed or assured. All forward-looking statements in this report are based upon information available to the Company on the date of this report. The Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events, or otherwise.

Guidance given in this report regarding capacity, fuel consumption, fuel prices, fuel hedging and unit costs are forward-looking statements. Forward-looking statements are subject to a number of factors that could cause the Company's actual results to differ materially from the Company's expectations. The following factors, in addition to other possible factors not listed, could cause the Company's actual results to differ materially from those expressed in forward-looking statements: risks related to the Merger, including fulfillment of conditions, receipt of consents and approvals, and the inability to realize the contemplated benefits of the Merger; risks arising from the Chapter 11 Cases, including reorganization risks, and liquidity risks; the materially weakened financial condition of the Company, resulting from its significant losses in recent years; the potential impact on the demand for air travel resulting from downturns in economic conditions; the Company's ability to secure financing for all of its scheduled aircraft deliveries; the potential requirement for the Company to maintain reserves under its credit card processing agreements, which could materially adversely impact the Company's liquidity; the ability of the Company to generate additional revenues and reduce its costs; continued high and volatile fuel prices and further increases in the price of fuel, and the availability of fuel; reliance on third-party distribution channels for distribution of a significant portion of the Company's airline tickets; the Company's substantial indebtedness and other obligations; the ability of the Company to satisfy certain covenants and conditions in certain of its financing and other agreements; changes in economic and other conditions beyond the Company's control, and the volatile results of the Company's operations; the fiercely and increasingly competitive business environment faced by the Company; industry consolidation and alliance changes; low fare levels by historical standards and the Company's reduced pricing power; changes in the Company's corporate or business strategy; delays in scheduled aircraft deliveries or failure of new aircraft to perform as expected; dependence on a limited number of suppliers for aircraft, aircraft engines and parts; extensive government regulation of the Company's business; increasingly stringent environmental regulations; conflicts overseas or terrorist attacks; uncertainties with respect to the Company's international operations; outbreaks of a disease (such as SARS, avian flu or the H1N1 virus) that affects travel behavior; uncertainties with respect to the Company's relationships with unionized and other employee work groups; higher than normal numbers of pilot retirements and a potential shortage of pilots; increased insurance costs and potential reductions of available insurance coverage; the Company's ability to retain key management personnel; potential failures or disruptions of the Company's computer, communications or other technology systems; losses and adverse publicity resulting from any accident involving the Company's aircraft; interruptions or disruptions in service at one or more of the Company's primary market airports; the heavy taxation of the airline industry; inability to realize the full value of intangible assets or long-lived assets, resulting in material impairment charges; and interruptions or disruptions in relationships with third-party regional airlines or other third-party service providers. The Risk Factors contained in the Company's Securities and Exchange Commission filings, including the 2012 Form 10-K, could cause the Company's actual results to differ materially from historical results and from those expressed in forward-looking statements.

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PART I: FINANCIAL INFORMATION
Item 1. Financial Statements

AMERICAN AIRLINES, INC.
DEBTOR AND DEBTOR IN POSSESSION
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited) (In millions)

	Three Months Ended March 31, 2013	2012
Revenues		
Passenger	$4,614	$4,557
Regional Affiliates	679	670
Cargo	155	168
Other revenues	637	636
Total operating revenues	6,085	6,031
Expenses		
Aircraft fuel	2,199	2,166
Wages, salaries and benefits	1,312	1,616
Regional payments to AMR Eagle	269	285
Other rentals and landing fees	342	324
Maintenance, materials and repairs	318	279
Depreciation and amortization	241	256
Commissions, booking fees and credit card expense	276	266
Aircraft rentals	164	143
Food service	139	124
Special charges and merger related	28	11
Other operating expenses	750	662
Total operating expenses	6,038	6,132
Operating Income (Loss)	47	(101)
Other Income (Expense)		
Interest income	4	6
Interest expense (contractual interest expense equals $(181) and $(183) for the three months ended March 31, 2013 and March 31, 2012, respectively)	(174)	(178)
Interest capitalized	12	12
Related party interest — net	(3)	(3)
Miscellaneous — net	(9)	(10)
	(170)	(173)
Income (Loss) Before Reorganization Items, Net	(123)	(274)
Reorganization Items, Net	(160)	(1,402)
Income (Loss) Before Income Taxes	(283)	(1,676)
Income tax (benefit)	(30)	—
Net Earnings (Loss)	$(253)	$(1,676)

The accompanying notes are an integral part of these financial statements.

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AMERICAN AIRLINES, INC.
DEBTOR AND DEBTOR IN POSSESSION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited) (In millions)

	Three Months Ended March 31, 2013	2012
Net Earnings (Loss)	$(253)	$(1,676)
Other Comprehensive Income (Loss), Before Tax:		
Defined benefit pension plans and retiree medical:		
Amortization of actuarial (gain) loss and prior service cost	(33)	56
Current year change	—	2
Benefit plan modifications	—	—
Derivative financial instruments:		
Change in fair value	(15)	48
Reclassification into earnings	(1)	(26)
Unrealized gain (loss) on investments		
Net change in value	(1)	—
Other Comprehensive Income (Loss) Before Tax	(50)	80
Income tax expense on other comprehensive income	—	—
Comprehensive Income (Loss)	$(303)	$(1,596)

The accompanying notes are an integral part of these financial statements.

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AMERICAN AIRLINES, INC.
DEBTOR AND DEBTOR IN POSSESSION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited) (In millions)

	March 31, 2013	December 31, 2012
Assets		
Current Assets		
Cash	$599	$474
Short-term investments	3,636	3,408
Restricted cash and short-term investments	853	850
Receivables, net	1,223	1,105
Inventories, net	565	550
Fuel derivative contracts	66	65
Other current assets	529	559
Total current assets	7,471	7,011
Equipment and Property		
Flight equipment, net	10,094	10,185
Other equipment and property, net	2,079	2,081
Purchase deposits for flight equipment	721	710
	12,894	12,976
Equipment and Property Under Capital Leases		
Flight equipment, net	212	222
Other equipment and property, net	56	60
	268	282
International slots and route authorities	708	708
Domestic slots and airport operating and gate lease rights, less accumulated amortization, net	155	161
Other assets	2,119	2,126
	$23,615	$23,264

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AMERICAN AIRLINES, INC.
DEBTOR AND DEBTOR IN POSSESSION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited) (In millions)

	March 31, 2013	December 31, 2012
Liabilities and Stockholder’s Equity (Deficit)		
Current Liabilities		
Accounts payable	$1,408	$1,212
Accrued liabilities	1,984	2,010
Air traffic liability	5,180	4,524
Payable to affiliates, net	2,754	2,753
Current maturities of long-term debt	1,256	1,388
Current obligations under capital leases	29	31
Total current liabilities	12,611	11,918
Long-term debt, less current maturities	6,673	6,762
Obligations under capital leases, less current obligations	375	381
Pension and postretirement benefits	6,730	6,780
Other liabilities, deferred gains and deferred credits	1,708	1,691
Liabilities Subject to Compromise	5,783	5,694
Stockholder’s Equity (Deficit)		
Common stock	—	—
Additional paid-in capital	4,470	4,469
Accumulated other comprehensive income (loss)	(3,138)	(3,088)
Accumulated deficit	(11,597)	(11,343)
	(10,265)	(9,962)
	$23,615	$23,264

The accompanying notes are an integral part of these financial statements.

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AMERICAN AIRLINES, INC.
DEBTOR AND DEBTOR IN POSSESSION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited) (In millions)

	Three Months Ended March 31, 2013	2012
Net Cash Provided by (used in) Operating Activities	$679	$1,025
Cash Flow from Investing Activities:		
Capital expenditures, including aircraft lease deposits	(882)	(236)
Net decrease (increase) in short-term investments	(228)	(726)
Net decrease (increase) in restricted cash and short-term investments	(3)	(33)
Proceeds from sale of equipment, property, and investments/subsidiaries	26	15
Net cash provided by (used in) investing activities	(1,087)	(980)
Cash Flow from Financing Activities:		
Payments on long-term debt and capital lease obligations	(392)	(314)
Proceeds from:		
Issuance of debt	161	—
Sale-leaseback transactions	764	324
Funds transferred to affiliates, net	—	36
Other	—	—
Net cash provided by (used in) financing activities	533	46
Net increase (decrease) in cash	125	91
Cash at beginning of period	474	280
Cash at end of period	$599	$371

The accompanying notes are an integral part of these financial statements.

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AMERICAN AIRLINES, INC.
DEBTOR AND DEBTOR IN POSSESSION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Chapter 11 Reorganization

Overview

On November 29, 2011 (the Petition Date), AMR Corporation (AMR), its principal subsidiary, American Airlines, Inc. (the Company) and certain of AMR's other direct and indirect domestic subsidiaries (collectively, the Debtors) filed voluntary petitions for relief (the Chapter 11 Cases) under Chapter 11 of the United States Bankruptcy Code (the Bankruptcy Code), in the United States Bankruptcy Court for the Southern District of New York (the Bankruptcy Court). The Chapter 11 Cases are being jointly administered under the caption "In re AMR Corporation, et al., Case No. 11-15463-SHL."

The Company and the other Debtors are operating as "debtors in possession" under the jurisdiction of the Bankruptcy Court and the applicable provisions of the Bankruptcy Code. In general, as debtors in possession under the Bankruptcy Code, we are authorized to continue to operate as an ongoing business but may not engage in transactions outside the ordinary course of business without the prior approval of the Bankruptcy Court. The Bankruptcy Code enables the Company to continue to operate its business without interruption, and the Bankruptcy Court has granted additional relief covering, among other things, obligations to (i) employees, (ii) taxing authorities, (iii) insurance providers, (iv) independent contractors for improvement projects, (v) foreign vendors, (vi) other airlines pursuant to certain interline agreements, and (vii) certain vendors deemed critical to the Debtors' operations.

While operating as debtors in possession under Chapter 11 of the Bankruptcy Code, the Debtors may sell or otherwise dispose of or liquidate assets or settle liabilities, subject to the approval of the Bankruptcy Court or otherwise as permitted in the ordinary course of business. On April 15, 2013, the Company and other Debtors filed with the Bankruptcy Court its proposed Plan of Reorganization (the Plan) and related Disclosure Statement. The Debtors have an exclusive period to solicit and obtain acceptances of the Plan through and including July 29, 2013. It is possible that the Plan as filed may be challenged and undergo revision, perhaps substantially, prior to the time that it is finally approved by the Bankruptcy Court and submitted to the Debtors' stakeholders for a vote. The ultimate plan of reorganization, which would be subject to acceptance by the requisite majorities of empowered stakeholders under the Bankruptcy Code and approval by the Bankruptcy Court, could materially change the amounts and classifications in the Condensed Consolidated Financial Statements. See Note 13 to the Condensed Consolidated Financial Statements for further information on the plan of reorganization.

The Company's Chapter 11 Cases followed an extended effort by the Company to restructure its business to strengthen its competitive and financial position. However, the Company's substantial cost disadvantage compared to its larger competitors, all of which restructured their costs and debt through Chapter 11, became increasingly untenable given the accelerating impact of global economic uncertainty and resulting revenue instability, volatile and rising fuel prices, and intensifying competitive challenges.

Notwithstanding any indications of value that may be contained in the Plan, no assurance can be given as to the ultimate value, if any, that may be ascribed to the Debtors' various prepetition liabilities and other securities. The Company cannot predict what the ultimate value of any of its or the other Debtors' securities may be.

General Information

Notices to Creditors; Effect of Automatic Stay. The Debtors have notified all known current or potential creditors that the Chapter 11 Cases were filed. Subject to certain exceptions under the Bankruptcy Code, the filing of the Debtors' Chapter 11 Cases automatically enjoined, or stayed, the continuation of most judicial or administrative proceedings or filing of other actions against the Debtors or their property to recover on, collect or secure a claim arising prior to the Petition Date. Thus, for example, most creditor actions to obtain possession of property from the Debtors, or to create, perfect or enforce any lien against the property of the Debtors, or to collect on monies owed or otherwise exercise rights or remedies with respect to a prepetition claim, are enjoined unless and until the Bankruptcy Court lifts the automatic stay as to any such claim. Vendors are being paid for goods furnished and services provided after the Petition Date in the ordinary course of business.

Appointment of Creditors' Committee. On December 5, 2011, the U.S. Trustee appointed the Creditors' Committee (Creditors' Committee) for the Chapter 11 Cases.

Retirement and Life Insurance Benefits. See Note 8 to the Condensed Consolidated Financial Statements for information regarding modifications to retirement and life insurance benefits.

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Rejection of Executory Contracts. Under section 365 and other relevant sections of the Bankruptcy Code, the Debtors may assume, assume and assign, or reject certain executory contracts and unexpired leases, including, without limitation, agreements relating to aircraft and aircraft engines (collectively, Aircraft Property) and leases of real property, subject to the approval of the Bankruptcy Court and certain other conditions. As of March 31, 2013, the Bankruptcy Court had entered orders granting the Debtors' motions to assume 537 and reject 12 unexpired leases of non-residential real property and had entered various orders extending, by the Debtors' agreement with certain landlords, the date by which the Debtors must assume or reject an additional 24 unexpired leases of non-residential real property.

In general, rejection of an executory contract or unexpired lease is treated as a prepetition breach of the executory contract or unexpired lease in question and, subject to certain exceptions, relieves the Debtors from performing their future obligations under such executory contract or unexpired lease but entitles the contract counterparty or lessor to a prepetition general unsecured claim for damages caused by such deemed breach. Counterparties to such rejected contracts or leases have the right to file claims against the Debtors' estate for such damages. Generally, the assumption of an executory contract or unexpired lease requires the Debtors to cure existing defaults under such executory contract or unexpired lease.

Any description of an executory contract or unexpired lease elsewhere in these Notes or in the report to which these Notes are attached, including where applicable the Debtors' express termination rights or a quantification of their obligations, must be read in conjunction with, and is qualified by, any rights the Debtors or counterparties have under section 365 of the Bankruptcy Code.

The Debtors expect that liabilities subject to compromise and resolution in the Chapter 11 Cases will arise in the future as a result of damage claims created by the Debtors' rejection of various executory contracts and unexpired leases. Due to the uncertain nature of many of the potential rejection claims, the magnitude of such claims is not reasonably estimable at this time. Such claims may be material (see "Liabilities Subject to Compromise" in Note 1 to the Condensed Consolidated Financial Statements).

Special Protection Applicable to Leases and Secured Financing of Aircraft and Aircraft Equipment. Notwithstanding the general discussion above of the impact of the automatic stay, under section 1110 of the Bankruptcy Code, beginning 60 days after filing a petition under Chapter 11, certain secured parties, lessors and conditional sales vendors may have a right to take possession of certain qualifying Aircraft Property that is leased or subject to a security interest or conditional sale contract, unless the Debtors, subject to approval by the Bankruptcy Court, agree to perform under the applicable agreement, and cure any defaults as provided in section 1110 (other than defaults of a kind specified in section 365(b)(2) of the Bankruptcy Code). Taking such action does not preclude the Debtors from later rejecting the applicable lease or abandoning the Aircraft Property subject to the related security agreement, or from later seeking to renegotiate the terms of the related financing.

The Debtors may extend the 60-day period by agreement of the relevant financing party, with Bankruptcy Court approval. In the absence of an agreement or cure as described above or such an extension, the financing party may take possession of the Aircraft Property and enforce its contractual rights or remedies to sell, lease or otherwise retain or dispose of such equipment.

The 60-day period under section 1110 in the Chapter 11 Cases expired on January 27, 2012. In accordance with the Bankruptcy Court's Order Authorizing the Debtors to (i) Enter into Agreements Under Section 1110(a) of the Bankruptcy Code, (ii) Enter into Stipulations to Extend the Time to Comply with Section 1110 of the Bankruptcy Code and (iii) File Redacted Section 1110(b) Stipulations, dated December 23, 2011, the Debtors have entered into agreements to extend the automatic stay or agreed to perform and cure defaults under financing agreements with respect to certain aircraft in their fleet and other Aircraft Property. The Debtors have reached agreement on revised terms with respect to substantially all of the aircraft for which the Debtors expect to negotiate revised terms, subject in a number of instances to certain conditions, including reaching agreement on definitive documentation. The ultimate outcome of these negotiations cannot be predicted with certainty. To the extent the Debtors are unable to reach definitive agreements with Aircraft Property financing parties, those parties may seek to repossess the subject Aircraft Property. The loss of a significant number of aircraft could result in a material adverse effect on the Debtors' financial and operating performance.

Magnitude of Potential Claims. On February 27, 2012, the Debtors filed with the Bankruptcy Court schedules and statements of financial affairs setting forth, among other things, the assets and liabilities of the Debtors, subject to the assumptions filed in connection therewith. All of the schedules are subject to further amendment or modification. Bankruptcy Rule 3003(c)(3) requires the Bankruptcy Court to fix the time within which proofs of claim must be filed in a Chapter 11 case pursuant to section 501 of the Bankruptcy Code. This Bankruptcy Rule also provides that any creditor who asserts a claim against the Debtors that arose prior to the Petition Date and whose claim (i) is not listed on the Debtors' schedules or (ii) is listed on the schedules as disputed, contingent, or unliquidated, must file a proof of claim. On May 4, 2012, the Bankruptcy Court entered an order that established July 16, 2012 at 5:00 p.m. (Eastern Time) (the Bar Date) as the deadline to file proofs of claim against any Debtor. More information regarding the filing of proofs of claim can be obtained at www.amrcaseinfo.com. Information on this website is not incorporated into or otherwise made a part of this report.

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As of April 10, 2013, approximately 13,400 claims totaling about $290.0 billion have been filed with the Bankruptcy Court against the Debtors. Of those claims, approximately 350 claims aggregating approximately $58 million were filed after the Bar Date. We expect new and amended claims to be filed in the future, including claims amended to assign values to claims originally filed with no designated value. We intend to dispute the claims filed after the Bar Date as not having been filed timely and in accordance with the Bankruptcy Code. We have identified, and we expect to continue to identify, many claims that we believe should be disallowed by the Bankruptcy Court because they are duplicative, are without merit, are overstated or for other reasons. As of April 10, 2013, the Bankruptcy Court has disallowed approximately $100.2 billion of claims and has not yet ruled on our other objections to claims, the disputed portions of which aggregate to an additional $16.1 billion. We expect to continue to file objections in the future. Because the process of analyzing and objecting to claims is ongoing, the amount of disallowed claims may increase significantly in the future. The Debtors have recorded amounts for claims for which there was sufficient information to estimate the claim.

Differences between amounts scheduled by the Debtors and claims by creditors will be investigated and resolved in connection with the claims resolution process. In light of the expected number of creditors, the claims resolution process may take considerable time to complete. Accordingly, the ultimate number and amount of allowed claims is not presently known, nor can the ultimate recovery with respect to allowed claims be presently ascertained.

Collective Bargaining Agreements. Section 1113(c) of the Bankruptcy Code provides a process for the modification and/or rejection of collective bargaining agreements (CBAs). Through this process, American was able to achieve new CBAs with each of its unions (TWU, APFA and APA), covering nine unionized work groups.

In September 2012, the Bankruptcy Court authorized American to reject its pilot CBA, and thereafter American began implementing certain terms and conditions of employment for pilots. American and the APA continued to negotiate in good faith toward a new pilot agreement, and those negotiations resulted in a new pilot CBA that was approved by the Bankruptcy Court on December 19, 2012. A small group of American pilots is appealing the Bankruptcy Court's decisions granting American's request to reject the pilot CBA and approving the new pilot CBA, and those appeals are pending in the U.S. District Court for the Southern District of New York.

American Eagle Airlines, Inc. (AMR Eagle) also engaged in the Section 1113(c) process with its unions, and ultimately achieved new CBAs with AFA, ALPA and all four TWU-represented work groups.

In addition, American's pilots, flight attendants, and ground employee unions and the US Airways, Inc. pilots union have agreed to terms for improved CBAs, effective upon the closing of AMR's proposed merger with US Airways Group, Inc. (US Airways Group) (see Note 12 and Note 13 to the Condensed Consolidated Financial Statements for further information regarding the merger). The US Airways, Inc. flight attendants union has also reached a tentative agreement with US Airways, Inc., which includes support for the merger. American's unions representing pilots and flight attendants are working with their counterparts at US Airways, Inc. to determine representation and single agreement protocols to be used to integrate workforce after the merger.

Merger Agreement and Plan of Reorganization. See Notes 12 and 13 to the Condensed Consolidated Financial Statements for information regarding the Merger Agreement and Plan.

Availability and Utilization of Net Operating Losses. The availability and utilization of net operating losses (and utilization of alternative minimum tax credits) after the Debtors' emergence from Chapter 11 is uncertain at this time and will be highly influenced by the composition of the plan of reorganization that is ultimately pursued. On January 27, 2012, the Bankruptcy Court issued a Final Order Establishing Notification Procedures for Substantial Claimholders and Equityholders and Approving Restrictions on Certain Transfers of Interests in the Debtors' Estates, which restricted trading in the Company's common stock and established certain procedures and potential restrictions with respect to the transfer of claims. The order was intended to prevent, or otherwise institute procedures and notification requirements with respect to, certain transfers of AMR Common Stock and unsecured claims against the Debtors that could impair the ability of the Debtors to use their net operating loss carryovers and certain other tax attributes on a reorganized basis. However, the Original Procedures did not envision the proposed merger between AMR and US Airways Group and, if implemented to take into account the proposed merger or an equivalent transaction, might have unduly restricted the amount of claims that may be accumulated and retained by certain holders. Accordingly, on February 22, 2013, the Debtors filed a motion with the Bankruptcy Court to revise the

Original Procedures (as so revised, the Revised Procedures).

On April 11, 2013, the Bankruptcy Court entered an order (the Revised Order) approving the Revised Procedures. With respect to holders of unsecured claims against the Debtors, the Revised Procedures establish a process in which holders of unsecured claims in excess of a threshold amount may be required to file one or more Notices of Substantial Claim Ownership, and, under certain circumstances, may be required to sell all or a portion of any unsecured claims acquired during the Chapter 11 Cases. The Revised Procedures potentially apply to any person that beneficially owns either (1) more than $190 million of claims against the Debtors or (2) a lower amount of claims which, when added to certain specified interests, including stock, in AMR or

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US Airways Group, would result in such holder holding the “Applicable Percentage,” generally 4.5 percent, of the reorganized Debtors. In connection with the filing of a Notice of Substantial Claim Ownership, a holder must indicate if it will agree to refrain from acquiring additional AMR and US Airways Group common stock and such other specified interests until after the effective date of the Debtors' Chapter 11 plan of reorganization, and to dispose of any such interests acquired since February 22, 2013. This can affect the manner in which the Revised Procedures apply to certain holders.

The Revised Procedures did not alter the procedures applicable with respect to “Substantial Equityholders,” namely persons who are, or as a result of a transaction would become, the beneficial owner of approximately 4.5 percent of the outstanding shares of AMR Common Stock.

Any acquisition, disposition, or other transfer of equity or claims in violation of the restrictions set forth in the Revised Order will be null and void ab initio and/or subject to sanctions as an act in violation of the automatic stay under sections 105(a) and 362 of the United States Bankruptcy Code.

Liabilities Subject to Compromise

The following table summarizes the components of liabilities subject to compromise included on the Condensed Consolidated Balance Sheet as of March 31, 2013 and December 31, 2012:

(in millions)

	March 31, 2013	December 31, 2012
Long-term debt	$358	$358
Estimated allowed claims on aircraft lease and debt obligations and facility lease and bond obligations	3,874	3,716
Pension and postretirement benefits	1,237	1,250
Accounts payable and other accrued liabilities	314	370
Other	—	—
Total liabilities subject to compromise	$5,783	$5,694

Long-term debt, including undersecured debt, classified as subject to compromise as of March 31, 2013 and December 31, 2012 consisted of (in millions):

	March 31, 2013	December 31, 2012
Secured variable and fixed rate indebtedness due through 2023 (effective rates from 1.00% - 13.00% at March 31, 2013)	$172	$172
6.00%—8.50% special facility revenue bonds due through 2036	186	186
	$358	$358

Liabilities subject to compromise refers to prepetition obligations which may be impacted by the Chapter 11 reorganization process. These amounts represent the Debtors’ current estimate of known or potential prepetition obligations to be resolved in connection with the Chapter 11 Cases.

In accordance with ASC 852, substantially all of the Company’s unsecured debt has been classified as liabilities subject to compromise. Additionally, certain of the Company’s undersecured debt instruments have also been classified as liabilities subject to compromise.

Pursuant to the Support Agreement, as defined and further described in Note 12 to the Condensed Consolidated Financial Statements, the Debtors agreed to allow certain post-petition unsecured claims on obligations. As a result, the Company recorded interest charges of $116 million to liabilities subject to compromise to recognize post-petition interest expense on unsecured obligations.

As a result of the modifications to the retirement benefits as discussed in Note 8 to the Condensed Consolidated Financial Statements, a portion of the pension and postretirement benefits liability, primarily relating to retiree medical and other benefits, was classified as liabilities subject to compromise. as of March 31, 2013.

Differences between liabilities the Debtors have estimated and the claims filed, or to be filed, will be investigated and resolved in connection with the claims resolution process. The Company will continue to evaluate these liabilities throughout the Chapter

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11 Cases and adjust amounts as necessary. Such adjustments may be material. In light of the expected number of creditors, the claims resolution process may take considerable time to complete. Accordingly, the ultimate number and amount of allowed claims is not presently known.

Reorganization Items, net

Reorganization items refer to revenues, expenses (including professional fees), realized gains and losses and provisions for losses that are realized or incurred in the Chapter 11 Cases. The following table summarizes the components included in reorganization items, net on the Consolidated Statements of Operations for the three months ended March 31, 2013 and March 31, 2012:

(in millions)

	Three Months Ended March 31,	
	2013	2012
Pension and postretirement benefits	$—	$—
Aircraft and facility financing renegotiations and rejections [(1)(2)(3)]	136	1,357
Professional fees	39	45
Other	(15)	—
Total reorganization items, net	$160	$1,402

(1) Amounts include allowed claims (claims approved by the Bankruptcy Court) and estimated allowed claims relating to the rejection or modification of financings related to aircraft. The Debtors record an estimated claim associated with the rejection or modification of a financing when the applicable motion is filed with the Bankruptcy Court to reject or modify such financing and the Debtors believe that it is probable the motion will be approved, and there is sufficient information to estimate the claim. Modifications of the financings related to certain aircraft remain subject to conditions, including reaching agreement on definitive documentation. See above, “Special Protection Applicable to Leases and Secured Financing of Aircraft and Aircraft Equipment,” for further information.

(2) Amounts include allowed claims (claims approved by the Bankruptcy Court) and estimated allowed claims relating to entry of orders treating as unsecured claims with respect to facility agreements supporting certain issuances of special facility revenue bonds. The Debtors record an estimated claim associated with the treatment of claims with respect to facility agreements when the applicable motion is filed with the Bankruptcy Court and the Debtors believe that it is probable that the motion will be approved, and there is sufficient information to estimate the claim. See above, “Rejection of Executory Contracts,” for further information.

(3) Pursuant to the Support Agreement, as defined and further described in Note 12 to the Condensed Consolidated Financial Statements, the Debtors agreed to allow certain post-petition unsecured claims on obligations. As a result, the Company recorded reorganization charges to adjust estimated allowed claim amounts previously recorded on rejected special facility revenue bonds of $127 million, which is included in the table above.

Claims related to reorganization items are reflected in liabilities subject to compromise on the Condensed Consolidated Balance Sheet as of March 31, 2013.

2. Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with United States (U.S.) generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, these financial statements contain all adjustments, consisting of normal recurring accruals, necessary to present fairly the financial position, results of operations and cash flows for the periods indicated. Results of operations for the periods presented herein are not necessarily indicative of results of operations for the entire year.

American is a wholly owned subsidiary of AMR. The Condensed Consolidated Financial Statements also include the accounts of variable interest entities for which the Company is the primary beneficiary. For further information, refer to the consolidated financial statements and footnotes included in the American Annual Report on Form 10-K filed on February 20, 2013, as amended by the Form 10-K/A filed on April 16, 2013 (2012 Form 10-K).

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In accordance with GAAP, the Debtors have applied ASC 852 “Reorganizations” (ASC 852), in preparing the Condensed Consolidated Financial Statements. ASC 852 requires that the financial statements, for periods subsequent to the Chapter 11 Cases, distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Accordingly, certain revenues, expenses (including professional fees), realized gains and losses and provisions for losses that are realized or incurred in the Chapter 11 Cases are recorded in reorganization items, net on the accompanying Consolidated Statement of Operations. In addition, prepetition obligations that may be impacted by the Chapter 11 reorganization process have been classified on the Condensed Consolidated Balance Sheet in liabilities subject to compromise. These liabilities are reported at the amounts expected to be allowed by the Bankruptcy Court, even if they may be settled for lesser amounts.

Certain of our non-U.S. subsidiaries were not part of the Chapter 11 filings. Since the non-US subsidiaries not part of the bankruptcy filing do not have significant transactions, we do not separately disclose the condensed combined financial statements of such non-U.S. subsidiaries in accordance with the requirements of reorganization accounting.

These Condensed Consolidated Financial Statements have also been prepared on a going concern basis, which contemplates continuity of operations, realization of assets and satisfaction of liabilities in the ordinary course of business. Accordingly, the Condensed Consolidated Financial Statements do not include any adjustments relating to the recoverability of assets and classification of liabilities that might be necessary should the Debtors be unable to continue as a going concern.

As a result of the Chapter 11 Cases, the satisfaction of our liabilities and funding of ongoing operations are subject to uncertainty and, accordingly, there is a substantial doubt of the Company’s ability to continue as a going concern. The accompanying Condensed Consolidated Financial Statements do not purport to reflect or provide for the consequences of the Chapter 11 Cases, other than as set forth under “liabilities subject to compromise” on the accompanying Condensed Consolidated Balance Sheet and “income (loss) before reorganization items” and “reorganization items, net” on the accompanying Consolidated Statement of Operations (see Note 1 to the Condensed Consolidated Financial Statements). In particular, the financial statements do not purport to show (1) as to assets, their realizable value on a liquidation basis or their availability to satisfy liabilities; (2) as to prepetition liabilities, the amounts that may be allowed for claims or contingencies, or the status and priority thereof; or (3) as to operations, the effect of any changes that may be made to the Debtors’ business.

3. Commitments, Contingencies and Guarantees

Restructuring of Agreements with The Boeing Company and Amendment of Agreement with Airbus S.A.S.

American entered into an agreement on January 11, 2013 (the Restructuring Agreement) with Boeing that provides for the assumption and restructuring of certain existing aircraft purchase agreements (the Restructured Aircraft Purchase Agreements) between Boeing and American, the entering into of a definitive purchase agreement (the MAX purchase agreement) with respect to Boeing 737 MAX aircraft (the MAX aircraft), certain financing commitments for the Boeing 787 aircraft (the 787 aircraft) and certain Boeing 737-8 aircraft (the 737 aircraft), the assumption of certain other aircraft spare parts, support and services agreements, and a comprehensive settlement of the relationship among American and its affiliates and Boeing and certain affiliates of Boeing, including all claims asserted by Boeing and such affiliates in the Chapter 11 Cases, with certain limited exceptions.

The Bankruptcy Court issued an order on January 23, 2013 approving the Restructuring Agreement, assumption of the Restructured Aircraft Purchase Agreements, and the MAX purchase agreement. The Restructured Aircraft Purchase Agreements provide for the substitution of 787-8 aircraft for certain 787-9 aircraft, an accelerated delivery schedule for the 787 aircraft with deliveries scheduled to commence in November 2014 and continue in each calendar year through September 2018, and the confirmation of the purchase of the Boeing 787 aircraft, which previously had been subject to certain reconfirmation rights. Under the Restructured Aircraft Purchase Agreements, American will have the option to purchase 40 737 aircraft, 13 777 aircraft and 58 787 aircraft.

Pursuant to the Restructuring Agreement, American entered into the MAX purchase agreement pursuant to which American will acquire 100 MAX aircraft, equipped with new, more fuel efficient engines. The MAX purchase agreement constitutes the definitive purchase agreement contemplated by, and supersedes, the agreement entered into by American and Boeing on July 19, 2011 (the 2011 MAX order) that provided for the commitment of American to purchase such MAX aircraft (referred to in the 2011 MAX order as 737RE aircraft). The 2011 MAX order was subject to a number of contingencies, including the parties entering into a definitive purchase agreement and Boeing's approval of the launch of the Boeing 737 re-engined aircraft program, which was approved in August, 2011. Under the MAX purchase agreement, MAX aircraft are scheduled to be delivered to American in each of the years 2018 through 2022. In addition, under the MAX purchase agreement, American will have the option to purchase 60 additional MAX aircraft in the years 2020-2025.

American also, on January 11, 2013, entered into an amendment to the A320 Family Aircraft Purchase Agreement with Airbus, dated July 20, 2011 (the Airbus Amendment) specifying the scheduled delivery months of certain aircraft and revising the date by which American must notify Airbus of the engine selection of certain aircraft types. The Airbus Amendment became effective on

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January 23, 2013, when the Court entered an order approving assumption of the A320 Family Purchase Agreement. Agreements pursuant to which Airbus agreed to providing financing for the purchase of certain aircraft also were assumed.

American had total aircraft acquisition commitments as of March 31, 2013 as follows:

		Boeing				Airbus		
		737 Family	737 MAX	777-300 ER	787 Family	A320 Family	A320 NEO	Total
Remainder of 2013	Purchase	22	—	5	—	—	—	27
	Lease	—	—	—	—	20	—	20
2014	Purchase	16	—	6	2	—	—	24
	Lease	4	—	—	—	35	—	39
2015	Purchase	—	—	2	11	—	—	13
	Lease	20	—	—	—	30	—	50
2016	Purchase	—	—	2	13	—	—	15
	Lease	20	—	—	—	25	—	45
2017	Purchase	—	—	—	9	—	10	19
	Lease	20	—	—	—	20	—	40
2018 and beyond	Purchase	—	100	—	7	—	120	227
	Lease	—	—	—	—	—	—	—
Total	Purchase	38	100	15	42	—	130	325
	Lease	64	—	—	—	130	—	194

As of March 31, 2013, and subject to assumption of certain of the related agreements, payments for the above purchase commitments and certain engines will approximate \$1.6 billion in the remainder of 2013, \$1.9 billion in 2014, \$1.7 billion in 2015, \$2.1 billion in 2016, \$2.1 billion in 2017, and \$12.6 billion for 2018 and beyond. These amounts are net of purchase deposits currently held by the manufacturers. American has granted Boeing a security interest in American's purchase deposits with Boeing. The Company's purchase deposits totaled \$721 million as of March 31, 2013.

As of March 31, 2013, and subject to assumption of certain of the related agreements, total future lease payments for all leased aircraft, including aircraft not yet delivered, will approximate \$624 million in the remainder of 2013, \$945 million in 2014, \$1.2 billion in 2015, \$1.4 billion in 2016, \$1.6 billion in 2017, and \$11.7 billion in 2018 and beyond.

In 2010, American and Japan Airlines (JAL) entered into a Joint Business Agreement (JBA) under which, amongst other things, American provided JAL a guarantee of certain minimum incremental revenue resulting from the successful operation of the joint business for the first three years following its implementation (which period will end June 30, 2015), subject to certain terms and conditions. The amount required to be paid by the Company under the guarantee in any one of such years may not exceed \$100 million, and is reduced if capacity for one of such years is less than a defined base year period capacity. Based on current Trans-Pacific capacity, the guarantee in any one of such years may not exceed approximately \$85 million. As of March 31, 2013, based on an expected probability model, American had a recorded guarantee liability that is not material.

Capacity Purchase Agreements with Third Party Regional Airlines

During 2012, American entered into capacity purchase agreements with SkyWest Airlines, Inc. (SkyWest) and with ExpressJet Airlines, Inc. (ExpressJet), both wholly owned subsidiaries of SkyWest, Inc., to provide 50-seat regional jet feed. Both airlines operate the services under the American Eagle® brand. SkyWest began service from Los Angeles International Airport on November 15, 2012, and ExpressJet began service from Dallas-Ft. Worth International Airport on February 14, 2013. In addition, Chautauqua Airlines, Inc. (Chautauqua) continues to operate under the brand AmericanConnection® under a capacity purchase agreement with American.

On January 23, 2013, American entered into a 12 year capacity purchase agreement with Republic Airline Inc. (Republic), a subsidiary of Republic Airways Holdings, to provide large regional jet flying. Through the agreement, Republic will acquire 47 Embraer E-175 aircraft featuring a two-class cabin with 12 first class seats and 64 seats in

the main cabin. The aircraft, which will fly under the American Eagle® brand, will phase into operation at approximately two to three aircraft per month beginning in mid-2013. All 47 aircraft are expected to be in operation by the first quarter of 2015.
As of March 31, 2013, American's minimum fixed obligations under its capacity purchase agreements with third party regional airlines were approximately $257 million in the remainder of 2013, $521 million in 2014, $670 million in 2015, $676 million in

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2016, $520 million in 2017 and $4.4 billion in 2018 and beyond. These obligations contemplate minimum levels of flying by the third party airlines under the respective agreements and also reflect assumptions regarding certain costs associated with the minimum levels of flying such as the cost of fuel, insurance, catering, property tax and landing fees. Accordingly, actual payments under these agreements could differ materially from the minimum fixed obligations set forth above.

Other

As a result of the filing of the Chapter 11 Cases, attempts to prosecute, collect, secure or enforce remedies with respect to prepetition claims against the Debtors are subject to the automatic stay provisions of Section 362(a) of the Bankruptcy Code, except in such cases where the Bankruptcy Court has entered an order modifying or lifting the automatic stay. Notwithstanding the general application of the automatic stay described above, governmental authorities, both domestic and foreign, may determine to continue actions brought under their regulatory powers. Therefore, the automatic stay may have no effect on certain matters, and the Debtors cannot predict the impact, if any, that its Chapter 11 Cases might have on its commitments and obligations.

4. Depreciation and Amortization

Accumulated depreciation of owned equipment and property at March 31, 2013 and December 31, 2012 was $10.6 billion and $10.4 billion, respectively. Accumulated amortization of equipment and property under capital leases at March 31, 2013 and December 31, 2012 was $219 million and $205 million, respectively.

5. Income Taxes

The Company provides a valuation allowance for deferred tax assets when it is more likely than not that some portion, or all, of its deferred tax assets will not be realized. The Company’s deferred tax asset valuation allowance increased from $5.1 billion as of December 31, 2012 to $5.2 billion as of March 31, 2013, including the impact of comprehensive income for the three months ended March 31, 2013 and changes from other adjustments. These other adjustments include the realization of an income tax expense credit of approximately $30 million recorded for the three months ended March 31, 2013 by the Company as a result of passage of the American Taxpayer Relief Act of 2012. There was no amount of adjustment recorded by the Company during the quarter ended March 31, 2012.

Under current accounting rules, the Company is required to consider all items (including items recorded in other comprehensive income) in determining the amount of tax benefit that results from a loss from continuing operations and that should be allocated to continuing operations. Due to the significant volatility of items impacting other comprehensive income on a quarterly basis, the Company generally does not record any such tax benefit allocation until all items impacting other comprehensive income are known for the annual period. Thus, any such interim tax benefit allocation may subsequently be subject to reversal.

6. Indebtedness and Leases

Long-term debt classified as not subject to compromise consisted of (in millions):

	March 31, 2013	December 31, 2012
Secured variable and fixed rate indebtedness due through 2023 (effective rates from 1.00%-13.00% at March 31, 2013)	$3,004	$3,297
Enhanced equipment trust certificates (EETC) due through 2025 (rates from 4.00%-10.375% at March 31, 2013)	1,851	1,741
6.00%-8.50% special facility revenue bonds due through 2036	1,314	1,313
7.50% senior secured notes due 2016	1,000	1,000
AAdvantage Miles advance purchase (net of discount of $50 million) (effective rate 8.3%)	733	772
Other	27	27
	7,929	8,150
Less current maturities	1,256	1,388
Long-term debt, less current maturities	$6,673	$6,762

The financings listed in the table above are considered not subject to compromise. For information regarding the liabilities subject to compromise, see Note 1 to the Condensed Consolidated Financial Statements.

The Company's future long-term debt and operating lease payments have changed as its ordered aircraft are delivered and such deliveries have been financed. As of March 31, 2013, maturities of long-term debt (including sinking fund requirements) for the next five years are:

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Years Ending December 31 (in millions)	Principal Not Subject to Compromise	Principal Subject to Compromise	Total Principal Amount
Remainder of 2013	$1,004	$93	$1,097
2014	870	152	1,022
2015	768	5	773
2016	1,762	5	1,767
2017	503	42	545

Principal Not Subject to Compromise and Subject to Compromise includes payments not made due to the Chapter 11 Cases of $451 million and $64 million, respectively.

Future minimum lease payments required under operating leases that have initial or remaining non-cancelable lease terms in excess of a year as of March 31, 2013, were: remainder of 2013 – $853 million, 2014 – $1.0 billion, 2015 – $977 million, 2016 – $900 million, 2017 – $860 million, and 2018 and beyond – $5.1 billion. As of March 31, 2013, $201 million and $163 million are included on the accompanying balance sheet in Liabilities Subject to Compromise and Accrued liabilities and other liabilities and deferred credits, respectively, relating to rent expense being recorded in advance of future operating lease payments.

As of March 31, 2013, AMR had issued guarantees covering approximately $1.5 billion of American's tax-exempt bond debt (and interest thereon) and $4.1 billion of American's secured debt (and interest thereon). American had issued guarantees covering approximately $842 million of AMR's unsecured debt (and interest thereon).

EETC Transactions

On March 12, 2013, American closed its private offering of two tranches of enhanced equipment trust certificates (the Series 2013-1 EETCs) in the aggregate face amount of $664 million. The Series 2013-1 EETCs are comprised of a senior tranche of Class A Certificates with an interest rate of 4.00% per annum and a final expected distribution date of July 15, 2025, and a junior tranche of Class B Certificates with an interest rate of 5.625% per annum and a final expected distribution date of January 15, 2021. The Series 2013-1 EETCs represent an interest in the assets of two separate pass through trusts, each of which hold equipment notes issued or expected to be issued by American. Interest on the issued and outstanding equipment notes will be payable semiannually on January 15 and July 15 of each year, commencing on July 15, 2013, and principal on such equipment notes is scheduled for payment on January 15 and July 15 of certain years, commencing on January 15, 2014. The equipment notes are secured by eight currently owned Boeing 737-823 aircraft and one currently owned Boeing 777-223ER aircraft and are expected to be secured by four new Boeing 777-323ER aircraft currently scheduled for delivery to American during the period from April 2013 to July 2013. The certificates were offered in the U.S. to qualified institutional buyers, as defined in, and in reliance on, Rule 144A under the Securities Act of 1933, as amended (the Securities Act).

The Company filed a motion with the Bankruptcy Court on October 9, 2012, requesting entry of an order authorizing American to, among other things: (i) obtain postpetition financing in an amount of up to $1.5 billion secured on a first priority basis by, among other things, up to 41 Boeing 737-823 aircraft, 14 Boeing 757-223 aircraft, one Boeing 767-323ER aircraft and 19 Boeing 777-223ER aircraft as part of a new enhanced equipment trust certificate (EETC) financing (the Refinancing EETC) to be offered pursuant to Rule 144A under the Securities Act, and (ii) use cash on hand (including proceeds of the Refinancing EETC) to indefeasibly repay the existing prepetition obligations secured by such aircraft, as applicable, which are currently financed through, as the case may be, an EETC financing entered into by American in July 2009 (the Series 2009-1 Pass Through Certificates), a secured notes financing entered into by American in July 2009 (the 2009-2 Senior Secured Notes) and an EETC financing entered into by American in October 2011 (the Series 2011-2 Pass Through Certificates and, together with the Series 2009-1 Pass Through Certificates and the 2009-2 Senior Secured Notes, the Existing Financings), in each case without the payment of any make-whole amount or other premium or prepayment penalty. American expects the Refinancing EETC structure to be substantially similar to the structure of the Series 2011-2 Pass Through Certificates, other than the economic terms (such as the interest rate) and certain terms and conditions to be in effect during its current Chapter 11 bankruptcy case.

The Bankruptcy Court approved the motion on January 17, 2013 and entered an order (the EETC Order) pursuant to such effect on February 1, 2013. The trustees for the Existing Financings have appealed the EETC Order and judgments rendered in certain related adversary proceedings. The appeals are currently being briefed before the Second Circuit Court of Appeals and will be fully submitted by April 30, 2013. The Company intends to continue to assert vigorously its rights to repay the Existing Financings without the payment of any make-whole amount or other premium or prepayment penalty, and the Company is considering all of its options, including the payment of the Existing Financings and closing the Refinancing EETC notwithstanding such appeal. There can be no assurance that the refinancing EETC will be able to be effected on acceptable terms, if at all.

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Sale-leaseback Arrangements

American has entered into sale-leaseback arrangements with certain leasing companies to finance 32 Boeing 737-800 aircraft scheduled to be delivered from April 2013 through 2014. The financings of each aircraft under these arrangements are subject to certain terms and conditions. In addition, in some instances, they are also subject to collaboration with the Creditors' Committee and other key stakeholders and to the approval of the Bankruptcy Court. During the first three months of 2013, American financed 8 Boeing 737-800 and three Boeing 777-300ER aircraft under sale-leaseback arrangements, which are accounted for as operating leases. These sale-leaseback transactions resulted in gains which are being amortized over the respective remaining lease terms.

Collateral Related Covenants

Certain of American’s debt financing agreements contain loan to value ratio covenants and require American to periodically appraise the collateral. Pursuant to such agreements, if the loan to value ratio exceeds a specified threshold, American is required, as applicable, to subject additional qualifying collateral (which in some cases may include cash collateral), or pay down such financing, in whole or in part, with premium (if any), or pay additional interest on the related indebtedness, as described below.

Specifically, American is required to meet certain collateral coverage tests on a periodic basis on two financing transactions: (1) 10.5% $450 million Senior Secured Notes due 2012 (the 10.5% Notes) and (2) Senior Secured Notes, as described below:

	10.5% Notes		Senior Secured Notes
Frequency of Appraisals	Semi-Annual (April and October)		Semi-Annual (June and December)
LTV Requirement	43%; failure to meet collateral test requires posting of additional collateral		1.5x Collateral valuation to amount of debt outstanding (67% LTV); failure to meet collateral test results in American paying 2% additional interest until the ratio is at least 1.5x; additional collateral can be posted to meet this requirement
LTV as of Last Measurement Date	47.5%		38.8%
Collateral Description	143 aircraft consisting of:		Generally, certain route authorities, take-off and landing slots, and rights to airport facilities used by American to operate certain services between the U.S. and London Heathrow, Tokyo Narita/Haneda, and China
	Type	# of Aircraft	
	MD-80	74	
	B757-200	41	
	B767-200ER	3	
	B767-300ER	25	
	TOTAL	143	

At March 31, 2013, the Company was in compliance with the most recently completed collateral coverage tests for the Senior Secured Notes. As of March 31, 2013, American had $41 million of cash collateral posted with respect to the 10.5% notes, which matured in 2012. The Company has not satisfied the debt with respect to the 10.5% notes due to the ongoing Chapter 11 Cases.

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Other

Almost all of the Company’s aircraft assets (including aircraft and aircraft-related assets eligible for the benefits of section 1110 of the Bankruptcy Code) are encumbered, and the Company has a very limited quantity of assets which could be used as collateral in financing.

The Chapter 11 Cases triggered defaults on substantially all debt and lease obligations of the Debtors. However, under section 362 of the Bankruptcy Code, the commencement of a Chapter 11 case automatically stays most creditor actions against the Debtors’ estates.

As discussed in Note 1 to the Condensed Consolidated Financial Statements, the Company has been using the benefits afforded by the Bankruptcy Code to restructure the terms of much of its indebtedness and lease obligations. The Company cannot predict at this time the outcome of its efforts to restructure its indebtedness and lease obligations. It is possible that holders of the Company's unsecured indebtedness may lose a portion of their investment depending on the outcome of the Chapter 11 Cases.

7. Fair Value Measurements

The Company utilizes the market approach to measure fair value for its financial assets and liabilities. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. The Company’s short-term investments classified as Level 2 primarily utilize broker quotes in a non-active market for valuation of these securities. The Company’s fuel derivative contracts, which consist primarily of collars (consisting of a purchased call option and a sold put option) and call spreads (consisting of a purchased call option and a sold call option), are valued using energy and commodity market data which is derived by combining raw inputs with quantitative models and processes to generate forward curves and volatilities. Heating oil, jet fuel and crude oil are the primary underlying commodities in the hedge portfolio. No changes in valuation techniques or inputs occurred during the three months ended March 31, 2013.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

(in millions)	Fair Value Measurements as of March 31, 2013			
Description	Total	Level 1	Level 2	Level 3
Short-term investments [1, 2]				
Money market funds	$415	$415	$—	$—
Government agency investments	609	—	609	—
Repurchase investments	280	—	280	—
Corporate obligations	1,749	—	1,749	—
Bank notes / Certificates of deposit / Time deposits	583	—	583	—
	3,636	415	3,221	—
Restricted cash and short-term investments [1]	853	853	—	—
Fuel derivative contracts, net [1]	66	—	66	—
Total	$4,555	$1,268	$3,287	$—

[1] Unrealized gains or losses on short-term investments, restricted cash and short-term investments and derivatives qualifying for hedge accounting are recorded in Accumulated other comprehensive income (loss) at each measurement date.

[2] The Company’s short-term investments mature in one year or less except for $350 million of Bank notes/Certificates of deposit/Time deposits, $609 million of U.S. Government agency investments and $470 million of Corporate obligations which have maturity dates exceeding one year.

No significant transfers between Level 1 and Level 2 occurred during the three months ended March 31, 2013. The Company’s policy regarding the recording of transfers between levels is to reflect any such transfers at the end of the reporting period.

As of March 31, 2013, the Company had no exposure to European sovereign debt.

The fair values of the Company’s long-term debt classified as Level 2 were estimated using quoted market prices or discounted cash flow analyses, based on the Company’s current estimated incremental borrowing rates for similar types of borrowing arrangements. All of the Company's long term debt not classified as subject to compromise is classified as Level 2.

The carrying value and estimated fair values of the Company's long-term debt, including current maturities, not classified as subject to compromise, were (in millions):

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	March 31, 2013		December 31, 2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Secured variable and fixed rate indebtedness	$3,004	$2,883	$3,297	$3,143
Enhanced equipment trust certificates	1,851	1,946	1,741	1,811
6.0%—8.5% special facility revenue bonds	1,314	1,453	1,313	1,308
7.50% senior secured notes	1,000	1,150	1,000	1,074
AAdvantage Miles advance purchase	733	739	772	779
Other	27	27	27	27
	$7,929	$8,198	$8,150	$8,142

The carrying value and estimated fair value of the Company's long-term debt, including current maturities, classified as subject to compromise, were (in millions):

	March 31, 2013		December 31, 2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Secured variable and fixed rate indebtedness	$172	$148	$172	$154
6.0%—8.5% special facility revenue bonds	186	194	186	186
	$358	$342	$358	$340

All of the Company's long term debt classified as subject to compromise is classified as Level 2.

8. Retirement Benefits

The following tables provide the components of net periodic benefit cost for the three months ended March 31, 2013 and 2012 (in millions):

	Pension Benefits Three Months Ended March 31,	
	2013	2012
Components of net periodic benefit cost		
Service cost	$1	$104
Interest cost	163	191
Expected return on assets	(180)	(166)
Amortization of:		
Prior service cost	7	4
Unrecognized net (gain) loss	23	61
Net periodic benefit cost	$14	$194

	Retiree Medical and Other Benefits Three Months Ended March 31,	
	2013	2012
Components of net periodic benefit cost		
Service cost	$—	$15
Interest cost	13	38
Expected return on assets	(4)	(4)
Amortization of:		
Prior service cost	(61)	(7)
Unrecognized net (gain) loss	(2)	(2)
Net periodic benefit cost	$(54)	$40

The Company is required to make minimum contributions to its defined benefit pension plans under the minimum funding requirements of ERISA, the Pension Funding Equity Act of 2004, the Pension Protection Act of 2006, and the Pension Relief Act

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of 2010. As a result of the Chapter 11 Cases, AMR contributed $33 million to its U.S. defined benefit pension plans during the first quarter of 2013 covering post-petition periods. The Company’s remaining 2013 contributions to its defined benefit pension plans are subject to the Chapter 11 proceedings. Prior to the closing of the Merger (see Note 13 to the Condensed Consolidated Financial Statements for further information), AMR and/or its subsidiaries will make all minimum required contributions to each AMR compensation and benefit plan that are required to have been made and were not made prior to the effective date of the Merger. As a result of the Company only contributing the post-petition portion of required contributions, the PBGC filed a lien against certain assets of the Company in 2012.

Recent Modifications to Pension and Other Post-Employment Benefits

The Company's defined benefit pension plans were frozen effective November 1, 2012. Eligible employees began to receive a replacement benefit under the $uper $aver 401(k) Plan on November 1, 2012.

In December 2012, the Pilot A Plan, a defined benefit plan, was amended to remove the lump-sum option and the installment option forms of benefit effective December 31, 2012. A small group of American pilots is appealing the Bankruptcy Court's decision authorizing American to eliminate the lump sum option and installment option forms of benefit. This is the same group of pilots that is appealing the Bankruptcy Court's decisions authorizing American to reject the pilot CBA and approving the new pilot CBA. All of these appeals have been consolidated, and are pending in the U.S. District Court for the Southern District of New York.

The Pilot B Plan, a defined contribution plan, was terminated on November 30, 2012. Plan B assets will be distributed to pilots in mid-2013.

On July 6, 2012, the Company commenced an adversary proceeding in the Bankruptcy Court seeking a determination on the issue of vesting for former employees who retired and initiated retiree medical coverage before November 1, 2012. The Court held a hearing on January 23, 2013 and has not ruled on this matter as of the date of this report. The Company has been negotiating with the retiree committee since July 2012, seeking a consensual agreement to terminate subsidized retiree medical coverage and life insurance coverage. Those negotiations are continuing.

As a result of the modifications to the retirement benefits as discussed above, a portion of the pension and postretirement benefits liability, primarily relating to retiree medical and other benefits, was classified as liabilities subject to compromise. See Note 1 to the Condensed Consolidated Financial Statements for the breakout of liabilities subject to compromise, including that related to pension and postretirement benefits.

9. Special Charges and Merger Related Expenses

Special Charges

Based on agreements reached with various workgroups in 2012, the Company expects to reduce a total of approximately 10,500 positions. Consequently, during 2012, the Company recorded charges for severance related costs associated with the voluntary and involuntary reductions in certain work groups. The severance charges will be paid through the end of 2013.

The following table summarizes the components of the Company’s special charges and the remaining accruals for these charges (in millions) as of March 31, 2013:

	Facility Exit Costs	Employee Charges	Total
Remaining accrual at December 31, 2012	$4	192	$196
Special charges	4	8	12
Non-cash charges	(4)	—	(4)
Adjustments	—	—	—
Payments	—	(61)	(61)
Remaining accrual at March 31, 2013	$4	$139	$143

Merger Related Expenses

Merger related expenses for the three months ended March 31, 2013 were $16 million. See Note 13 to the Condensed Consolidated Financial Statements for information on the Merger Agreement.

10. Financial Instruments and Risk Management

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As part of the Company's risk management program, it uses a variety of financial instruments, primarily heating oil, jet fuel, and Brent crude collars (consisting of a purchased call option and a sold put option) and call spreads (consisting of a purchased call option and a sold call option), as cash flow hedges to mitigate commodity price risk. The Company does not hold or issue derivative financial instruments for trading purposes. As of March 31, 2013, the Company had fuel derivative contracts outstanding covering 19 million barrels of jet fuel that will be settled over the next 18 months. A deterioration of the Company's liquidity position and its Chapter 11 filing may negatively affect the Company's ability to hedge fuel in the future.

For the three months ended March 31, 2013 and March 31, 2012, the Company recognized a decrease of approximately $8 million and $29 million, respectively, in fuel expense on the accompanying consolidated statements of operations related to its fuel hedging agreements, including the ineffective portion of the hedges. The net fair value of the Company's fuel hedging agreements at March 31, 2013 and December 31, 2012, representing the amount the Company would receive upon termination of the agreements (net of settled contract assets), totaled $61 million and $62 million, respectively. As of March 31, 2013, the Company estimates that during the next twelve months it will reclassify from Accumulated other comprehensive loss into earnings approximately $1 million in net gains.

The impact of cash flow hedges on the Company's Condensed Consolidated Financial Statements is depicted below (in millions):

Fair Value of Aircraft Fuel Derivative Instruments (all cash flow hedges)

Asset Derivatives as of				Liability Derivatives as of			
March 31, 2013		December 31, 2012		March 31, 2013		December 31, 2012	
Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Fuel derivative contracts	$66	Fuel derivative contracts	$65	Accrued liabilities	$—	Accrued liabilities	$—

Effect of Aircraft Fuel Derivative Instruments on Statements of Operations (all cash flow hedges)

Amount of Gain (Loss) Recognized in OCI on Derivative [1] for the quarter ended March 31		Location of Gain (Loss) Reclassified from Accumulated OCI into Income [1]	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income [1] for the quarter ended March 31,		Location of Gain (Loss) Recognized in Income on Derivative [2]	Amount of Gain (Loss) Recognized in Income on Derivative [2] for the quarter ended March 31,	
2013	2012		2013	2012		2013	2012
$(13)	$48	Aircraft Fuel	$1	$26	Aircraft Fuel	$7	$3

1. Effective portion of gain (loss)
2. Ineffective portion of gain (loss)

The Company is party to certain interest rate swap agreements that are accounted for as cash flow hedges. Ineffectiveness for these instruments is required to be measured at each reporting period. The ineffectiveness and fair value associated with all of the Company's interest rate cash flow hedges for all periods presented was not material.

While certain of the Company's fuel derivatives are subject to enforceable master netting agreements with its counterparties, the Company does not offset its fuel derivative assets and liabilities in its Condensed Consolidated Balance Sheets. Certain of these agreements would also allow for the offsetting of fuel derivatives with interest rate derivatives. The impact of offsetting derivative instruments is depicted below (in millions):

As of March 31, 2013:

			Gross asset (liability) not offset in Balance Sheet		
Gross asset (liability)	Gross asset (liability)	Net recognized asset (liability) in Balance	Financial Instruments	Cash Collateral Received	Net Amount

		offset in Balance Sheet	Sheet			(Posted)	
Fuel derivatives	$						
Net sales	$	252,180	100.0%	$223,993	100.0%	$215,451	100.0%
Gross profit		83,388	33.1 %	74,347	33.2 %	70,812	32.9 %
SG&A		67,770	26.9 %	60,227	26.9 %	59,929	27.8 %
Income from operations	$	15,618	6.2 %	$14,120	6.3 %	$10,883	5.1 %

Wholesale shipments by category for the last three fiscal years are summarized below:

	2015		**2014**		**2013**	
Wood	$93,073	36.9%	$86,577	38.7%	$87,935	40.8%
Upholstery	156,768	62.2%	135,831	60.6%	125,403	58.2%
Other	2,339	0.9 %	1,585	0.7 %	2,113	1.0 %

)

Reclassifications out of accumulated other comprehensive income (loss) for the three months ended March 31, 2013 are as follows (in millions):

Details about accumulated other comprehensive income (loss) components	Amount reclassified from accumulated other comprehensive income (loss)		Affected line item in the statement where net income (loss) is presented
Amortization of pension and retiree medical liability			
Prior service cost	$(54	)	[1]
Actuarial loss	21		[1]
Derivative financial instruments			
Cash flow hedges	(1	)	Aircraft fuel
Total reclassifications for the period	$(34	)	

[1]These accumulated other comprehensive income components are included in the computation of net periodic pension and retiree medical costs. See Note 8 to the Condensed Consolidated Financial Statements for additional details.

12. Merger Agreement

Description of Agreement and Plan of Merger

On February 13, 2013, AMR, US Airways Group, Inc., a Delaware corporation (US Airways Group), and AMR Merger Sub, Inc., a Delaware corporation and wholly owned subsidiary of AMR (Merger Sub), entered into an Agreement and Plan of Merger (the Merger Agreement), providing for a business combination of AMR and US Airways Group. The Merger Agreement provides that, upon the terms and subject to the conditions set forth in the Merger Agreement, Merger Sub will merge with and into US Airways Group (the Merger), with US Airways Group surviving as a wholly owned subsidiary of AMR. AMR and US Airways Group anticipate that immediately following the merger closing, AMR will change its name to American Airlines Group Inc. (AAG). Following the Merger, AAG will own, directly or indirectly, all of the equity interests of American, US Airways Group and their direct and indirect subsidiaries. The Merger Agreement and the transactions contemplated thereby, including the Merger, are subject to the approval of the Bankruptcy Court, and are to be effected pursuant to a plan of reorganization (the Plan) of the

Debtors in connection with the Chapter 11 Cases. The Plan was filed on April 15, 2013, and is subject to confirmation and consummation in accordance with the requirements of the Bankruptcy Code.

Subject to the terms and conditions of the Merger Agreement, which has been approved by the boards of directors of the respective parties, upon completion of the Merger, US Airways Group stockholders will receive one share of common stock of AAG (AAG Common Stock) for each share of US Airways Group common stock. The aggregate number of shares of AAG Common Stock issuable to holders of US Airways Group equity instruments (including stockholders and holders of convertible notes, options, stock appreciation rights and restricted stock units) will represent 28% of the diluted capitalization of AAG after giving effect to

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the Plan. The remaining 72% diluted equity ownership of AAG will be distributable, pursuant to the Plan, to the Debtors' stakeholders, labor unions and certain employees.

All of the equity interests in AAG will be issued solely pursuant to the Merger Agreement or the Plan. Pursuant to the proposed Plan filed with the Bankruptcy Court on April 15, 2013, holders of AMR equity interests are expected to receive a recovery on such interests in the form of a distribution of AAG common stock. Implementation of the Plan and the making of any distributions thereunder are subject to confirmation thereof in accordance with the provisions of the Bankruptcy Code, the occurrence of the effective date under the Plan and the consummation of the Merger.

The Merger is intended to qualify, for federal income tax purposes, as a reorganization under the provisions of Section 368(a) of the Internal Revenue Code of 1986, as amended.

The Merger Agreement provides that, upon consummation of the Merger, the board of directors of the combined company will initially consist of 12 members, composed of (i) Thomas W. Horton, AMR's current chairman, chief executive officer and president, who will serve as chairman of AAG until the earlier of (A) one year after the closing of the Merger and (B) the day immediately prior to the first annual meeting of stockholders of the combined company (provided that such meeting will not occur prior to May 1, 2014), (ii) W. Douglas Parker, US Airways Group current chief executive officer, who will serve as chief executive officer of AAG and will serve as chairman of AAG following the end of Mr. Horton's term, (iii) two independent directors designated by AMR, (iv) three independent directors designated by US Airways Group, and (iv) five independent directors designated by a search committee consisting of representatives of the Creditors' Committee and certain representatives of creditors signatory to the support agreement with AMR referred to below. One of such independent directors will serve as lead independent director. Subject to applicable law, prior to the Merger, senior executives from each of AMR and US Airways Group will engage in a planning process for integration purposes.

AMR and US Airways Group have each made customary representations, warranties and covenants in the Merger Agreement, including, among others, covenants to conduct their businesses in the ordinary and usual course between the execution of the Merger Agreement and the consummation of the Merger, subject to certain restrictions as set forth in the Merger Agreement. In addition, the Merger Agreement contains “no shop” provisions that restrict each party's ability to initiate, solicit or knowingly encourage or facilitate competing third-party proposals for any transaction involving a merger of such party or the acquisition of a significant portion of its stock or assets, although each party may consider competing, unsolicited proposals and enter into discussions or negotiations regarding such proposals, if its board of directors determines that any such acquisition proposal constitutes, or is reasonably likely to lead to, a superior proposal and that the failure to take such action is reasonably likely to be inconsistent with its fiduciary duties under applicable law.

US Airways Group has agreed to certain additional customary covenants in the Merger Agreement, including, among others, subject to certain exceptions, (i) to cause a stockholder meeting to be held to consider adoption of the Merger Agreement and (ii) for its board of directors to recommend adoption of the Merger Agreement by US Airways Group stockholders. AMR has also agreed to certain additional customary covenants in the Merger Agreement, including, among others, subject to certain exceptions, (i) to pursue confirmation of the Plan and (ii) for its board of directors to recommend adoption of the Merger Agreement by the Debtors' stakeholders.

Consummation of the Merger is subject to customary conditions, including, among others: (i) approval by the stockholders of US Airways Group; (ii) expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 and the receipt of certain other regulatory approvals; (iii) absence of any order or injunction prohibiting the consummation of the Merger; (iv) Bankruptcy Court confirmation of the Plan, which must contain certain specified provisions defined in the Merger Agreement; (v) subject to certain exceptions, the accuracy of representations and warranties with respect to the business of AMR or US Airways Group, as applicable; (vi) each of AMR and US Airways Group having performed their respective obligations pursuant to the Merger Agreement; and (vii) receipt by each of the Company and US Airways Group of a customary tax opinion.

The Merger Agreement contains certain termination rights for AMR and US Airways Group, and further provides that, upon termination of the Merger Agreement under specified circumstances, (i) AMR may be required to pay US Airways Group a termination fee of $135 million in the event it terminates the agreement to enter into a superior proposal and $195 million if US Airways Group terminates the Merger Agreement in the event of a knowing and deliberate breach of the Merger Agreement by AMR and (ii) US Airways Group may be required to pay AMR a termination fee of $55 million in the event it terminates the agreement to enter into a superior proposal and $195 million if AMR terminates the Merger Agreement in the event of a knowing and deliberate breach of the Merger Agreement by US Airways Group.

On February 22, 2013, the Debtors filed a motion for entry of the Merger Support Order, which is defined as an order of the Bankruptcy Court approving the Merger Agreement and certain related matters contemplated thereby in the form required by the Merger Agreement. The Bankruptcy Court conducted a hearing on the Debtors' motion on March 27, 2013. As of April 16, 2013,

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the Bankruptcy Court has not entered the Merger Support Order in the form required by the Merger Agreement. If the Merger Support Order is not entered on or before May 14, 2013, the Merger Agreement may be terminated in accordance with its termination provisions. Unless and until the Merger Support Order is entered, the Merger Agreement is not binding on or enforceable against AMR, US Airways Group or AMR Merger Sub. Based on the Bankruptcy Court hearing on March 27, 2013 to consider the Merger Support Motion and any related objections and the memorandum of decision issued by the Bankruptcy Court on April 11, 2013, AMR and US Airways Group anticipate that the Bankruptcy Court will enter an order that fails to meet all of the requirements of the Merger Agreement. AMR and US Airways Group are discussing how to address this anticipated issue.

Support Agreement and Term Sheet

On February 13, 2013, AMR and the other Debtors entered into a Support and Settlement Agreement (the Support Agreement) with certain significant holders of certain prepetition claims against one or more of the Debtors (such holders of claims, the Consenting Creditors), aggregating approximately $1.2 billion of prepetition unsecured claims. Pursuant to the terms of the Support Agreement, each Consenting Creditor has agreed, among other things, and subject to certain conditions, to (a) vote in favor of a Plan, which must include certain terms specified in a Term Sheet attached to the Support Agreement (the Term Sheet), (b) generally support confirmation and consummation of the Plan and (c) not to support or solicit any plan in opposition to the Plan. Confirmation and consummation of the Plan are subject to compliance with the provisions of the Bankruptcy Code and to the closing of the Merger.

The Support Agreement may be terminated upon the occurrence of certain events, including: (a) certain breaches by the Debtors or Consenting Creditors under the Support Agreement; (b) termination of the Merger Agreement or the announcement by AMR or US Airways Group of their intent to terminate the Merger Agreement (in which case the Support Agreement would terminate automatically); (c) the failure to meet certain milestones with respect to achieving confirmation and consummation of the Plan; (d) the filing, amendment or modification of certain documents, including the Plan, in a manner materially inconsistent with the Support Agreement and materially adverse to a Consenting Creditor (in which case the Support Agreement can be terminated by such Consenting Creditor solely with respect to itself); (e) the amendment or modification of the Merger Agreement in a manner that is materially adverse to a Consenting Creditor (in which case the Support Agreement can be terminated by such Consenting Creditor solely with respect to itself); and (f) if the volume weighted average price of US Airways Group common stock for the thirty trading days ending on the last trading day immediately prior to the date of termination is less than $10.40. Termination of the Support Agreement would give the Consenting Creditors the right to withdraw their support of the Plan.

As described in the Term Sheet, the Plan implements the Merger, incorporates a compromise and settlement of certain intercreditor and intercompany claim issues, and is to contain the following provisions relating to the treatment of prepetition unsecured claims against the Debtors and equity interests in AMR:

- Unless they elect to receive alternative treatment, holders of prepetition unsecured claims against AMR or American that also are guaranteed by either such company (Double-Dip Unsecured Claims) will receive shares of preferred stock of AAG (the AAG Preferred Stock) that will be mandatorily convertible into shares of AAG Common Stock on each of the 30th, 60th, 90th and 120th day after the effective date of the Plan. Upon the conversion of the remaining AAG Preferred Stock on the 120th day after the effective date of the Plan, all AAG Preferred Stock will have been converted to AAG Common Stock and no AAG Preferred Stock will remain outstanding. The conversion price of the AAG Preferred Stock will vary on each conversion date, based on the volume weighted average price of the shares of the AAG Common Stock on the five trading days immediately preceding each conversion date, at a 3.5% discount, subject to a cap and a floor price. The AAG Preferred Stock allocable to the Double-Dip Unsecured Claims will have a face amount equal to the allowed amount of their claims, including post-petition interest at the non-default rate;
- Holders of prepetition unsecured claims (other than claims of the Debtors' unions) that are not Double-Dip Unsecured Claims (and holders of Double-Dip Unsecured Claims that elect to receive such treatment) will receive shares of AAG Preferred Stock, as well as shares of AAG Common Stock;
- Holders of existing AMR equity interests (including stock, warrants, restricted stock units and options) will receive a distribution of shares of AAG Common Stock representing 3.5% of the total number of shares of AAG Common Stock (on an as-converted basis) in addition to the potential to receive shares of AAG Common Stock above such

amount; and

- The satisfaction of certain labor-related claims through the allocation to such claims of shares of AAG Common Stock representing 23.6% of the total number of such shares of AAG Common Stock ultimately distributed to holders of prepetition general unsecured claims against the Debtors.

In each case, the distributions made to each of the foregoing stakeholders will be adjusted to take into account any reserves made for disputed claims under the Plan. The Debtors have filed a motion with the Bankruptcy Court seeking approval of the Support Agreement.

13. Subsequent Events

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Filing of Plan of Reorganization, Disclosure Statement and Form S-4

On April 15, 2013, the Company and other Debtors filed with the Bankruptcy Court the Plan of Reorganization (the Plan) and a related Disclosure Statement (the Disclosure Statement), which contemplate that AMR will emerge from Chapter 11 and merge with US Airways Group (as further described in Note 12 to the Condensed Consolidated Financial Statements). The Plan addresses various subjects with respect to the Debtors, including the resolution of pre-petition obligations as well as the capital structure and corporate governance after exit from the Chapter 11 Cases. The Plan further provides that, upon the effectiveness of the Plan and the Merger, which are anticipated to occur contemporaneously, all shares of existing AMR common stock and other equity interests in AMR will be cancelled and any rights with respect thereto will cease to exist.

Generally, for purposes of the Plan, all 20 Debtors will be "substantively consolidated" into three nodes, consisting of: (i) AMR Debtors, (ii) American Debtors, and (iii) Eagle Debtors. As among the AMR Debtors, the American Debtors, and the Eagle Debtors, the Plan will separately classify creditor claims. However, pursuant to the compromises incorporated into the Plan relating to certain inter-creditor issues and the treatment of intercompany claims among the Debtors, general unsecured claims of similar rank and priority will be treated the same under the Plan regardless of the Debtor against which such claim was filed.

The Plan contains provisions related to the treatment of prepetition unsecured claims against the Debtors and equity interests in AMR as described in Note 13 to the Condensed Consolidated Financial Statements under "Support Agreement and Term Sheet."

On April 15, 2013, the Company also filed a Form S-4 registration statement with the Securities and Exchange Commission (the SEC) to register the shares of AAG Common Stock that will be issued to stockholders of US Airways Group as consideration in the Merger in exchange for their US Airways Group common stock. The AAG Common Stock cannot be issued to US Airways Group stockholders until the SEC declares the registration statement to be effective.

The Company and other Debtors have until July 29, 2013 to solicit and obtain acceptances for the Plan. To be accepted by holders of claims against the Debtors, the Plan must be approved by at least one-half in number and two-thirds in dollar amount of claims actually voting in each impaired class. Under certain circumstances set forth in Section 1129(b) of the Bankruptcy Code, the Bankruptcy Court may confirm a plan even if such plan has not been accepted by all impaired classes of claims and equity interests. A class of claims or equity interests that does not receive or retain any property under the plan on account of such claims or interests is deemed to have voted to reject the plan. The precise requirements and evidentiary showing for confirming a plan notwithstanding its rejection by one or more impaired classes of claims or equity interests depends upon a number of factors, including the status and seniority of the claims or equity interests in the rejecting class (i.e., secured claims or unsecured claims, subordinated or senior claims, preferred or common stock).

The information contained in the Disclosure Statement is subject to change, whether as a result of amendments to the Plan of Reorganization, actions of third parties or otherwise.

Nothing contained in this Form 10-Q is intended to be, nor should it be construed as, a solicitation for a vote on the Plan. The Plan will become effective only if it receives the requisite approval and is confirmed by the Bankruptcy Court. There can be no assurance that the Bankruptcy Court will confirm the Plan of Reorganization or that any such plan will be implemented successfully.

Other

On April 3, 2013, the Bankruptcy Court entered an order approving a stipulation providing that, among other things, (i) the 1990 and 1994 series of special facility revenue bonds that financed certain improvements at John F. Kennedy International Airport (JFK) will be treated as general unsecured claims, (ii) the Debtors may continue to use any premises and improvements at JFK or LaGuardia Airport financed by the 1990 or 1994 series of special facility revenue bonds, (iii) the Debtors will assume the leases at JFK that currently relate to the 2002 and 2005 series of special facility revenue bonds, and (iv) the Debtors' use of premises at JFK will continue to be governed by those leases as well as any other leases that may apply (including leases with the Port Authority of New York and New Jersey). As a result, the Company expects a claim of $171 million, of which $124 million has been previously accrued, plus post-petition interest.

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

First Quarter Developments

In the first quarter of 2013, the Company continued its transformation and built on the substantial progress made in 2012 in restoring the Company to industry leadership, profitability and growth. The Company also announced the AMR Merger Agreement with US Airways Group on February 14, 2013 and filed its Plan of Reorganization (the Plan) with the Bankruptcy Court on April 15, 2013.

On February 13, 2013, AMR, US Airways Group, and AMR Merger Sub, Inc. entered into an Agreement and Plan of Merger providing for a business combination of AMR and US Airways Group. The Merger Agreement provides that, upon the terms and subject to the conditions set forth in the Merger Agreement, AMR Merger Sub, Inc., a wholly-owned subsidiary of AMR, will merge with and into US Airways Group, with US Airways Group surviving as a wholly-owned subsidiary of AMR. In the event that the Merger Agreement is terminated for any reason, the Chapter 11 Cases will continue and AMR will prepare and propose an alternative plan of reorganization which could contemplate, among other things, consolidation with another entity, the sale or disposition of certain of AMR's assets, or AMR's emergence as a standalone entity. If AMR were to emerge on an independent basis, AMR believes that it should be able to achieve its targeted cost savings of approximately $2 billion each year and its targeted annual revenue enhancements of $1 billion by 2017, although there can be no assurance that it would be able to do so. See Note 12 to the Condensed Consolidated Financial Statements for information on the Merger Agreement.
The Plan and related Disclosure Statement contemplate that AMR will emerge from Chapter 11 and merge with US Airways Group. The Plan addresses various subjects with respect to the Debtors, including the resolution of pre-petition obligations as well as the capital structure and corporate governance after exit from the Chapter 11 Cases. See Note 13 to the Condensed Consolidated Financial Statements for information on the Plan and Disclosure Statement.
Other first quarter highlights include the following:

•	American closed its private offering of the Series 2013-1 EETCs in the aggregate face amount of $664 million. See Note 6 to the Co7 style="FONT-SIZE: 10pt; FONT-FAMILY: Times New Roman, Times, serif; WIDTH: 7%; VERTICAL-ALIGN: bottom; BORDER-BOTTOM: #000000 1px solid; TEXT-ALIGN: right; BACKGROUND-COLOR: #ffffff">0.6	%	671	0.3%					
Income (loss) from operations		$ 6,170	2.5%	$ (528)	-0.2%	$(528)	-0.2%	$(1,452)	-0.7%

The following tables present operating results on a comparable store basis for each comparative set of periods. Table A compares the results of the 53 stores that were open and operating for all of 2015 and 2014. Table B compares the results of the 51 stores that were open and operating for all of 2014 and 2013.

Comparable Store Results:

	Table A: 2015 vs 2014 (53 Stores)				Table B: 2014 vs 2013 (51 Stores)			
	2015		2014		2014		2013	
Net sales	$225,444	100.0%	$199,048	100.0%	$194,092	100.0%	$187,146	100.0%
Gross profit	112,815	50.0 %	99,591	50.0 %	96,905	49.9 %	90,626	48.4 %
SG&A expense	105,347	46.7 %	97,325	48.9 %	94,726	48.8 %	90,389	48.3 %
Income (loss) from operations	$7,468	3.3 %	$2,266	1.1 %	$2,179	1.1 %	$237	0.1 %

The following tables present operating results for all other stores which were not comparable year-over-year. Each table includes the results of stores that either opened or closed at some point during the 24 months of each comparative set of periods.

All Other (Non-Comparable) Store Results:

	2015 vs 2014 All Other Stores						2014 vs 2013 All Other Stores			
	2015			2014			2014		2013	
Net sales	$	23,935	100.0%	$	17,583	100.0%	$22,539	100.0%	$12,234	100.0%
Gross profit		12,188	50.9 %		8,866	50.4 %	11,552	51.3 %	5,843	47.8 %
SG&A expense		12,863	53.7 %		10,443	59.4 %	13,042	57.9 %	6,861	56.1 %
New store pre-opening costs		623	2.6	(15	)	(5.8)				
Commissions, booking fees and credit card expense	276	10	3.7 %							
Aircraft rentals	164	21	14.8	(c)						
Food service	139	15	11.6 %	(d)						
Special charges and merger related	28	17	*	(e)						
Other operating expenses	750	88	13.3	(f)						
Total operating expenses	$6,038	$(94)	(1.5)%							

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(a) Wages, salaries and benefits decreased primarily as a result of modifications to pension and other post-employment benefits and reductions in certain work groups during 2012. See Note 8 and Note 9 to the Condensed Consolidated Financial Statements for further information, respectively.
(b) Maintenance, materials and repairs increased primarily due to timing of materials and repairs expenses.
(c) Aircraft rental expense increased primarily due to new aircraft deliveries in 2013.
(d) Food service increased primarily as a result of increased passengers boarded and enhanced product offerings.
(e) Special charges increased primarily as a result of merger related expenses.
(f) Other operating expenses increased primarily due to increases in outsourced services and volatility in foreign exchange rates.

OTHER INCOME (EXPENSE)

Other income (expense) consists of interest income and expense, interest capitalized and miscellaneous—net.

A decrease in short-term investment rates caused a decrease in interest income of $1.6 million, or 28.1 percent, to $4 million for the first quarter 2013 compared to the same period last year. Interest expense increased $4 million, or 2.6 percent, to $174 million primarily as a result of post-petition interest expense on unsecured obligations that the debtors agreed to allow pursuant to the Support Agreement, partially offset by a decrease in interest expense as a result of the Company's restructuring efforts under the Chapter 11 Cases as described in Note 1 to the Condensed Consolidated Financial Statements.

REORGANIZATION ITEMS, NET

Reorganization items refer to revenues, expenses (including professional fees), realized gains and losses and provisions for losses that are realized or incurred as a direct result of the Chapter 11 Cases. The following table summarizes the components included in reorganization items, net on the Consolidated Statements of Operations for the three months ended March 31, 2013 and March 31, 2012:

(in millions)

	Three Months Ended March 31,	
	2013	2012
Pension and postretirement benefits	$—	$—
Aircraft and facility financing renegotiations and rejections (1)(2)(3)	136	1,357
Professional fees	39	45
Other	(15)	—
Total reorganization items, net	$160	$1,402

(1) Amounts include allowed claims (claims approved by the Bankruptcy Court) and estimated allowed claims relating to the rejection or modification of financings related to aircraft. The Debtors record an estimated claim associated with the rejection or modification of a financing when the applicable motion is filed with the Bankruptcy Court to reject or modify such financing and the Debtors believe that it is probable the motion will be approved, and there is sufficient information to estimate the claim. Modifications of the financings related to certain aircraft remain subject to conditions, including reaching agreement on definitive documentation. See above, "Special Protection Applicable to Leases and Secured Financing of Aircraft and Aircraft Equipment," for further information.

(2) Amounts include allowed claims (claims approved by the Bankruptcy Court) and estimated allowed claims relating to entry of orders treating as unsecured claims with respect to facility agreements supporting certain issuances of special facility revenue bonds. The Debtors record an estimated claim associated with the treatment of claims with respect to facility agreements when the applicable motion is filed with the Bankruptcy Court and the Debtors believe that it is probable that the motion will be approved, and there is sufficient information to estimate the claim. See above, "Rejection of Executory Contracts," for further information.

(3) Pursuant to the Support Agreement, as defined and further described in Note 13 to the Condensed Consolidated Financial Statements, the Debtors agreed to allow certain post-petition unsecured claims on obligations. As a

result, the Company recorded reorganization charges to adjust estimated allowed claim amounts previously recorded on rejected special facility revenue bonds of $127 million, which is included in the table above.

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Claims related to reorganization items are reflected in liabilities subject to compromise on the Condensed Consolidated Balance Sheet as of March 31, 2013.

INCOME TAX

The Company recorded a net tax (benefit) of approximately $(30) million associated with its net loss for the three months ended March 31, 2013 due to the Company realizing a valuation allowance release for refundable credits allowed as a result of passage of the American Taxpayer Relief Act of 2012. See Note 5 to the Condensed Consolidated Financial Statements. The Company did not record a net tax provision (benefit) associated with its net loss for the three months ended March 31, 2012 due to the Company providing a valuation allowance, as discussed in Note 5 to the Condensed Consolidated Financial Statements.

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OPERATING STATISTICS

The following table provides statistical information for American and Regional Affiliates for the three months ended March 31, 2013 and 2012.

	Three Months Ended March 31, 2013		2012	
American Airlines, Inc. Mainline Jet Operations				
Revenue passenger miles (millions)	30,139		29,960	
Available seat miles (millions)	37,392		37,918	
Cargo ton miles (millions)	410		445	
Passenger load factor	80.6	%	79.0	%
Passenger revenue yield per passenger mile (cents)	15.31		15.21	
Passenger revenue per available seat mile (cents)	12.34		12.02	
Cargo revenue yield per ton mile (cents)	37.72		37.80	
Operating expenses per available seat mile, excluding Regional Affiliates (cents) (*)	14.13		14.22	
Fuel consumption (gallons, in millions)	592		592	
Fuel price per gallon (dollars)	3.27		3.23	
Operating aircraft at period-end	621		610	
Regional Affiliates				
Revenue passenger miles (millions)	2,393		2,370	
Available seat miles (millions)	3,319		3,333	
Passenger load factor	72.1	%	71.1	%

(*)Excludes $754 million and $742 million of expense incurred related to Regional Affiliates in 2013 and 2012, respectively.

Operating aircraft at March 31, 2013, included:

American Airlines Aircraft		AMR Eagle Aircraft	
Boeing 737-800	204	Bombardier CRJ-700	47
Boeing 757-200	106	Embraer RJ-135	19
Boeing 767-200 ER	14	Embraer RJ-140	59
Boeing 767-300 ER	58	Embraer RJ-145	118
Boeing 777-200 ER	47	Super ATR	6
Boeing 777-300 ER	5	Total	249
McDonnell Douglas MD-80	187		
Total	621		

The average aircraft age for American's and AMR Eagle's aircraft is 14.7 years and 10.4 years, respectively.

Almost all of the Company's owned aircraft are encumbered by liens granted in connection with financing transactions entered into by the Company.

Of the operating aircraft listed above, five Boeing 757-200 aircraft, two McDonnell Douglas MD-80 aircraft, and two Boeing 767-200 Extended Range aircraft were in temporary storage as of March 31, 2013.

Owned and leased aircraft not operated by the Company at March 31, 2013, included:

American Airlines Aircraft		AMR Eagle Aircraft	
Boeing 737-800	1	Saab 340B	41
Boeing 757-200	2	Total	41
McDonnell Douglas MD-80	36		
Total	39		

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The following table summarizes the aircraft contractually obligated to American under capacity purchase agreements with third party regional airlines at March 31, 2013:

	Fleet Type		
Carrier	Bombardier CRJ-200	Embraer RJ-140	Total
Republic			—
SkyWest	12	—	12
ExpressJet	11	—	11
Chautauqua	—	15	15
Total	23	15	38

Of the aircraft listed above, one SkyWest CRJ RJ-200 aircraft was on operational reserve as of March 31, 2013.
See Note 3 to the Condensed Consolidated Financial Statements for additional information on the Company's capacity purchase agreements with third party regional airlines.

All aircraft, excluding the SAAB 340B aircraft and aircraft operated by third party regional airlines, are owned or leased by American as as of March 31, 2013.

See Note 1 to the Condensed Consolidated Financial Statements for information on the Company's activities under section 1110 of the Bankruptcy Code. See Note 3 to the Condensed Consolidated Financial Statements for information on the Company's acquisition commitments, payments and options.

REGIONAL AFFILIATES

The following table summarizes the combined capacity purchase activity for Regional Affiliates for the three months ended March 31, 2013 and 2012 (in millions):

	Three Months Ended March 31,	
	2013	2012
Revenues:		
Regional Affiliates	679	670
Other	40	40
	719	710
Expenses:		
Regional payments	303	311
Other incurred expenses	451	431
	754	742

In addition, passengers connecting to American's flights from Regional Affiliates' flights generated passenger revenues for American flights of $433 million and $427 million in the three months ended March 31, 2013 and 2012, respectively, which are included in Revenues - Passenger in the consolidated statements of operations.

Critical Accounting Policies and Estimates

The preparation of the Company’s financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. The Company believes its estimates and assumptions are reasonable; however, actual results and the timing of the recognition of such amounts could differ from those estimates. The Company has identified the following critical accounting policies and estimates used by management in the preparation of the Company’s financial statements: claims resolution process, long-lived assets, international slots and route authorities, passenger revenue, frequent flyer program, stock compensation, pensions and retiree medical and other benefits, income taxes and derivatives accounting. These policies and estimates are described in the 2012 Form 10-K.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

There have been no material changes in market risk from the information provided in Item 7A. Quantitative and Qualitative Disclosures About Market Risk of the Company's 2012 Form 10-K. The change in market risk for aircraft fuel is discussed below for informational purposes.

The risk inherent in the Company's market risk sensitive instruments and positions is the potential loss arising from adverse changes in the price of fuel, foreign currency exchange rates and interest rates as discussed below. The sensitivity analyses presented do not consider the effects that such adverse changes may have on overall economic activity, nor do they consider additional actions management may take to mitigate the Company's exposure to such changes. Therefore, actual results may differ. The Company does not hold or issue derivative financial instruments for trading purposes. See Note 10 to the Condensed Consolidated Financial Statements for further information.

Aircraft Fuel The Company's earnings are substantially affected by changes in the price and availability of aircraft fuel. In order to provide a measure of control over price and supply, the Company trades and ships fuel and maintains fuel storage facilities to support its flight operations. The Company also manages the price risk of fuel costs through the use of hedging contracts, which consist primarily of collars (consisting of a purchased call option and a sold put option) and call spreads (consisting of a purchased call option and a sold call option). Heating oil, jet fuel and crude oil are the primary underlying commodities in the hedge portfolio. Market risk is estimated as a hypothetical 10 percent increase in the March 31, 2013 and 2012 cost per gallon of fuel. Based on projected fuel usage for the next twelve months, such an increase would result in an increase to Aircraft fuel expense of approximately $582 million, inclusive of the impact of effective fuel hedge instruments outstanding at March 31, 2013, and assumes the Company's fuel hedging program remains effective. Such an increase would have resulted in an increase to projected Aircraft fuel expense of approximately $658 million in the twelve months ended December 31, 2012, inclusive of the impact of fuel hedge instruments outstanding at December 31, 2011.

As of March 31, 2013, the Company had cash flow hedges covering approximately 28 percent of its estimated remaining 2013 fuel requirements. Comparatively, as of March 31, 2012, the Company had hedged approximately 32 percent of its estimated remaining 2012 fuel requirements. The consumption hedged for the remainder of 2013 is capped at an average price of approximately $2.98 per gallon of jet fuel. Seven percent of estimated remaining 2013 fuel requirements is hedged using call spreads with protection capped at an average price of approximately $3.28 per gallon of jet fuel. Twenty-one percent of estimated remaining 2013 fuel requirements is hedged using collars with an average floor price of approximately $2.49 per gallon of jet fuel. The capped and floor prices exclude taxes and transportation costs. A deterioration of the Company's financial position could negatively affect the Company's ability to hedge fuel in the future.

Ineffectiveness is inherent in hedging jet fuel with derivative positions based in crude oil or other crude oil related commodities. The Company assesses, both at the inception of each hedge and on an ongoing basis, whether the derivatives that are used in its hedging transactions are highly effective in offsetting changes in cash flows of the hedged items. In doing so, the Company uses a regression model to determine the correlation of the change in prices of the commodities used to hedge jet fuel (e.g., NYMEX Heating oil) to the change in the price of jet fuel. The Company also monitors the actual dollar offset of the hedges' market values as compared to hypothetical jet fuel hedges. The fuel hedge contracts are generally deemed to be "highly effective" if the R-squared is greater than 80 percent and the dollar offset correlation is within 80 percent to 125 percent. The Company discontinues hedge accounting prospectively if it determines that a derivative is no longer expected to be highly effective as a hedge or if it decides to discontinue the hedging relationship.

Item 4. Controls and Procedures

The term "disclosure controls and procedures" is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the Exchange Act). This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission. An evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of the effectiveness of the Company's disclosure controls and procedures as of December 31, 2012. Based on that evaluation, the Company's management, including the CEO and CFO, concluded that the Company’s disclosure controls and procedures were effective as of March 31, 2013. During the quarter ending on March 31, 2013, there was no change in the Company’s internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

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PART II: OTHER INFORMATION
Item 1. Legal Proceedings
As previously discussed, on November 29, 2011 the Debtors filed voluntary petitions for relief under the Bankruptcy Code. Each of the Debtors continues to operate its business and manage its property as a debtor in possession pursuant to sections 1107 and 1108 of the Bankruptcy Code. As a result of the current Chapter 11 Cases, attempts to prosecute, collect, secure or enforce remedies with respect to pre-petition claims against the Debtors are subject to the automatic stay provisions of section 362(a) of the Bankruptcy Code, including, except in such cases where the Bankruptcy Court has entered an order modifying or lifting the automatic stay, the litigation described below. Notwithstanding the general application of the automatic stay described above, governmental authorities, both domestic and foreign, may determine to continue actions brought under their regulatory powers. Therefore, the automatic stay may have no effect on certain matters described below.
On February 22, 2006, the Company received a letter from the Swiss Competition Commission informing the Company that it is investigating whether the Company and certain other cargo carriers entered into agreements relating to fuel surcharges, security surcharges, war-risk surcharges, and customs clearance surcharges. On March 11, 2008, the Company received a request for information from the Swiss Competition Commission concerning, among other things, the scope and organization of the Company's activities in Switzerland. On November 8, 2012, the Swiss Competition Commission issued a preliminary order finding that the Company participated in an illegal conspiracy to set cargo fuel, security, and war risk surcharges, and recommending that the Company should be fined 2,225,310 Swiss Francs. The Company disputes the allegation in the Swiss order and intends to vigorously defend itself under Swiss law. On January 23, 2007, the Brazilian competition authorities, as part of an ongoing investigation, conducted an unannounced search of the Company's cargo facilities in Sao Paulo, Brazil. On April 24, 2008, the Brazilian competition authorities charged the Company with violating Brazilian competition laws. On December 31, 2009, the Brazilian competition authorities made a non-binding recommendation to the Brazilian competition tribunal that it find the Company in violation of competition laws and levy a fine in an unspecified amount. The Brazilian authorities are investigating whether the Company and certain other foreign and domestic airlines violated Brazilian competition laws by illegally conspiring to set fuel surcharges on cargo shipments. The Company is vigorously contesting the allegations and the preliminary findings of the Brazilian competition authorities. The Company intends to cooperate fully with all pending investigations.
In addition, the Company has received inquiries from a number of other jurisdictions, including Australia and South Korea, regarding the Company's practices relating to setting fuel charges. The Company has timely responded to all such inquiries.
On April 12, 2011, American filed an antitrust lawsuit against Travelport and Orbitz in Federal District Court for the Northern District of Texas. On October 20, 2011, American sought leave to file new antitrust claims against the defendants based on facts learned through discovery. The lawsuit, as amended, alleged, among other things, that (i) the defendants engaged in anticompetitive practices to preserve their monopoly power over American's ability to distribute its products through their subscribers and (ii) such actions have prevented American from employing new competing technologies and allowed the defendants to continue to charge American supracompetitive fees.
On December 22, 2011, Travelport brought counterclaims against American alleging that American's direct connect efforts violate the antitrust laws. On August 16, 2012, the federal district court dismissed Travelport's counterclaims. On February 5, 2013, Travelport filed a motion for reconsideration of the federal district court's August 16, 2012 order dismissing its counterclaims and to amend its counterclaims to assert a new claim against American. The proposed new counterclaim alleged that American participated in a conspiracy with rival airlines and Farelogix, Inc., a technology provider to American, to reduce and eliminate competition from Travelport and other GDSs and to coordinate their negotiations with Travelport and other GDSs.
American settled its disputes with Travelport and Orbitz on March 12, 2013 and March 29, 2013, respectively, subject to approval of the Bankruptcy Court. Under the terms of the settlement between American and Travelport, (i) the parties amended their current distribution and content agreements and extended such agreements for multiple years, (ii) Travelport agreed to provide certain monetary payments to American, and (iii) the parties released one another from any and all claims asserted, or that could have been asserted, in connection with the lawsuit. Under the terms of

the settlement between American and Orbitz, the parties released one another from any and all claims asserted, or that could have been asserted, in connection with the lawsuit. The Bankruptcy Court is scheduled to consider the settlement on April 23 2013.

The Company is engaged in other legal proceedings from time to time. Legal proceedings can be complex and take many months, or even years, to reach resolution, with the final outcome depending on a number of variables, some of which are not within the control of the Company. Therefore, although the Company will vigorously defend itself in each of the actions described above and such other legal proceedings, the ultimate resolution and potential financial impact on the Company is uncertain.

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Item 6. Exhibits

Exhibits required to be filed by Item 601 of Regulation S-K. Where the amount of securities authorized to be issued under any of American's long-term debt agreements does not exceed 10 percent of American's assets, pursuant to paragraph (b) (4) of Item 601 of Regulation S-K, in lieu of filing such as an exhibit, American hereby agrees to furnish to the Commission upon request a copy of any agreement with respect to such long-term debt.

The following exhibits are included herein:

10.1	2012 Omnibus Restructure Agreement by and between American Airlines, Inc. and The Boeing Company dated as of January 11, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities Exchange Act of 1934, as amended.
10.2	Supplemental Agreement No. 3 to Purchase Agreement No. 3219 by and between American Airlines, Inc., and The Boeing Company dated as of February 1, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities Exchange Act of 1934, as amended.
10.3	Supplemental Agreement No. 36 to Purchase Agreement No. 1977 by and between American Airlines, Inc., and the Boeing Company dated as of February 1, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities Exchange Act of 1934, as amended.
10.4	Supplemental Agreement No. 33 to Purchase Agreement No. 1980 by and between American Airlines, Inc., and The Boeing Company dated as of February 1, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities Exchange Act of 1934, as amended.
10.5	Supplemental Agreement No. 34 to Purchase Agreement No. 1980 by and between American Airlines, Inc. and The Boeing Company dated as of February 1, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities Exchange Act of 1934, as amended.
10.6	Supplemental Agreement No. 35 to Purchase Agreement No. 1980 by and between American Airlines, Inc. and The Boeing Company dated as of February 13, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities Exchange Act of 1934, as amended.
10.7	Purchase Agreement No. 03735 by and between American Airlines, Inc., and The Boeing Company dated as of February 1, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities Exchange Act of 1934, as amended.
10.8	Amendment No. 1 to A320 Family Aircraft Purchase Agreement by and between American Airlines, Inc. and Airbus S.A.S. dated as of January 11, 2013. Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request under Rule 24b-2 of the Securities and Exchange Act of 1934, as amended.
12	Computation of ratio of earnings to fixed charges for the three months ended March 31, 2013 and 2012.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a).
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a).
32	Certification pursuant to Rule 13a-14(b) and section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code).
101	The following materials from American's Quarterly Report on Form 10-Q for the quarter ended March 31, 2013, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statements of Operations, (ii) the Condensed Consolidated Balance Sheets, (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) Notes to Condensed Consolidated Financial Statements, tagged as blocks of text.*
*	Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of

1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

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ADDITIONAL INFORMATION

American files annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy these reports, statements or other information filed by American at the SEC's Public Reference Room at Room 1580, 100 F Street NE, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. The SEC filings of American are also available to the public from commercial document retrieval services and at the website maintained by the SEC at www.sec.gov. You can also find the SEC filings of American on its website, www.aa.com.

The SEC allows American to incorporate information by reference into this Form 10-Q. This means that American can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this Form 10-Q, except for any information that is superseded by information that is included directly in this Form 10-Q or incorporated by reference subsequent to the date of this Form 10-Q. American does not incorporate the contents of its website into this Form 10-Q.

American has made and expects to make public disclosures of certain information regarding American, including, but not limited to, disclosures regarding the Merger, to investors and the general public by means of certain social media sites, including, but not limited to, Facebook and Twitter and by means of a joint merger website maintained by AMR and US Airways Group. Investors are encouraged to (i) follow American (@AmericanAir) on Twitter, (ii) “like” American (www.facebook.com/AmericanAirlines) on its Facebook page and (iii) visit www.aaarriving.com for updated information regarding AMR, US Airways Group, and the Merger. American does not incorporate the contents of its social media posts or the joint merger website into this Form 10-Q.

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	American Airlines, Inc.	
Date: April 18, 2013	BY:	[/s/ Isabella D. Goren] Isabella D. Goren Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)

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Purchase obligations (3)

- - - - -

Total

$39,412 $32,642 $27,381 $20,533 $13,966 $43,106 $177,040

(1) Does not reflect a reduction for the impact of any company owned life insurance proceeds to be received. Currently, we have life insurance policies with net death benefits of $3,087 to provide funding for these obligations. See Note 11 to the Consolidated Financial Statements for more information.

(2) Does not reflect a reduction for the impact of sublease income to be received. See Note 17 to the Consolidated Financial Statements for more information.

(3) The Company is not a party to any long-term supply contracts with respect to the purchase of raw materials or finished goods. At the end of fiscal year 2015, we had approximately $15,076 in open purchase orders, primarily for imported inventories, which are in the ordinary course of business. We also have a firm commitment to purchase transportation equipment in fiscal 2016 totaling approximately $4,670.

(4) Lease guarantees relate to payments we would only be required to make in the event of default on the part of the guaranteed parties.

Off-Balance Sheet Arrangements

We utilize stand-by letters of credit in the procurement of certain goods in the normal course of business. We lease land and buildings that are primarily used in the operation of BHF stores and Zenith distribution facilities. We have guaranteed certain lease obligations of licensee operators as part of our retail strategy. See Contractual Obligations and Commitments table above and Note 17 to the Consolidated Financial Statements, included in Item 8 of this Annual Report on Form 10-K, for further discussion of operating leases and lease guarantees, including descriptions of the terms of such commitments and methods used to mitigate risks associated with these arrangements.

Contingencies

We are involved in various claims and litigation as well as environmental matters, which arise in the normal course of business. Although the final outcome of these legal and environmental matters cannot be determined, based on the facts presently known, it is our opinion that the final resolution of these matters will not have a material adverse effect on our financial position or future results of operations.

Critical Accounting Policies and Estimates

Our consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") which requires that certain estimates and assumptions be made that affect the amounts and disclosures reported in those financial statements and the related accompanying notes. Actual results could differ from these estimates and assumptions. We use our best judgment in valuing these estimates and may, as warranted, solicit external advice. Estimates are based on current facts and circumstances, prior experience and other assumptions believed to be reasonable. The following critical accounting policies, some of which are impacted significantly by judgments, assumptions and estimates, affect our consolidated financial statements.

Consolidation – The consolidated financial statements include the accounts of Bassett Furniture Industries, Incorporated and its majority-owned subsidiaries for whom we have operating control. In accordance with ASC Topic 810, *Consolidation,* we have evaluated our licensees and certain other entities to determine whether they are variable interest entities ("VIEs") of which we are the primary beneficiary and thus would require consolidation in our financial statements. To date we have concluded that none of our licensees nor any other of our counterparties represent VIEs.

Revenue Recognition - Revenue is recognized when the risks and rewards of ownership and title to the product have transferred to the buyer. This generally occurs upon the shipment of goods to independent dealers or, in the case of Company-owned retail stores, upon delivery to the customer. Our wholesale payment terms generally vary from 30 to 60 days. For retail sales, we typically receive a significant portion of the purchase price as a customer deposit upon order, with the balance typically collected upon delivery. An estimate for returns and allowances has been provided in recorded sales. The contracts with our licensee store owners do not provide for any royalty or license fee to be paid to us. For our logistical services segment, line-haul freight revenue and home delivery revenue are recognized upon delivery to the destination. Warehousing services revenue is based upon warehouse space occupied by a customer's goods and inventory movements in and out of a warehouse and is recognized as such services are provided.

Staff Accounting Bulletin No. 104, *Revenue Recognition* ("SAB 104") outlines the four basic criteria for recognizing revenue as follows: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the seller's price to the buyer is fixed or determinable, and (4) collectibility is reasonably assured. SAB 104 further asserts that if collectibility of all or a portion of the revenue is not reasonably assured, revenue recognition should be deferred until payment is received. During fiscal 2015 and 2014, there were no dealers for which these criteria were not met.

Allowance for Doubtful Accounts - We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Our accounts receivable reserves were $1,175 and $1,249 at November 28, 2015 and November 29, 2014, respectively, representing 5.3% and 7.6% of our gross accounts receivable balances at those dates, respectively. The allowance for doubtful accounts is based on a review of specifically identified customer accounts in addition to an overall aging analysis. We evaluate the collectibility of our receivables from our licensees and other customers on a quarterly basis based on factors such as their financial condition, our collateral position, potential future plans with licensees and other similar factors. Our allowance for doubtful accounts represents our best estimate of potential losses on our accounts and notes receivable and is adjusted accordingly based on historical experience, current developments and present economic conditions and trends. Although actual losses have not differed materially from our previous estimates, future losses could differ from our current estimates. Unforeseen events such as a licensee or customer bankruptcy filing could have a material impact on our results of operations.

Inventories - Inventories are stated at the lower of cost or market. Cost is determined for domestic furniture inventories using the last-in, first-out method. The cost of imported inventories is determined on a first-in, first-out basis. We estimate an inventory reserve for excess quantities and obsolete items based on specific identification and historical write-offs, taking into account future demand and market conditions. Our reserves for excess and obsolete inventory were $1,397 and $1,412 at November 28, 2015 and November 29, 2014, respectively, representing 2.3% and 2.4%, respectively, of our inventories on a last-in, first-out basis. If actual demand or market conditions in the future are less favorable than those estimated, additional inventory write-downs may be required.

Valuation Allowance on Deferred Tax Assets – We evaluate our deferred income tax assets to determine if valuation allowances are required or should be adjusted. A valuation allowance is established against our deferred tax assets based on consideration of all available evidence, both positive and negative, using a "more likely than not" standard. This assessment 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. During fiscal 2014, reductions in the reserve related to changes in laws which impact our ability to recover certain state net operating loss carryforwards resulted in a credit to income of $974, which is included in our net income tax expense for 2014. The remaining valuation allowance at November 28, 2015 is $0.

Goodwill – Goodwill represents the excess of the purchase price over the value assigned to tangible assets and liabilities and identifiable intangible assets of businesses acquired. The acquisition of assets and liabilities and any resulting goodwill is allocated to the respective reporting unit; Wood, Upholstery, Retail or Logistical Services. We review goodwill at the reporting unit level annually for impairment or more frequently if events or circumstances indicate that assets might be impaired.

In accordance with ASC Topic 350, *Intangibles – Goodwill & Other,* the goodwill impairment test consists of a two-step process, if necessary. However, we first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in ASC Topic 350. The more likely than not threshold is defined as having a likelihood of more than 50 percent. If, after assessing the totality of events or circumstances, we determine that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary and our goodwill is considered to be unimpaired. However, if based on our qualitative assessment we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we will proceed with performing the two-step process. Based on our qualitative assessment as described above, we have concluded that our goodwill in the amount of $11,588 is not impaired as of November 28, 2015.

The first step compares the carrying value of each reporting unit that has goodwill with the estimated fair value of the respective reporting unit. Should the carrying value of a reporting unit be in excess of the estimated fair value of that reporting unit, the second step is performed whereby we must calculate the implied fair value of goodwill by deducting the fair value of all tangible and intangible net assets of the reporting unit from the fair value of the reporting unit. This second step represents a hypothetical purchase price allocation as if we had acquired the reporting unit on that date. Our impairment methodology uses a discounted cash flow analysis requiring certain assumptions and estimates to be made regarding future profitability of the reporting unit and industry economic factors. While we believe such assumptions and estimates are reasonable, the actual results may differ materially from the projected amounts.

Other Intangible Assets – Intangible assets acquired in a business combination and determined to have an indefinite useful life are not amortized but are tested for impairment annually or between annual tests when an impairment indicator exists. The recoverability of indefinite-lived intangible assets is assessed by comparison of the carrying value of the asset to its estimated fair value. If we determine that the carrying value of the asset exceeds its estimated fair value, an impairment loss equal to the excess would be recorded. At November 28, 2015, our indefinite-lived intangible assets other than goodwill consist of trade names acquired in the acquisition of Zenith and have a carrying value of $2,490.

Definite-lived intangible assets are amortized over their respective estimated useful lives and reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. We estimate the useful lives of our intangible assets and ratably amortize the value over the estimated useful lives of those assets. If the estimates of the useful lives should change, we will amortize the remaining book value over the remaining useful lives or, if an asset is deemed to be impaired, a write-down of the value of the asset may be required at such time. At November 28, 2015 our definite-lived intangible assets consist of customer relationships and customized technology applications acquired in the acquisition of Zenith with a total carrying value of $3,604.

Impairment of Long-Lived Assets - We periodically evaluate whether events or circumstances have occurred that indicate long-lived assets may not be recoverable or that the remaining useful life may warrant revision. When such events or circumstances are present, we assess the recoverability of long-lived assets by determining whether the carrying value will be recovered through the expected undiscounted future cash flows resulting from the use of the asset. In the event the sum of the expected undiscounted future cash flows is less than the carrying value of the asset, an impairment loss equal to the excess of the asset’s carrying value over its fair value is recorded. When analyzing our real estate properties for potential impairment, we consider such qualitative factors as our experience in leasing and selling real estate properties as well as specific site and local market characteristics. Upon the closure of a Bassett Home Furnishings store, we generally write off all tenant improvements which are only suitable for use in such a store.

Recent Accounting Pronouncements

See note 2 to our Consolidated Financial Statements regarding the impact or potential impact of recent accounting pronouncements upon our financial position and results of operations.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk from changes in the value of foreign currencies. Substantially all of our imports purchased outside of North America are denominated in U.S. dollars. Therefore, we believe that gains or losses resulting from changes in the value of foreign currencies relating to foreign purchases not denominated in U.S. dollars would not be material to our results from operations in fiscal 2015.

We are exposed to market risk from changes in the cost of raw materials used in our manufacturing processes, principally wood, woven fabric, and foam products. An increase in the rate of in home construction could result in increases in wood and fabric costs from current levels, and the cost of foam products, which are petroleum-based, is sensitive to changes in the price of oil.

We are also exposed to commodity price risk related to diesel fuel prices for fuel used in our logistical services segment. We manage our exposure to that risk primarily through the application of fuel surcharges to our customers.

We have potential exposure to market risk related to conditions in the commercial real estate market. Our retail real estate holdings of $3,120 and $6,302 at November 28, 2015 and November 29, 2014, respectively, for stores formerly operated by licensees as well as our holdings of $27,175 and $27,843 at November 28, 2015 and November 29, 2014, respectively, for Company-owned stores could suffer significant impairment in value if we are forced to close additional stores and sell or lease the related properties during periods of weakness in certain markets. Additionally, if we are required to assume responsibility for payment under the lease obligations of $2,537 and $3,296 which we have guaranteed on behalf of licensees as of November 28, 2015 and November 29, 2014, respectively, we may not be able to secure sufficient sub-lease income in the current market to offset the payments required under the guarantees.

	Number of Locations	Aggregate Square Footage	Net Book Value (in thousands)
Real estate occupied by Company-owned and operated stores, included in property and equipment, net (1)	11	276,887	$ 27,175
Investment real estate leased to others	2	41,021	3,120
Total Company investment in retail real estate	13	317,908	$ 30,295

(1) Includes two properties encumbered under mortgages totaling $1,709 at November 28, 2015.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of Bassett Furniture Industries, Incorporated and Subsidiaries

We have audited the accompanying consolidated balance sheets of Bassett Furniture Industries, Incorporated and Subsidiaries as of November 28, 2015 and November 29, 2014, and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended November 28, 2015. Our audits also included Financial Statement Schedule II - Analysis of Valuation and Qualifying Accounts for each of the three years in the period ended November 28, 2015. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Bassett Furniture Industries, Incorporated and Subsidiaries at November 28, 2015 and November 29, 2014, and the consolidated results of their operations and their cash flows for each of the three years in the period ended November 28, 2015, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Bassett Furniture Industries, Incorporated and Subsidiaries’ internal control over financial reporting as of November 28, 2015, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework), and our report dated January 21, 2016 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Richmond, Virginia

January 21, 2016

Consolidated Balance Sheets

Bassett Furniture Industries, Incorporated and Subsidiaries

November 28, 2015 and November 29, 2014

(In thousands, except share and per share data)

	2015	2014
<u>Assets</u>		
Current assets		
Cash and cash equivalents	$36,268	$26,673
Short-term investments	23,125	23,125
Accounts receivable, net of allowance for doubtful accounts of $1,175 and $1,249 as of November 28, 2015 and November 29, 2014, respectively	21,197	15,228
Inventories	59,896	57,272
Other current assets	6,798	7,796
Total current assets	147,284	130,094
Property and equipment, net	96,104	74,812
Other long-term assets		
Deferred income taxes, net	13,471	14,969
Goodwill and other intangible assets	17,682	1,730
Other	8,002	19,141
Total other long-term assets	39,155	35,840
Total assets	$282,543	$240,746
<u>Liabilities and Stockholders' Equity</u>		
Current liabilities		
Accounts payable	$20,916	$22,251
Accrued compensation and benefits	14,345	8,931
Customer deposits	23,999	22,202
Dividends payable	2,184	2,102
Current portion of long-term debt	5,273	316
Other accrued liabilities	13,133	10,971
Total current liabilities	79,850	66,773
Long-term liabilities		
Post employment benefit obligations	12,694	11,498
Notes payable	8,500	1,902
Other long-term liabilities	4,133	3,741
Total long-term liabilities	25,327	17,141
Commitments and Contingencies		

Stockholders' equity		
Common stock, $5 par value; 50,000,000 shares authorized; issued and outstanding 10,916,021 at November 28, 2015 and 10,493,393 at November 29, 2014	54,580	52,467
Retained earnings	120,904	106,339
Additional paid-in-capital	4,560	-
Accumulated other comprehensive loss	(2,678)	(1,974)
Total stockholders' equity	177,366	156,832
Total liabilities and stockholders' equity	$282,543	$240,746

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

Consolidated Statements of Income

Bassett Furniture Industries, Incorporated and Subsidiaries

For the years ended November 28, 2015, November 29, 2014, and November 30, 2013

(In thousands, except per share data)

	2015	**2014**	**2013**
Sales revenue:			
Furniture and accessories	$387,405	$340,738	$321,286
Logistics	43,522	-	-
Total sales revenue	430,927	340,738	321,286
Cost of furniture and accessories sold	179,291	158,317	155,292
Selling, general and administrative expenses excluding new store pre-opening costs	224,050	166,073	155,318
New store pre-opening costs	623	1,217	671
Lease exit costs	419	-	-
Asset impairment charges	106	-	-
Management restructuring costs	449	-	-
Income from operations	25,989	15,131	10,005
Remeasurement gain on acquisition of affiliate	7,212	-	-
Income from Continued Dumping & Subsidy Offset Act	1,156	-	-
Income from unconsolidated affiliated company	220	661	770
Interest expense	(607)	(188)	(255)
Other loss, net	(2,102)	(997)	(2,333)
Income before income taxes	31,868	14,607	8,187
Income tax expense	11,435	5,308	3,091
Net income	$20,433	$9,299	$5,096
Net income per share			
Basic income per share	$1.91	$0.88	$0.48
Diluted income per share	$1.88	$0.87	$0.47
Dividends per share			
Regular dividends	$0.34	$0.28	$0.22
Special dividend	$0.20	$0.20	$0.20

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

Consolidated Statements of Comprehensive Income

Bassett Furniture Industries, Incorporated and Subsidiaries

For the years ended November 28, 2015, November 29, 2014, and November 30, 2013

(In thousands)

	2015	**2014**	**2013**
Net income	$20,433	$9,299	$5,096
Other comprehensive loss:			
Actuarial adjustment to supplemental executive retirement defined benefit plan (SERP)	(1,135)	(918)	(310)
Income taxes related to SERP	431	358	119
Other comprehensive loss, net of tax	(704)	(560)	(191)
Total comprehensive income	$19,729	$8,739	$4,905

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

Consolidated Statements of Cash Flows

Bassett Furniture Industries, Incorporated and Subsidiaries

For the years ended November 28, 2015, November 29, 2014, and November 30, 2013

(In thousands)

	2015	2014	2013
Operating activities:			
Net income	$20,433	$9,299	$5,096
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	10,137	7,316	6,198
Equity in undistributed income of investments and unconsolidated affiliated companies	(220)	(661)	(770)
Non-cash asset impairment charges	106	-	-
Non-cash portion of lease exit costs	419	-	-
Remeasurement gain on acquisition of affiliate	(7,212)	-	-
Tenant improvement allowances received from lessors	1,283	3,060	-
Collateral deposited with insurance carrier	-	(1,150)	-
Impairment and lease exit charges on retail real estate	-	-	416
Deferred income taxes	1,930	544	2,282
Other, net	2,082	264	677
Changes in operating assets and liabilities			
Accounts receivable	(2,354)	775	(686)
Inventories	(2,624)	(4,203)	4,847
Other current and long-term assets	1,494	1,548	(4,819)
Customer deposits	1,796	5,912	3,961
Accounts payable and accrued liabilities	5,128	7,257	(6,562)
Net cash provided by operating activities	32,398	29,961	10,640
Investing activities:			
Purchases of property and equipment	(13,974)	(17,980)	(14,302)
Proceeds from sales of property and equipment	2,981	5,157	958
Cash paid for business acquisition, net of cash acquired	(7,323)	-	-
Capital contribution to affiliate	(1,345)	-	-
Proceeds from sale of affiliate	-	2,348	2,348
Proceeds from maturities and sales of investments	-	5,000	-
Purchases of investments	-	-	(28,125)
Cash received on notes receivable and other	-	320	89
Net cash used in investing activities	(19,661)	(5,155)	(39,032)
Financing activities:			
Cash dividends	(5,786)	(5,155)	(2,935)
Proceeds from exercise of stock options	4,031	297	313
Issuance of common stock	325	311	393

Repurchases of common stock	(2,071)	(5,602)	(1,750)
Taxes paid related to net share settlement of equity awards	(178)	(489)	(226)
Excess tax benefits from stock-based compensation	1,998	300	313
Proceeds from equipment loan	1,307	-	-
Payments on notes	(2,768)	(528)	(549)
Other, net	-	-	-
Net cash used in financing activities	(3,142)	(10,866)	(4,441)
Change in cash and cash equivalents	9,595	13,940	(32,833)
Cash and cash equivalents - beginning of year	26,673	12,733	45,566
Cash and cash equivalents - end of year	$36,268	$26,673	$12,733

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

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Consolidated Statements of Stockholders' Equity

Bassett Furniture Industries, Incorporated and Subsidiaries

For the years ended November 28, 2015, November 29, 2014, and November 30, 2013

(In thousands, except share and per share data)

	Common Stock Shares	Amount	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total
Balance, November 24, 2012	10,836,840	$54,184	$ -	$104,319	$ (1,223)	$157,280
Comprehensive income						
Net income	-	-	-	5,096	-	5,096
Actuarial adjustment to SERP	-	-	-	-	(191)	(191)
Regular dividends ($0.22 per share)	-	-	-	(2,393)	-	(2,393)
Special dividend ($0.20 per share)	-	-	-	(2,172)	-	(2,172)
Issuance of common stock	160,128	801	(104)	-	-	697
Purchase and retirement of common stock	(137,650)	(688)	(937)	(324)	-	(1,949)
Stock-based compensation	-	-	728	-	-	728
Excess tax benefits from Stock-based compensation	-	-	313	-	-	313
Balance, November 30, 2013	10,859,318	54,297	-	104,526	(1,414)	157,409
Comprehensive income						
Net income	-	-	-	9,299	-	9,299
Actuarial adjustment to SERP, net of tax	-	-	-	-	(560)	(560)
Regular dividends ($0.28 per share)	-	-	-	(2,983)	-	(2,983)
Special dividend ($0.20 per share)	-	-	-	(2,102)	-	(2,102)
Issuance of common stock	69,619	348	260	-	-	608
Purchase and retirement of common stock	(435,544)	(2,178)	(1,511)	(2,401)	-	(6,090)
Stock-based compensation	-	-	951	-	-	951
Excess tax benefits from Stock-based compensation	-	-	300	-	-	300
Balance, November 29, 2014	10,493,393	52,467	-	106,339	(1,974)	156,832
Comprehensive income						
Net income	-	-	-	20,433	-	20,433

Actuarial adjustment to SERP, net of tax	-	-	-	-	(704)	(704)
Regular dividends ($0.34 per share)	-	-	-	(3,684)	-	(3,684)
Special dividend ($0.20 per share)	-	-	-	(2,184)	-	(2,184)
Issuance of common stock	503,814	2,519	3,511	-	-	6,030
Purchase and retirement of common stock	(81,186)	(406)	(1,843)		-	(2,249)
Stock-based compensation	-	-	894	-	-	894
Excess tax benefits from Stock-based compensation	-	-	1,998	-	-	1,998
Balance, November 28, 2015	10,916,021	$54,580	$ 4,560	$120,904	$ (2,678)	$177,366

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

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Notes to Consolidated Financial Statements

(In thousands, except share and per share data)

1. Description of Business

Bassett Furniture Industries, Incorporated (together with its consolidated subsidiaries, “Bassett”, “we”, “our”, the “Company”) based in Bassett, Va., is a leading manufacturer, marketer and retailer of branded home furnishings. Bassett’s full range of furniture products and accessories, designed to provide quality, style and value, are sold through an exclusive nation-wide network of 93 retail stores known as Bassett Home Furnishings (referred to as “BHF”). Of the 93 stores, the Company owns and operates 60 stores (“Company-owned retail stores”) with the other 33 being independently owned (“licensee operated”). We also distribute our products through other multi-line furniture stores, many of which feature Bassett galleries or design centers, specialty stores and mass merchants.

We sourced approximately 37% of our wholesale products from various countries, with the remaining volume produced at our three domestic manufacturing facilities.

Zenith Acquisition

Prior to February 2, 2015 we held a 49% interest in Zenith Freight Lines, LLC (“Zenith”) for which we used the equity method of accounting. On February 2, 2015 we acquired the remaining 51% ownership interest (see Note 3, Business Combinations). Zenith provides over-the-road transportation of furniture, operates regional freight terminal, warehouse and distribution facilities in eleven states, and manages various home delivery facilities that service Bassett Home Furnishings stores and other clients in local markets around the United States. With the acquisition of Zenith, we established our logistical services operating segment.

2. **Significant Accounting Policies**

Basis of Presentation and Principles of Consolidation

Our fiscal year ends on the last Saturday in November, which periodically results in a 53-week year. Fiscal 2015 and 2014 each contained 52 weeks, whereas Fiscal 2013 contained 53 weeks. The Consolidated Financial Statements include the accounts of Bassett Furniture Industries, Incorporated and our majority-owned subsidiaries in which we have a controlling interest. All significant intercompany balances and transactions are eliminated in consolidation. Accordingly, the results of Zenith have been consolidated with our results since the date of the acquisition. Sales of logistical services from Zenith to our wholesale and retail segments have been eliminated, and Zenith’s operating costs and expenses since the date of acquisition are included in selling, general and administrative expenses in our condensed consolidated statements of net income. The financial statements have been prepared in accordance with generally accepted accounting principles in the United States ("GAAP"). Unless otherwise indicated, references in the Consolidated Financial Statements to fiscal 2015, 2014 and 2013 are to Bassett's fiscal year ended November 28, 2015, November 29, 2014 and November 30, 2013, respectively. References to the “ASC” included hereinafter refer to the Accounting Standards Codification established by the Financial Accounting Standards Board as the source of authoritative GAAP.

For comparative purposes, certain amounts in the 2014 and 2013 financial statements have been reclassified to conform to the 2015 presentation. See “Recent Accounting Pronouncements” below regarding the impact of our adoption of Accounting Standards Update 2015-17 upon the classification of deferred tax assets in our consolidated balance sheets.

The equity method of accounting was used for our investment in Zenith prior to the date of acquisition because we exercised significant influence but did not maintain a controlling interest. Consolidated net income includes our proportionate share of the net income or net loss of Zenith prior to the date of the acquisition.

We analyzed our licensees under the requirements for variable interest entities (“VIEs”). All of these licensees operate as BHF stores and are furniture retailers. We sell furniture to these licensees, and in some cases have extended credit beyond normal terms, made lease guarantees, guaranteed loans, or loaned directly to the licensees. We have recorded reserves for potential exposures related to these licensees. See Note 17 for disclosure of leases and lease guarantees. Based on financial projections and best available information, all licensees have sufficient equity to carry out their principal operating activities without subordinated financial support. Furthermore, we believe that the power to direct the activities that most significantly impact the licensees’ operating performance continues to lie with the ownership of the licensee dealers. Our rights to assume control over or otherwise influence the licensees’ significant activities only exist pursuant to our license and security agreements and are in the nature of protective rights as contemplated under ASC Topic 810. We completed our assessment for other potential VIEs, and concluded that there were none. We will continue to reassess the status of potential VIEs including when facts and circumstances surrounding each potential VIE change.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Some of the more significant estimates include allowances for doubtful accounts, calculation of inventory reserves, valuation of income tax reserves, lease guarantees, insurance reserves, and assumptions related to our post-employment benefit obligations. Actual results could differ from those estimates.

Revenue Recognition

Revenue is recognized when the risks and rewards of ownership and title to the product have transferred to the buyer. This occurs upon the shipment of goods to independent dealers or, in the case of Company-owned retail stores, upon delivery to the customer. We offer terms varying from 30 to 60 days for wholesale customers. For retail sales, we typically collect a significant portion of the purchase price as a customer deposit upon order, with the balance typically collected upon delivery. These deposits are carried on our balance sheet as a current liability until delivery is fulfilled. Estimates for returns and allowances have been recorded as a reduction to revenue. The contracts with our licensee store owners do not provide for any royalty or license fee to be paid to us. Revenue is reported net of any taxes collected. For our logistical services segment, line-haul freight revenue and home delivery revenue are recognized upon the completion of delivery to the destination. Warehousing services revenue is based upon warehouse space occupied by a customer’s goods and inventory movements in and out of a warehouse and is recognized as such services are provided.

Staff Accounting Bulletin No. 104, *Revenue Recognition* (“SAB 104”) outlines the four basic criteria for recognizing revenue as follows: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the seller’s price to the buyer is fixed or determinable, and (4) collectability is reasonably assured. SAB 104 further asserts that if collectability of all or a portion of the revenue is not reasonably assured, revenue recognition should be deferred until payment is received. During fiscal 2015, 2014 and 2013, there were no dealers for which these criteria were not met. As of and subsequent to November 30, 2013 there have been no dealers that remained on a cost recovery basis.

Cash Equivalents

The Company considers cash on hand, demand deposits in banks and all highly liquid investments with an original maturity of three months or less to be cash and cash equivalents. Our short-term investments, which consist of certificates of deposit, are not considered cash equivalents since they have original maturities of greater than three months.

Accounts Receivable

Substantially all of our trade accounts receivable is due from customers located within the United States. We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. The allowance for doubtful accounts is based on a review of specifically identified accounts in addition to an overall aging analysis. Judgments are made with respect to the collectibility of accounts receivable based on historical experience and current economic trends. Actual losses could differ from those estimates. A significant portion of our trade accounts receivable and allowance for doubtful accounts are attributable to amounts owed to us by our licensees, with the remaining receivables due primarily from national account customers, traditional distribution channel customers and logistical services customers. The percentages of our trade accounts receivable and related allowance for doubtful accounts owed to us by our licensees were as follows at November 28, 2015 and November 29, 2014:

	2015	**2014**
Portion of trade accounts receivable owed by licensees	34 %	46 %
Portion of allowance for doubtful accounts attributable to licensees	32 %	58 %

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Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Concentrations of Credit Risk and Major Customers

Financial instruments that subject us to credit risk consist primarily of investments, accounts and notes receivable and financial guarantees. Investments are managed within established guidelines to mitigate risks. Accounts and notes receivable and financial guarantees subject us to credit risk partially due to the concentration of amounts due from and guaranteed on behalf of independent licensee customers. At November 28, 2015 and November 29, 2014, our aggregate exposure from receivables and guarantees related to customers consisted of the following:

	2015	2014
Accounts receivable, net of allowances (Note 5)	$21,197	$15,228
Notes receivable, net of allowances	10	592
Contingent obligations under lease and loan guarantees, less amounts recognized (Note 17)	2,441	3,046
Total credit risk exposure related to customers	$23,648	$18,866

At November 28, 2015, approximately 26% of the aggregate risk exposure, net of reserves, shown above was attributable to three customers. At November 29, 2014, approximately 24% of the aggregate risk exposure, net of reserves, shown above was attributable to two customers. In fiscal 2015, 2014 and 2013, no customer accounted for more than 10% of total net sales.

We have no foreign manufacturing or retail operations. We define export sales as sales to any country or territory other than the United States or its territories or possessions. Our export sales were approximately $4,516, $4,774, and $4,603 in fiscal 2015, 2014, and 2013, respectively. All of our export sales are invoiced and settled in U.S. dollars.

Inventories

Inventories (retail merchandise, finished goods, work in process and raw materials) are stated at the lower of cost or market. Cost is determined for domestic manufactured furniture inventories using the last-in, first-out (“LIFO”) method because we believe this methodology provides better matching of revenue and expenses. The cost of imported inventories is determined on a first-in, first-out (“FIFO”) basis. Inventories accounted for under the LIFO method represented 43% and 40% of total inventory before reserves at November 28, 2015 and November 29, 2014, respectively. We estimate inventory reserves for excess quantities and obsolete items based on specific identification and historical write-offs, taking into account future demand and market conditions. If actual demand or market conditions in the future are less favorable than those estimated, additional inventory write-downs may be required.

Property and Equipment

Property and equipment is comprised of all land, buildings and leasehold improvements and machinery and equipment used in the manufacturing and warehousing of furniture, our Company-owned retail operations, our logistical services operations, and corporate administration. This property and equipment is stated at cost less accumulated depreciation. Depreciation is computed over the estimated useful lives of the respective assets utilizing the straight-line method. Buildings and improvements are generally depreciated over a period of 10 to 39 years. Machinery and equipment are generally depreciated over a period of 5 to 10 years. Leasehold improvements are amortized based on the underlying lease term, or the asset’s estimated useful life, whichever is shorter.

Retail Real Estate

Retail real estate is comprised of owned and leased properties which have been utilized by licensee operated BHF stores, including properties which are now leased or subleased to non-licensee tenants. These properties are located in high traffic, upscale locations that are normally occupied by large successful national retailers. This real estate is stated at cost less accumulated depreciation and is depreciated over the useful lives of the respective assets utilizing the straight line method. Buildings and improvements are generally depreciated over a period of 10 to 39 years. Leasehold improvements are amortized based on the underlying lease term, or the asset’s estimated useful life, whichever is shorter. As of November 28, 2015 and November 29, 2014, the cost of retail real estate included land totaling $990 and $1,990, respectively, and building and leasehold improvements of $6,178 and $8,831, respectively. As of November 28, 2015 and November 29, 2014, accumulated depreciation of retail real estate was $4,160 and $4,631, respectively. The net book value of our retail real estate is included in other long-term assets in our consolidated balance sheets. Depreciation expense was $184, $400, and $484 in fiscal 2015, 2014, and 2013, respectively, and is included in other loss, net, in our consolidated statements of income.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

During the year ended November 28, 2015 we closed on the sale of our retail real estate investment property located in Sugerland, Texas and received cash in the amount of $2,835. During fiscal 2015 we recognized a non-cash charge of $182 to write down the carrying value of the Sugarland real estate to the selling price.

During the year ended November 29, 2014 we received proceeds from the disposition of retail real estate totaling $5,157. During the first quarter of fiscal 2014 we received $1,407 from the sale of our retail real estate investment property in Henderson, Nevada. During the third quarter of fiscal 2014 we received net proceeds in the amount of $3,750 from the sale of our retail real estate investment property located in Denver, Colorado. There were no material gains or losses associated with these dispositions during fiscal 2014, however an impairment charge in the amount of $416 was recognized during fiscal 2013 to write down the carrying value of the Henderson real estate to the selling price for which it was under contract.

The fiscal 2015 and 2014 sales proceeds described above are included in proceeds from sales of property and equipment in the accompanying consolidated statements of cash flows. The fiscal 2015 and 2013 impairment charges described above are included in other loss, net, in our consolidated statements of income.

Goodwill

Goodwill represents the excess of the fair value of consideration given over the fair value of the tangible assets and liabilities and identifiable intangible assets of businesses acquired. The acquisition of assets and liabilities and the resulting goodwill is allocated to the respective reporting unit: Wood, Upholstery, Retail or Logistical Services. We review goodwill at the reporting unit level annually for impairment or more frequently if events or circumstances indicate that assets might be impaired.

In accordance with ASC Topic 350, *Intangibles – Goodwill & Other,* the goodwill impairment test consists of a two-step process, if necessary. However, we first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in ASC Topic 350. The more likely than not threshold is defined as having a likelihood of more than 50 percent. If, after assessing the totality of events or circumstances, we determine that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary and our goodwill is considered to be unimpaired. However, if based on our qualitative assessment we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we will proceed with performing the two-step process. Based on our qualitative assessment as described above, we have concluded that our goodwill is not impaired as of November 28, 2015.

The first step compares the carrying value of each reporting unit that has goodwill with the estimated fair value of the respective reporting unit. Should the carrying value of a reporting unit be in excess of the estimated fair value of that reporting unit, the second step is performed whereby we must calculate the implied fair value of goodwill by deducting the fair value of all tangible and intangible net assets of the reporting unit from the fair value of the reporting unit. This second step represents a hypothetical application of the acquisition method of accounting as if we had acquired the reporting unit on that date. Our impairment methodology uses a discounted cash flow analysis requiring certain assumptions and estimates to be made regarding future profitability of the reporting unit and industry economic factors. While we believe such assumptions and estimates are reasonable, the actual results may differ materially from the projected amounts.

Other Intangible Assets

Intangible assets acquired in a business combination and determined to have an indefinite useful life are not amortized but are tested for impairment annually or between annual tests when an impairment indicator exists. The recoverability of indefinite-lived intangible assets is assessed by comparison of the carrying value of the asset to its estimated fair value. If we determine that the carrying value of the asset exceeds its estimated fair value, an impairment loss equal to the excess would be recorded.

Definite-lived intangible assets are amortized over their respective estimated useful lives and reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. We estimate the useful lives of our intangible assets and ratably amortize the value over the estimated useful lives of those assets. If the estimates of the useful lives should change, we will amortize the remaining book value over the remaining useful lives or, if an asset is deemed to be impaired, a write-down of the value of the asset may be required at such time.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Impairment of Long Lived Assets

We periodically evaluate whether events or circumstances have occurred that indicate long-lived assets may not be recoverable or that the remaining useful life may warrant revision. When such events or circumstances are present, we assess the recoverability of long-lived assets by determining whether the carrying value will be recovered through the expected undiscounted future cash flows resulting from the use and eventual disposition of the asset. In the event the sum of the expected undiscounted future cash flows is less than the carrying value of the asset, an impairment loss equal to the excess of the asset's carrying value over its fair value is recorded. Fair value is determined based on discounted cash flows or appraised values depending on the nature of the assets. The long-term nature of these assets requires the estimation of cash inflows and outflows several years into the future.

When analyzing our real estate properties for potential impairment, we consider such qualitative factors as our experience in leasing and selling real estate properties as well as specific site and local market characteristics. Upon the closure of a Bassett Home Furnishings store, we generally write off all tenant improvements which are only suitable for use in such a store.

Income Taxes

We account for income taxes under the liability method which requires that we recognize deferred tax assets and liabilities for the future tax consequences attributable to 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. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

We recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. Despite our belief that our liability for unrecognized tax benefits is adequate, it is often difficult to predict the final outcome or the timing of the resolution of any particular tax matters. We may adjust these liabilities as relevant circumstances evolve, such as guidance from the relevant tax authority or our tax advisors, or resolution of issues in the courts. These adjustments are recognized as a component of income tax expense in the period in which they are identified.

We evaluate our deferred income tax assets to determine if valuation allowances are required or should be adjusted. A valuation allowance is established against our deferred tax assets based on consideration of all available evidence, both positive and negative, using a “more likely than not” standard. This assessment 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. See Note 11.

New Store Pre-Opening Costs

Income (loss) from operations for fiscal 2015, 2014 and 2013 includes new store pre-opening costs of $623, $1,217 and $671, respectively. Such costs consist of expenses incurred at the new store location during the period prior to its opening and include, among other things, facility occupancy costs such as rent and utilities and local store personnel costs related to pre-opening activities including training. New store pre-opening costs do not include costs which are capitalized in accordance with our property and equipment capitalization policies, such as leasehold improvements and store fixtures and equipment. Such capitalized costs associated with new stores are depreciated commencing with the opening of the store. There are no pre-opening costs associated with stores acquired from licensees, as such locations were already in operation at the time of their acquisition.

Shipping and Handling Costs

Costs incurred to deliver wholesale merchandise to customers are recorded in selling, general and administrative expense and totaled $18,624, $16,162, and $15,685 for fiscal 2015, 2014 and 2013, respectively. Costs incurred to deliver retail merchandise to customers are also recorded in selling, general and administrative expense and totaled $15,383, $12,844, and $10,855 for fiscal 2015, 2014 and 2013, respectively.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Advertising

Costs incurred for producing and distributing advertising and advertising materials are expensed when incurred and are included in selling, general and administrative expenses. Advertising costs totaled $16,228, $15,614, and $14,750 in fiscal 2015, 2014, and 2013, respectively.

Insurance Reserves

We have self-funded insurance programs in place to cover workers' compensation and health insurance. These insurance programs are subject to various stop-loss limitations. We accrue estimated losses using historical loss experience. Although we believe that the insurance reserves are adequate, the reserve estimates are based on historical experience, which may not be indicative of current and future losses. We adjust insurance reserves, as needed, in the event that future loss experience differs from historical loss patterns.

Supplemental Cash Flow Information

In connection with our acquisition of Zenith, non-cash financing activities included the issuance of 89,485 shares of our common stock valued at $1,675, and the issuance of a note payable with a discounted fair value of $8,436. See Note 3 for additional information regarding the fair value of the consideration given for the acquisition of Zenith. There were no material non-cash investing or financing activities during fiscal 2014 or 2013.

Recent Accounting Pronouncements

In April 2014, the FASB issued Accounting Standards Update No. 2014-08 (ASU 2014-08), which updated the guidance in ASC Topic 205, Presentation of Financial Statements, and ASC Topic 360, Property, Plant and Equipment. The amendments in ASU 2014-08 change the criteria for reporting discontinued operations for all public and nonpublic entities. The amendments also require new disclosures about discontinued operations and disposals of components of an entity that do not qualify for discontinued operations reporting. This guidance will become effective for all disposals (or classifications as held for sale) of components of an entity that occur within annual periods beginning on or after December 15, 2014, and interim periods within those years, and therefore will become effective for us as of the beginning of our 2016 fiscal year. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09 (ASU 2014-09), which creates ASC Topic 606, Revenue from Contracts with Customers, and supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, including most industry-specific revenue recognition guidance throughout the Industry Topics of the Codification. In addition, ASU 2014-09 supersedes the cost guidance in Subtopic 605-35, Revenue Recognition—Construction-Type and Production-Type Contracts, and creates new Subtopic 340-40, Other Assets and Deferred Costs—Contracts with Customers. In summary, the core principle of Topic 606 is to recognize revenue when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. Companies are allowed to select between two transition methods: (1) a full retrospective transition method with the application of the new guidance to each prior reporting period presented, or (2) a retrospective transition method that recognizes the cumulative effect on prior periods at the date of adoption together with additional footnote disclosures. The amendments in ASU 2014-09 are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period, and early application is not permitted. Therefore the amendments in ASU 2014-09 will become effective for us as of the beginning of our 2019 fiscal year. We are currently evaluating the impact that the adoption of ASU 2014-09 will have on our consolidated financial statements and have not made any decision on the method of adoption.

In January 2015, the FASB issued Accounting Standards Update No. 2015-01, Income Statement — Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items. ASU 2015-01 eliminates the concept of reporting extraordinary items, but retains current presentation and disclosure requirements for an event or transaction that is of an unusual nature or of a type that indicates infrequency of occurrence. Transactions that meet both criteria would now also follow such presentation and disclosure requirements. For all entities, the guidance is effective for annual periods, and interim periods within those annual periods, beginning after 15 December 2015. Early adoption is permitted; however, adoption must occur at the beginning of an annual period. Therefore the amendments in ASU 2015-01 will become effective for us as of the beginning of our 2017 fiscal year. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

In July 2015, the FASB issued Accounting Standards Update No. 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. ASU 2015-11 requires that inventory within the scope of this Update be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amendments in this Update do not apply to inventory that is measured using last-in, first-out (LIFO) or the retail inventory method. The amendments apply to all other inventory, which includes inventory that is measured using first-in, first-out (FIFO) or average cost. For all entities, the guidance is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2016. Early adoption is permitted. Therefore the amendments in ASU 2015-11 will become effective for us as of the beginning of our 2018 fiscal year. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

In July 2015, the FASB issued Accounting Standards Update No. 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement Period Adjustments. ASU 2015-16 requires that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The amendments in this Update require that the acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. Any current period adjustments to provisional amounts that would have impacted a prior period's earnings had they been recognized at the acquisition date are required to be presented separately on the face of the income statement or disclosed in the notes. The amendments in this Update are effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. The amendments in this Update should be applied prospectively to adjustments to provisional amounts that occur after the effective date of this Update with earlier application permitted for financial statements that have not been issued. Therefore the amendments in ASU 2015-16 will become effective for us as of the beginning of our 2017 fiscal year. The adoption of this guidance is not expected to have a material impact upon our financial condition or results of operations.

In November 2015, the FASB issued Accounting Standards Update No. 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. Current GAAP requires an entity to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. To simplify the presentation of deferred income taxes, ASU 2015-17 requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The

current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in this Update. The amendments in this Update are effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Earlier application is permitted for all entities as of the beginning of an interim or annual reporting period. We have elected to adopt this update as of the fourth quarter of fiscal 2015. Accordingly, deferred tax assets in the amount of $5,268 which were formerly classified as current assets at November 29, 2014 have been reclassified as non-current assets in our consolidated balance sheet.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

3. Business Combination – Acquisition of Zenith

Prior to February 2, 2015 we held a 49% interest in Zenith for which we used the equity method of accounting. Zenith provides domestic transportation and warehousing services primarily to furniture manufacturers and distributors and also provides home delivery services to furniture retailers. We historically have contracted with Zenith to provide substantially all of our domestic freight, transportation and warehousing needs for the wholesale business. In addition, Zenith provides home delivery services for many of our Company-owned retail stores. On February 2, 2015, we acquired the remaining 51% of Zenith in exchange for cash, Bassett common stock and a note payable with a total fair value of $19,111. The value of the Bassett common stock was based on the closing market price of our shares on the acquisition date, discounted for lack of marketability due to restrictions on the seller's ability to transfer the shares. The restrictions on one half of the shares expire on the first anniversary of the acquisition, with the remainder expiring on the second anniversary. The note is payable in three annual installments of $3,000 each beginning February 2, 2016, and has been discounted to its fair value as of the date of the acquisition based on our estimated borrowing rate.

The carrying value of our 49% interest in Zenith prior to the acquisition was $9,480 (see Note 9, Unconsolidated Affiliated Company). In connection with the acquisition, this investment was remeasured to a fair value of $16,692 resulting in the recognition of a gain of $7,212 during the year ended November 28, 2015. The impact of this gain upon our basic and diluted earnings per share for the year ended November 28, 2015 is approximately $0.41 net of the related tax expense. The remeasured fair value of our prior interest in Zenith was estimated based on the fair value of the consideration transferred to acquire the remaining 51% of Zenith less an estimated control premium.

Under the acquisition method of accounting, the fair value of the consideration transferred along with the fair value of our previous 49% interest in Zenith was allocated to the tangible and intangible assets acquired and the liabilities assumed based on their estimated fair values as of the acquisition date with the remaining unallocated amount recorded as goodwill.

The total fair value of the acquired business was determined as follows:

Fair value of consideration transferred in exchange for 51% of Zenith:	
Cash	$9,000
Bassett common stock, 89,485 shares, par value $5.00 per share, fair value at closing $18.72 per share	1,675

Note payable	8,436
Total fair value of consideration transferred to seller	19,111
Less effective settlement of previous amounts payable to Zenith at acquisition	(3,622)
Total fair value of consideration net of effective settlement	15,489
Fair value of Bassett's previous 49% interest in Zenith	16,692
Total fair value of acquired business	$32,181

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

The preliminary allocation of the fair value of the acquired business was based upon a preliminary valuation. Our estimates and assumptions are subject to change as we obtain additional information for our estimates during the measurement period (up to one year from the acquisition date). The primary areas of the preliminary allocation of the fair value of consideration transferred that are not yet finalized relate to the fair values of certain tangible and intangible assets acquired and the residual goodwill. The preliminary allocation of the fair value of the acquired business is as follows:

Identifiable assets acquired:	
Acquired cash and cash equivalents	$1,677
Accounts receivable, net	3,399
Prepaid expenses and other current assets	496
Property and equipment	18,110
Other long-term assets	646
Intangible assets	6,362
Total identifiable assets acquired	30,690
Liabilities assumed:	
Accounts payable and accrued liabilities	(4,038)
Notes payable	(4,329)
Total liabilities assumed	(8,367)
Net identifiable assets acquired	22,323
Goodwill	9,858
Total net assets acquired	$32,181

Goodwill was determined based on the residual difference between the fair value of the consideration transferred and the value assigned to tangible and intangible assets and liabilities. Approximately $6,982 of the acquired goodwill is deductible for tax purposes. Among the factors that contributed to a purchase price resulting in the recognition of goodwill were Zenith's reputation for best-in-class, fully integrated logistical services which are uniquely tailored to the needs of the furniture industry, as well as their ability to provide expedited delivery service which is increasingly in demand in the furniture industry.

A portion of the fair value of consideration transferred has been provisionally assigned to identifiable intangible assets as follows:

Description:	Useful Life In Years	Fair Value
Customer relationships	15	$3,038
Trade names	Indefinite	2,490
Technology - customized applications	7	834
Total acquired intangible assets		$6,362

The finite-lived intangible assets are being amortized on a straight-line basis over their useful lives. The indefinite-lived intangible asset and goodwill are not amortized but will be tested for impairment annually or between annual tests if an indicator of impairment exists.

The fair values of consideration transferred and net assets acquired were determined using a combination of Level 2 and Level 3 inputs as specified in the fair value hierarchy in ASC 820, *Fair Value Measurements and Disclosures*. See Note 4.

Acquisition costs related to the Zenith acquisition totaled $209 during the year ended November 28, 2015 and are included in selling, general and administrative expenses in the consolidated statements of income. The acquisition costs are primarily related to legal, accounting and valuation services.

Zenith’s revenue since February 2, 2015 included in our consolidated statement of income for the year ended November 28, 2015 is $43,522 after the elimination of intercompany transactions. Net income of Zenith included in our consolidated statement of income for the year ended November 28, 2015 is $2,078. The pro forma results of operations for the acquisition of Zenith have not been presented because they are not material to our consolidated results of operations.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

4. Financial Instruments, Investments and Fair Value Measurements

Financial Instruments

Our financial instruments include cash and cash equivalents, short-term investments in certificates of deposit, accounts receivable, cost method investments, accounts payable and long-term debt. Because of their short maturities, the carrying amounts of cash and cash equivalents, short-term investments in certificates of deposit, accounts receivable, and accounts payable approximate fair value. Our cost method investments generally involve entities for which it is not practical to determine fair values.

Investments

Our short-term investments of $23,125 at both November 28, 2015 and November 29, 2014 consisted of certificates of deposit (CDs) with original terms of twelve months, bearing interest at rates ranging from 0.28% to 1.00%. At November 28, 2015, the weighted average remaining time to maturity of the CDs was approximately seven months and the weighted average yield of the CDs was approximately 0.42%. Each CD is placed with a Federally insured financial institution and all deposits are within Federal deposit insurance limits. As the CDs mature, we expect to reinvest them in CDs of similar maturities of up to one year. Due to the nature of these investments and their relatively short maturities, the carrying amount of the short-term investments at November 28, 2015 and November 29, 2014 approximates their fair value.

Fair Value Measurement

The Company accounts for items measured at fair value in accordance with ASC Topic 820, *Fair Value Measurements and Disclosures*. ASC 820's valuation techniques are based on observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect our market assumptions. ASC 820 classifies these inputs into the following hierarchy:

Level 1 Inputs– Quoted prices for identical instruments in active markets.

Level 2 Inputs– Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs– Instruments with primarily unobservable value drivers.

We believe that the carrying amounts of our current assets and current liabilities approximate fair value due to the short-term nature of these items. The recurring estimate of the fair value of our notes payable for disclosure purposes (see Note 10) involves Level 3 inputs. Our primary non-recurring fair value estimates typically involve business acquisitions (Note 3) which involve a combination of Level 2 and Level 3 inputs, and asset impairments (Note 15) which utilize Level 3 inputs.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

5. **Accounts Receivable**

Accounts receivable consists of the following:

	November 28, 2015	November 29, 2014
Gross accounts receivable	$ 22,372	$ 16,477
Allowance for doubtful accounts	(1,175)	(1,249)
Net accounts receivable	$ 21,197	$ 15,228

Activity in the allowance for doubtful accounts was as follows:

	2015	2014
Balance, beginning of the year	$1,249	$1,607
Acquired allowance on accounts receivable (Note 3)	209	-
Reductions to allowance, net	(283)	(358)
Balance, end of the year	$1,175	$1,249

We believe that the carrying value of our net accounts receivable approximates fair value. The inputs into these fair value estimates reflect our market assumptions and are not observable. Consequently, the inputs are considered to be Level 3 as specified in the fair value hierarchy in ASC Topic 820, *Fair Value Measurements and Disclosures*. See Note 4.

6. **Inventories**

Inventories consist of the following:

	November 28, 2015	November 29, 2014
Wholesale finished goods	$ 31,253	$ 31,399
Work in process	318	298
Raw materials and supplies	9,793	8,109
Retail merchandise	27,680	26,428
Total inventories on first-in, first-out method	69,044	66,234
LIFO adjustment	(7,751)	(7,550)
Reserve for excess and obsolete inventory	(1,397)	(1,412)
	$ 59,896	$ 57,272

We source a significant amount of our wholesale product from other countries. During 2015, 2014 and 2013, purchases from our two largest vendors located in China and Vietnam were $25,190, $26,707 and $24,217 respectively.

We estimate an inventory reserve for excess quantities and obsolete items based on specific identification and historical write-offs, taking into account future demand, market conditions and the respective valuations at LIFO. The need for these reserves is primarily driven by the normal product life cycle. As products mature and sales volumes decline, we rationalize our product offerings to respond to consumer tastes and keep our product lines fresh. If actual demand or market conditions in the future are less favorable than those estimated, additional inventory write-downs may be required. In determining reserves, we calculate separate reserves on our wholesale and retail inventories. Our wholesale inventories tend to carry the majority of the reserves for excess quantities and obsolete inventory due to the nature of our distribution model. These wholesale reserves primarily represent design and style obsolescence. Typically, product is not shipped to our retail warehouses until a consumer has ordered and paid a deposit for the product. We do not typically hold retail inventory for stock purposes. Consequently, floor sample inventory and inventory for delivery to customers account for the majority of our inventory at retail. Retail reserves are based on accessory and clearance floor sample inventory in our stores and any inventory that is not associated with a specific customer order in our retail warehouses.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Activity in the reserves for excess quantities and obsolete inventory by segment are as follows:

	Wholesale Segment	Retail Segment	Total
Balance at November 30, 2013	$ 1,001	$ 292	$ 1,293
Additions charged to expense	1,666	331	1,997
Write-offs	(1,607)	(271)	(1,878)
Balance at November 29, 2014	1,060	352	1,412
Additions charged to expense	2,442	430	2,872
Write-offs	(2,415)	(472)	(2,887)
Balance at November 28, 2015	$ 1,087	$ 310	$ 1,397

7. **Property and Equipment**

Property and equipment consist of the following:

	November 28, 2015	November 29, 2014
Land	$ 12,311	$ 11,371
Buildings and leasehold improvements	104,265	90,204
Machinery and equipment	85,490	70,184
Property and equipment at cost	202,066	171,759
Less accumulated depreciation	(105,962)	(96,947)
Property and equipment, net	$ 96,104	$ 74,812

The net book value of our property and equipment by reportable segment is a follows:

	November 28, 2015	November 29, 2014
Wholesale	$ 17,763	$ 14,933

Retail - Company-owned stores	60,810	59,879
Logistical Services	17,531	-
Total property and equipment, net	$ 96,104	$ 74,812

Depreciation expense associated with the property and equipment shown above was included in income from operations in our consolidated statements of income as follows:

	2015	**2014**	**2013**
Cost of goods sold (1)	$599	$542	$595
Selling, general and adminstrative expenses (2)	9,627	6,814	5,279
Total depreciation expense included in income from operations	$10,226	$7,356	$5,874

(1) All associated with our wholesale segment for fiscal 2015, 2014 and 2013.
(2) Includes depreciation associated with our retail segment of $5,970, $5,782 and $4,531 for fiscal 2015, 2014 and 2013, respectively. Fiscal 2015 includes depreciation associated with our logistical services segment of $2,366.

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Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

8. **Goodwill and Other Intangible Assets**

At November 28, 2015 goodwill and other intangible assets consisted of the following:

	Gross Carrying Amount	Accumulated Amortization	Intangible Assets, Net
Intangibles subject to amortization:			
Customer relationships	$ 3,038	$ (169)	$ 2,869
Technology - customized applications	834	(99)	735
Total intangible assets subject to amortization	3,872	(268)	3,604
Intangibles not subject to amortization:			
Trade names	2,490	-	2,490
Goodwill	11,588	-	11,588
Total goodwill and other intangible assets	$ 17,950	$ (268)	$ 17,682

At November 29, 2014 our only intangible asset was goodwill with a carrying value of $1,730.

Changes in the carrying amounts of goodwill by reportable segment were as follows:

	Wholesale	Retail	Logistics	Total
Balance as of November 29, 2014	$ 1,128	$602	$ -	$1,730
Goodwill arising from acquisition of Zenith	3,711	1,218	4,929	9,858
Balance as of November 28, 2015	$ 4,839	$1,820	$ 4,929	$11,588

The goodwill recognized in connection with our acquisition of Zenith remains subject to future adjustments before the close of the measurement period in the first quarter of fiscal 2016. Refer to Note 3, Business Combinations, for additional information regarding the Zenith acquisition. There were no changes in the carrying value of our goodwill during fiscal 2014, and there were no accumulated impairment losses on goodwill as of November 28, 2015 or November 29, 2014.

Amortization expense associated with intangible assets during the year ended November 28, 2015 was $268 and is included in selling, general and administrative expense in our consolidated statement of income. All expense arising from the amortization of intangible assets is associated with our logistical services segment. There was no amortization expense recognized during fiscal 2014 or 2013. Estimated future amortization expense for intangible assets that exist at November 28, 2015 is as follows:

Fiscal 2016	$322
Fiscal 2017	322
Fiscal 2018	322
Fiscal 2019	322
Fiscal 2020	322
Thereafter	1,994
Total	$3,604

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

9. **Unconsolidated Affiliated Companies**

Zenith Freight Lines, LLC

Prior to February 2, 2015 we owned 49% of Zenith and accounted for our investment under the equity method. Our investment in Zenith at November 29, 2014 was $7,915 and is included in other assets in our condensed consolidated balance sheet. The balance of our investment in Zenith was adjusted for our equity in the earnings of Zenith through February 2, 2015 of $220, and increased by $1,345 representing our 49% share of a $2,745 capital contribution made to Zenith, a portion of which was used for retirement of certain of Zenith's debt prior to the acquisition. This activity resulted in a carrying value for our investment in Zenith of $9,480 on the date of acquisition. See Note 3 regarding the remeasurement of this carrying value to fair value in connection with the acquisition and the resulting gain.

Prior to the acquisition on February 2, 2015, we recorded the following income from Zenith in our consolidated statements of income:

	2015	**2014**	**2013**
Earnings recognized	$220	$661	$770

At November 29, 2014, we owed Zenith $2,628 for services rendered to us. Prior to the acquisition, we paid Zenith approximately $6,863, $31,308 and $29,313, for freight expense and logistical services in fiscal 2015, 2014, and 2013, respectively. We believe the transactions with Zenith were recorded at current market rates.

International Home Furnishings Center

In connection with the sale of our interest in International Home Furnishings Center, Inc. ("IHFC") on May 2, 2011, to International Market Centers, L.P. ("IMC"), $6,106 of the sales proceeds were placed in escrow at the time of the sale to cover various contingencies. At various times during fiscal 2012, 2013 and 2014, the contingencies were satisfied without loss to the Company and the funds were released to us. During fiscal 2014 and 2013 we received the final two payments of sales proceeds in the amount of $2,348 each which are included in cash flows from investing activities in our consolidated statements of cash flows.

In addition to the proceeds described above, at the time of the sale we acquired a minority interest in IMC in exchange for $1,000. IMC is majority owned by funds managed by Bain Capital Partners and a subsidiary of certain investment funds managed by Oaktree Capital Management, L.P. Our investment in IMC is included in other long-term assets in the accompanying consolidated balance sheets and is accounted for using the cost method as we do not have significant influence over IMC.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

10. **Notes Payable and Bank Credit Facility**

Our notes payable consist of the following:

	November 28, 2015		
	Principal Balance	Unamortized Discount	Net Carrying Amount
Zenith acquisition note payable	$9,000	$ (312)	$ 8,688
Transportation equipment notes payable	2,152	-	2,152
Real estate notes payable	2,933	-	2,933
Total debt	14,085	(312)	13,773
Less current portion	(5,477)	204	(5,273)
Total long-term debt	$8,608	$ (108)	$ 8,500

	November 29, 2014		
	Principal Balance	Unamortized Discount	Net Carrying Amount
Real estate notes payable	$2,218	$ -	$ 2,218
Less current portion	(316)	-	(316)
Total long-term debt	$1,902	$ -	$ 1,902

The future maturities of our notes payable are as follows:

Fiscal 2016	$5,477
Fiscal 2017	4,112

Fiscal 2018	3,803
Fiscal 2019	543
Fiscal 2020	150
Thereafter	-
	$14,085

Zenith Acquisition Note Payable

As part of the consideration given for our acquisition of Zenith on February 2, 2015, we issued an unsecured note payable to the former owner in the amount of $9,000. The note is payable in three annual installments $3,000 beginning February 2, 2016. Interest is payable annually at the one year LIBOR rate, which was established at 0.62% on February 2, 2015 and resets on each anniversary of the note. The note was recorded at its fair value in connection with the acquisition resulting in a debt discount that is amortized to the principal amount through the recognition of non-cash interest expense over the term of the note. Interest expense resulting from the amortization of the discount for the year ended November 28, 2015 was $252. The current portion of the note due within one year, net of the current portion of the unamortized discount, is $2,796 at November 28, 2015.

Transportation Equipment Notes Payable

Certain of the transportation equipment operated in our logistical services segment is financed by notes payable in the amount of $2,152. These notes are payable in fixed monthly payments of principal and interest at the fixed rate of 3.75%, with remaining terms of nineteen to forty months. The current portion of these notes due within one year at November 28, 2015 is $901. The notes are secured by tractors, trailers and local delivery trucks with a total net book value of $3,796 at November 28, 2015.

Real Estate Notes Payable

Two of our retail real estate properties have been financed through commercial mortgages with interest rates of 6.73%. These mortgages are collateralized by the respective properties with net book values totaling approximately $5,993 and $6,127 at November 28, 2015 and November 29, 2014, respectively. The total balance outstanding under these mortgages was $1,709 and $2,218 at November 28, 2015 and November 29, 2014, respectively. The current portion of these mortgages due within one year was $351 and $316 as of November 28, 2015 and November 29, 2014, respectively.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Certain of the real estate located in Conover, NC and operated in our logistical services segment is subject to a note payable in the amount of $1,224. The note is payable in monthly installments of principal and interest at the fixed rate of 3.75% through October 2016, at which time the remaining balance on the note of approximately $1,004 will be due. Therefore, the entire balance due on this note is included in the current portion of our long-term debt at November 28, 2015. The note is secured by land and buildings with a total net book value of $6,226 at November 28, 2015.

Fair Value

We believe that the carrying amount of our notes payable approximates fair value at both November 28, 2015 and November 29, 2014. In estimating the fair value, we utilize current market interest rates for similar instruments. The inputs into these fair value calculations reflect our market assumptions and are not observable. Consequently, the inputs are considered to be Level 3 as specified in the fair value hierarchy in ASC Topic 820, *Fair Value Measurements and Disclosures*. See Note 4.

Bank Credit Facility

Our credit facility with our bank provides for a line of credit of up to $15,000. This credit facility is secured by our accounts receivable and inventory. The facility contains covenants requiring us to maintain certain key financial ratios. We are in compliance with all covenants under the agreement and expect to remain in compliance for the foreseeable future. The line matured in December 2015 but has been temporarily extended while we are in negotiations with our bank for a new line, which we expect to obtain during the first quarter of fiscal 2016 under substantially similar terms, except that the line is expected to be unsecured.

We have $1,970 outstanding under standby letters of credit against our line, leaving availability under our credit line of $13,030. In addition, we have outstanding standby letters of credit with another bank totaling $356.

Total interest paid during fiscal 2015, 2014 and 2013 was $277, 176 and $244, respectively.

11. **Post-Employment Benefit Obligations**

Supplemental Retirement Income Plan

We have an unfunded Supplemental Retirement Income Plan (the “Supplemental Plan”) that covers one current and certain former executives. Upon retirement, the Supplemental Plan provides for lifetime monthly payments in an amount equal to 65% of the participant’s final average compensation as defined in the Supplemental Plan, which is reduced by certain social security benefits to be received and other benefits provided by us. The Supplemental Plan also provides a death benefit that is calculated as (a) prior to retirement death, which pays the beneficiary 50% of final average annual compensation for a period of 120 months, or (b) post-retirement death, which pays the beneficiary 200% of final average compensation in a single payment. We own life insurance policies on these executives with a current net death benefit of $3,087 at November 28, 2015 and we expect to substantially fund this death benefit through the proceeds received upon the death of the executive. Funding for the remaining cash flows is expected to be provided through operations. There are no benefits payable as a result of a termination of employment for any reason other than death or retirement, other than a change of control provision which provides for the immediate vesting and payment of the retirement benefit under the Supplemental Plan in the event of an employment termination resulting from a change of control.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Summarized information for the plan measured as of the end of each year presented, is as follows:

	2015	2014
Change in Benefit Obligation:		
Projected benefit obligation at beginning of year	$10,376	$9,775
Service cost	105	78
Interest cost	374	373
Actuarial losses	1,372	1,084
Benefits paid	(549)	(934)
Projected benefit obligation at end of year	$11,678	$10,376
Accumulated Benefit Obligation	$10,967	$9,748
Discount rate used to value the ending benefit obligations:	3.75 %	3.75 %
Amounts recognized in the consolidated balance sheet:		
Current liabilities	$749	$724
Noncurrent liabilities	10,929	9,652
Total amounts recognized	$11,678	$10,376
Amounts recognized in accumulated other comprehensive income:		
Transition obligation	$127	$170
Actuarial loss	4,223	3,046
Net amount recognized	$4,350	$3,216
Total recognized in net periodic benefit cost and accumulated other comprehensive income:	$1,851	$1,535

	2015	2014	2013
Components of Net Periodic Pension Cost:			
Service cost	$105	$78	$71
Interest cost	374	373	350
Amortization of transition obligation	42	42	42
Amortization of other loss	195	123	81
Net periodic pension cost	$716	$616	$544

Assumptions used to determine net periodic pension cost:			
Discount rate	3.75%	3.75%	4.25%
Increase in future compensation levels	3.00%	3.00%	3.00%

Estimated Future Benefit Payments (with mortality):	
Fiscal 2016	749
Fiscal 2017	717
Fiscal 2018	684
Fiscal 2019	652
Fiscal 2020	619
Fiscal 2021 through 2024	4,442

Of the $4,350 recognized in accumulated other comprehensive income at November 28, 2015, $42 of net transition obligation and $323 of net loss are expected to be recognized as components of net periodic pension cost during fiscal 2016.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Deferred Compensation Plan

We have an unfunded Deferred Compensation Plan that covers one current and certain former executives and provides for voluntary deferral of compensation. This plan has been frozen with no additional participants or benefits permitted. We recognized expense of $248, $134, and $288 in fiscal 2015, 2014, and 2013, respectively, associated with the plan. The expense for fiscal 2014 is net of a credit to income of $124 due to a change in our estimate of the future obligation of a former employee. Our liability under this plan was $2,085 and $2,174 as of November 28, 2015 and November 29, 2014, respectively. The non-current portion of this obligation is included in post-employment benefit obligations in our consolidated balance sheets, with the current portion included in accrued compensation and benefits.

Defined Contribution Plan

We have a qualified defined contribution plan (Employee Savings/Retirement Plan) that covers substantially all employees who elect to participate and have fulfilled the necessary service requirements. Employee contributions to the Plan are matched at the rate of 20% of up to 8% of gross pay, regardless of years of service. Expense for employer matching contributions was $662, $397 and $340 during fiscal 2015, 2014 and 2013, respectively. The increase in contribution expense for fiscal 2015 over prior years was largely due to an increase in the matching rate from 15% in 2014 to 20% in 2015, as well as the acquisition of Zenith.

12. **Accumulated Other Comprehensive Loss**

The activity in accumulated other comprehensive loss for the fiscal years ended November 28, 2015 and November 29, 2014, which is comprised solely of post-retirement benefit costs related to our SERP, is as follows:

Balance at November 30, 2013	$(1,414)
Actuarial losses	(1,084)
Net pension amortization reclassified from accumulated other comprehensive loss	166

Tax effects	358
Balance at November 29, 2014	(1,974)
Actuarial losses	(1,372)
Net pension amortization reclassified from accumulated other comprehensive loss	237
Tax effects	431
Balance at November 28, 2015	$(2,678)

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

13. **Capital Stock and Stock Compensation**

We account for our stock-based employee and director compensation plans in accordance with ASC 718, *Compensation – Stock Compensation*. ASC 718 requires recognition of the cost of employee services received in exchange for an award of equity instruments in the financial statements over the period the employee is required to perform the services in exchange for the award (presumptively the vesting period) which we recognize on a straight-line basis. Compensation expense related to restricted stock and stock options included in selling, general and administrative expenses in our consolidated statements of income for fiscal 2015, 2014 and 2013 was as follows:

	2015	2014	2013
Stock based compensation expense	$894	$951	$728

Stock Option Plans

In 1997, we adopted an Employee Stock Plan (the "1997 Plan"), and reserved for issuance 950,000 shares of common stock. An additional 500,000 shares of common stock were authorized for issuance in 2000. In addition, the terms of the 1997 Plan allow for the re-issuance of any stock options which have been forfeited before being exercised. Options granted under the 1997 Plan may be for such terms and exercised at such times as determined by the Organization, Compensation, and Nominating Committee of the Board of Directors. Vesting periods typically range from one to three years. There are no shares available for grant under the 1997 Plan at November 28, 2015, however up to 500,000 shares associated with outstanding grants under the 1997 Plan may become available for grant under the 2010 Plan (see below).

On April 14, 2010, our shareholders approved the Bassett Furniture Industries, Incorporated 2010 Stock Incentive Plan (the "2010 Plan"). All present and future non-employee directors, key employees and outside consultants for the Company are eligible to receive incentive awards under the 2010 Plan. Our Organization, Compensation and Nominating Committee (the "Compensation Committee") selects eligible key employees and outside consultants to receive awards under the 2010 Plan in its discretion. Our Board of Directors or any committee designated by the Board of Directors selects eligible non-employee directors to receive awards under the 2010 Plan in its discretion. Five hundred thousand (500,000) shares of common stock are reserved for issuance under the 2010 Plan. In addition, up to 500,000 shares that are represented by outstanding awards under the 1997 Employee Stock Plan which are forfeited, expire or are canceled after the effective date of the 2010 Plan will be added to the reserve and may be used for new awards under the 2010 Plan. Participants may receive the following types of incentive awards under the 2010 Plan: stock options, stock appreciation rights, payment shares, restricted stock, restricted stock units and performance shares. Stock options may be incentive stock options or non-qualified stock options. Stock appreciation rights may be granted in tandem with stock options or as a freestanding award. Non-employee directors and outside consultants are eligible to receive restricted stock and restricted stock units only. We expect to issue new common stock upon the exercise of options.

The fair value of each option award is estimated on the date of grant using the Black-Scholes option pricing model. The risk free rate is based on the U.S. Treasury rate for the expected life at the time of grant, volatility is based on the average long-term implied volatilities of peer companies, the expected life is based on the estimated average of the life of options using the simplified method, and forfeitures are estimated on the date of grant based on certain historical data. We utilize the simplified method to determine the expected life of our options due to insufficient exercise activity during recent years as a basis from which to estimate future exercise patterns.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Stock Options

There were no new grants of options made in 2015, 2014 or 2013.

Changes in the outstanding options under our plans during the year ended November 28, 2015 were as follows:

	Number of Shares	**Weighted Average Exercise Price Per Share**
Outstanding at November 29, 2014	437,250	$ 11.94
Granted	-	-
Exercised	(351,000)	12.09
Forfeited/Expired	(2,000)	8.02
Outstanding at November 28, 2015	84,250	11.42
Exercisable at November 28, 2015	84,250	$ 11.42

Changes in the non-vested options under our plans during the year ended November 28, 2015 were as follows:

	Number of Shares	**Weighted Average Grant Date Fair Value Per Share**
Non-vested options outstanding at November 29, 2014	22,750	$ 8.04
Granted	-	-

Vested	(20,750)	8.05
Forfeited/Expired	(2,000)	8.02
Non-vested options outstanding at November 28, 2015	-	-

Additional information regarding our outstanding stock options at November 28, 2015 is as follows:

				Options Outstanding			Options Exercisable	
Range of Exercise Prices				**Shares**	**Weighted Average Remaining Contractual Life (Years)**	**Weighted Average Exercise Price**	**Shares**	**Weighted Average Exercise Price**
$	3.23	-	$6.45	1,000	4.6	$ 4.38	1,000	$ 4.38
$	6.45	-	$9.67	22,750	5.6	8.02	22,750	8.02
$	9.68	-	$12.90	28,000	1.9	10.60	28,000	10.60
$	12.91	-	$16.13	32,500	1.4	14.73	32,500	14.73
				84,250			84,250	
Aggregate intrinsic value				$ 1,714			$ 1,714	

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Additional information regarding activity in our stock options during fiscal 2015, 2014 and 2013 is as follows:

	2015	**2014**	**2013**
Total intrinsic value of options exercised	$5,934	$236	$387
Total fair value of options vested	87	200	363
Total cash received from the exercise of options	4,031	382	413
Excess tax benefits recognized as additional paid-in capital upon the exercise of options	1,899	72	106

Restricted Shares

Changes in the outstanding non-vested restricted shares during the year ended November 28, 2015 were as follows:

	Number of Shares	**Weighted Average Grant Date Fair Value Per Share**
Non-vested restricted shares outstanding at November 29, 2014	123,737	$ 15.28
Granted	54,354	21.81
Vested	(26,337)	15.42
Forfeited	(17,600)	17.00
Non-vested restricted shares outstanding at November 28, 2015	134,154	$ 17.68

Restricted share awards granted in fiscal 2015 included the grant of 46,000 shares on January 14, 2015 which were subject to a performance condition as well as a service condition. The performance condition was based on a measure of the Company’s operating cash flow for 2014 and has now been satisfied. They will remain subject to an additional two-year service requirement and will vest on the third anniversary of the grant. The remaining grants for 2015 consisted of 6,354 restricted shares granted to our non-employee directors on April 1, 2015 which will vest on the first anniversary of the grant, and 2,000 shares granted to an employee on July 14, 2015 which will vest on the third anniversary of the grant.

During fiscal 2015, 26,337 restricted shares were vested and released, of which 13,998 shares had been granted to employees and 12,339 shares to directors. Of the shares released to employees, 4,836 shares were withheld by the Company to cover withholding taxes of $154. During fiscal 2014 and 2013, 31,234 shares and 11,550 shares, respectively, were withheld to cover withholding taxes of $489 and $202, respectively, arising from the vesting of restricted shares. Excess tax benefits of $99, $228 and $207 were recognized during fiscal 2015, 2014 and 2013, respectively, as additional paid-in capital upon the release of vested shares.

Additional information regarding our outstanding non-vested restricted shares at November 28, 2015 is as follows:

Grant Date	**Restricted Shares Outstanding**	**Share Value at Grant Date Per Share**	**Remaining Restriction Period (Years)**
July 17, 2013	37,800	$16.64	2.6
January 15, 2014	48,000	14.12	1.1
January 14, 2015	40,000	20.21	2.1
April 1, 2015	6,354	28.33	0.3
July 14, 2015	2,000	38.02	2.6
	134,154		

Unrecognized compensation cost related to these non-vested restricted shares at November 28, 2015 is $636, expected to be recognized over approximately a two and one-half year period.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

Employee Stock Purchase Plan

In 2000, we adopted and implemented an Employee Stock Purchase Plan (“ESPP”) that allows eligible employees to purchase a limited number of shares of our stock at 85% of market value. Under the ESPP we sold 19,053, 25,677 and 38,206 shares to employees in fiscal 2015, 2014 and 2013, respectively, which resulted in an immaterial amount of compensation expense.

14. **Income Taxes**

The components of the income tax provision (benefit) are as follows:

	2015	2014	2013
Current:			
Federal	$7,972	$4,168	$759
State	1,533	596	50
Deferred:			
Increase (decrease) in valuation allowance	(70)	(974)	136
Federal	1,520	221	1,970
State	480	1,297	176
Total	$11,435	$5,308	$3,091

Excess tax benefits in the amount of $1,998, $300 and $313 were recognized as additional paid-in capital during fiscal 2015, 2014 and 2013, respectively, resulting from the exercise of stock options and the release of restricted shares.

A reconciliation of the statutory federal income tax rate and the effective income tax rate, as a percentage of income before income taxes, is as follows:

	2015	2014	2013
Statutory federal income tax rate	35.0%	35.0%	34.0%
Adjustments to state net operating loss carryforwards	-	3.3	-
Change in income tax valuation allowance	(0.1)	(3.7)	1.7
Change in income tax reserves	0.1	(1.7)	0.1
State income tax, net of federal benefit	4.4	4.9	3.7
Benefit of goodwill basis difference	(3.2)	-	-
Other	(0.3)	(1.5)	(1.7)
Effective income tax rate	35.9%	36.3%	37.8%

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

The income tax effects of temporary differences and carryforwards, which give rise to significant portions of the deferred income tax assets and deferred income tax liabilities, are as follows:

	November 28, 2015	**November 29, 2014**
Deferred income tax assets:		
Trade accounts receivable	$ 506	$ 483
Inventories	2,420	2,384
Notes receivable	1,795	1,599
Retirement benefits	6,992	6,093
State net operating loss carryforwards	927	1,141
Unrealized loss from affiliates	356	595
Lease termination accruals	219	167
Net deferred rents	2,674	2,251
Other	1,946	1,699
Gross deferred income tax assets	17,835	16,412
Valuation allowance	-	(70)
Total deferred income tax assets	17,835	16,342
Deferred income tax liabilities:		
Property and equipment	3,093	282
Intangible assets	860	-
Unrealized gains from affiliates	8	963
Prepaid expenses and other	403	128
Total deferred income tax liabilities	4,364	1,373
Net deferred income tax assets	$ 13,471	$ 14,969

At the beginning of fiscal 2014 we carried a valuation allowance of $1,044 which was primarily related to state net operating loss carryforwards for which it was considered to be more likely than not that they would not be utilized prior to their expiration. During fiscal 2014 we reduced our valuation allowance related to adjustments to state net operating loss carryforwards primarily due to state tax law changes resulting in a credit to income of $974, or $0.09 per basic and diluted share. The remaining balance in the valuation allowance at November 28, 2015 and November 29, 2014 was $0 and $70, respectively.

The following table represents a summary of the valuation allowances against deferred tax assets:

	2015	2014	2013
Balance, beginning of the year	$70	$1,044	$908
Additions charged to expense		-	136
Deductions reducing expense	(70)	(974)	-
Balance, end of the year	$-	$70	$1,044

We have state net operating loss carryforwards available to offset future taxable state income of $12,715, which expire in varying amounts between 2015 and 2030. Realization is dependent on generating sufficient taxable income prior to expiration of the loss carryforwards.

Income taxes paid, net of refunds received, during 2015, 2014 and 2014 were $5,906, $2,367, and $2,723, respectively.

As of November 29, 2014, the gross amount of unrecognized tax benefits was approximately $1,236, exclusive of interest and penalties. Substantially all of this balance, along with additional amounts recognized during fiscal 2015, has been effectively settled as of November 28, 2015. We regularly evaluate, assess and adjust the related liabilities in light of changing facts and circumstances, which could cause the effective tax rate to fluctuate from period to period.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

The following table summarizes the activity related to our gross unrecognized tax benefits:

	2015	2014	2013
Balance, beginning of the year	$1,236	$1,497	$1,228
Gross increases	12	-	401
Gross decreases due to settlements	(1,236)	(221)	-
Gross decreases primarily due to the expiration of statutes	-	(40)	(132)
Balance, end of the year	$12	$1,236	$1,497

We recognize interest and penalties related to unrecognized tax benefits in income tax expense. During fiscal 2015, 2014, and 2013, we recognized $(144), $7, and $23 of interest expense recovery and $3, $10, and $31 of penalty recovery (expense), respectively, related to the unrecognized benefits noted above in our consolidated statements of income. At November 28, 2015 and November 29, 2014, the balance of accrued interest and penalties associated with unrecognized tax benefits was not material. At November 29, 2014, $1,370 was included in other accrued liabilities in our consolidated balance sheet representing the entire amount of our gross unrecognized tax benefits along with the accrued interest and penalties thereon. The balance at November 28, 2015 was not material.

Significant judgment is required in evaluating the Company's federal and state tax positions and in the determination of its tax provision. Despite our belief that the liability for unrecognized tax benefits is adequate, it is often difficult to predict the final outcome or the timing of the resolution of any particular tax matter. We may adjust these liabilities as relevant circumstances evolve, such as guidance from the relevant tax authority, or resolution of issues in the courts. These adjustments are recognized as a component of income tax expense in the period in which they are identified. The Company also cannot predict when or if any other future tax payments related to these tax positions may occur.

We remain subject to examination for tax years 2012 through 2014 for all of our major tax jurisdictions. The examination of our 2012 and 2013 federal tax returns was completed in 2015 and did not result in a significant adjustment to income tax expense.

The IRS released the final and re-proposed tangible property regulations in September of 2013. While the regulations are now final, they were effective for tax years beginning on or after January 1, 2014, which for the Company was fiscal 2015. We comply with the regulations and the related administrative procedures. The regulations did not have a significant impact on our financial statements.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

15. **Restructuring, asset impairment, and other charges**

Asset Impairment Charges and Lease Exit Costs

During fiscal 2015 income from operations included $106 of non-cash asset impairment charges and a $419 charge for the accrual of lease exit costs, both incurred in connection with the closing of our Company-owned retail store location in Memphis, Tennessee.

There were no asset impairment charges or lease exit costs incurred against income from operations during fiscal 2014 or 2013. See Note 2 regarding non-operating impairment charges incurred in connection with our investments in retail real estate.

Management Restructuring Costs

During the year ended November 28, 2015, we recognized $449 of expense related to severance payable to a former executive, who left the Company in April, 2015. As of November 28, 2015, all required payments of severance have been disbursed. These management restructuring costs were incurred within our wholesale segment. There were no restructuring charges incurred in fiscal 2014 or 2013.

The following table summarizes the activity related to our accrued lease exit costs:

	2015	2014
Balance, beginning of the year	$433	$907
Provisions associated with Company-owned retail stores	419	-
Provisions made to adjust previous estimates	111	14

Payments on unexpired leases, net of sublease rent received	(410)	(510)
Accretion of interest on obligations	13	22
Balance, end of the year	$566	$433
Current portion included in other accrued liabilities	$351	$117
Long-term portion included in other long-term liabilities	215	316
	$566	$433

16. **Income from the Continued Dumping and Subsidy Offset Act**

During the year ended November 28, 2015, we recognized income of $1,156 arising from distributions received from U.S. Customs and Border Protection (“Customs”) under the Continued Dumping and Subsidy Offset Act of 2000 (“CDSOA”). These distributions primarily represent amounts previously withheld by Customs pending the resolution of claims filed by certain manufacturers who did not support the antidumping petition (“Non-Supporting Producers”) challenging certain provisions of the CDSOA and seeking to share in the distributions. The Non-Supporting Producers’ claims were dismissed by the courts and all appeals were exhausted in 2014. While it is possible that we may receive additional distributions from Customs, we cannot estimate the likelihood or amount of any future distributions.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

17. **Leases and Lease Guarantees**

Leases

We lease land and buildings that are used in the operation of our Company-owned retail stores as well as in the operation of certain of our licensee-owned stores, and we lease land and buildings at various locations throughout the continental United States for warehousing and distribution hubs used in our logistical services segment. We also lease tractors, trailers and local delivery trucks used in our logistical services segment. Our real estate lease terms range from one to 15 years and generally have renewal options of between five and 15 years. Some store leases contain contingent rental provisions based upon sales volume. Our transportation equipment leases have terms ranging from two to seven years with fixed monthly rental payments plus variable charges based upon mileage. The following schedule shows future minimum lease payments under non-cancellable operating leases with terms in excess of one year as of November 25, 2015:

	Retail Stores	**Distribution Centers**	**Transportation Equipment**	**Total**
Fiscal 2016	$18,490	$ 4,087	$ 2,779	$25,356
Fiscal 2017	16,651	3,946	1,979	22,576
Fiscal 2018	14,140	2,696	806	17,642
Fiscal 2019	12,251	1,731	755	14,737
Fiscal 2020	10,916	1,230	671	12,817
Thereafter	27,461	4,278	30	31,769
Total future minimum lease payments	$99,909	$ 17,968	$ 7,020	$124,897

Lease expense was $26,382, $19,903 and $18,403 for 2015, 2014, and 2013, respectively.

In addition to subleasing certain of these properties, we own retail real estate which we in turn lease to licensee operators of BHF stores. We also own real estate for closed stores which we lease to non-licensees. The following schedule shows minimum future rental income related to pass-through rental expense on subleased property as well as rental income on real estate owned by Bassett.

Fiscal 2016	$2,132
Fiscal 2017	2,119
Fiscal 2018	1,589
Fiscal 2019	1,247
Fiscal 2020	1,194
Thereafter	359
Total minimum future rental income	$8,640

Real estate rental income (loss), net of expense (including lease costs, depreciation, insurance, and taxes), related to licensee stores and other investment real estate, was $(181), $(248) and $(594) in 2015, 2014 and 2013, respectively, and is reflected in other expense, net in the accompanying consolidated statements of income.

Guarantees

As part of the strategy for our store program, we have guaranteed certain lease obligations of licensee operators. Lease guarantees range from one to ten years. We were contingently liable under licensee lease obligation guarantees in the amount of $2,494 and $3,164 at November 28, 2015 and November 29, 2014, respectively.

In the event of default by an independent dealer under the guaranteed lease, we believe that the risk of loss is mitigated through a combination of options that include, but are not limited to, arranging for a replacement dealer, liquidating the collateral, and pursuing payment under the personal guarantees of the independent dealer. The proceeds of the above options are estimated to cover the maximum amount of our future payments under the guarantee obligations, net of reserves. The fair value of lease guarantees (an estimate of the cost to the Company to perform on these guarantees) at November 28, 2015 and November 29, 2014, were not material.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

18. **Contingencies**

We are involved in various claims and actions, including environmental matters, which arise in the normal course of business. Although the final outcome of these matters cannot be determined, based on the facts presently known, it is our opinion that the final resolution of these matters will not have a material adverse effect on our financial position or future results of operations.

19. **Earnings Per Share**

The following table sets forth the computation of basic and diluted earnings per share:

	2015	**2014**	**2013**
Numerator:			
Net income	$20,433	$9,299	$5,096
Denominator:			
Denominator for basic income per share - weighted average shares	10,701,829	10,552,462	10,721,652
Effect of dilutive securities	141,198	140,569	150,897
Denominator for diluted income per share — weighted average shares and assumed conversions	10,843,027	10,693,031	10,872,549
Basic income per share:			
Net income per share — basic	$1.91	$0.88	$0.48
Diluted income per share:			
Net income per share — diluted	$1.88	$0.87	$0.47

For fiscal 2015, 2014 and 2013, the following potentially dilutive shares were excluded from the computations as there effect was anti-dilutive:

	2015	2014	2013
Stock options	-	150,000	472,500
Unvested restricted shares	8,354	-	81,295
Total anti-dilutive securities	8,354	150,000	553,795

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Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

20. **Segment Information**

We have strategically aligned our business into three reportable segments as defined in ASC 280, *Segment Reporting*, and as described below:

Wholesale. The wholesale home furnishings segment is involved principally in the design, manufacture, sourcing, sale and distribution of furniture products to a network of Bassett stores (Company-owned and licensee-owned stores retail stores) and independent furniture retailers. Our wholesale segment includes our wood and upholstery operations as well as all corporate selling, general and administrative expenses, including those corporate expenses related to both Company- and licensee-owned stores.

Retail – Company-owned stores. Our retail segment consists of Company-owned stores and includes the revenues, expenses, assets and liabilities and capital expenditures directly related to these stores.

Logistical services. With our acquisition of Zenith on February 2, 2015, we created the logistical services operating segment which reflects the operations of Zenith. In addition to providing shipping, delivery and warehousing services for the Company, Zenith also provides similar services to other customers, primarily in the furniture industry. Revenue from the performance of these services to other customers is included in logistics revenue in our condensed consolidated statement of income. Zenith's operating costs are included in selling, general and administrative expenses and total $73,722 for the year ended November 28, 2015 since the date of acquisition. Amounts charged by Zenith to the Company for logistical services prior to the date of acquisition are included in selling, general and administrative expenses, and our equity in the earnings of Zenith prior to the date of acquisition is included in other loss, net, in the accompanying statements of income.

Inter-company sales elimination represents the elimination of wholesale sales to our Company-owned stores and the elimination of Zenith logistics revenue from our wholesale and retail segments. Inter-company income elimination includes the embedded wholesale profit in the Company-owned store inventory that has not been realized. These profits will be recorded when merchandise is delivered to the retail consumer. The inter-company income elimination also includes rent paid by our retail stores occupying Company-owned real estate, and the elimination of shipping and handling charges from Zenith for services provided to our wholesale and retail operations.

Prior to the beginning of fiscal 2015, our former investments and real estate segment included our short-term investments, our holdings of retail real estate previously leased as licensee stores, and our former equity investment in Zenith prior to acquisition. This segment has been eliminated and the assets formerly reported therein are now considered to be part of our wholesale segment. The earnings and costs associated with these assets, including our equity in the income of Zenith prior to the date of acquisition, will continue to be included in other loss, net, in our condensed consolidated statements of income.

Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

The following table presents segment information for each of the last three fiscal years:

	2015	2014	2013
Net Sales			
Wholesale	$252,180	$223,993	$215,451
Retail	249,379	216,631	199,380
Logistical services	77,250	-	-
Inter-company eliminations:			
Furniture and accessories	(114,154)	(99,886)	(93,545)
Logistical services	(33,728)	-	-
Consolidated	$430,927	$340,738	$321,286
Income (loss) from Operations			
Wholesale	$15,618	$14,120	$10,883
Retail	6,170	(528)	(1,452)
Logistical services	3,528	-	-
Inter-company elimination	1,647	1,539	574
Lease exit costs	(419)	-	-
Asset impairment charges	(106)	-	-
Management restructuring costs	(449)	-	-
Consolidated income from operations	$25,989	$15,131	$10,005
Depreciation and Amortization			
Wholesale	$2,075	$1,972	$1,826
Retail	5,428	5,344	4,372
Logistical services	2,634	-	-
Consolidated	$10,137	$7,316	$6,198
Capital Expenditures			
Wholesale	$4,898	$4,527	$3,839
Retail	7,077	13,836	10,846
Logistical services	1,999	-	-
Consolidated	$13,974	$18,363	$14,685
Identifiable Assets			
Wholesale	$146,878	$154,319	$148,518
Retail	88,878	86,471	77,331
Logistical services	46,787	-	-

Consolidated	$282,543	$240,746	$225,849

A breakdown of wholesale sales by product category for each of the last three fiscal years is provided below:

	2015	**2014**	**2013**
Wood	37 %	39 %	41 %
Upholstery	63 %	61 %	59 %
	100 %	100 %	100 %

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Notes to Consolidated Financial Statements -Continued

(In thousands, except share and per share data)

21. **Quarterly Results of Operations**

	2015 First Quarter (1)	**Second Quarter (2)**	**Third Quarter**	**Fourth Quarter (3)**
Sales revenue:				
Furniture and accessories	$89,548	$99,467	$97,107	$101,283
Logistics	3,259	12,086	13,904	14,273
Total sales revenue	92,807	111,553	111,011	115,556
Cost of furniture and accessories sold	41,930	46,921	44,824	45,616
Income from operations	2,877	6,714	7,692	8,706
Net income	5,956	4,529	4,266	5,682
Basic earnings per share	0.57	0.42	0.39	0.53
Diluted earnings per share	0.56	0.42	0.39	0.52

	2014 First Quarter (4)	**Second Quarter**	**Third Quarter**	**Fourth Quarter**
Sales revenue:				
Furniture and accessories	$75,647	$85,185	$85,186	$94,720
Logistics	-	-	-	-
Total sales revenue	75,647	85,185	85,186	94,720
Cost of furniture and accessories sold	35,394	39,872	40,168	42,883
Income from operations	1,086	3,891	3,399	6,755
Net income	843	2,551	2,256	3,649
Basic earnings per share	0.08	0.24	0.22	0.35
Diluted earnings per share	0.08	0.24	0.21	0.35

All quarters shown above for fiscal 2015 and 2014 consist of 13 week fiscal periods.

Sales revenue from logistics is recognized from the date of our acquisition of Zenith, February 2, 2015. Prior to the acquisition of Zenith, net income included our 49% equity in the earnings of Zenith, which is included in other loss, net in our consolidated statements of income.

(1) Income from operations includes asset impairment charges and lease exit costs totaling $525 (see Note 15). Net income includes a gain of $7,212, net of income tax effects of approximately $2,777, resulting from the remeasurement of our prior ownership interest in Zenith upon acquisition (see Note 3).
(2) Income from operations includes management restructuring charges of $449 (see Note 15). Net income includes income of $1,066 from the CDSOA, net of related income tax effects of approximately $410 (see Note 16).
(3) Net income includes the effect of a $1,111 tax benefit arising from purchase accounting adjustments relating to the gain recorded on the remeasurement of our prior ownership in Zenith.
(4) Net income includes $662 of income from death benefits from life insurance policies covering a former executive.

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

None.

ITEM 9A. CONTROLS AND PROCEDURES

As of the end of the period covered by this Annual Report on Form 10-K, our principal executive officer and principal financial officer have evaluated the effectiveness of our “disclosure controls and procedures” (“Disclosure Controls”). Disclosure Controls, as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), are procedures that are designed with the objective of ensuring that information required to be disclosed in our reports filed under the Exchange Act, such as this Annual Report, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure Controls are also designed with the objective of ensuring that such information is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Our management, including the CEO and CFO, does not expect that our Disclosure Controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based upon their controls evaluation, our CEO and CFO have concluded that our Disclosure Controls are effective at a reasonable assurance level.

We are responsible for establishing and maintaining adequate internal control over financial reporting in accordance with Exchange Act Rule 13a-15. With the participation of our CEO and CFO, our management conducted an evaluation of the effectiveness of our internal control over financial reporting as of November 28, 2015 based on the criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The scope of our efforts to comply with Section 404 of the Sarbanes-Oxley Act with respect to fiscal 2015 included all of our operations other than those we acquired in fiscal 2015 related to the acquisition of Zenith Freight Lines, LLC (“Zenith”). In accordance with the SEC’s published guidance, because we acquired the operations of Zenith during the fiscal year, we excluded these operations from our efforts to comply with Section 404 Rules with respect to fiscal 2015. Total assets as of November 28, 2015 and total revenues for the year ending November 28, 2015 for Zenith were $30,836 and $43,522, respectively. SEC rules require that we complete our assessment of the internal control over financial reporting of the acquisition within one year after the date of the acquisition. Based on this evaluation, excluding the operations of Zenith discussed above, management concluded that our internal control over financial reporting was effective as of November 28, 2015, based on those criteria. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

Ernst & Young LLP, the Company’s independent registered public accounting firm, has issued an attestation report on the effectiveness of the Company’s internal control over financial reporting.

Changes in internal control over financial reporting.

There have been no changes in our internal controls over financial reporting during our fourth fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of Bassett Furniture Industries, Incorporated and Subsidiaries

We have audited Bassett Furniture Industries, Incorporated and Subsidiaries' internal control over financial reporting as of November 28, 2015, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). Bassett Furniture Industries, Incorporated and Subsidiaries' management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

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

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

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

As indicated in the accompanying Management’s Report on Internal Control over Financial Reporting, management’s assessment of and conclusion on the effectiveness of internal control over financial reporting did not include the internal controls of Zenith Freight Lines, LLC, which is included in the 2015 consolidated financial statements of Bassett Furniture Industries, Incorporated and Subsidiaries and constituted $30.8 million of total assets as of November 28, 2015 and $43.5 million of revenues for the year then ended. Our audit of internal control over financial reporting of Bassett Furniture Industries, Incorporated and Subsidiaries also did not include an evaluation of the internal control over financial reporting of Zenith Freight Lines, LLC.

In our opinion, Bassett Furniture Industries, Incorporated and Subsidiaries maintained, in all material respects, effective internal control over financial reporting as of November 28, 2015, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Bassett Furniture Industries, Incorporated and Subsidiaries as of November 28, 2015 and November 29, 2014, and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended November 28, 2015 of Bassett Furniture Industries, Incorporated and Subsidiaries and our report dated January 21, 2016 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Richmond, Virginia

January 21, 2016

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information to be contained in the Proxy Statement under the captions “Election of Directors,” “Board and Board Committee Information,” and “Section 16(a) Beneficial Ownership Reporting Compliance” is incorporated herein by reference thereto. Please see section entitled “Executive Officers of the Registrant” in Item 4b of Part I of this report for information concerning executive officers.

The Registrant has a code of ethics that applies to all of its employees, officers and directors. The code of ethics is available on the Registrant’s website at www.bassettfurniture.com and the Registrant will post any amendments to, or waivers, from, the code of ethics on that website.

ITEM 11. EXECUTIVE COMPENSATION

The information to be contained in the Proxy Statement under the captions “Organization, Compensation and Nominating Committee Report,” “Compensation Discussion and Analysis,” “Executive Compensation,” and “Director Compensation” is incorporated herein by reference thereto.

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

The information to be contained in the Proxy Statement under the headings “Principal Stockholders and Holdings of Management” and “Equity Compensation Plan Information” is incorporated herein by reference thereto.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information to be contained in the Proxy Statement under the captions "Board and Board Committee Information" and "Other Transactions" is incorporated herein by reference thereto.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information to be contained in the Proxy Statement under the caption "Audit and Other Fees" is incorporated herein by reference thereto.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a)(1) (a)Bassett Furniture Industries, Incorporated and Subsidiaries Audited Consolidated Financial Statements for the years ended November 28, 2015, November 29, 2014 and November 30, 2013.

(2) Financial Statement Schedule:

Schedule II- Analysis of Valuation and Qualifying Accounts for the years ended November 28, 2015, November 29, 2014 and November 26, 2011

(3) Listing of Exhibits

3A.	Articles of Incorporation as amended are incorporated herein by reference to Form 10-Q for the fiscal quarter ended February 28, 1994.
3B.	By-laws as amended to date are incorporated herein by reference to Exhibit 3b to Form 10-Q for the fiscal quarter ended August 25, 2012, filed October 4, 2012.
4.	Fourth Amended and Restated Credit Agreement with BB&T dated December 9, 2012 and First Amendment to Fourth Amended and Restated Credit Agreement with BB&T dated December 18, 2012. Registrant hereby agrees to furnish the SEC, upon request, other instruments defining the rights of holders of long-term debt of the Registrant.
*10A.	Bassett 1993 Long Term Incentive Stock Option Plan is incorporated herein by reference to the Registrant's Registration Statement on Form S-8 (no.33-52405) filed on February 25, 1994.
*10B.	Bassett Executive Deferred Compensation Plan is incorporated herein by reference to Form 10-K for the fiscal year ended November 30, 1997.
*10C.	Bassett Supplemental Retirement Income Plan is incorporated herein by reference to Form 10-K for the fiscal year ended November 30, 1997.
*10E.	Bassett 1997 Employee Stock Plan is incorporated herein by reference to the Registrant's Registration Statement on Form S-8 (no. 333-60327) filed on July 31, 1998.
*10F.	Bassett Furniture 2005 Non-Employee Directors Stock Incentive Plan is incorporated herein by reference to the Registrant's definitive proxy statement on Schedule 14A filed on January 28, 2005.
*10G.	Bassett Furniture 2005 Non-Employee Directors Stock Incentive Form Grant Letter for Restricted Stock Award is incorporated herein by reference to Form 10-K for the fiscal year ended November 26, 2005.

*10H.	Bassett Furniture Directors Compensation is incorporated herein by reference to Form 10-K for the fiscal year ended November 26, 2005.
*10I.	Bassett Furniture Industries, Inc. 1997 Employee Stock Plan Form Stock Option Award Agreement is incorporated herein by reference to Form 10-K for the fiscal year ended November 26, 2005.
*10J.	Bassett Furniture Industries, Inc. 1997 Employee Stock Plan Form Grant Letter for Restricted Stock Award is incorporated herein by reference to Form 10-K for the fiscal year ended November 26, 2005.
*10K.	Bassett Furniture Industries, Inc. 2010 Stock Incentive Plan is incorporated herein by reference to Form 8-K filed on April 14, 2010.
*10L.	Form of Performance Share Award Agreement, Restricted Stock Award Agreement and Stock Option Award Agreement under the Bassett Furniture Industries, Inc. 2010 Stock Incentive Plan is incorporated herein by reference to Form 10-K for the fiscal year ended November 29, 2014.
*10M.	Schedule of Terms for Employment Continuity Agreements with Certain Executive Officers is incorporated herein by reference to Form 10-Q for the quarterly period ended March 1, 2014.
*10N.	Restated Supplemental Retirement Income Plan, effective May 1, 2014, is incorporated herein by reference to Form 10-Q for the quarterly period ended May 31, 2014.

21.	List of subsidiaries of the Registrant
23A.	Consent of Independent Registered Public Accounting Firm
31A.	Certification of Robert H. Spilman, Jr., President and Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31B.	Certification of J. Michael Daniel, Senior Vice President and Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32A.	Certification of Robert H. Spilman, Jr., President and Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32B.	Certification of J. Michael Daniel, Senior Vice President and Chief Financial Officer, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.	The following financial statements from the Company's Annual Report on Form 10-K for the year ended November 28, 2015, formatted in Extensible Business Reporting Language ("XBRL"): (i) consolidated balance sheets, (ii) consolidated statements of operations, (iii) consolidated statements of cash flows, (iv) consolidated statements of stockholders' equity, and (v) the notes to the consolidated financial statements, tagged as blocks of text.
101.INS**	XBRL Instance
101.SCH**	XBRL Taxonomy Extension Schema
101.CAL**	XBRL Taxonomy Extension Calculation
101.DEF**	XBRL Taxonomy Extension Definition
101.LAB**	XBRL Taxonomy Extension Labels
101.PRE**	XBRL Taxonomy Extension Presentation

* Management contract or compensatory plan or arrangement of the Company.

** XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

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 to be signed on its behalf by the undersigned, thereunto duly authorized.

BASSETT FURNITURE INDUSTRIES, INCORPORATED (Registrant)

By: /s/ Robert H. Spilman, Jr. Date: January 21, 2016
Robert H. Spilman, Jr.

President and Chief Executive Officer

Director

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

By: /s/ Paul Fulton Date: January 21, 2016
Paul Fulton

Chairman of the Board of Directors

By: /s/ Peter W. Brown Date: January 21, 2016
Peter W. Brown

Director

By: /s/ Kristina K. Cashman Date: January 21, 2016
Kristina K. Cashman

Director

By: /s/ Howard H. Haworth Date: January 21, 2016
Howard H. Haworth

Director

By: /s/ George W. Henderson, III Date: January 21, 2016
George W. Henderson, III

Director

By: /s/ J. Walter McDowell Date: January 21, 2016
J. Walter McDowell
Director

By: /s/ Dale C. Pond Date: January 21, 2016
Dale C. Pond

Director

By: /s/ William C. Wampler, Jr. Date: January 21, 2016
William C. Wampler, Jr.

Director

By: /s/ William C. Warden, Jr. Date: January 21, 2016
William C. Warden, Jr.

Director

By: /s/ J. Michael Daniel Date: January 21, 2016
J. Michael Daniel

Senior Vice President and Chief Financial Officer

(Principal Financial and Accounting Officer)

Bassett Furniture Industries, Incorporated
Schedule II

Analysis of Valuation and Qualifying Accounts
For the Years Ended November 28, 2015, November 29, 2014 and November 30, 2013
(amounts in thousands)

	Balance Beginning of Period	Additions Charged to Cost and Expenses	Deductions (1)	Other	Balance End of Period
For the Year Ended November 30, 2013:					
Reserve deducted from assets to which it applies					
Allowance for doubtful accounts	$ 1,789	$ 361	$ (543)	$ -	$ 1,607
Notes receivable valuation reserves	$ 4,139	$ -	$ -	$ -	$ 4,139
Income tax valuation allowance	$ 908	$ 136	$ -	$ -	$ 1,044
For the Year Ended November 29, 2014:					
Reserve deducted from assets to which it applies					
Allowance for doubtful accounts	$ 1,607	$ 77	$ (435)	$ -	$ 1,249
Notes receivable valuation reserves	$ 4,139	$ -	$ -	$ -	$ 4,139
Income tax valuation allowance	$ 1,044	$ -	$ (974)	$ -	$ 70
For the Year Ended November 28, 2015:					
Reserve deducted from assets to which it applies					
Allowance for doubtful accounts	$ 1,249	$ (216)	$ (67)	$ 209 (2)	$ 1,175
Notes receivable valuation reserves	$ 4,139	$ 582	$ (75)	$ -	$ 4,646
Income tax valuation allowance	$ 70	$ -	$ (70)	$ -	$ -

(1) Deductions are for the purpose for which the reserve was created. Deductions from the income tax valuation allowance for the year ended November 30, 2013 were due to the removal of the majority of our valuation allowance.
(2) Represents reserves of acquired company at date of acquisition.