UNIFIRST CORP
Form 10-Q
July 09, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended **May 30, 2015**

OR

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

For the transition period from ________________ to ________________

Commission file number: **001-08504**

UNIFIRST CORPORATION

(Exact name of Registrant as Specified in Its Charter)

Massachusetts	**04-2103460**

(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
68 Jonspin Road, Wilmington, MA	**01887**
(Address of Principal Executive Offices)	(Zip Code)

(978) 658-8888
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Smaller Reporting Company Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

The number of outstanding shares of UniFirst Corporation Common Stock and Class B Common Stock at July 3, 2015 were 15,245,588 and 4,854,519, respectively.

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UniFirst Corporation

Quarterly Report on Form 10-Q

For the Quarter ended May 30, 2015

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

UniFirst Corporation and Subsidiaries

Consolidated Statements of Income

(Unaudited)

(In thousands, except per share data)	**Thirteen weeks ended May 30, 2015**	**Thirteen weeks ended May 31, 2014**	**Thirty-nine weeks ended May 30, 2015**	**Thirty-nine weeks ended May 31, 2014**
Revenues	$365,574	$352,238	$1,097,397	$1,042,909
Operating expenses:				
Cost of revenues (1)	221,995	216,644	665,222	640,341
Selling and administrative expenses (1)	72,205	67,996	221,832	203,478
Depreciation and amortization	19,022	18,109	55,851	53,237
Total operating expenses	313,222	302,749	942,905	897,056
Income from operations	52,352	49,489	154,492	145,853
Other (income) expense:				
Interest expense	221	109	648	533
Interest income	(784)	(773)	(2,532)	(2,415)
Foreign exchange loss	72	39	1,323	41
Total other (income) expense	(491)	(625)	(561)	(1,841)
Income before income taxes	52,843	50,114	155,053	147,694
Provision for income taxes	20,344	19,170	59,695	56,641
Net income	$32,499	$30,944	$95,358	$91,053
Income per share – Basic:				
Common Stock	$1.70	$1.62	$4.99	$4.78
Class B Common Stock	$1.36	$1.30	$3.99	$3.82
Income per share – Diluted:				
Common Stock	$1.61	$1.53	$4.72	$4.52

Income allocated to – Basic:				
Common Stock	$25,817	$24,493	$75,650	$71,971
Class B Common Stock	$6,483	$6,127	$18,954	$17,962
Income allocated to – Diluted:				
Common Stock	$32,310	$30,637	$94,644	$89,992
Weighted average number of shares outstanding – Basic:				
Common Stock	15,207	15,102	15,173	15,069
Class B Common Stock	4,773	4,722	4,752	4,701
Weighted average number of shares outstanding – Diluted:				
Common Stock	20,118	19,977	20,057	19,921
Dividends per share:				
Common Stock	$0.0375	$0.0375	$0.1125	$0.1125
Class B Common Stock	$0.0300	$0.0300	$0.0900	$0.0900

(1) Exclusive of depreciation on the Company’s property, plant and equipment and amortization of its intangible assets.

The accompanying notes are an integral part of these

Consolidated Financial Statements.

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UniFirst Corporation and Subsidiaries

Consolidated Statements of Comprehensive Income

(Unaudited)

(In thousands)	**Thirteen weeks ended May 30, 2015**	**Thirteen weeks ended May 31, 2014**	**Thirty-nine weeks ended May 30, 2015**	**Thirty-nine weeks ended May 31, 2014**
Net Income	$32,499	$30,944	$95,358	$91,053
Other comprehensive (loss) income:				
Foreign currency translation adjustments	62	2,338	(16,830)	(2,077)
Pension benefit liabilities, net of income taxes	—	—	(1,266)	—
Change in fair value of derivatives, net of income taxes	219	—	(425)	—
Derivative financial instruments loss reclassified	70	—	70	—
Other comprehensive (loss) income	351	2,338	(18,451)	(2,077)
Comprehensive income	$32,850	$33,282	$76,907	$88,976

The accompanying notes are an integral part of these

Consolidated Financial Statements.

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UniFirst Corporation and Subsidiaries

Consolidated Balance Sheets

(Unaudited)

(In thousands, except share data)	**May 30, 2015**	**August 30, 2014(a)**
Assets		
Current Assets:		
Cash and cash equivalents	$235,672	$191,769
Receivables, less reserves of $9,050 and $5,114, respectively	157,871	152,523
Inventories	83,897	78,858
Rental merchandise in service	144,535	146,449
Prepaid and deferred income taxes	5,336	13,342
Prepaid expenses and other current assets	16,523	6,349
Total current assets	643,834	589,290
Property, plant and equipment:		
Land, buildings and leasehold improvements	400,236	393,584
Machinery and equipment	534,916	512,842
Motor vehicles	192,466	166,573
Total property, plant and equipment	1,127,618	1,072,999
Less -- accumulated depreciation	612,137	586,717
Total property, plant and equipment, net	515,481	486,282
Goodwill	313,670	303,648
Customer contracts, net	39,221	40,210
Other intangible assets, net	1,095	1,267
Deferred income taxes	1,237	1,403
Other assets	3,070	2,061
Total assets	$1,517,608	$1,424,161
Liabilities and shareholders' equity		
Current liabilities:		
Loans payable and current maturities of long-term debt	$3,376	$7,704
Accounts payable	56,542	59,177
Accrued liabilities	105,996	100,818
Accrued and deferred income taxes	22,991	23,342
Total current liabilities	188,905	191,041

Long-term liabilities:		
Long-term debt, net of current maturities	—	155
Accrued liabilities	57,419	50,235
Accrued and deferred income taxes	54,569	48,271
Total long-term liabilities	111,988	98,661
Commitments and contingencies (Note 10)		
Shareholders' equity:		
Preferred stock, $1.00 par value; 2,000,000 shares authorized; no shares issued and outstanding	—	—
Common Stock, $0.10 par value; 30,000,000 shares authorized; 15,245,588 and 15,189,947 issued and outstanding as of May 30, 2015 and August 30, 2014, respectively	1,525	1,519
Class B Common Stock, $0.10 par value; 20,000,000 shares authorized; 4,854,519 and 4,860,519 issued and outstanding as of May 30, 2015 and August 30, 2014, respectively	485	486
Capital surplus	66,912	59,415
Retained earnings	1,168,777	1,075,572
Accumulated other comprehensive (loss) income	(20,984)	(2,533)
Total shareholders' equity	1,216,715	1,134,459
Total liabilities and shareholders' equity	$1,517,608	$1,424,161

(a) Derived from audited financial statements

The accompanying notes are an integral part of these

Consolidated Financial Statements.

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UniFirst Corporation and Subsidiaries

Consolidated Statements of Cash Flows

(Unaudited)

Thirty-nine weeks ended	**May 30,**	**May 31,**
(In thousands)	**2015**	**2014**
Cash flows from operating activities:		
Net income	$95,358	$91,053
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation	49,270	46,432
Amortization of intangible assets	6,581	6,805
Amortization of deferred financing costs	156	156
Share-based compensation	4,413	4,541
Accretion on environmental contingencies	452	537
Accretion on asset retirement obligations	503	756
Deferred income taxes	6,668	(134)
Changes in assets and liabilities, net of acquisitions:		
Receivables	(9,463)	(11,573)
Inventories	(5,714)	4,550
Rental merchandise in service	1,417	(8,882)
Prepaid expenses and other current assets	(7,812)	(2,108)
Accounts payable	(2,106)	(11,445)
Accrued liabilities	10,283	4,874
Prepaid and accrued income taxes	8,408	6,713
Net cash provided by operating activities	158,414	132,275
Cash flows from investing activities:		
Acquisition of businesses, net of cash acquired	(19,815)	(841)
Capital expenditures	(82,272)	(74,466)
Other	(1,160)	480
Net cash used in investing activities	(103,247)	(74,827)
Cash flows from financing activities:		
Proceeds from loans payable and long-term debt	5,401	7,107
Payments on loans payable and long-term debt	(9,580)	(109,383)
Proceeds from exercise of Common Stock options, including excess tax benefits	8,055	5,630
Taxes withheld and paid related to net share settlement of equity awards	(5,002)	(3,527)
Payment of cash dividends	(2,151)	(2,145)
Net cash used in financing activities	(3,277)	(102,318)
Effect of exchange rate changes on cash	(7,987)	(1,588)

Net increase (decrease) in cash and cash equivalents	43,903	(46,458)
Cash and cash equivalents at beginning of period	191,769	197,479
Cash and cash equivalents at end of period	$235,672	$151,021

The accompanying notes are an integral part of these

Consolidated Financial Statements.

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UniFirst Corporation and Subsidiaries

Notes to Consolidated Financial Statements

1. Basis of Presentation

These Consolidated Financial Statements of UniFirst Corporation ("Company") have been prepared, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States ("US GAAP") have been condensed or omitted pursuant to such rules and regulations; however, the Company believes that the information furnished reflects all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair statement of results for the interim period.

It is suggested that these Consolidated Financial Statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended August 30, 2014. There have been no material changes in the accounting policies followed by the Company during the current fiscal year. Results for an interim period are not indicative of any future interim periods or for an entire fiscal year.

2. Recent Accounting Pronouncements

In July 2013, the FASB issued updated accounting guidance on the presentation of unrecognized tax benefits. This update provides that an entity's unrecognized tax benefits, or a portion of its unrecognized tax benefits, should be presented in its financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, with one exception. That exception states that, to the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position, or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. This guidance was effective for annual reporting periods, and any interim periods within those annual periods, that began after December 15, 2013 and was to be applied prospectively, with early adoption permitted. The Company adopted this guidance on August 31, 2014 and the adoption did not have a material impact on its financial statements.

In May 2014, the FASB issued updated accounting guidance for revenue recognition. This update provides a comprehensive new revenue recognition model that requires revenue to be recognized in a manner to depict the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services. This guidance was originally scheduled to be effective for annual reporting periods, and any interim periods within those annual periods, that began after December 15, 2016 and allowed for either full retrospective or modified retrospective application, with early adoption not permitted. Accordingly, the standard will be effective for the Company on August 27, 2017. On April 1, 2015, the FASB voted in favor of proposing a one year delay of the effective date and to permit companies to voluntarily adopt the new standard as of the original effective date. The Company is currently evaluating the adoption method it will apply and the impact that this guidance will have on its financial statements and related disclosures.

In February 2015, the FASB issued updated accounting guidance on consolidation requirements. This update changes the guidance with respect to the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. This guidance is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015, with early adoption permitted. Accordingly, the standard will be effective for the Company on August 28, 2016. The Company expects that adoption of this guidance will not have a material impact on its financial statements.

In April 2015, the FASB issued updated guidance on the presentation of debt issuance costs. This update changes the guidance with respect to presenting such costs in the balance sheet as a direct deduction from the related debt liability rather than as an asset. Amortization of the costs is reported as interest expense. This guidance is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015, with early adoption permitted. Accordingly, the standard will be effective for the Company on August 28, 2016. The Company expects that adoption of this guidance will not have a material impact on its financial statements.

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3. Business Acquisitions

During the thirty-nine weeks ended May 30, 2015, the Company completed four business acquisitions with an aggregate purchase price of approximately $19.8 million. The results of operations of these acquisitions have been included in the Company’s consolidated financial results since their respective acquisition dates. These acquisitions were not significant in relation to the Company’s consolidated financial results and, therefore, pro forma financial information has not been presented.

4. Fair Value Measurements

US GAAP establishes a framework for measuring fair value and establishes disclosure requirements about fair value measurements. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

The fair value hierarchy prescribed under US GAAP contains three levels as follows:

Level 1 –	Quoted prices in active markets for identical assets or liabilities.
Level 2 –	Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
Level 3 –	Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

All financial assets or liabilities that are measured at fair value on a recurring basis (at least annually) have been segregated into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date. The assets or liabilities measured at fair value on a recurring basis are summarized in the tables below (in thousands):

	As of May 30, 2015			
	Level 1	**Level 2**	**Level 3**	**Fair Value**
Assets:				
Cash equivalents	$43,660	$—	$ —	$43,660
Pension plan assets	—	4,691	—	4,691
Total assets at fair value	$43,660	$4,691	$ —	$48,351

Liabilities:				
Foreign currency forward contracts	$—	$577	$—	$577
Total liabilities at fair value	$—	$577	$—	$577

	As of August 30, 2014			
	Level 1	**Level 2**	**Level 3**	**Fair Value**
Assets:				
Cash equivalents	$47,552	$—	$ —	$47,552
Pension plan assets	—	5,008	—	5,008
Total assets at fair value	$47,552	$5,008	$ —	$52,560

The Company’s cash equivalents listed above represent money market securities and are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices. The Company does not adjust the quoted market price for such financial instruments.

The Company’s pension plan assets listed above represent guaranteed deposit accounts that are maintained and operated by Prudential Retirement Insurance and Annuity Company (“PRIAC”). All assets are merged with the general assets of PRIAC and are invested predominantly in privately placed securities and mortgages. At the beginning of each calendar year, PRIAC notifies the Company of the annual rates of interest which will be applied to the amounts held in the guaranteed deposit account during the next calendar year. In determining the interest rate to be applied, PRIAC considers the investment performance of the underlying assets of the prior year; however, regardless of the investment performance the Company is contractually guaranteed a minimum rate of return.

The Company’s foreign currency forward contracts represent contracts the Company has entered into to exchange Canadian dollars for U.S. dollars at fixed exchange rates in order to manage its exposure related to certain forecasted Canadian dollar denominated sales of one of its subsidiaries. These contracts were included in current accrued liabilities as of May 30, 2015. The fair value of the forward contracts is based on similar exchange traded derivatives and are, therefore, included within Level 2 of the fair value hierarchy.

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5. Derivative Instruments and Hedging Activities

The Company uses derivative financial instruments to mitigate its exposure to fluctuations in foreign currencies on certain forecasted transactions denominated in foreign currencies. US GAAP requires that all our derivative instruments be recorded on the balance sheet at fair value. All subsequent changes in a derivative's fair value are recognized in income, unless specific hedge accounting criteria are met.

Derivative instruments that qualify for hedge accounting are classified as a hedge of the variability of cash flows to be received or paid related to a recognized asset, liability or forecasted transaction. Changes in the fair value of a derivative that is highly effective and designated as a cash flow hedge are recognized in accumulated other comprehensive income (loss) until the hedged item or forecasted transaction is recognized in earnings. We perform an assessment at the inception of the hedge and on a quarterly basis thereafter, to determine whether our derivatives are highly effective in offsetting changes in the value of the hedged items. Any changes in the fair value resulting from hedge ineffectiveness are immediately recognized as income or expense.

In January 2015, the Company entered into sixteen forward contracts to exchange Canadian dollars ("CAD") for U.S. dollars at fixed exchange rates in order to manage its exposure related to certain forecasted CAD denominated sales of one of its subsidiaries. The hedged transactions are specified as the first amount of CAD denominated revenues invoiced by one of the Company's domestic subsidiaries each fiscal quarter, beginning in the third fiscal quarter of 2015 and continuing through the second fiscal quarter of 2019. In total, the Company will sell approximately 31.0 million CAD at an average Canadian-dollar exchange rate of 0.7825 over these quarterly periods. The Company concluded that the forward contracts met the criteria to qualify as a cash flow hedge under US GAAP. Accordingly, the Company has reflected all changes in the fair value of the forward contracts in accumulated other comprehensive income (loss), a component of shareholders' equity. Upon the maturity of each foreign exchange forward contract, the gain or loss on the contract will be recorded as an adjustment to revenues.

As of May 30, 2015, the Company had forward contracts with a notional value of approximately 27.8 million CAD outstanding and recorded the fair value of the contracts of $0.6 million in current accrued liabilities and a corresponding loss of $0.4 million in accumulated other comprehensive income (loss), which was net of the associated tax benefit. During the thirteen and thirty-nine weeks ended May 30, 2015, the Company reclassified $0.1 million from accumulated other comprehensive income (loss) to revenue, related to the derivative financial instruments. The loss in accumulated other comprehensive income (loss) as of May 30, 2015 is expected to be reclassified to revenues prior to its maturity on February 22, 2019.

6. Employee Benefit Plans

Defined Contribution Retirement Savings Plan

The Company has a defined contribution retirement savings plan with a 401(k) feature for all eligible employees not under collective bargaining agreements. The Company matches a portion of the employee's contribution and may make an additional contribution at its discretion. Contributions charged to expense under the plan for the thirteen weeks ended May 30, 2015 and May 31, 2014 were \$3.8 million and \$4.0 million, respectively. Contributions charged to expense under the plan for the thirty-nine weeks ended May 30, 2015 and May 31, 2014 were \$11.8 million and \$12.2 million, respectively.

Pension Plans and Supplemental Executive Retirement Plans

The Company maintains an unfunded Supplemental Executive Retirement Plan for certain eligible employees of the Company, a non-contributory defined benefit pension plan covering union employees at one of its locations, and a frozen pension plan the Company assumed in connection with its acquisition of Textilease Corporation in fiscal 2004. The amounts charged to expense related to these plans for the thirteen weeks ended May 30, 2015 and May 31, 2014 were \$0.9 million and \$0.6 million, respectively. The amounts charged to expense related to these plans for the thirty-nine weeks ended May 30, 2015 and May 31, 2014 were \$2.6 million and \$1.9 million, respectively.

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7. Net Income Per Share

The Company calculates net income per share in accordance with US GAAP, which requires the Company to allocate income to its unvested participating securities as part of its earnings per share (“EPS”) calculations. The following table sets forth the computation of basic earnings per share using the two-class method for amounts attributable to the Company’s shares of Common Stock and Class B Common Stock (in thousands, except per share data):

	Thirteen weeks ended		**Thirty-nine weeks ended**	
	May 30, 2015	**May 31, 2014**	**May 30, 2015**	**May 31, 2014**
Net income	$32,499	$30,944	$95,358	$91,053
Allocation of net income for Basic:				
Common Stock	$25,817	$24,493	$75,650	$71,971
Class B Common Stock	6,483	6,127	18,954	17,962
Unvested participating shares	199	324	754	1,120
	$32,499	$30,944	$95,358	$91,053
Weighted average number of shares for Basic:	&nbs			