

LANCASTER COLONY CORP
Form 10-Q
May 08, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2013

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 000-04065

Lancaster Colony Corporation

(Exact name of registrant as specified in its charter)

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Ohio
(State or other jurisdiction of
incorporation or organization)

13-1955943
(I.R.S. Employer
Identification No.)

37 West Broad Street

Columbus, Ohio
(Address of principal executive offices)

43215
(Zip Code)

614-224-7141
(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. (Check one):

Large Accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller Reporting Company
Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes No

As of April 26, 2013, there were approximately 27,316,000 shares of Common Stock, without par value, outstanding.

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LANCASTER COLONY CORPORATION AND SUBSIDIARIES

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Condensed Consolidated Financial Statements
LANCASTER COLONY CORPORATION AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS****(UNAUDITED)**

(Amounts in thousands, except share data)	March 31, 2013	June 30, 2012
ASSETS		
Current Assets:		
Cash and equivalents	\$ 100,611	\$ 191,636
Receivables (less allowance for doubtful accounts, March-\$853; June-\$678)	91,705	73,326
Inventories:		
Raw materials	32,865	36,005
Finished goods and work in process	58,643	73,699
Total inventories	91,508	109,704
Deferred income taxes and other current assets	23,812	17,073
Total current assets	307,636	391,739
Property, Plant and Equipment:		
Land, buildings and improvements	145,031	140,337
Machinery and equipment	291,889	276,951
Total cost	436,920	417,288
Less accumulated depreciation	244,954	233,158
Property, plant and equipment-net	191,966	184,130
Other Assets:		
Goodwill	89,840	89,840
Other intangible assets-net	6,559	7,267
Other noncurrent assets	7,624	9,659
Total	\$ 603,625	\$ 682,635
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	\$ 40,171	\$ 40,708
Accrued liabilities	35,828	31,963
Total current liabilities	75,999	72,671
Other Noncurrent Liabilities		
Deferred Income Taxes	30,466	31,627
	14,458	14,070
Shareholders Equity:		
Preferred stock-authorized 3,050,000 shares; outstanding-none		
Common stock-authorized 75,000,000 shares; outstanding March-27,315,855 shares; June-27,286,861 shares	102,109	100,015
Retained earnings	1,124,665	1,208,027
Accumulated other comprehensive loss	(11,850)	(12,162)

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Common stock in treasury, at cost	(732,222)	(731,613)
Total shareholders' equity	482,702	564,267
Total	\$ 603,625	\$ 682,635

See accompanying notes to condensed consolidated financial statements.

Table of Contents**LANCASTER COLONY CORPORATION AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME****(UNAUDITED)**

(Amounts in thousands, except per share data)	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Net Sales	\$ 279,511	\$ 271,098	\$ 896,642	\$ 857,400
Cost of Sales	220,687	217,296	690,445	678,309
Gross Margin	58,824	53,802	206,197	179,091
Selling, General and Administrative Expenses	26,517	25,848	80,693	74,915
Operating Income	32,307	27,954	125,504	104,176
Other Income:				
Other income-Continued Dumping and Subsidy Offset Act			293	2,701
Interest Income and Other-Net	(63)	39	(88)	73
Income Before Income Taxes	32,244	27,993	125,709	106,950
Taxes Based on Income	10,411	9,771	41,937	37,097
Net Income	\$ 21,833	\$ 18,222	\$ 83,772	\$ 69,853
Net Income Per Common Share:				
Basic and Diluted	\$ 0.80	\$ 0.67	\$ 3.06	\$ 2.56
Cash Dividends Per Common Share	\$ 0.38	\$ 0.36	\$ 6.12	\$ 1.05
Weighted Average Common Shares Outstanding:				
Basic	27,259	27,216	27,244	27,237
Diluted	27,287	27,251	27,275	27,268

See accompanying notes to condensed consolidated financial statements.

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LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

(Amounts in thousands)	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Net Income	\$ 21,833	\$ 18,222	\$ 83,772	\$ 69,853
Other Comprehensive Income:				
Defined Benefit Pension and Postretirement Benefit Plans:				
Amortization of loss, before tax	166	81	500	243
Amortization of prior service asset, before tax	(1)	(1)	(3)	(3)
Total Other Comprehensive Income, Before Tax	165	80	497	240
Tax Attributes of Items in Other Comprehensive Income:				
Amortization of loss, tax	(62)	(30)	(186)	(91)
Amortization of prior service asset, tax	1	1	1	1
Total Other Comprehensive Income, Tax	(61)	(29)	(185)	(90)
Other Comprehensive Income, Net of Tax	104	51	312	150
Comprehensive Income	\$ 21,937	\$ 18,273	\$ 84,084	\$ 70,003

See accompanying notes to condensed consolidated financial statements.

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LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

(Amounts in thousands)	Nine Months Ended March 31,	
	2013	2012
Cash Flows From Operating Activities:		
Net income	\$ 83,772	\$ 69,853
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	15,124	15,158
Deferred income taxes and other noncash changes	(652)	4,364
Stock-based compensation expense	2,211	1,991
Loss (gain) on sale of property	318	(16)
Pension plan activity	(45)	(1,095)
Changes in operating assets and liabilities:		
Receivables	(19,463)	(22,869)
Inventories	18,196	11,601
Other current assets	(5,796)	1,088
Accounts payable and accrued liabilities	1,243	5,088
Net cash provided by operating activities	94,908	85,163
Cash Flows From Investing Activities:		
Payments on property additions	(19,125)	(12,178)
Proceeds from sale of property	1,099	385
Other-net	(788)	(913)
Net cash used in investing activities	(18,814)	(12,706)
Cash Flows From Financing Activities:		
Purchase of treasury stock	(609)	(8,315)
Payment of dividends	(167,134)	(28,641)
Excess tax benefit from stock-based compensation	624	193
Net cash used in financing activities	(167,119)	(36,763)
Net change in cash and equivalents	(91,025)	35,694
Cash and equivalents at beginning of year	191,636	132,266
Cash and equivalents at end of period	\$ 100,611	\$ 167,960
Supplemental Disclosure of Operating Cash Flows:		
Cash paid during the period for income taxes	\$ 47,416	\$ 30,187

See accompanying notes to condensed consolidated financial statements.

Table of Contents**LANCASTER COLONY CORPORATION AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(Tabular amounts in thousands, except per share data)

Note 1 Summary of Significant Accounting Policies***Basis of Presentation***

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and SEC Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, the interim condensed consolidated financial statements reflect all adjustments necessary for a fair presentation of the results of operations and financial position for such periods. All such adjustments reflected in the interim condensed consolidated financial statements are considered to be of a normal recurring nature. The results of operations for any interim period are not necessarily indicative of results for the full year. Accordingly, these financial statements should be read in conjunction with the financial statements and notes thereto contained in our 2012 Annual Report on Form 10-K. Unless otherwise noted, the term year and references to a particular year pertain to our fiscal year, which begins on July 1 and ends on June 30; for example, 2013 refers to fiscal 2013, which is the period from July 1, 2012 to June 30, 2013.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation. Purchases of property, plant and equipment included in accounts payable and excluded from the property additions and the change in accounts payable in the Condensed Consolidated Statements of Cash Flows were as follows:

	March 31,	
	2013	2012
Construction in progress in accounts payable	\$ 2,704	\$ 244

Earnings per Share

Earnings per share (EPS) is computed based on the weighted average number of shares of common stock and common stock equivalents (restricted stock and stock-settled stock appreciation rights) outstanding during each period. Unvested shares of restricted stock granted to employees are considered participating securities since employees receive nonforfeitable dividends prior to vesting and, therefore, are included in the earnings allocation in computing EPS under the two-class method. Basic EPS excludes dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted EPS is computed by dividing income available to common shareholders by the diluted weighted average number of common shares outstanding during the period, which includes the dilutive potential common shares associated with nonparticipating restricted stock and stock-settled stock appreciation rights.

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LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts in thousands, except per share data)

Basic and diluted net income per common share were calculated as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Net income	\$ 21,833	\$ 18,222	\$ 83,772	\$ 69,853
Net income available to participating securities	(29)	(36)	(311)	(125)
Net income available to common shareholders	\$ 21,804	\$ 18,186	\$ 83,461	\$ 69,728
Weighted average common shares outstanding basic	27,259	27,216	27,244	27,237
Incremental share effect from:				
Nonparticipating restricted stock	2	2	3	4
Stock-settled stock appreciation rights	26	33	28	27
Weighted average common shares outstanding diluted	27,287	27,251	27,275	27,268
Net income per common share basic and diluted	\$ 0.80	\$ 0.67	\$ 3.06	\$ 2.56

Significant Accounting Policies

There were no changes to our Significant Accounting Policies from those disclosed in our 2012 Annual Report on Form 10-K.

Note 2 Impact of Recently Issued Accounting Standards

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-02, *Comprehensive Income: Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* (ASU 13-02) which adds new disclosure requirements for items reclassified out of accumulated other comprehensive income. ASU 13-02 effectively replaces the requirements previously outlined in ASU No. 2011-05, *Comprehensive Income: Presentation of Comprehensive Income* and ASU No. 2011-12,

Comprehensive Income: Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05 . The requirements of ASU 13-02 are effective for fiscal years, and interim periods within those years, beginning after December 15, 2012, with early adoption permitted. As ASU 13-02 relates to disclosure requirements only, we do not expect the adoption of this guidance to have an impact on our financial position, results of operations or cash flows.

Note 3 Goodwill and Other Intangible Assets

Goodwill attributable to the Specialty Foods segment was approximately \$89.8 million at March 31, 2013 and June 30, 2012.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts in thousands, except per share data)

The following table summarizes our identifiable other intangible assets, all included in the Specialty Foods segment:

	March 31, 2013	June 30, 2012
Trademarks (40-year life)		
Gross carrying value	\$ 370	\$ 370
Accumulated amortization	(202)	(196)
Net carrying value	\$ 168	\$ 174
Customer Relationships (12 to 15-year life)		
Gross carrying value	\$ 13,020	\$ 13,020
Accumulated amortization	(6,629)	(5,927)
Net carrying value	\$ 6,391	\$ 7,093
Total net carrying value	\$ 6,559	\$ 7,267

Amortization expense relating to these assets was as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Amortization expense	\$ 236	\$ 253	\$ 708	\$ 835

Total annual amortization expense for each of the next five years is estimated to be as follows:

2014	\$ 946
2015	\$ 946
2016	\$ 775
2017	\$ 604
2018	\$ 604

Note 4 Long-Term Debt

At March 31, 2013 and June 30, 2012, we had an unsecured credit agreement under which we may borrow, on a revolving credit basis, up to a maximum of \$120 million at any one time, with potential to expand the total credit availability to \$200 million based on obtaining consent of the issuing banks and certain other conditions. The facility expires on April 18, 2017, and all outstanding amounts are then due and payable. Interest is variable based upon formulas tied to LIBOR or an alternative base rate defined in the credit agreement, at our option. We must also pay facility fees that are tied to our then-applicable consolidated leverage ratio. Loans may be used for general corporate purposes. Based on the long-term nature of this facility, when we have outstanding borrowings under this facility, we will classify the outstanding balance as long-term debt.

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At March 31, 2013 and June 30, 2012, we had no borrowings outstanding under this facility. At March 31, 2013, we had approximately \$3.4 million of standby letters of credit outstanding, which reduced the amount available for borrowing under the credit agreement. We paid no interest for the three and nine months ended March 31, 2013 and 2012. At March 31, 2013 and June 30, 2012, we were in compliance with all applicable provisions and covenants of this facility, and we exceeded the requirements of the financial covenants by substantial margins. At March 31, 2013, we were not aware of any event that would constitute a

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(Tabular amounts in thousands, except per share data)

default under the facility.

The facility contains certain restrictive covenants, including limitations on indebtedness, asset sales and acquisitions. There are two principal financial covenants: an interest expense test that requires us to maintain an interest coverage ratio not less than 2.5 to 1 at the end of each fiscal quarter; and an indebtedness test that requires us to maintain a consolidated leverage ratio not greater than 3 to 1 at all times. The interest coverage ratio is calculated by dividing Consolidated EBIT (as defined more specifically in the credit agreement) by Consolidated Interest Expense (as defined more specifically in the credit agreement), and the leverage ratio is calculated by dividing Consolidated Debt (as defined more specifically in the credit agreement) by Consolidated EBITDA (as defined more specifically in the credit agreement).

Note 5 Pension Benefits

We and certain of our operating subsidiaries have sponsored multiple defined benefit pension plans covering union workers at certain locations. As a result of restructuring activities in recent years, we no longer have any active employees continuing to accrue service cost or otherwise eligible to receive plan benefits. Benefits being paid under the plans are primarily based on negotiated rates and years of service. We contribute to these plans at least the minimum amount required by regulation.

The following table summarizes the components of net periodic benefit income for our pension plans:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Components of net periodic benefit income				
Interest cost	\$ 408	\$ 483	\$ 1,224	\$ 1,449
Expected return on plan assets	(595)	(599)	(1,785)	(1,797)
Amortization of unrecognized net loss	172	89	516	267
Net periodic benefit income	\$ (15)	\$ (27)	\$ (45)	\$ (81)

For the three and nine months ended March 31, 2013, we made no pension plan contributions and we do not expect to make any contributions to our pension plans during 2013.

Note 6 Postretirement Benefits

We and certain of our operating subsidiaries provide multiple postretirement medical and life insurance benefit plans. We recognize the cost of benefits as the employees render service. Postretirement benefits are funded as incurred.

The following table summarizes the components of net periodic benefit cost for our postretirement plans:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Components of net periodic benefit cost				
Service cost	\$ 8	\$ 6	\$ 24	\$ 18

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Interest cost	28	37	84	111
Amortization of unrecognized net gain	(6)	(8)	(16)	(24)
Amortization of prior service asset	(1)	(1)	(3)	(3)
Net periodic benefit cost	\$ 29	\$ 34	\$ 89	\$ 102

For the three and nine months ended March 31, 2013, we made approximately \$27,000 and \$81,000, respectively, in contributions to our postretirement medical and life insurance benefit plans. We expect to

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(Tabular amounts in thousands, except per share data)

make approximately \$0.1 million more in contributions to our postretirement medical and life insurance benefit plans during the remainder of 2013.

Note 7 Stock-Based Compensation

Our shareholders approved the adoption of and subsequent amendments to the Lancaster Colony Corporation 2005 Stock Plan (the 2005 Plan). The 2005 Plan reserved 2,000,000 common shares for issuance to our employees and directors, and all awards granted under the 2005 Plan will be exercisable at prices not less than fair market value as of the date of the grant. The vesting period for awards granted under the 2005 Plan varies as to the type of award granted, but generally these awards have a maximum term of five years.

Stock-Settled Stock Appreciation Rights

We use periodic grants of stock-settled stock appreciation rights (SSSARs) as a vehicle for rewarding certain employees with long-term incentives for their efforts in helping to create long-term shareholder value. We calculate the fair value of SSSARs grants using the Black-Scholes option-pricing model. Our policy is to issue shares upon SSSARs exercise from new shares that had been previously authorized.

In February 2013 and 2012, we granted SSSARs to various employees under the terms of our 2005 Plan. The following table summarizes information relating to each of these grants:

	2013	2012
SSSARs granted	108	185
Weighted average grant date fair value per right	\$ 9.04	\$ 9.08
Assumptions used in fair value calculations:		
Risk-free interest rate	0.33%	0.41%
Dividend yield	2.09%	2.11%
Volatility factor of the expected market price of our common stock	23.23%	24.31%
Weighted average expected life in years	2.67	2.76
Estimated forfeiture rate	2.00%	4.00%

For each of these grants, the volatility factor was estimated based on actual historical volatility of our stock for a time period equal to the term of the SSSARs. The expected average life was determined based on historical exercise experience for this type of grant. The SSSARs from each grant vest one-third on the first anniversary of the grant date, one-third on the second anniversary of the grant date and one-third on the third anniversary of the grant date.

We recognize compensation expense over the requisite service period. Compensation expense was reflected in Cost of Sales or Selling, General and Administrative Expenses based on the grantees' salaries expense classification and was allocated to each segment appropriately. We recorded tax benefits and gross windfall tax benefits related to SSSARs. These windfall tax benefits were included in the financing section of the Condensed Consolidated Statements of Cash Flows. The following table summarizes SSSARs compensation expense and tax benefits recorded:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Compensation expense	\$ 282	\$ 453	\$ 1,081	\$ 1,099
Tax benefits	\$ 99	\$ 159	\$ 378	\$ 385

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Intrinsic value of exercises	\$ 87	\$ 138	\$ 1,371	\$ 281
Gross windfall tax benefits	\$ 41	\$ 58	\$ 490	\$ 122

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(Tabular amounts in thousands, except per share data)

The total fair values of SSSARs vested were as follows:

	Nine Months Ended March 31,	
	2013	2012
Fair value of vested rights	\$ 1,469	\$ 1,107

The following table summarizes the activity relating to SSSARs granted under the 2005 Plan for the nine months ended March 31, 2013:

	Number of Rights	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life in Years	Aggregate Intrinsic Value
Outstanding at beginning of period	446	\$ 60.55		
Exercised	(124)	\$ 52.82		
Granted	108	\$ 72.67		
Forfeited	(5)	\$ 63.50		
Outstanding at end of period	425	\$ 65.88	3.65	\$ 4,723
Exercisable and vested at end of period	162	\$ 61.21	2.76	\$ 2,552
Vested and expected to vest at end of period	416	\$ 65.86	3.65	\$ 4,629

At March 31, 2013, there was approximately \$1.8 million of unrecognized compensation expense related to SSSARs that we will recognize over a weighted-average period of approximately 2.29 years.

Restricted Stock

We use periodic grants of restricted stock as a vehicle for rewarding our nonemployee directors and certain employees with long-term incentives for their efforts in helping to create long-term shareholder value.

In November 2012 and 2011, we granted shares of restricted stock to our seven nonemployee directors under the terms of the 2005 Plan. The following table summarizes information relating to each of these grants:

	Nine Months Ended March 31,	
	2013	2012
Nonemployee directors		

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Restricted stock granted	7	7
Grant date fair value	\$ 490	\$ 490
Weighted average grant date fair value per award	\$ 73.29	\$ 65.97

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts in thousands, except per share data)

The 2013 grant vests over a one-year period, and all of these shares are expected to vest. Dividends earned on the stock during the vesting period will be paid to the directors at the time the stock vests. The 2012 grant vested during the second quarter of 2013, and the directors were paid the related dividends.

In February 2013 and 2012, we granted shares of restricted stock to various employees under the terms of the 2005 Plan. The following table summarizes information relating to each of these grants:

	Nine Months Ended March 31,	
	2013	2012
Employees		
Restricted stock granted	8	25
Grant date fair value	\$ 572	\$ 1,693
Weighted average grant date fair value per award	\$ 72.67	\$ 68.12
Estimated forfeiture rate	3.00%	4.00%

The restricted stock under each of these employee grants vests on the third anniversary of the grant date. Under the terms of the grants, employees receive dividends on unforfeited restricted stock regardless of their vesting status. Approximately 23,000 shares of employee restricted stock vested in 2013.

We recognize compensation expense over the requisite service period. Compensation expense was reflected in Cost of Sales or Selling, General and Administrative Expenses based on the grantees' salaries expense classification and was allocated to each segment appropriately. We recorded tax benefits and gross windfall tax benefits related to restricted stock. Windfall tax benefits, if any, were included in the financing section of the Condensed Consolidated Statements of Cash Flows. The following table summarizes restricted stock compensation expense and tax benefits recorded:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Compensation expense	\$ 306	\$ 343	\$ 1,130	\$ 892
Tax benefits	\$ 107	\$ 120	\$ 395	\$ 312
Gross windfall tax benefits	\$ 124	\$ 56	\$ 134	\$ 71

The total fair values of restricted stock vested were as follows:

	Nine Months Ended March 31,	
	2013	2012
Fair value of vested shares	\$ 1,837	\$ 645

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(Tabular amounts in thousands, except per share data)

The following table summarizes the activity relating to restricted stock granted under the 2005 Plan for the nine months ended March 31, 2013:

	Number of Shares	Weighted Average Grant Date Fair Value
Unvested restricted stock at beginning of period	62	\$ 63.25
Granted	15	\$ 72.95
Vested	(30)	\$ 60.56
Forfeited	(1)	\$ 61.85
Unvested restricted stock at end of period	46	\$ 68.16

At March 31, 2013, there was approximately \$2.0 million of unrecognized compensation expense related to restricted stock that we will recognize over a weighted-average period of approximately 1.92 years.

Note 8 Income Taxes

The gross tax contingency reserve at March 31, 2013 was approximately \$2.0 million and consisted of tax liabilities of approximately \$1.0 million and penalties and interest of approximately \$1.0 million. We classified approximately \$0.2 million of the gross tax contingency reserve as current liabilities as these amounts are expected to be resolved within the next 12 months. The remaining liability of approximately \$1.8 million was included in other noncurrent liabilities. We expect that the amount of these liabilities will change within the next 12 months; however, we do not expect the change to have a significant effect on our financial position or results of operations. We recognize interest and penalties related to these tax liabilities in income tax expense.

Note 9 Business Segment Information

The following summary of financial information by business segment is consistent with the basis of segmentation and measurement of segment profit or loss presented in our June 30, 2012 consolidated financial statements. The March 31, 2013 identifiable assets by reportable segment are generally consistent with that of June 30, 2012. However, the amount of Corporate assets declined because of the decrease in cash, which is treated as a Corporate asset, due to the payment of the December 2012 special dividend.

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Net Sales				
Specialty Foods	\$ 247,098	\$ 237,432	\$ 768,613	\$ 740,604
Glassware and Candles	32,413	33,666	128,029	116,796
Total	\$ 279,511	\$ 271,098	\$ 896,642	\$ 857,400
Operating Income				
Specialty Foods	\$ 33,648	\$ 29,561	\$ 126,790	\$ 109,510
Glassware and Candles	1,587	973	7,809	2,272

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Corporate Expenses	(2,928)	(2,580)	(9,095)	(7,606)
Total	\$ 32,307	\$ 27,954	\$ 125,504	\$ 104,176

Note 10 Commitments and Contingencies

We currently are party to various legal proceedings, including an action brought by a competitor in our Glassware and Candles segment alleging defamation of the competitor by us. The plaintiff's complaint did

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LANCASTER COLONY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Tabular amounts in thousands, except per share data)

not specify damages. The case is set for jury trial beginning May 20, 2013 in the U.S. District Court of South Carolina. We believe we have meritorious defenses in this matter and intend to defend ourselves vigorously. As of March 31, 2013, we have not recorded a loss contingency for this matter. While we believe that the ultimate outcome of this and various other proceedings we face, individually and in the aggregate, will not have a material adverse effect on our financial position or liquidity, litigation is always subject to inherent uncertainties, and unfavorable rulings could occur, which could have a material impact on net income for the period in which the ruling occurs and future periods.

The Continued Dumping and Subsidy Offset Act of 2000 (CDSOA) provides for the distribution of monies collected by U.S. Customs from anti-dumping cases to qualifying domestic producers. Our reported CDSOA receipts totaled approximately \$0.3 million in the second quarter of 2013, as compared to approximately \$2.7 million in the second quarter of 2012.

CDSOA remittances relate to certain candles being imported from the People's Republic of China. CDSOA provisions for remittances apply only to duties collected on products imported prior to October 2007. Accordingly, we may receive some level of annual distributions for an undetermined period of years in the future as the monies collected that relate to entries filed prior to October 2007 are administratively finalized by U.S. Customs. Without further legislative action, we expect these distributions will eventually cease.

Cases have been brought in U.S. courts challenging certain aspects of CDSOA. In two separate cases, the U.S. Court of International Trade (CIT) ruled that the procedure for determining recipients eligible to receive CDSOA distributions is unconstitutional. The U.S. Court of Appeals for the Federal Circuit reversed both CIT decisions and the U.S. Supreme Court did not hear either case. This allowed the appellate court decisions to stand, but other legal challenges to CDSOA are still pending.

We are unable to determine, at this time, what the ultimate outcome of other litigation will be, and it is possible that further legal action, potential additional changes in the law and other factors could affect the amount of funds available for distribution, including funds relating to entries prior to October 2007. Accordingly, we cannot predict the amount of future distributions, if any, we may receive. Any change in CDSOA distributions could affect our earnings and cash flow.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations
LANCASTER COLONY CORPORATION AND SUBSIDIARIES**

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS**

(Tabular dollars in thousands)

Our fiscal year begins on July 1 and ends on June 30. Unless otherwise noted, references to "year" pertain to our fiscal year; for example, 2013 refers to fiscal 2013, which is the period from July 1, 2012 to June 30, 2013.

The following discussion should be read in conjunction with our condensed consolidated financial statements and the notes thereto, all included elsewhere in this report. The forward-looking statements in this section and other parts of this report involve risks and uncertainties including statements regarding our plans, objectives, goals, strategies, and financial performance. Our actual results could differ materially from the results anticipated in these forward-looking statements as a result of factors set forth under the caption "Forward-Looking Statements."

OVERVIEW

Business Overview

Lancaster Colony Corporation is a diversified manufacturer and marketer of consumer products focusing primarily on specialty foods for the retail and foodservice markets. We also manufacture and market candles for the food, drug and mass markets. Although not material to our consolidated operations, we are also engaged in the distribution of various products, including glassware and candles, to select commercial markets. Our operations are organized in two reportable segments: Specialty Foods and Glassware and Candles. The sales of each segment are predominately domestic.

In recent years, our strategy has shifted away from operating businesses in a variety of industries towards emphasizing the growth and success we have achieved in our Specialty Foods segment.

We view our food operations as having the potential to achieve future growth in sales and profitability due to attributes such as:

leading retail market positions in several branded products with a high-quality perception;

a broad customer base in both retail and foodservice accounts;

well-regarded culinary expertise among foodservice accounts;

recognized leadership in foodservice product development;

experience in integrating complementary business acquisitions; and

historically strong cash flow generation that supports growth opportunities.

Within the Specialty Foods segment, our goal is to grow both retail and foodservice sales over time by:

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leveraging the strength of our retail brands to increase current product sales and introduce new products;

growing our foodservice sales through the strength of our reputation in product development and quality; and

pursuing acquisitions that meet our strategic criteria.

We have made substantial capital investments to support our existing food operations and future growth opportunities. Based on our current plans and expectations, we believe that our total consolidated capital expenditures for 2013 will total approximately \$25 million.

Summary of 2013 Results

The following is a comparative overview of our consolidated operating results for the three and nine months ended March 31, 2013 and 2012.

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Net sales for the three months ended March 31, 2013 increased 3% to approximately \$279.5 million from the prior-year total of \$271.1 million. This sales increase reflects higher sales in the Specialty Foods segment, largely due to higher retail volumes. Glassware and Candles net sales declined as a result of lower candle volumes. The third quarter gross margin increased 9% to approximately \$58.8 million from the prior-year total of \$53.8 million. The higher level of net sales and a more favorable sales mix contributed to the improved gross margin. Net income for the three months ended March 31, 2013 totaled approximately \$21.8 million, or \$.80 per diluted share. Net income totaled approximately \$18.2 million in the third quarter of the prior year, or \$.67 per diluted share.

Year-to-date net sales for the period ended March 31, 2013 increased 5% to approximately \$896.6 million from the prior-year total of \$857.4 million. Gross margin increased 15% to approximately \$206.2 million from the prior year-to-date total of \$179.1 million. Net income for the nine months ended March 31, 2013 totaled approximately \$83.8 million, or \$3.06 per diluted share. Net income totaled approximately \$69.9 million in the nine months ended March 31, 2012, or \$2.56 per diluted share.

RESULTS OF CONSOLIDATED OPERATIONS*Net Sales and Gross Margin*

	Three Months Ended March 31,			Nine Months Ended March 31,			Change	
	2013	2012	Change	2013	2012	Change		
Net Sales								
Specialty Foods	\$ 247,098	\$ 237,432	\$ 9,666	4%	\$ 768,613	\$ 740,604	\$ 28,009	4%
Glassware and Candles	32,413	33,666	(1,253)	(4)%	128,029	116,796	11,233	10%
Total	\$ 279,511	\$ 271,098	\$ 8,413	3%	\$ 896,642	\$ 857,400	\$ 39,242	5%
Gross Margin	\$ 58,824	\$ 53,802	\$ 5,022	9%	\$ 206,197	\$ 179,091	\$ 27,106	15%
Gross Margin as a Percentage of Net Sales	21.0%	19.8%			23.0%	20.9%		

Consolidated net sales for the third quarter and nine months ended March 31, 2013 increased 3% and 5%, respectively. For the quarter, increased sales within the Specialty Foods segment were partially offset by lower sales within the Glassware and Candles segment. The sales increase for the nine-month period reflected higher sales in both operating segments.

For the three and nine months ended March 31, 2013, net sales of the Specialty Foods segment increased by 4%. For the quarter, the net sales increase was mainly influenced by increased retail volumes, including that provided by recently-introduced products. Overall foodservice sales volumes for the quarter were relatively comparable to year ago levels. The impact of pricing to the quarter was immaterial. Both the retail and foodservice sales increased for the year-to-date period. Higher product pricing contributed approximately a quarter of the segment's net sales growth for the nine-month period. The current year's growth in foodservice sales occurred largely among existing customers. Additionally, the success of recently-introduced products also benefited retail channel sales. For both comparable periods of 2013, retail net sales also benefited from lower levels of consumer-directed promotional costs.

Net sales of the Glassware and Candles segment for the three months ended March 31, 2013 decreased by 4% on lower candle volume. Net sales of the Glassware and Candles segment increased by 10% for the nine months ended March 31, 2013. The increase in net sales for the nine-month period was influenced by the growth of seasonal candle programs.

As a percentage of sales, our consolidated gross margin for the three and nine months ended March 31, 2013 was 21.0% and 23.0%, respectively, as compared to 19.8% and 20.9% achieved in the prior-year comparative periods.

In the Specialty Foods segment, gross margin percentages improved for both the three and nine months ended March 31, 2013, reflecting factors such as improved sales volumes, a more favorable sales mix and modestly favorable ingredient costs (especially for soybean oil, flour and sweeteners). We estimate that lower material costs beneficially affected the segment's gross margins by less than one percent of segment net sales for both the three and nine months ended March 31, 2013. For the year-to-date period, margins also

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benefited from higher pricing. Looking forward into the final quarter of 2013, we anticipate comparative results to be challenged by the prior year's volume of new product roll-outs, less favorable material cost comparisons than experienced in the third quarter and potentially higher promotional costs.

Gross margin percentages in the Glassware and Candles segment for both the three and nine months ended March 31, 2013, improved, as influenced by a more beneficial customer and product mix. For the year-to-date period, margins also reflected higher sales and production levels as well as modestly lower wax costs.

Selling, General and Administrative Expenses

	Three Months Ended March 31,			Nine Months Ended March 31,		
	2013	2012	Change	2013	2012	Change
SG&A Expenses	\$ 26,517	\$ 25,848	\$ 669 3%	\$ 80,693	\$ 74,915	\$ 5,778 8%
SG&A Expenses as a Percentage of Net Sales	9.5%	9.5%		9.0%	8.7%	

Consolidated selling, general and administrative costs totaled approximately \$26.5 million and \$80.7 million for the three and nine months ended March 31, 2013, respectively, compared to the \$25.8 million and \$74.9 million incurred for the three and nine months ended March 31, 2012. These increases were influenced by higher sales, greater personnel costs and increased costs associated with previously idled held-for-sale real estate.

Operating Income

The foregoing factors contributed to consolidated operating income totaling approximately \$32.3 million and \$125.5 million for the three and nine months ended March 31, 2013, respectively. By segment, our operating income can be summarized as follows:

Three Months Ended March 31,	Nine Months Ended March 31,
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