DELTA APPAREL INC
Form 10-Q
May 05, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended March 27, 2010

OR

o **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 1-15583

DELTA APPAREL, INC.

(Exact name of registrant as specified in its charter)

GEORGIA	**58-2508794**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
322 South Main Street Greenville, SC	**29601**
(Address of principal executive offices)	(Zip Code)

(864) 232-5200

(Registrant s telephone number, including area code)

(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.

Yes þ No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes þ No o

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 a large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

Yes o No þ

As of May 3, 2010, there were outstanding 8,516,293 shares of the registrant s common stock, par value of $0.01 per share, which is the only class of outstanding common or voting stock of the registrant.

INDEX

Table of Contents

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements

DELTA APPAREL, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(Amounts in thousands, except share and per share data)
(Unaudited)

	March 27, 2010	June 27, 2009
Assets		
Current assets:		
Cash	$ 555	$ 654
Accounts receivable, net	62,258	57,884
Income taxes receivable		1,755
Inventories, net	125,871	125,887
Prepaid expenses and other current assets	3,474	3,387
Deferred income taxes	3,492	3,475
Total current assets	195,650	193,042
Property, plant and equipment, net	36,142	36,480
Goodwill	17,426	16,814
Intangibles, net	8,192	7,114
Other assets	3,312	3,543
Total assets	$ 260,722	$ 256,993
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 35,005	$ 34,103
Accrued expenses	19,465	17,852
Income taxes payable	211	
Current portion of long-term debt	5,718	5,718
Total current liabilities	60,399	57,673
Long-term debt, less current maturities	77,045	85,936
Deferred income taxes	1,566	1,223
Other liabilities	1,866	16
Total liabilities	140,876	144,848
Stockholders equity:		
Preferred stock $0.01 par value, 2,000,000 shares authorized; none issued and outstanding		
Common stock $0.01 par value, 15,000,000 shares authorized, 9,646,972 shares issued, and 8,516,293 and 8,502,699 shares outstanding as of March 27, 2010 and June 27, 2009, respectively	96	96

Additional paid-in capital	58,947	58,301
Retained earnings	70,284	63,763
Accumulated other comprehensive loss	(143)	(565)
Treasury stock 1,130,679 and 1,144,273 shares as of March 27, 2010 and June 27, 2009, respectively	(9,338)	(9,450)
Total stockholders equity	119,846	112,145
Total liabilities and stockholders equity	$ 260,722	$ 256,993

See accompanying notes to condensed consolidated financial statements.

3

Table of Contents

DELTA APPAREL, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Income
(Amounts in thousands, except per share data)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	March 27, 2010	March 28, 2009	March 27, 2010	March 28, 2009
Net sales	$ 107,942	$ 85,685	$ 298,224	$ 250,458
Cost of goods sold	82,739	68,915	227,600	198,327
Gross profit	25,203	16,770	70,624	52,131
Selling, general and administrative expenses	20,345	14,450	59,164	45,850
Other income (expense), net	56	(34)	189	(49)
Operating income	4,914	2,286	11,649	6,232
Interest expense, net	948	1,028	2,805	3,669
Income before provision for income taxes	3,966	1,258	8,844	2,563
Provision for income taxes	1,008	95	2,324	131
Net income	$ 2,958	$ 1,163	$ 6,520	$ 2,432
Basic earnings per share	$ 0.35	$ 0.14	$ 0.77	$ 0.29
Diluted earnings per share	$ 0.34	$ 0.14	$ 0.76	$ 0.29
Weighted average number of shares outstanding	8,516	8,503	8,513	8,501
Dilutive effect of stock options	215	2	65	1
Weighted average number of shares assuming dilution	8,731	8,505	8,578	8,502

See accompanying notes to condensed consolidated financial statements.

Table of Contents

DELTA APPAREL, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Amounts in thousands)
(Unaudited)

	Nine Months Ended	
	March 27, 2010	March 28, 2009
Operating activities:		
Net income	$ 6,520	$ 2,432
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,172	5,375
Deferred income taxes	326	(453)
Loss on disposal of property and equipment	56	55
Non-cash stock compensation	1,385	648
Changes in operating assets and liabilities, net of effect of acquisitions:		
Accounts receivable	(4,368)	12,310
Inventories	52	(11,723)
Prepaid expenses and other current assets	(87)	(98)
Income taxes receivable	1,966	(1,433)
Other non-current assets	233	25
Accounts payable and accrued expenses	4,013	1,519
Other liabilities	(927)	135
Net cash provided by operating activities	14,341	8,792
Investing activities:		
Purchases of property and equipment	(3,855)	(2,681)
Proceeds from sale of property, plant and equipment	6	11
Cash paid for business	(1,700)	(2,592)
Net cash used in investing activities	(5,549)	(5,262)
Financing activities:		
Proceeds from long-term debt	296,161	263,165
Repayment of long-term debt	(305,052)	(266,119)
Net cash used in financing activities	(8,891)	(2,954)
Net (decrease) increase in cash	(99)	576
Cash at beginning of period	654	586
Cash at end of period	$ 555	$ 1,162

Supplemental cash flow information:		
Cash paid for interest	$ 2,571	$ 3,781
Cash paid for income taxes, net of refunds	$ 301	$ 1,837
Non-cash financing activity issuance of common stock	$ 118	$ 41

See accompanying notes to condensed consolidated financial statements.

DELTA APPAREL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note A Basis of Presentation

We prepared the accompanying interim condensed consolidated financial statements in accordance with the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. We believe these condensed consolidated financial statements reflect all adjustments (consisting of only normal recurring accruals) considered necessary for a fair presentation. Operating results for the three and nine months ended March 27, 2010 are not necessarily indicative of the results that may be expected for our fiscal year ending July 3, 2010. For more information regarding our results of operations and financial position, refer to the consolidated financial statements and footnotes included in our Form 10-K for our fiscal year ended June 27, 2009, filed with the Securities and Exchange Commission.

Delta Apparel, the Company, and we, us and our are used interchangeably to refer to Delta Apparel, Inc. togethe its wholly-owned subsidiaries, M.J. Soffe, LLC (Soffe), Junkfood Clothing Company (Junkfood), To The Game, LLC (To The Game), Art Gun, LLC (Art Gun) and other subsidiaries, as appropriate to the context.

Note B Accounting Policies

Our accounting policies are consistent with those described in our Summary of Significant Accounting Policies in our Form 10-K for our fiscal year ended June 27, 2009, which was a 52-week year, filed with the Securities and Exchange Commission. We operate on a 52-53 week fiscal year ending on the Saturday closest to June 30. The 2010 fiscal year will be a 53-week year ending on July 3, 2010.

Note C New Accounting Standards

In June 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Codification No. 105, *FASB Accounting Standards and the Hierarchy of Generally Accepted Accounting Principles* (ASC 105). ASC 105 replaces SFAS 162 and establishes the FASB Accounting Standards Codification (Codification) as the single source of authoritative U.S. generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities, except for rules and interpretive releases by the Securities and Exchange Commission (SEC) which are sources of authoritative GAAP for SEC registrants. ASC 105 and the Codification are effective for interim and annual periods ending after September 15, 2009. We adopted ASC 105 on June 28, 2009, and all references made to GAAP within our consolidated financial statements now use the new Codification numbering system. The Codification does not change or alter existing GAAP and, therefore, the adoption of ASC 105 did not have an impact on our financial position, results of operations or cash flows.

In December 2007, the FASB issued Codification No. 805, *Business Combinations* (ASC 805) to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects. ASC 805 applies to all transactions or other events in which an entity obtains control of one or more businesses, and combinations achieved without the transfer of consideration. ASC 805 is effective for business combinations for the first annual reporting period beginning on or after December 15, 2008. We accounted for the Art Gun, LLC acquisition in accordance with ASC 805 on the acquisition date, December 28, 2009, which is described in **Note N Art Gun Acquisition**. ASC 805 will impact our accounting for any future business combinations, but the effect will depend on the circumstances of the particular acquisition.

In February 2009, the FASB issued a position regarding ASC 805, *Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies*. This position requires an asset or liability arising from a contingency in a business combination to be recognized at fair value if fair value can be reasonably determined. If fair value cannot be reasonably determined, then the asset or liability will need to be recognized in accordance with ASC 450, *Accounting for Contingencies*. The guidelines issued under the position are effective for assets and liabilities arising from contingencies in business combinations for the first annual reporting period beginning on or after December 15, 2008. We accounted for the Art Gun, LLC acquisition in accordance with ASC 805 on the acquisition date, December 28, 2009, which is described in **Note N Art Gun Acquisition**. ASC 805 will impact our accounting for any future business combinations, but the effect will depend on the circumstances of the particular acquisition.

In April 2008, the FASB issued a position for *Determination of the Useful Life of Intangible Assets* under Codification No. 350, *Goodwill and Other Intangible Assets* (ASC 350). The position amends the factors that must be considered in developing renewal or extension assumptions used to determine the useful life over which to amortize the cost of a recognized intangible asset under ASC

Table of Contents

350. ASC 305 is effective for fiscal years beginning after December 15, 2008 and the interim periods within those fiscal years. We accounted for the Art Gun, LLC acquisition in accordance with ASC 350 on the acquisition date, December 28, 2009, which is described in **Note N Art Gun Acquisition**. ASC 350 will impact our accounting for any future acquisitions of intangible assets, but the effect will depend on the circumstances of the particular acquisition.
In November 2008, the FASB issued Codification No. 323, *Equity Method Investment Accounting Considerations* (ASC 323). ASC 323 clarifies accounting for certain transactions and impairment considerations involving the equity method, including initial measurement, decrease in investment value and change in level of ownership or degree of influence. ASC 323 is effective on a prospective basis for fiscal years beginning on or after December 15, 2008. We adopted ASC 323 on June 28, 2009, and the adoption did not have an impact on our financial statements.
In June 2009, the FASB issued Accounting Standards Update No. 2009-17, *Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities* (ASU 2009-17) as a further clarification to Codification No. 810-10, *Consolidation of Variable Interest Entities*. ASU 2009-17, upon adoption, requires the use of a qualitative analysis to determine the primary beneficiary of a variable interest entity (VIE), amends the guidance for determining if an entity is a VIE and enhances the disclosure requirements regarding an enterprise s involvement with a VIE. ASU 2009-17 is effective for fiscal years beginning after November 25, 2009. We are currently evaluating the effect that the adoption of ASU 2009-17 will have on our financial position and results of operations, but do not expect that the adoption of ASU 2009-17 will have a material impact on our financial statements.
In January 2010, the FASB issued Accounting Standards Update No. 2010-06, *Improving Disclosures about Fair Value Measurements* (ASU 2010-06), an amendment to ASC Topic 820, *Fair Value Measurements and Disclosures*. This amendment requires an entity to: disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers, and present separate information for Level 3 activity pertaining to gross purchases, sales, issuances, and settlements. ASU 2010-06 is effective for interim and annual reporting beginning after December 15, 2009. We adopted ASU 2010-06 as of December 27, 2009, and the adoption had no impact on our financial position and results of operations.
In February 2010, the FASB issued Accounting Standards Update No. 2010-09, *Amendments to Certain Recognition and Disclosure Requirements* (ASU 2010-09), an amendment to ASC Topic 855, *Subsequent Events*. This amendment removed the requirement for an SEC registrant to disclose the date through which subsequent events are evaluated. This guidance was effective immediately and we adopted these new requirements for the period ended March 27, 2010. The adoption of ASU 2010-09 had no impact on our financial position and results of operations.

Note D Inventories

Inventories, net of reserves, consist of the following (in thousands):

	March 27, 2010	June 27, 2009
Raw materials	$ 10,601	$ 9,626
Work in process	20,441	21,842
Finished goods	94,829	94,419
	$ 125,871	$ 125,887

Raw materials include finished yarn and direct materials for the activewear segment and include direct materials, finished fabric and blank t-shirts for the retail-ready segment.

Note E Debt

On September 21, 2007, Delta Apparel, Junkfood and Soffe entered into a Third Amended and Restated Loan and Security Agreement (the Amended Loan Agreement) with Wachovia Bank, National Association, as Agent, and the financial institutions named in the Amended Loan Agreement as Lenders. The Amended Loan Agreement provided us with a $100 million credit line (subject to borrowing base limitations based on the value and type of collateral provided) that matures on September 12, 2012. On March 30, 2009 we invoked the accordion feature in the Amended

Loan Agreement, amending the credit facility to increase the maximum line of credit from $100 million to $110 million and adding PNC Bank, National Association to the syndicate of lenders under the facility with a $10 million commitment. Proceeds of the loans under the Amended Loan Agreement may be used for general operating, working capital, other corporate purposes, and to finance fees and expenses under the facility.

The credit facility is secured by a first-priority lien on substantially all of the real and personal property of Delta Apparel, Junkfood, Soffe, To The Game and Art Gun. All loans under the Amended Loan Agreement bear interest at rates based on either an adjusted

LIBOR rate plus an applicable margin or the bank s prime rate plus an applicable margin. The facility requires installment payments of approximately $0.2 million per month in connection with fixed asset amortization, and these amounts reduce the amount of availability under the facility. Annual facility fees are 0.25% of the amount by which $110 million exceeds the average daily principal balance of the outstanding loans and letters of credit accommodations, and are charged monthly based on the principal balances during the immediately preceding month.
Our credit facility includes the financial covenant that if the amount of availability falls below $10 million, our Fixed Charge Coverage Ratio (as defined in the Amended Loan Agreement) for the preceding 12 month period must not be less than 1.1 to 1.0, and otherwise includes customary conditions to funding, covenants, and events of default. At March 27, 2010, we had $75.0 million outstanding under our credit facility at an average interest rate of 2.8%, and had the ability to borrow an additional $31.5 million. As of March 27, 2010, our Fixed Charge Coverage Ratio was 3.7 for the preceding 12 months, thus exceeding the 1.1 requirement allowing access to, if needed, the total amount of availability provided for under the Amended Loan Agreement. We expect to continue to meet the Fixed Charge Coverage Ratio for fiscal year 2010.

Our credit facility contains limitations on, or prohibitions of, cash dividends. We are allowed to make cash dividends in amounts such that the aggregate amount paid to shareholders since May 16, 2000 does not exceed twenty-five percent (25%) of our cumulative net income calculated from May 16, 2000 to the date of determination. At March 27, 2010, there was $13.3 million of retained earnings free of restrictions for the payment of dividends.

The credit facility contains a subjective acceleration clause and a springing lockbox arrangement (as defined in ASC 470, *Balance Sheet Classification of Borrowings Outstanding*), whereby remittances from customers are forwarded to our general bank account and do not reduce the outstanding debt until and unless a specified event or an event of default occurs. Pursuant to ASC 470, we classify borrowings under the facility as non-current debt.

In the fourth quarter of fiscal year 2007, we entered into a loan agreement with Banco Ficohsa, a Honduran bank, for our capital expansion in Honduras. This loan is secured by a first-priority lien on the assets of our Honduran operations. During the first quarter of fiscal year 2009, the loan was amended to a fixed interest rate of 6% through June 2010, at which time the interest rate increases to 6.5% for the remainder of the term. The loan is payable monthly, has a five-year term and is denominated in U.S. dollars. At March 27, 2010, we had $7.8 million outstanding on this loan.

Note F Selling, General and Administrative Expense

We include in selling, general and administrative expenses, costs incurred subsequent to the receipt of finished goods at our distribution facilities, such as the cost of stocking, warehousing, picking and shipping goods for delivery to our customers. In the third quarter of fiscal years 2010 and 2009, these distribution costs, which were included in selling, general and administrative expenses, totaled $3.5 million and $3.4 million, respectively. Distribution costs included in selling, general and administrative expenses for the first nine months of fiscal years 2010 and 2009 were $10.0 million and $10.3 million, respectively. Selling, general and administrative expenses also include costs related to sales associates, administrative personnel cost, advertising and marketing expenses, royalty payments on licensed products and other general and administrative expenses.

Note G Stock Options and Incentive Stock Awards

We maintain certain stock-based compensation plans that are described in Note 12 to the Consolidated Financial Statements included in our 2009 Annual Report to Shareholders. We account for these plans pursuant to ASC No. 718, *Share-Based Payment*, and the Securities and Exchange Commission Staff Accounting Bulletin No. 110 (SAB 110).

<u>Delta Apparel Stock Option Plan (Option Plan)</u>

We expensed $0.1 million in each of the third quarters of fiscal year 2010 and 2009 in connection with our Option Plan. During the first nine months of fiscal years 2010 and 2009, we expensed $0.2 million and $0.6 million, respectively. As of March 27, 2010, there was $0.5 million of total unrecognized compensation cost related to non-vested stock options under the Option Plan. This cost is expected to be recognized over a period of 2.25 years. Stock compensation expense is included in the cost of sales and selling, general and administrative expense line items of our statements of income on a straight-line basis over the vesting periods of each grant.

<u>Delta Apparel Incentive Stock Award Plan (Award Plan)</u>

For the third quarter of fiscal years 2010 and 2009, we expensed $0.6 million and $20 thousand, respectively, in connection with our Award Plan. During the first nine months of fiscal years 2010 and 2009, we expensed $1.2 million and $26 thousand, respectively. Stock compensation expense is included in the cost of sales and selling, general and administrative expense line items of our statements of income over the vesting periods.

Note H Purchase Contracts

We have entered into agreements, and have fixed prices, to purchase natural gas, yarn and finished fabric for use in our manufacturing operations. In addition, we have contracts to purchase finished apparel and headwear products. At March 27, 2010, minimum payments under these non-cancelable contracts were as follows (in thousands):

Natural gas	$ 426
Yarn	31,671
Finished fabric	350
Finished apparel and headwear products	11,455
	$ 43,902

Note I Segment Reporting

We operate our business in two distinct segments: activewear and retail-ready. Although the two segments are similar in their production processes and regulatory environment, they are distinct in their economic characteristics, products and distribution methods.

The activewear segment is comprised of our business units primarily focused on garment styles that are characterized by low fashion risk and includes our Delta and FunTees businesses. We market, distribute and manufacture unembellished knit apparel under the following labels: Delta Pro Weight®, Delta Magnum Weight, Quail Hollow, Healthknit, QH, and Fun Tees. The products are typically sold to screen printing companies. Primarily within our FunTees operations, we manufacture unembellished and embellished private label custom apparel products to major branded sportswear companies, retailers and corporate industry programs.

The retail-ready segment is comprised of our business units primarily focused on more specialized apparel garments and headwear to meet consumer preferences and fashion trends and includes our Soffe, Junkfood, To The Game and Art Gun businesses. These branded embellished and unembellished products are sold through specialty and boutique stores, high-end and mid-tier retail chains, sporting goods stores, college bookstores and to the U.S. military. Our products in this segment are marketed under the primary brands of Soffe®, Intensity Athletics®, Junk Food®, and The Game®, as well as other labels. To The Game and Art Gun have been included in the retail-ready segment since their acquisition on March 29, 2009 and December 28, 2009, respectively.

Our chief operating decision maker evaluates performance and allocates resources based on profit or loss from operations before interest, income taxes and special charges (Segment Operating Income (Loss)). Our Segment Operating Income (Loss) may not be comparable to similarly titled measures used by other companies. The accounting policies of our reportable segments are the same as those described in Note B. Intercompany transfers between operating segments are transacted at cost and have been eliminated within the segment amounts shown in the following table.

Information about our operations as of and for the three and nine month periods ended March 27, 2010 and March 28, 2009, by operating segment, is as follows (in thousands):

	Activewear	Retail-Ready	Consolidated
Three months ended March 27, 2010:			
Net sales	$ 61,685	$ 46,257	$ 107,942
Segment operating income	1,368	3,546	4,914
Segment assets	140,291	120,431	260,722
Purchases of property, plant and equipment	1,092	577	1,669
Three months ended March 28, 2009:			
Net sales	$ 53,313	$ 32,372	$ 85,685
Segment operating (loss) income	(543)	2,829	2,286
Segment assets	148,363	112,855	261,218

Purchases of property, plant and equipment	345	370	715

	Activewear	Retail-Ready	Consolidated
Nine months ended March 27, 2010:			
Net sales	$ 154,209	$ 144,015	$ 298,224
Segment operating (loss) income	(355)	12,004	11,649
Purchases of property, plant and equipment	2,503	1,352	3,855
Nine months ended March 28, 2009:			
Net sales	$ 144,271	$ 106,187	$ 250,458
Segment operating (loss) income	(4,919)	11,151	6,232
Purchases of property, plant and equipment	959	1,722	2,681

The following table reconciles the segment operating income to the consolidated income before income taxes (in thousands).

	Three Months Ended		Nine Months Ended	
	March 27, 2010	March 28, 2009	March 27, 2010	March 28, 2009
Segment operating income	$ 4,914	$ 2,286	$ 11,649	$ 6,232
Unallocated interest expense	948	1,028	2,805	3,669
Consolidated income before taxes	$ 3,966	$ 1,258	$ 8,844	$ 2,563

Note J Income Taxes

Our effective income tax rate for the three months ended March 27, 2010 increased to 25.4% compared to 7.6% for the same period of the prior year. Our effective income tax rate for the nine month period ended March 27, 2010 increased to 26.3% compared to 5.1% for the same period of the prior year. The primary driver for the increase in fiscal year 2010 is due to the percentage of earnings in domestic taxable, foreign taxable and tax-free locations relative to the total pre-tax income in a given period. Profits that are permanently reinvested in the tax-free zone of Honduras are relatively fixed since this amount is based on cost-plus determination based on our production output. Therefore, our effective tax rate has increased during the current fiscal year because our U.S. profits have increased while our Honduran tax-free profits have remained relatively constant. The higher effective tax rate compared to the prior year third quarter negatively impacted our earnings by $0.08 per share and is expected to have a further negative impact on our earnings per share in the fourth quarter compared to the prior year. We expect our overall effective tax rate to be in the range of 26% to 27% for fiscal year 2010 compared with 13.1% in fiscal year 2009.

As of March 27, 2010, we had a deferred tax asset related to charitable contributions carryforwards for federal income tax purposes. Based on our projected earnings for fiscal year 2010 and the remaining years until the carryforwards expire, we now believe that the deferred tax asset related to these charitable contributions will be realized and no valuation allowance is necessary. As such, during the quarter ended March 27, 2010, we reversed the remaining valuation allowance on the charitable contribution carryfowards.

We file income tax returns in the U.S. federal jurisdiction and various state, local and foreign jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state, local or non-U.S. income tax examinations by tax authorities for our tax years before 2006. However, net operating loss carryforwards remain subject to examination to the extent they are carried forward and impact a year that is open to examination by tax authorities.

Note K Factored Receivables

During the first quarter of fiscal year 2010, we terminated our factoring agreement under which we previously assigned a portion of our trade accounts receivable relating to our Junkfood business. Prior to the termination, we accounted for our factoring agreement as a sale in accordance with FASB Codification No. 860, *Transfers and Servicing*. The assignment of these receivables was without recourse, provided that the customer orders were approved by the factor prior to shipment of the goods, up to a maximum for each individual account. The agreement did not include provisions for advances from the factor against the assigned receivables. The factor funded the accounts receivable upon collection, or, exclusive of disputed claims, 90 days after the due date. The amount due from the factor was included in our accounts receivable on our balance sheet and changes in the amount due from factor were included in our cash flow from operations. At March 27, 2010, our accounts receivable less allowances was $62.3 million, comprised of $65.9 million in unfactored accounts receivable and $3.6 million in allowances. At June 27, 2009, our accounts receivable less allowances was $55.9 million, comprised of $57.3 million in unfactored accounts receivable, $1.6 million due from factor, and $3.0 million in allowances.

Table of Contents

Note L Derivatives

We use interest rate swap and collar agreements to manage our interest rate exposure and reduce the impact of future interest rate changes. We do not use these financial instruments for trading or speculative purposes. The following table includes information regarding our interest rate swap and collar agreements as of March 27, 2010:

	Effective Date	Notional Amount	LIBOR Rate	Maturity Date
Collar Agreement	April 2, 2007	$15 million	4.33% - 5.50%	April 1, 2010
Interest Rate Swap	April 2, 2007	$15 million	5.06%	April 1, 2010
Interest Rate Swap	April 1, 2009	$15 million	1.57%	April 1, 2011
Interest Rate Swap	March 1, 2010	$15 million	1.11%	September 1, 2011

We account for derivatives under Codification No. 815, *Derivatives and Hedging* (ASC 815). ASC 815 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and hedging activities. It requires the recognition of all derivative instruments as either assets or liabilities in the Consolidated Balance Sheets and measurement of those instruments at fair value. The fair value hierarchy has three levels based on the reliability of the inputs used to determine fair value. The fair value of the interest rate swap and collar agreements was derived from discounted cash flow analyses based on the terms of the contract and the forward interest rate curve adjusted for our credit risk, which is considered a level two input based on the fair value hierarchy. As of March 27, 2010, the fair value of the liability for the interest rate swap and collar agreements was $0.2 million. We have assessed these agreements and concluded that the swap and collar agreements match the exact terms of the underlying debt to which they are related and therefore are considered perfectly-effective hedges. Therefore, changes in the derivatives fair values are deferred and recorded as a component of accumulated other comprehensive loss. The changes in fair value of the interest rate swap and collar agreements resulted in an accumulated other comprehensive loss, net of taxes, of $0.1 million as of March 27, 2010.

The following table summarizes the fair value of our derivatives and its presentation in the consolidated balance sheets as of March 27, 2010 and June 27, 2009 (in thousands).

	March 27, 2010	June 27, 2009
Accrued expenses	$ 4	$ 902
Other liabilities	228	16
Deferred tax liabilities	(89)	(353)
Accumulated other comprehensive loss	$ 143	$ 565