

UNIFIRST CORP
Form 10-Q
July 03, 2013

**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 25, 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: **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)

Edgar Filing: UNIFIRST CORP - Form 10-Q

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 June 27, 2013 were 15,122,075 and 4,873,277, respectively.

UniFirst Corporation

Quarterly Report on Form 10-Q

For the Quarter ended May 25, 2013

Table of Contents

Part I – FINANCIAL INFORMATION

Item 1 – Financial Statements

Consolidated Statements of Income for the Thirteen and Thirty-nine Weeks ended May 25, 2013 and May 26, 2012

Consolidated Statements of Comprehensive Income for the Thirteen and Thirty-nine Weeks ended May 25, 2013 and May 26, 2012

Consolidated Balance Sheets as of May 25, 2013 and August 25, 2012

Consolidated Statements of Cash Flows for the Thirty-nine Weeks ended May 25, 2013 and May 26, 2012

Notes to Consolidated Financial Statements

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

Item 3 – Quantitative and Qualitative Disclosures About Market Risk

Item 4 – Controls and Procedures

Part II – OTHER INFORMATION

Item 1 – Legal Proceedings

Item 1A – Risk Factors

Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds

Item 3 – Defaults Upon Senior Securities

Item 4 – Mine Safety Disclosures

Item 5 – Other Information

Item 6 – Exhibits

Signatures

Exhibit Index

Certifications

Ex-31.1 Section 302 Certification of CEO

Ex-31.2 Section 302 Certification of CFO

Ex-32.1 Section 906 Certification of CEO

Ex-32.2 Section 906 Certification of CFO



PART I – FINANCIAL INFORMATION**ITEM 1. FINANCIAL STATEMENTS****UniFirst Corporation and Subsidiaries****Consolidated Statements of Income***(Unaudited)*

| | Thirteen weeks ended | | Thirty-nine weeks ended | |
|----------------------------------------------|-----------------------------|----------------|--------------------------------|----------------|
| | May 25, | May 26, | May 25, | May 26, |
| | 2013 | 2012 | 2013 | 2012 |
| (In thousands, except per share data) | | | | |
| Revenues | \$335,764 | \$320,931 | \$1,002,639 | \$943,915 |
| Operating expenses: | | | | |
| Cost of revenues (1) | 208,066 | 202,433 | 618,038 | 599,009 |
| Selling and administrative expenses (1) | 64,786 | 59,108 | 194,891 | 179,429 |
| Depreciation and amortization | 17,115 | 16,718 | 51,065 | 49,615 |
| Total operating expenses | 289,967 | 278,259 | 863,994 | 828,053 |
| Income from operations | 45,797 | 42,672 | 138,645 | 115,862 |
| Other (income) expense: | | | | |
| Interest expense | 464 | 511 | 1,324 | 1,639 |
| Interest income | (781) | (656) | (2,472) | (2,036) |
| Exchange rate loss | 283 | 457 | 321 | 1,028 |
| Total other (income) expense | (34) | 312 | (827) | 631 |
| Income before income taxes | 45,831 | 42,360 | 139,472 | 115,231 |
| Provision for income taxes | 17,109 | 14,901 | 53,348 | 42,774 |
| Net income | \$28,722 | \$27,459 | \$86,124 | \$72,457 |
| Income per share – Basic: | | | | |
| Common Stock | \$1.51 | \$1.45 | \$4.53 | \$3.83 |
| Class B Common Stock | \$1.21 | \$1.16 | \$3.63 | \$3.06 |
| Income per share – Diluted: | | | | |
| Common Stock | \$1.43 | \$1.37 | \$4.29 | \$3.63 |

Income allocated to – Basic:

| | | | | |
|----------------------|----------|----------|----------|----------|
| Common Stock | \$22,638 | \$21,587 | \$67,793 | \$56,926 |
| Class B Common Stock | \$5,647 | \$5,381 | \$16,880 | \$14,214 |

Income allocated to – Diluted:

| | | | | |
|--------------|----------|----------|----------|----------|
| Common Stock | \$28,307 | \$26,993 | \$84,747 | \$71,205 |
|--------------|----------|----------|----------|----------|

Weighted average number of shares outstanding – Basic:

| | | | | |
|----------------------|--------|--------|--------|--------|
| Common Stock | 14,993 | 14,905 | 14,960 | 14,872 |
| Class B Common Stock | 4,675 | 4,644 | 4,656 | 4,642 |

Weighted average number of shares outstanding – Diluted:

| | | | | |
|--------------|--------|--------|--------|--------|
| Common Stock | 19,820 | 19,646 | 19,751 | 19,600 |
|--------------|--------|--------|--------|--------|

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.

UniFirst Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income
(Unaudited)

| | Thirteen weeks ended | | Thirty-nine weeks ended | |
|------------------------------------------------|-----------------------------|----------------|--------------------------------|----------------|
| | May 25, | May 26, | May 25, | May 26, |
| (In thousands) | 2013 | 2012 | 2013 | 2012 |
| Net Income | \$28,722 | \$27,459 | \$86,124 | \$72,457 |
| Other comprehensive income (loss), net of tax: | | | | |
| Foreign currency translation adjustments | (1,084) | (3,971) | (3,574) | (6,281) |
| Pension benefit liabilities, net (1) | — | — | 50 | — |
| Other comprehensive income (loss) | (1,084) | (3,971) | (3,524) | (6,281) |
| Comprehensive income | 27,638 | 23,488 | 82,600 | 66,176 |

(1) Net of less than \$0.1 million of tax expense for the thirty-nine weeks ended May 25, 2013.

UniFirst Corporation and Subsidiaries

Consolidated Balance Sheets

(Unaudited)

| (In thousands, except share data) | May 25, 2013 | August 25, 2012(a) |
|-----------------------------------------------------------------|-------------------------|-------------------------------|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 175,591 | \$ 120,123 |
| Receivables, less reserves of \$7,851 and \$5,152, respectively | 147,170 | 135,327 |
| Inventories | 72,355 | 75,420 |
| Rental merchandise in service | 133,741 | 138,284 |
| Prepaid and deferred income taxes | 12,813 | 12,785 |
| Prepaid expenses | 9,565 | 5,741 |
| Total current assets | 551,235 | 487,680 |
| Property, plant and equipment: | | |
| Land, buildings and leasehold improvements | 373,530 | 355,568 |
| Machinery and equipment | 461,576 | 425,274 |
| Motor vehicles | 153,411 | 141,370 |
| Total property, plant and equipment | 988,517 | 922,212 |
| Less -- accumulated depreciation | 539,994 | 510,008 |
| Total property, plant and equipment, net | 448,523 | 412,204 |
| Goodwill | 288,620 | 288,137 |
| Customer contracts, net | 42,530 | 48,580 |
| Other intangible assets, net | 1,446 | 1,951 |
| Other assets | 2,428 | 1,982 |
| Total assets | \$ 1,334,782 | \$ 1,240,534 |
| Liabilities and shareholders' equity | | |
| Current liabilities: | | |
| Loans payable and current maturities of long-term debt | \$ 110,716 | \$ 6,831 |
| Accounts payable | 55,531 | 52,340 |
| Accrued liabilities | 85,641 | 78,174 |
| Accrued income taxes | 1,462 | 8,180 |
| Total current liabilities | 253,350 | 145,525 |
| Long-term liabilities: | | |
| Long-term debt, net of current maturities | 155 | 100,155 |
| Accrued liabilities | 44,933 | 43,420 |

Edgar Filing: UNIFIRST CORP - Form 10-Q

| | | |
|------------------------------------------------------------------------------------------------------------------------------------|-------------|-------------|
| Accrued and deferred income taxes | 54,488 | 54,509 |
| Total long-term liabilities | 99,576 | 198,084 |
| Commitments and contingencies (Note 8) | | |
| 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; 15,121,575 and 15,064,069 issued and outstanding, respectively | 1,512 | 1,506 |
| Class B Common Stock, \$0.10 par value; 20,000,000 shares authorized; 4,873,277 and 4,885,277 issued and outstanding, respectively | 487 | 488 |
| Capital surplus | 47,449 | 42,984 |
| Retained earnings | 928,661 | 844,676 |
| Accumulated other comprehensive income | 3,747 | 7,271 |
| Total shareholders' equity | 981,856 | 896,925 |
| Total liabilities and shareholders' equity | \$1,334,782 | \$1,240,534 |

(a) Derived from audited financial statements

The accompanying notes are an integral part of these

Consolidated Financial Statements.

UniFirst Corporation and Subsidiaries**Consolidated Statements of Cash Flows***(Unaudited)*

| Thirty-nine weeks ended | May 25, | May 26, |
|-------------------------------------------------------------------------------|----------------|----------------|
| (In thousands) | 2013 | 2012 |
| Cash flows from operating activities: | | |
| Net income | \$86,124 | \$72,457 |
| Adjustments to reconcile net income to cash provided by operating activities: | | |
| Depreciation | 43,718 | 41,644 |
| Amortization of intangible assets | 7,347 | 7,971 |
| Amortization of deferred financing costs | 178 | 178 |
| Share-based compensation | 5,051 | 5,202 |
| Accretion on environmental contingencies | 407 | 474 |
| Accretion on asset retirement obligations | 497 | 473 |
| Deferred income taxes | 79 | 362 |
| Changes in assets and liabilities, net of acquisitions: | | |
| Receivables | (12,099) | (12,985) |
| Inventories | 3,070 | (320) |
| Rental merchandise in service | 4,332 | (14,475) |
| Prepaid expenses | (3,824) | (4,870) |
| Accounts payable | 3,279 | 2,629 |
| Accrued liabilities | 8,255 | 2,411 |
| Prepaid and accrued income taxes | (6,914) | 5,666 |
| Net cash provided by operating activities | 139,500 | 106,817 |
| Cash flows from investing activities: | | |
| Acquisition of businesses, net of cash acquired | (1,953) | — |
| Capital expenditures | (81,087) | (59,325) |
| Other | (185) | (436) |
| Net cash used in investing activities | (83,225) | (59,761) |
| Cash flows from financing activities: | | |
| Proceeds from loans payable and long-term debt | 4,102 | 40,410 |
| Payments on loans payable and long-term debt | (22) | (55,845) |
| Proceeds from exercise of Common Stock options | 2,750 | 2,000 |
| Taxes withheld and paid related to net share settlement of equity awards | (3,332) | — |
| Payment of cash dividends | (2,138) | (2,129) |
| Net cash provided by (used in) financing activities | 1,360 | (15,564) |
| Effect of exchange rate changes | (2,167) | (1,483) |
| Net increase in cash and cash equivalents | 55,468 | 30,009 |

Edgar Filing: UNIFIRST CORP - Form 10-Q

| | | |
|--------------------------------------------------|-----------|----------|
| Cash and cash equivalents at beginning of period | 120,123 | 48,812 |
| Cash and cash equivalents at end of period | \$175,591 | \$78,821 |

The accompanying notes are an integral part of these
Consolidated Financial Statements.

UniFirst Corporation and Subsidiaries

Notes to Consolidated Financial Statements

1. Basis of Presentation

These Consolidated Financial Statements of UniFirst Corporation (the “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 financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended August 25, 2012. 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.

Certain prior year amounts have been reclassified to conform to current year presentation. These reclassifications did not impact current or historical net income or shareholder’s equity.

2. Recent Accounting Pronouncements

In May 2011, the FASB issued updated accounting guidance to amend existing requirements for fair value measurements and disclosures. The guidance expands the disclosure requirements around fair value measurements categorized in Level 3 of the fair value hierarchy and requires disclosure of the level in the fair value hierarchy of items that are not measured at fair value but whose fair value must be disclosed. It also clarifies and expands upon existing requirements for fair value measurements of financial assets and liabilities as well as instruments classified in shareholders’ equity. The guidance was effective for interim and annual financial periods beginning after December 15, 2011. The Company adopted this revised guidance on August 26, 2012 and the adoption did not have a material impact on its financial statements.

In June 2011, the FASB issued updated accounting guidance that improves the comparability, consistency, and transparency of financial reporting and increases the prominence of items reported in other comprehensive income by eliminating the option to present components of other comprehensive income as part of the statement of changes in shareholders' equity. The amendments to the existing standard require that all nonowner changes in shareholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The amendments to the existing standard do not change the current option for presenting components of OCI gross or net of the effect of income taxes, provided that such tax effects are presented in the statement in which OCI is presented or disclosed in the notes to the financial statements. Additionally, the standard does not affect the calculation or reporting of earnings per share. This guidance was effective for annual reporting periods, and any interim periods within those annual periods, that began after December 15, 2011 and is to be applied retrospectively, with early adoption permitted. The Company adopted this revised guidance on August 26, 2012 and the adoption did not have a material impact on its financial statements.

In September 2011, the FASB issued updated guidance intended to simplify how entities, both public and nonpublic, test for goodwill impairment. This guidance permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. Also, the guidance improves the examples of events and circumstances that an entity having a reporting unit with a zero or negative carrying amount should consider in determining whether to measure an impairment loss, if any, under the second step of the goodwill impairment test. This guidance was effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. The Company adopted this revised guidance on August 26, 2012 and the adoption did not have a material impact on its financial statements.

In February 2013, the FASB issued updated accounting guidance that improves the reporting of reclassifications out of accumulated other comprehensive income. The amendments in this updated guidance require an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under US GAAP to be reclassified in its entirety to net income. For other amounts that are not required under US GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under US GAAP that provide additional detail about those amounts. The guidance is effective for interim and annual financial periods beginning after December 15, 2012, with early adoption permitted. The Company does not expect this guidance to have a material impact on its financial statements.

3. Acquisitions

During the thirty-nine weeks ended May 25, 2013, the Company completed three acquisitions with an aggregate purchase price of approximately \$2.0 million. The results of operations of these acquisitions have been included in the Company's consolidated financial results since their respective acquisition dates. None of these acquisitions was 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 25, 2013

| | Level 1 | Level 2 | Level 3 | Fair Value |
|------------------|----------------|----------------|----------------|-------------------|
| Assets: | | | | |
| Cash equivalents | \$33,957 | \$ — | \$ — | \$33,957 |
| Total | \$33,957 | \$ — | \$ — | \$33,957 |

As of August 25, 2012

| | Level 1 | Level 2 | Level 3 | Fair Value |
|------------------|----------------|----------------|----------------|-------------------|
| Assets: | | | | |
| Cash equivalents | \$34,978 | \$ — | \$ — | \$34,978 |
| Total | \$34,978 | \$ — | \$ — | \$34,978 |

The Company's cash equivalents listed above represents 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.

5. 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 25, 2013 and May 26, 2012 were \$4.3 million and \$2.9 million, respectively. Contributions charged to expense under the plan for the thirty-nine weeks ended May 25, 2013 and May 26, 2012 were \$12.9 million and \$8.7 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 25, 2013 and May 26, 2012 were \$0.6 million and \$0.5 million, respectively. The amounts charged to expense related to these plans for the thirty-nine weeks ended May 25, 2013 and May 26, 2012 were \$1.7 million and \$1.6 million, respectively.

6. 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 25, | May 26, | May 25, | May 26, |
| | 2013 | 2012 | 2013 | 2012 |
| Net income | \$28,722 | \$27,459 | \$86,124 | \$72,457 |
| Allocation of net income for Basic: | | | | |
| Common Stock | \$22,638 | \$21,587 | \$67,793 | \$56,926 |
| Class B Common Stock | 5,647 | 5,381 | 16,880 | 14,214 |
| Unvested participating shares | 437 | 491 | 1,451 | 1,317 |
| | \$28,722 | \$27,459 | \$86,124 | \$72,457 |
| Weighted average number of shares for Basic: | | | | |
| Common Stock | 14,993 | 14,905 | 14,960 | 14,872 |
| Class B Common Stock | 4,675 | 4,644 | 4,656 | 4,642 |
| Unvested participating shares | 331 | 387 | 366 | 393 |
| | 19,999 | 19,936 | 19,982 | 19,907 |
| Earnings per share for Basic: | | | | |
| Common Stock | \$1.51 | \$1.45 | \$4.53 | \$3.83 |
| Class B Common Stock | \$1.21 | \$1.16 | \$3.63 | \$3.06 |

The Company is required to calculate diluted EPS for Common Stock using the more dilutive of the following two methods:

- The treasury stock method; or
- The two-class method assuming a participating security is not exercised or converted.

Edgar Filing: UNIFIRST CORP - Form 10-Q

For the thirteen and thirty-nine weeks ended May 25, 2013, the Company's diluted EPS assumes the conversion of all vested Class B Common Stock into Common Stock and uses the two-class method for its unvested participating shares. The following table sets forth the computation of diluted earnings per share of Common Stock for the thirteen and thirty-nine weeks ended May 25, 2013 as follows (in thousands, except per share data):

| | Thirteen weeks | | | Thirty-nine weeks | | |
|---------------------------------------------------------------------------|-----------------------|---------------|------------|--------------------------|---------------|------------|
| | ended May 25, 2013 | | | ended May 25, 2013 | | |
| | Earnings | | | Earnings | | |
| | to | Common | EPS | to | Common | EPS |
| | Common | Shares | | Common | Shares | |
| | Shareholders | | | Shareholders | | |
| As reported - Basic | \$22,638 | 14,993 | \$1.51 | \$67,793 | 14,960 | \$4.53 |
| Add: effect of dilutive potential common shares | | | | | | |
| Share-based awards | — | 152 | | — | 135 | |
| Class B Common Stock | 5,647 | 4,675 | | 16,880 | 4,656 | |
| Add: Undistributed earnings allocated to unvested participating shares | 426 | — | | 1,415 | — | |
| Less: Undistributed earnings reallocated to unvested participating shares | (404) | — | | (1,341) | — | |
| Diluted EPS – Common Stock | \$28,307 | 19,820 | \$1.43 | \$84,747 | 19,751 | \$4.29 |

Share-based awards that would result in the issuance of 27,347 shares of Common Stock were excluded from the calculation of diluted earnings per share for the thirteen weeks ended May 25, 2013 because they were anti-dilutive. There were no share-based awards that were excluded from the calculation of diluted earnings per share for the thirty-nine weeks ended May 25, 2013 because they were anti-dilutive.

For the thirteen and thirty-nine weeks ended May 26, 2012, the Company's diluted EPS assumes the conversion of all vested Class B Common Stock into Common Stock and uses the two-class method for its unvested participating shares. The following table sets forth the computation of diluted earnings per share of Common Stock for the thirteen and thirty-nine weeks ended May 26, 2012 as follows (in thousands, except per share data):

| | Thirteen weeks | | | Thirty-nine weeks | | |
|---------------------------------------------------------------------------|-----------------------|---------------|------------|--------------------------|---------------|------------|
| | ended May 26, 2012 | | | ended May 26, 2012 | | |
| | Earnings | Common | EPS | Earnings | Common | EPS |
| | to Common | Shares | | to Common | Shares | |
| | Shareholders | | | Shareholders | | |
| As reported - Basic | \$ 21,587 | 14,905 | \$ 1.45 | \$ 56,926 | 14,872 | \$ 3.83 |
| Add: effect of dilutive potential common shares | | | | | | |
| Share-based awards | — | 97 | | — | 86 | |
| Class B Common Stock | 5,381 | 4,644 | | 14,214 | 4,642 | |
| Add: Undistributed earnings allocated to unvested participating shares | 478 | — | | 1,279 | — | |
| Less: Undistributed earnings reallocated to unvested participating shares | (453) | — | | (1,214) | — | |
| Diluted EPS – Common Stock | \$ 26,993 | 19,646 | \$ 1.37 | \$ 71,205 | 19,600 | \$ 3.63 |

Share-based awards that would result in the issuance of 18,056 and 19,786 shares of Common Stock were excluded from the calculation of diluted earnings per share for the thirteen and thirty-nine weeks ended May 26, 2012, respectively, because they were anti-dilutive.

7. Asset Retirement Obligations

The Company recognizes asset retirement obligations in the period in which they are incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset. The Company continues to depreciate, on a straight-line basis, the amount added to property, plant and equipment and recognizes accretion expense in connection with the discounted liability over the various remaining lives which range from approximately one to thirty-one years.

A reconciliation of the Company's asset retirement liability is as follows (in thousands):

| | |
|-----------------------------------------|-----------------------------|
| | May 25, 2013 |
| Beginning balance as of August 25, 2012 | \$10,120 |
| Accretion expense | 497 |
| Ending balance as of May 25, 2013 | \$10,617 |

Asset retirement obligations are included in long-term accrued liabilities in the accompanying Consolidated Balance Sheet.

8. Commitments and Contingencies

The Company and its operations are subject to various federal, state and local laws and regulations governing, among other things, air emissions, wastewater discharges, and the generation, handling, storage, transportation, treatment and disposal of hazardous waste and other substances. In particular, industrial laundries use and must dispose of detergent waste water and other residues, and, in the past used perchloroethylene and other dry cleaning solvents. The Company is attentive to the environmental concerns surrounding the disposal of these materials and has, through the years, taken measures to avoid their improper disposal. In the past, the Company has settled, or contributed to the settlement of, actions or claims brought against the Company relating to the disposal of hazardous materials and there can be no assurance that the Company will not have to expend material amounts to remediate the consequences of any such disposal in the future.

US GAAP requires that a liability for contingencies be recorded when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated. Significant judgment is required to determine the existence of a liability, as well as the amount to be recorded. The Company regularly consults with attorneys and outside consultants in its consideration of the relevant facts and circumstances before recording a contingent liability. Changes in enacted laws, regulatory orders or decrees, management's estimates of costs, insurance proceeds, participation by other parties, the timing of payments and the input of outside consultants and attorneys based on changing legal or factual circumstances could have a material impact on the amounts recorded for environmental and other contingent liabilities.

Under environmental laws, an owner or lessee of real estate may be liable for the costs of removal or remediation of certain hazardous or toxic substances located on, or in, or emanating from, such property, as well as related costs of investigation and property damage. Such laws often impose liability without regard to whether the owner or lessee knew of, or was responsible for the presence of such hazardous or toxic substances. There can be no assurances that acquired or leased locations have been operated in compliance with environmental laws and regulations or that future uses or conditions will not result in the imposition of liability upon the Company under such laws or expose the Company to third-party actions such as tort suits. The Company continues to address environmental conditions under terms of consent orders negotiated with the applicable environmental authorities or otherwise with respect to sites located in or related to Woburn, Massachusetts, Somerville, Massachusetts, Springfield, Massachusetts, Uvalde, Texas, Stockton, California, three sites related to former operations in Williamstown, Vermont, as well as sites located in Goldsboro, North Carolina, Wilmington, North Carolina and Landover, Maryland.

The Company has accrued certain costs related to the sites described above as it has been determined that the costs are probable and can be reasonably estimated. The Company continues to implement mitigation measures and to monitor environmental conditions at the Somerville, Massachusetts site. The Company also has potential exposure related to an additional parcel of land (the "Central Area") related to the Woburn, Massachusetts site discussed above. Currently, the consent decree for the Woburn site does not define or require any remediation work in the Central Area. The United States Environmental Protection Agency (the "EPA") has provided the Company and other signatories to the consent decree with comments on the design and implementation of groundwater and soil remedies at the Woburn site and investigation of environmental conditions in the Central Area. The Company, and other signatories, have implemented and proposed to do additional work at the Woburn site but many of the EPA's comments remain to be resolved. The Company has accrued costs to perform certain work responsive to EPA's comments. In addition, the Company has responded to requests for information, and recently received notices of violation, from the EPA under the Clean Air Act regarding its handling of and operations with respect to the laundering of soiled towels, and the Company is addressing these matters.

The Company routinely reviews and evaluates sites that may require remediation and monitoring and determines its estimated costs based on various estimates and assumptions. These estimates are developed using its internal sources or by third party environmental engineers or other service providers. Internally developed estimates are based on:

- Management's judgment and experience in remediating and monitoring the Company's sites;
- Information available from regulatory agencies as to costs of remediation and monitoring;
- The number, financial resources and relative degree of responsibility of other potentially responsible parties (PRPs) who may be liable for remediation and monitoring of a specific site; and
- The typical allocation of costs among PRPs.

There is usually a range of reasonable estimates of the costs associated with each site. The Company's accruals reflect the amount within the range that constitutes its best estimate. Where it believes that both the amount of a particular

liability and the timing of the payments are reliably determinable, the Company adjusts the cost in current dollars using a rate of 3% for inflation until the time of expected payment and discounts the cost to present value using current risk-free interest rates. As of May 25, 2013, the risk-free interest rates utilized by the Company ranged from 2.0% to 3.2%.

For environmental liabilities that have been discounted, the Company includes interest accretion, based on the effective interest method, in selling and administrative expenses on the Consolidated Statements of Income. The changes to the Company's environmental liabilities for the thirty-nine weeks ended May 25, 2013 are as follows (in thousands):

| | May 25, 2013 |
|----------------------------------------------------|-----------------------------|
| Beginning balance as of August 25, 2012 | \$20,020 |
| Payments made for which reserves had been provided | (1,478) |
| Insurance proceeds received | 163 |
| Interest accretion | 407 |
| Change in discount rates | (702) |
| Balance as of May 25, 2013 | \$18,410 |

Anticipated payments and insurance proceeds of currently identified environmental remediation liabilities as of May 25, 2013, for the next five fiscal years and thereafter, as measured in current dollars, are reflected below.

| (In thousands) | 2013 | 2014 | 2015 | 2016 | 2017 | Thereafter | Total |
|-----------------------------------|-------------|-------------|-------------|-------------|-------------|-------------------|--------------|
| Estimated costs – current dollars | \$3,785 | \$2,470 | \$1,437 | \$950 | \$752 | \$ 11,861 | \$21,255 |
| Estimated insurance proceeds | — | (173) | (159) | (173) | (159) | (1,743) | (2,407) |
| Net anticipated costs | \$3,785 | \$2,297 | \$1,278 | \$777 | \$593 | \$ 10,118 | \$18,848 |
| Effect of inflation | | | | | | | 7,109 |
| Effect of discounting | | | | | | | (7,547) |
| Balance as of May 25, 2013 | | | | | | | \$18,410 |

Estimated insurance proceeds are primarily received from an annuity received as part of a legal settlement with an insurance company. Annual proceeds of approximately \$0.3 million are deposited into an escrow account which funds remediation and monitoring costs for three sites related to former operations in Williamstown, Vermont. Annual proceeds received but not expended in the current year accumulate in this account and may be used in future years for costs related to this site through the year 2027. As of May 25, 2013, the balance in this escrow account, which is held in a trust and is not recorded in the Company's Consolidated Balance Sheet, was approximately \$3.4 million. Also included in estimated insurance proceeds are amounts the Company is entitled to receive pursuant to legal settlements as reimbursements from three insurance companies for estimated costs at the site in Uvalde, Texas.

The Company's nuclear garment decontamination facilities are licensed by the Nuclear Regulatory Commission ("NRC"), or, in certain cases, by the applicable state agency, and are subject to regulation by federal, state and local authorities. There can be no assurance that such regulation will not lead to material disruptions in the Company's garment decontamination business.

From time to time, the Company is also subject to legal proceedings and claims arising from the conduct of its business operations, including litigation related to charges for certain ancillary services on invoices, personal injury claims, customer contract matters, employment claims and environmental matters as described above.

While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits and environmental contingencies, the Company believes that the aggregate amount of such liabilities, if any, in excess of amounts covered by insurance have been properly accrued in accordance with US GAAP. It is possible, however, that the future financial position or results of operations for any particular period could be materially affected by changes in the Company's assumptions or strategies related to these contingencies or changes out of the Company's control.

In addition, on December 31, 2012, the Company received a letter from counsel for New England Compounding Center (“NECC”) demanding, among other things, that the Company indemnify NECC regarding claims made against NECC, including those related to NECC’s highly-publicized compounding and sale of tainted methylprednisolone acetate. This demand relates to the limited, once-a-month cleaning services the Company provided to portions of NECC’s cleanroom facilities. Based on its preliminary review of this matter, the Company believes that NECC’s claims are without merit. The Company has notified its insurers of this claim and preliminary discussions concerning coverage have begun. In June 2013, the Company received a subpoena from the Plaintiffs’ Steering Committee appointed in conjunction with the NECC multi-district litigation proceeding seeking information relating to the NECC matter. While the Company is unable to ascertain the ultimate outcome of this matter, based on the information currently available, the Company believes that a loss with respect to this matter is neither probable nor remote, and the Company is unable to reasonably assess an estimate or range of estimates of any potential losses.

9. Income Taxes

The Company’s effective income tax rate was 37.3% and 38.3% for the thirteen and thirty-nine weeks ended May 25, 2013, respectively, as compared to 35.2% and 37.1% for the thirteen and thirty-nine weeks ended May 26, 2012. The increase in the effective income tax rate for the thirteen and thirty-nine weeks ended May 25, 2013 was primarily due to the fact that the Company’s 2012 rate benefited from the reversal of tax contingency reserves related to the resolution of certain state tax audits. In addition, the Company recognized \$0.4 million of tax expense in the thirty-nine weeks ended May 25, 2013 related to non-deductible compensation that was recorded in the first quarter of fiscal 2013. The Company recognizes interest and penalties related to uncertain tax positions as a component of income tax expense which is consistent with the recognition of these items in prior reporting periods. During the thirty-nine weeks ended May 25, 2013, there were no material changes in the amount of unrecognized tax benefits or the amount accrued for interest and penalties.

U.S. and Canadian federal income tax statutes have lapsed for filings up to and including fiscal years 2009 and 2005, respectively, and the Company recently concluded an audit of U.S. federal income taxes for 2010 and 2011. With a few exceptions, the Company is no longer subject to state and local income tax examinations for periods prior to fiscal 2008. The Company is not aware of any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will change significantly in the next 12 months.

10. Long-Term Debt

On May 5, 2011, the Company entered into a \$250.0 million unsecured revolving credit agreement (the “Credit Agreement”) with a syndicate of banks, which matures on May 4, 2016. Under the Credit Agreement, the Company is able to borrow funds at variable interest rates based on, at the Company’s election, the Eurodollar rate or a base rate, plus in each case a spread based on the Company’s consolidated funded debt ratio. Availability of credit requires compliance with certain financial and other covenants, including a maximum consolidated funded debt ratio and minimum consolidated interest coverage ratio as defined in the Credit Agreement. The Company tests its compliance with these financial covenants on a fiscal quarterly basis. At May 25, 2013, the interest rates applicable to the Company’s borrowings under the Credit Agreement would be calculated as LIBOR plus 100 basis points at the time of the respective borrowing. As of May 25, 2013, the Company had no outstanding borrowings, letters of credit amounting to \$47.3 million and \$202.7 million available for borrowing under the Credit Agreement.

On September 14, 2006, the Company issued \$100.0 million of floating rates notes (“Floating Rate Notes”) pursuant to a Note Purchase Agreement (“2006 Note Agreement”). The Floating Rate Notes mature on September 14, 2013, bear interest at LIBOR plus 50 basis points and may be repaid at face value two years from the date of issuance. The Company is currently in the process of evaluating whether it will repay or refinance the Floating Rate Notes as they mature. The Company believes that the repayment or refinancing of the Floating Rate Notes will not adversely affect its financial condition. If the Company chooses not to refinance, it would utilize its current cash reserves and, if necessary, borrowings under its Credit Agreement to satisfy this debt obligation. The Company believes that utilizing its cash in this manner would not negatively impact its liquidity or operations.

As of May 25, 2013, the Company was in compliance with all covenants under the Credit Agreement and the 2006 Note Agreement.

11. Segment Reporting

Operating segments are identified as components of an enterprise for which separate discrete financial information is available for evaluation by the chief operating decision-maker, or decision-making group, in making decisions on how to allocate resources and assess performance. The Company’s chief operating decision maker is the Company’s chief executive officer. The Company has six operating segments based on the information reviewed by its chief executive officer: US Rental and Cleaning, Canadian Rental and Cleaning, Manufacturing (“MFG”), Corporate, Specialty Garments Rental and Cleaning (“Specialty Garments”) and First Aid. The US Rental and Cleaning and Canadian Rental and Cleaning operating segments have been combined to form the US and Canadian Rental and Cleaning reporting segment, and as a result, the Company has five reporting segments.

The US and Canadian Rental and Cleaning reporting segment purchases, rents, cleans, delivers and sells, uniforms and protective clothing and non-garment items in the United States and Canada. The laundry locations of the US and Canadian Rental and Cleaning reporting segment are referred to by the Company as “industrial laundries” or “industrial laundry locations.”

The MFG operating segment designs and manufactures uniforms and non-garment items solely for the purpose of providing these goods to the US and Canadian Rental and Cleaning reporting segment. MFG revenues are generated when goods are shipped from the Company’s manufacturing facilities, or its subcontract manufacturers, to other Company locations. These revenues are recorded at a transfer price which is typically in excess of the actual manufacturing cost. Products are carried in inventory and subsequently placed in service and amortized at this transfer price. On a consolidated basis, intercompany revenues and income are eliminated and the carrying value of inventories and rental merchandise in service is reduced to the manufacturing cost. Income before income taxes from MFG net of the intercompany MFG elimination offsets the merchandise amortization costs incurred by the US and Canadian Rental and Cleaning reporting segment as the merchandise costs of this reporting segment are amortized and recognized based on inventories purchased from MFG at the transfer price which is above the Company’s manufacturing cost.

The Corporate operating segment consists of costs associated with the Company’s distribution center, sales and marketing, information systems, engineering, materials management, manufacturing planning, finance, budgeting, human resources, other general and administrative costs and interest expense. The revenues generated from the Corporate operating segment represent certain direct sales made by the Company directly from its distribution center. The products sold by this operating segment are the same products rented and sold by the US and Canadian Rental and Cleaning reporting segment. In the table below, no assets or capital expenditures are presented for the Corporate operating segment because no assets are allocated to this operating segment in the information reviewed by the chief executive officer. However, depreciation and amortization expense related to certain assets are reflected in income from operations and income before income taxes for the Corporate operating segment. The assets that give rise to this depreciation and amortization are included in the total assets of the US and Canadian Rental and Cleaning reporting segment as this is how they are tracked and reviewed by the Company. The majority of expenses accounted for within the Corporate segment relate to costs of the US and Canadian Rental and Cleaning segment, with the remainder of the costs relating to the Specialty Garment and First Aid segments.

The Specialty Garments operating segment purchases, rents, cleans, delivers and sells, specialty garments and non-garment items primarily for nuclear and cleanroom applications. The First Aid operating segment sells first aid cabinet services and other safety supplies as well as maintains wholesale distribution and pill packaging operations.

Edgar Filing: UNIFIRST CORP - Form 10-Q

The Company refers to the US and Canadian Rental and Cleaning, MFG, and Corporate reporting segments combined as its “core laundry operations,” which is included as a subtotal in the following tables (in thousands):

| Thirteen weeks ended | US and | | Net Interco MFG Elim | Corporate | Subtotal | | | Total |
|--------------------------------|---------------------------------------|------------|-------------------------------|------------------|--------------------------------------|-------------------------------|----------------------|--------------|
| | Canadian Rental and Cleaning | MFG | | | Core Laundry Operations | Specialty Garments | First Aid | |
| May 25, 2013 | | | | | | | | |
| Revenues | \$294,341 | \$41,859 | \$(41,859) | \$3,388 | \$297,729 | \$26,327 | \$11,708 | \$335,764 |
| Income (loss) from operations | \$48,030 | \$15,364 | \$(2,663) | \$(20,375) | \$40,356 | \$3,576 | \$1,865 | \$45,797 |
| Interest (income) expense, net | \$(716) | \$— | \$— | \$399 | \$(317) | \$— | \$— | \$(317) |
| Income (loss) before taxes | \$48,744 | \$15,243 | \$(2,663) | \$(20,777) | \$40,547 | \$3,418 | \$1,866 | \$45,831 |
| May 26, 2012 | | | | | | | | |
| Revenues | \$277,871 | \$39,954 | \$(39,954) | \$3,270 | \$281,141 | \$29,263 | \$10,527 | \$320,931 |
| Income (loss) from operations | \$42,538 | \$13,076 | \$(2,054) | \$(17,285) | \$36,275 | \$5,033 | \$1,364 | \$42,672 |
| Interest (income) expense, net | \$(770) | \$— | \$— | \$625 | \$(145) | \$— | \$— | \$(145) |
| Income (loss) before taxes | \$43,311 | \$13,117 | \$(2,053) | \$(17,974) | \$36,401 | \$4,595 | \$1,364 | \$42,360 |
| Thirty-nine weeks ended | US and Canadian | MFG | Net Interco | Corporate | Subtotal Core Laundry | Specialty Garments | First Aid | Total |

Edgar Filing: UNIFIRST CORP - Form 10-Q

| | Rental and Cleaning | | MFG Elim | | Operations | | | | |
|--------------------------------|-------------------------------|-----------|-------------|------------|------------|----------|----------|-------------|--|
| May 25, 2013 | | | | | | | | | |
| Revenues | \$883,424 | \$122,631 | \$(122,631) | \$10,494 | \$893,918 | \$76,804 | \$31,917 | \$1,002,639 | |
| Income (loss) from operations | \$147,712 | \$43,469 | \$(5,669) | \$(60,301) | \$125,211 | \$9,555 | \$3,879 | \$138,645 | |
| Interest (income) expense, net | \$(2,237) | \$— | \$— | \$1,089 | \$(1,148) | \$— | \$— | \$(1,148) | |
| Income (loss) before taxes | \$149,950 | \$43,263 | \$(5,669) | \$(61,414) | \$126,130 | \$9,462 | \$3,880 | \$139,472 | |
| May 26, 2012 | | | | | | | | | |
| Revenues | \$820,823 | \$116,332 | \$(116,332) | \$9,838 | \$830,661 | \$83,032 | \$30,222 | \$943,915 | |
| Income (loss) from operations | \$121,307 | \$35,576 | \$(2,153) | \$(56,024) | \$98,706 | \$14,175 | \$2,981 | \$115,862 | |
| Interest (income) expense, net | \$(1,877) | \$— | \$— | \$1,480 | \$(397) | \$— | \$— | \$(397) | |
| Income (loss) before taxes | \$123,176 | \$35,635 | \$(2,152) | \$(57,577) | \$99,082 | \$13,168 | \$2,981 | \$115,231 | |

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

SAFE HARBOR FOR FORWARD LOOKING STATEMENTS

This Quarterly Report on Form 10-Q and any documents incorporated by reference contain forward looking statements within the meaning of the federal securities laws. Forward looking statements contained in this Quarterly Report on Form 10-Q and any documents incorporated by reference are subject to the safe harbor created by the Private Securities Litigation Reform Act of 1995. Forward looking statements may be identified by words such as “estimates,” “anticipates,” “projects,” “plans,” “expects,” “intends,” “believes,” “seeks,” “could,” “should,” “may,” “will,” or their variations thereof, and similar expressions and by the context in which they are used. Such forward looking statements are based upon our current expectations and speak only as of the date made. Such statements are highly dependent upon a variety of risks, uncertainties and other important factors that could cause actual results to differ materially from those reflected in such forward looking statements. Such factors include, but are not limited to, uncertainties caused by the continuing adverse worldwide economic conditions, uncertainties regarding our ability to consummate and successfully integrate acquired businesses, uncertainties regarding any existing or newly-discovered expenses and liabilities related to environmental compliance and remediation, any adverse outcome of pending or future contingencies or claims, our ability to compete successfully without any significant degradation in our margin rates, seasonal fluctuations in business levels, our ability to preserve positive labor relationships and avoid becoming the target of corporate labor unionization campaigns that could disrupt our business, the effect of currency fluctuations on our results of operations and financial condition, our dependence on third parties to supply us with raw materials, any loss of key management or other personnel, increased costs as a result of any future changes in federal or state laws, rules and regulations or governmental interpretation of such laws, rules and regulations, uncertainties regarding the price levels of natural gas, electricity, fuel and labor, the impact of adverse economic conditions and the current tight credit markets on our customers and such customers’ workforces, the level and duration of workforce reductions by our customers, the continuing increase in domestic healthcare costs, demand and prices for our products and services, rampant criminal activity and instability in Mexico where our principal garment manufacturing plants are located, our ability to properly and efficiently design, construct, implement and operate our new CRM computer system, additional professional and internal costs necessary for compliance with recent and proposed future changes in Securities and Exchange Commission, New York Stock Exchange and accounting rules, strikes and unemployment levels, our efforts to evaluate and potentially reduce internal costs, economic and other developments associated with the war on terrorism and its impact on the economy, general economic conditions and other factors described under “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended August 25, 2012 and in other filings with the Securities and Exchange Commission. We undertake no obligation to update any forward looking statements to reflect events or circumstances arising after the date on which such statements are made.

Business Overview

UniFirst Corporation, together with its subsidiaries, hereunder referred to as “we”, “our”, the “Company”, or “UniFirst”, is one of the largest providers of workplace uniforms and protective clothing in the United States. We design, manufacture,

personalize, rent, clean, deliver, and sell a wide range of uniforms and protective clothing, including shirts, pants, jackets, coveralls, lab coats, smocks, aprons and specialized protective wear, such as flame resistant and high visibility garments. We also rent industrial wiping products, floor mats, facility service products and other non-garment items, and provide first aid cabinet services and other safety supplies, to a variety of manufacturers, retailers and service companies.

We serve businesses of all sizes in numerous industry categories. Typical customers include automobile service centers and dealers, delivery services, food and general merchandise retailers, food processors and service operations, light manufacturers, maintenance facilities, restaurants, service companies, soft and durable goods wholesalers, transportation companies, and others who require employee clothing for image, identification, protection or utility purposes. We also provide our customers with restroom supplies, including air fresheners, paper products and hand soaps.

At certain specialized facilities, we also decontaminate and clean work clothes that may have been exposed to radioactive materials and service special cleanroom protective wear. Typical customers for these specialized services include government agencies, research and development laboratories, high technology companies and utilities operating nuclear reactors.

We continue to expand into additional geographic markets through acquisitions and organic growth. We currently service over 240,000 customer locations in the United States, Canada and Europe from 219 customer service, distribution and manufacturing facilities.

As discussed and described in Note 11 to the Consolidated Financial Statements, we have five reporting segments: US and Canadian Rental and Cleaning, Manufacturing (“MFG”), Corporate, Specialty Garments Rental and Cleaning (“Specialty Garments”) and First Aid. We refer to the laundry locations of the US and Canadian Rental and Cleaning reporting segment as “industrial laundries” or “industrial laundry locations”, and to the US and Canadian Rental and Cleaning, MFG, and Corporate reporting segments combined as our “core laundry operations.”

Critical Accounting Policies and Estimates

The discussion of our financial condition and results of operations is based upon the Consolidated Financial Statements, which have been prepared in conformity with United States generally accepted accounting principles (“US GAAP”). As such, management is required to make certain estimates, judgments and assumptions that are believed to be reasonable based on the information available. These estimates and assumptions affect the reported amount of assets and liabilities, revenues and expenses, and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, the most important and pervasive accounting policies used and areas most sensitive to material changes from external factors. See Note 1 to the Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended August 25, 2012 for additional discussion of the application of these and other accounting policies.

Results of Operations

The following table presents certain selected financial data, including the percentage of revenues represented by each item, for the thirteen and thirty-nine weeks ended May 25, 2013 and the thirteen and thirty-nine weeks ended May 26, 2012. Cost of revenues presented in the table below include merchandise costs related to the amortization of rental merchandise in service and direct sales as well as labor and other production, service and delivery costs associated with operating our industrial laundries, Specialty Garments facilities, First Aid locations and our distribution center. Selling and administrative costs include costs related to our sales and marketing functions as well as general and administrative costs associated with our corporate offices and operating locations including information systems, engineering, materials management, manufacturing planning, finance, budgeting, and human resources.

| (In thousands, except percentages) | Thirteen weeks ended | | | | | Thirty-nine weeks ended | | | | | |
|------------------------------------|----------------------|-----------|--------------|-----------|----------|-------------------------|-----------|--------------|-----------|----------|--|
| | May 25, 2013 | % of Rev. | May 26, 2012 | % of Rev. | % Change | May 25, 2013 | % of Rev. | May 26, 2012 | % of Rev. | % Change | |
| Revenues | \$335,764 | 100.0% | \$320,931 | 100.0% | 4.6 % | \$1,002,639 | 100.0% | \$943,915 | 100.0% | 6.2 % | |
| Operating expenses: | | | | | | | | | | | |
| Cost of revenues (1) | 208,066 | 62.0 | 202,433 | 63.1 | 2.8 | 618,038 | 61.6 | 599,009 | 63.5 | 3.2 | |
| | 64,786 | 19.3 | 59,108 | 18.4 | 9.6 | 194,891 | 19.4 | 179,429 | 19.0 | 8.6 | |

Edgar Filing: UNIFIRST CORP - Form 10-Q

| | | | | | | | | | | |
|-----------------------------------------|----------|-------|----------|-------|---------|----------|--------|----------|-------|---------|
| Selling and administrative expenses (1) | | | | | | | | | | |
| Depreciation and amortization | 17,115 | 5.1 | 16,718 | 5.2 | 2.4 | 51,065 | 5.1 | 49,615 | 5.3 | 2.9 |
| Total operating expenses | 289,967 | 86.4 | 278,259 | 86.7 | 4.2 | 863,994 | 86.2 | 828,053 | 87.7 | 4.3 |
| Income from operations | 45,797 | 13.6 | 42,672 | 13.3 | 7.3 | 138,645 | 13.8 | 115,862 | 12.3 | 19.7 |
| Other (income) expense | (34) | 0.0 | 312 | 0.1 | (110.9) | (827) | (0.1) | 631 | 0.1 | (231.1) |
| Income before income taxes | 45,831 | 13.6 | 42,360 | 13.2 | 8.2 | 139,472 | 13.9 | 115,231 | 12.2 | 21.0 |
| Provision for income taxes | 17,109 | 5.1 | 14,901 | 4.6 | 14.8 | 53,348 | 5.3 | 42,774 | 4.5 | 24.7 |
| Net income | \$28,722 | 8.6 % | \$27,459 | 8.6 % | 4.6 % | \$86,124 | 8.6 % | \$72,457 | 7.7 % | 18.9 % |

(1) Exclusive of depreciation on our property, plant and equipment and amortization on our intangible assets.

General

We derive our revenues through the design, manufacture, personalization, rental, cleaning, delivering, and selling of a wide range of uniforms and protective clothing, including shirts, pants, jackets, coveralls, lab coats, smocks and aprons and specialized protective wear, such as flame resistant and high visibility garments. We also rent industrial wiping products, floor mats, facility service products, other non-garment items, and provide first aid cabinet services and other safety supplies, to a variety of manufacturers, retailers and service companies. We have five reporting segments, US and Canadian Rental and Cleaning, Manufacturing (“MFG”), Corporate, Specialty Garments Rental and Cleaning (“Specialty Garments”), and First Aid. We refer to the US and Canadian Rental and Cleaning, MFG, and Corporate reporting segments combined as our “core laundry operations.”

Cost of revenues include merchandise costs related to the amortization of rental merchandise in service and direct sales as well as labor and other production, service and delivery costs, and distribution costs associated with operating our core laundry operations, Specialty Garments facilities, and First Aid locations. Selling and administrative costs include costs related to our sales and marketing functions as well as general and administrative costs associated with our corporate offices and operating locations including information systems, engineering, materials management, manufacturing planning, finance, budgeting, and human resources.

The price of fuel and energy needed to run our vehicles and equipment is unpredictable and fluctuates based on events outside our control, including geopolitical developments, supply and demand for oil and gas, actions by OPEC and other oil and gas producers, war and unrest in oil producing countries, regional production patterns, limits on refining capacities, natural disasters and environmental concerns. Future increases in fuel costs could impact our results going forward.

The current worldwide economic uncertainty may negatively impact our revenues and operating performance in fiscal 2013 and beyond due to the impact on spending plans and employment levels of our customers and sales prospects. Throughout fiscal 2012 and into fiscal 2013, U.S. and Canadian unemployment rates remained high, which had a negative effect on wearer levels and, as a result, on our business.

Thirteen weeks ended May 25, 2013 compared with thirteen weeks ended May 26, 2012

Revenues

| (In thousands, except percentages) | May 25, | May 26, | Dollar | Percent | |
|------------------------------------|-----------|-----------|----------|---------|---|
| | 2013 | 2012 | Change | Change | |
| Core Laundry Operations | \$297,729 | \$281,141 | \$16,588 | 5.9 | % |
| Specialty Garments | 26,327 | 29,263 | (2,936) | (10.0) |) |
| First Aid | 11,708 | 10,527 | 1,181 | 11.2 | |
| Consolidated total | \$335,764 | \$320,931 | \$14,833 | 4.6 | % |

For the thirteen weeks ended May 25, 2013, our consolidated revenues increased by \$14.8 million from the comparable period in fiscal 2012, or 4.6%. This increase was due to a \$16.6 million increase in revenues from our core laundry operations. Core laundry operations' revenues increased to \$297.7 million for the thirteen weeks ended May 25, 2013 from \$281.1 million for the comparable period of fiscal 2012, or 5.9%. Excluding the effect of acquisitions and a weaker Canadian dollar, core laundry operations' revenues grew primarily due to organic growth of 5.9%, which is comprised of new sales, additions to our existing customer base and price increases offset by lost accounts and reductions to our existing customer base. Organic growth benefited from solid new account sales. In addition, certain annual price adjustments also contributed to the revenue growth during the quarter. Our revenues also benefitted from higher charges for lost and damaged merchandise as well as higher garment make-up and emblem charges compared to a year ago.

Specialty Garments' revenues decreased to \$26.3 million in the third fiscal quarter of 2013 from \$29.3 million in the comparable period of 2012, a decrease of 10.0%. This decrease was primarily the result of the completion of two large

power reactor rebuild projects in the fourth quarter of fiscal 2012. This segment's results are often affected by the timing and length of its customers' power reactor outages as well as its project-based activities. First Aid revenues increased by \$1.2 million, or 11.2%, for the thirteen weeks ended May 25, 2013 as compared to the same period in fiscal 2012 as a result of improved performance from the segment's wholesale distribution and pill packaging operations.

Cost of Revenues

For the thirteen weeks ended May 25, 2013, cost of revenues decreased to 62.0% of revenues, or \$208.1 million, from 63.1% of revenues, or \$202.4 million, for the thirteen weeks ended May 26, 2012. This decrease was primarily due to lower merchandise, energy and payroll costs as a percentage of revenues in our core laundry operations, primarily due to the revenue growth this segment experienced in the thirteen weeks ended May 25, 2013. In addition, the Company benefited from lower bad debt expense in the quarter compared to the comparable period in 2012. These lower costs as a percentage of revenues were partially offset by an increase in the cost of revenues for the Specialty Garments' segment as a percentage of revenues due to the revenue contraction that segment experienced during the quarter.

Selling and Administrative Expense

For the thirteen weeks ended May 25, 2013, selling and administrative expenses increased to 19.3% of revenues, or \$64.8 million, from 18.4% of revenues, or \$59.1 million, for the thirteen weeks ended May 26, 2012. This increase was primarily due to a settlement we entered into during the thirteen weeks ended May 26, 2012 related to environmental litigation. As a result of the settlement, we recognized a gain in the third quarter of our prior fiscal year of approximately \$6.7 million. Excluding the effect of this settlement, selling and administrative costs would have decreased from 20.5% of revenues in the thirteen weeks ended May 26, 2012 to the 19.3% of revenues for the thirteen weeks ended May 25, 2013. This decrease was primarily due to lower selling payroll costs as a percentage of revenues. In addition, comparisons also benefited from certain costs we incurred in the thirteen weeks ended May 26, 2012 associated with our company-wide initiative to update our customer service systems.

Depreciation and Amortization

Our depreciation and amortization expense was \$17.1 million, or 5.1% of revenues, for the thirteen weeks ended May 25, 2013 compared to \$16.7 million, or 5.2% of revenues, for the thirteen weeks ended May 26, 2012. The increase in depreciation and amortization expense was due to capital expenditure and acquisition activity in earlier periods.

Income from Operations

For the thirteen weeks ended May 25, 2013 and May 26, 2012, changes in our revenues and costs as discussed above resulted in the following changes in our income from operations:

| (In thousands, except percentages) | May 25, 2013 | May 26, 2012 | Dollar Change | Percent Change | |
|-------------------------------------------|-----------------------------|-----------------------------|--------------------------|---------------------------|---|
| Core Laundry Operations | \$40,356 | \$36,275 | \$4,081 | 11.3 | % |
| Specialty Garments | 3,576 | 5,033 | (1,457) | (29.0) |) |
| First Aid | 1,865 | 1,364 | 501 | 36.7 | |
| Consolidated total | \$45,797 | \$42,672 | \$3,125 | 7.3 | % |

Other (Income) Expense

Other (income) expense, which includes interest expense, interest income and exchange rate loss, was a nominal gain in the thirteen weeks ended May 25, 2013 compared to a loss of \$0.3 million in the thirteen weeks ended May 26, 2012. Net interest income in the thirteen weeks ended May 25, 2013 increased to \$0.3 million from \$0.1 million in the thirteen weeks ended May 26, 2012. The benefit related to a decrease in the interest rates affecting our variable rate debt. In addition, we experienced an exchange rate loss of \$0.3 million in the thirteen weeks ended May 25, 2013 compared to a loss of \$0.5 million in the comparable period of fiscal 2012.

Provision for Income Taxes

Our effective income tax rate was 37.3% for the thirteen weeks ended May 25, 2013, compared to 35.2% for the thirteen weeks ended May 26, 2012. Our effective tax rate was higher than the comparable period of 2012 primarily due to the fact that the 2012 rate benefited from the reversal of tax contingency reserves related to the resolution of certain state tax audits.

Thirty-nine weeks ended May 25, 2013 compared with Thirty-nine weeks ended May 26, 2012

Revenues

| (In thousands, except percentages) | May 25, | May 26, | Dollar | Percent | |
|------------------------------------|-------------|-----------|----------|---------|---|
| | 2013 | 2012 | Change | Change | |
| Core Laundry Operations | \$893,918 | \$830,661 | \$63,257 | 7.6 | % |
| Specialty Garments | 76,804 | 83,032 | (6,228) | (7.5) |) |
| First Aid | 31,917 | 30,222 | 1,695 | 5.6 | |
| Consolidated total | \$1,002,639 | \$943,915 | \$58,724 | 6.2 | % |

For the thirty-nine weeks ended May 25, 2013, our consolidated revenues increased by \$58.7 million from the comparable period in fiscal 2012, or 6.2%. The consolidated increase was primarily driven by a \$63.3 million increase in our core laundry operations' segment. Core laundry operations' revenues increased to \$893.9 million for the thirty-nine weeks ended May 25, 2013 from \$830.7 million for the comparable period of fiscal 2012, an increase of 7.6%. Excluding the effect of acquisitions and a slightly stronger Canadian dollar, revenues grew primarily due to organic growth of 7.4%, which is comprised of new sales, additions to our existing customer base and price increases offset by lost accounts and reductions to our existing customer base. Organic growth in the thirty-nine weeks ended May 25, 2013 benefited from new account sales as well as certain annual price adjustments. Our revenues also benefited from higher charges for lost and damaged merchandise as well as higher garment make-up and emblem charges compared to a year ago.

Specialty Garments' revenues decreased to \$76.8 million in the thirty-nine weeks ended May 25, 2013 from \$83.0 million in the comparable period of 2012, a decrease of 7.5%. This decrease was primarily due to the completion of two large power reactor rebuild projects in the fourth quarter of fiscal 2012, as well as weaker results from the segment's European operations. This segment's results are often affected by the timing and length of its customers' power reactor outages as well as its project-based activities. First Aid revenues increased by \$1.7 million, or 5.6%, in the thirty-nine weeks ended May 25, 2013 as compared with the same period in fiscal 2012 as a result of improved performance from the segment's wholesale distribution and pill packaging operations.

Cost of Revenues

For the thirty-nine weeks ended May 25, 2013, cost of revenues decreased to 61.6% of revenues, or \$618.0 million, from 63.5% of revenues, or \$599.0 million, for the thirty-nine weeks ended May 26, 2012. This decrease was primarily due to lower merchandise, energy, payroll, and other production costs as a percentage of revenues in our core laundry operations, primarily due to the strong revenue growth this segment experienced in the thirty-nine weeks ended May 25, 2013. These lower costs as a percentage of revenues were partially offset by an increase in the cost of revenues for the Specialty Garments' segment as a percentage of revenues due to the revenue contraction that segment experienced in the thirty-nine weeks ended May 25, 2013.

Selling and Administrative Expense

Our selling and administrative expenses increased to 19.4% of revenues, or \$194.9 million, for the thirty-nine weeks ended May 25, 2013 from 19.0% of revenues, or \$179.4 million, for the thirty-nine weeks ended May 26, 2012. This increase was primarily due to a settlement we entered into during the thirteen weeks ended May 26, 2012 related to environmental litigation. As a result of the settlement, we recognized a gain in the third quarter of our prior fiscal year of approximately \$6.7 million. Excluding the effect of this settlement, selling and administrative costs would have decreased from 19.7% of revenues in the thirty-nine weeks ended May 26, 2012 to the 19.4% of revenues in the thirty-nine weeks ended May 25, 2013. This decrease was primarily due to lower selling and administrative payroll costs as a percentage of revenues. In addition, comparisons benefited from certain costs we incurred in the thirty-nine weeks ended May 26, 2012 associated with our company-wide initiative to update our customer service systems.

Depreciation and Amortization

Our depreciation and amortization expense was \$51.1 million, or 5.1% of revenues, for the thirty-nine weeks ended May 25, 2013 compared to \$49.6 million, or 5.3% of revenues, for the thirty-nine weeks ended May 26, 2012. Depreciation and amortization expense increased due to capital expenditure and acquisition activity in earlier periods but decreased as a percentage of revenues due to the strong revenue growth we experienced in the thirty-nine weeks ended May 25, 2013.

Income from Operations

For the thirty-nine weeks ended May 25, 2013 and May 26, 2012, the revenue growth in our operations, as well as the change in our costs as discussed above, resulted in the following changes in our income from operations:

| (In thousands, except percentages) | May 25, | May 26, | Dollar | Percent | |
|------------------------------------|------------|------------|-----------|---------|---|
| | 2013 | 2012 | Change | Change | |
| Core Laundry Operations | \$ 125,211 | \$ 98,706 | \$ 26,505 | 26.9 | % |
| Specialty Garments | 9,555 | 14,175 | (4,620) | (32.6) |) |
| First Aid | 3,879 | 2,981 | 898 | 30.1 | |
| Consolidated total | \$ 138,645 | \$ 115,862 | \$ 22,783 | 19.7 | % |

Other (Income) Expense

Other (income) expense, which includes interest expense, interest income and foreign currency exchange (gain) loss, was a gain of \$0.8 million for the thirty-nine weeks ended May 25, 2013 as compared with a loss of \$0.6 million for the thirty-nine weeks ended May 26, 2012. The increase was primarily due to net interest income in the thirty-nine weeks ended May 25, 2013 of \$1.1 million compared to net interest income of \$0.4 million in the thirty-nine weeks ended May 26, 2012. This benefit related to a decrease in the interest rates affecting our variable rate debt as well as slightly lower average debt outstanding in the thirty-nine weeks ended May 25, 2013 compared to the comparable period of fiscal 2012. In addition, we experienced an exchange rate loss of \$0.3 million in the thirty-nine weeks ended May 25, 2013 compared to a loss of \$1.0 million in the comparable period of fiscal 2012.

Provision for Income Taxes

Our effective income tax rate was 38.3% for the thirty-nine weeks ended May 25, 2013, as compared to 37.1% for the thirty-nine weeks ended May 26, 2012. Our tax rate in the thirty-nine weeks ended May 25, 2013 was higher than in the comparable period of fiscal 2012 primarily due to the fact that the 2012 rate benefited from the reversal of tax contingency reserves related to the resolution of certain state tax audits as well as \$0.4 million of tax expense that we recognized in fiscal 2013 related to non-deductible compensation.

Liquidity and Capital Resources

General

As of May 25, 2013, we had cash and cash equivalents of \$175.6 million and working capital of \$297.9 million. In addition, we generated \$139.5 million and \$161.7 million in cash from operating activities in the nine months ended May 25, 2013 and the twelve months ended August 25, 2012, respectively. We believe that our current cash and cash equivalent balances, our cash generated from future operations and amounts available under our Credit Agreement (defined below) will be sufficient to meet our current anticipated working capital and capital expenditure requirements for at least the next 12 months.

Sources and Uses of Cash

During the thirty-nine weeks ended May 25, 2013, we generated cash from operating activities of \$139.5 million resulting primarily from net income of \$86.1 million, net of non-cash amounts charged for depreciation, amortization and accretion of \$52.1 million and share-based compensation of \$5.1 million. We also generated cash as a result of a decrease in inventories of \$3.1 million, a decrease in rental merchandise in service of \$4.3 million and an increase in accounts payable and accrued liabilities of \$11.5 million. These inflows were partially offset by an increase in receivables of \$12.1 million, an increase in prepaid expenses of \$3.8 million and a decrease in accrued income taxes of \$6.9 million. We used cash during this period to, among other things, invest \$81.1 million in capital expenditures, of which \$16.4 million related to our ongoing project to update our customer service system, as well as fund the acquisition of businesses in the amount of approximately \$2.0 million. In addition, we remitted \$3.3 million in taxes which were withheld in the form of Common Stock and related to the net settlement of equity awards.

We have accumulated \$60.1 million in cash outside the United States that is expected to be invested indefinitely in our foreign subsidiaries. If these funds were distributed to the U.S. in the form of dividends, we would likely be subject to additional U.S. income taxes.

Long-Term Debt and Borrowing Capacity

On May 5, 2011, we entered into a \$250.0 million unsecured revolving credit agreement (the "Credit Agreement") with a syndicate of banks, which matures on May 4, 2016. Under the Credit Agreement, we are able to borrow funds at variable interest rates based on, at our election, the Eurodollar rate or a base rate, plus in each case a spread based on our consolidated funded debt ratio. Availability of credit requires compliance with certain financial and other

covenants, including a maximum consolidated funded debt ratio and minimum consolidated interest coverage ratio as defined in the Credit Agreement. We test our compliance with these financial covenants on a fiscal quarterly basis. At May 25, 2013, the interest rates applicable to our borrowings under the Credit Agreement were calculated as LIBOR plus 100 basis points at the time of the respective borrowing. As of May 25, 2013, we had no outstanding borrowings, letters of credit amounting to \$47.3 million and \$202.7 million available for borrowing under the Credit Agreement.

On September 14, 2006, we issued \$100.0 million of floating rates notes (“Floating Rate Notes”) pursuant to a Note Purchase Agreement (“2006 Note Agreement”). The Floating Rate Notes mature on September 14, 2013, bear interest at LIBOR plus 50 basis points and may be repaid at face value two years from the date of issuance. We are currently in the process of evaluating whether we will repay or refinance the Floating Rate Notes as they mature. We believe that the repayment or refinancing of the Floating Rate Notes will not adversely affect our financial condition. If we choose not to refinance, we would utilize our current cash reserves and, if necessary, borrowings under our Credit Agreement to satisfy this debt obligation. We believe that utilizing our cash in this manner would not negatively impact our liquidity or operations.

As of May 25, 2013, we were in compliance with all covenants under the Credit Agreement and the 2006 Note Agreement.

Commitments and Contingencies

We are subject to various federal, state and local laws and regulations governing, among other things, air emissions, wastewater discharges, and the generation, handling, storage, transportation, treatment and disposal of hazardous wastes and other substances. In particular, industrial laundries currently use and must dispose of detergent waste water and other residues, and, in the past, used perchloroethylene and other dry cleaning solvents. We are attentive to the environmental concerns surrounding the disposal of these materials and have, through the years, taken measures to avoid their improper disposal. Over the years, we have settled, or contributed to the settlement of, actions or claims brought against us relating to the disposal of hazardous materials and there can be no assurance that we will not have to expend material amounts to remediate the consequences of any such disposal in the future.

US GAAP requires that a liability for contingencies be recorded when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated. Significant judgment is required to determine the existence of a liability, as well as the amount to be recorded. We regularly consult with attorneys and outside consultants in our consideration of the relevant facts and circumstances before recording a contingent liability. Changes in enacted laws, regulatory orders or decrees, management’s estimates of costs, insurance proceeds, participation by other parties, the timing of payments and the input of outside consultants and attorneys based on changing legal or factual circumstances could have a material impact on the amounts recorded for environmental and other contingent liabilities.

Under environmental laws, an owner or lessee of real estate may be liable for the costs of removal or remediation of certain hazardous or toxic substances located on, or in, or emanating from such property, as well as related costs of investigation and property damage. Such laws often impose liability without regard to whether the owner or lessee knew of, or was responsible for, the presence of such hazardous or toxic substances. There can be no assurances that acquired or leased locations have been operated in compliance with environmental laws and regulations or that future uses or conditions will not result in the imposition of liability upon our Company under such laws or expose our Company to third party actions such as tort suits. We continue to address environmental conditions under terms of consent orders negotiated with the applicable environmental authorities or otherwise with respect to sites located in or related to Woburn, Massachusetts, Somerville, Massachusetts, Springfield, Massachusetts, Uvalde, Texas, Stockton, California, three sites related to former operations in Williamstown, Vermont, as well as sites located in Goldsboro, North Carolina, Wilmington, North Carolina and Landover, Maryland.

We have accrued certain costs related to the sites described above as it has been determined that the costs are probable and can be reasonably estimated. We continue to implement mitigation measures and to monitor environmental conditions at the Somerville, Massachusetts site. We also have potential exposure related to an additional parcel of land (the "Central Area") related to the Woburn, Massachusetts site discussed above. Currently, the consent decree for the Woburn site does not define or require any remediation work in the Central Area. The United States Environmental Protection Agency (the "EPA") has provided us and other signatories to the consent decree with comments on the design and implementation of groundwater and soil remedies at the Woburn site and investigation of environmental conditions in the Central Area. We, and other signatories, have implemented and proposed to do additional work at the Woburn site but many of the EPA's comments remain to be resolved. We have accrued costs to perform certain work responsive to EPA's comments. In addition, we have responded to requests for information, and recently received notices of violation, from the EPA under the Clean Air Act regarding our handling of and operations with respect to the laundering of soiled towels, and we are addressing these matters.

We routinely review and evaluate sites that may require remediation and monitoring and determine our estimated costs based on various estimates and assumptions. These estimates are developed using our internal sources or by third-party environmental engineers or other service providers. Internally developed estimates are based on:

- Management's judgment and experience in remediating and monitoring our sites;
- Information available from regulatory agencies as to costs of remediation and monitoring;
- The number, financial resources and relative degree of responsibility of other potentially responsible parties (PRPs) who may be liable for remediation and monitoring of a specific site; and
- The typical allocation of costs among PRPs.

Edgar Filing: UNIFIRST CORP - Form 10-Q

There is usually a range of reasonable estimates of the costs associated with each site. Our accruals represent the amount within the range that constitutes our best estimate. When we believe that both the amount of a particular liability and the timing of the payments are reliably determinable, we adjust the cost in current dollars using a rate of 3% for inflation until the time of expected payment and discount the cost to present value using current risk-free interest rates. As of May 25, 2013, the risk-free interest rates we utilized ranged from 2.0% to 3.2%.

For environmental liabilities that have been discounted, we include interest accretion, based on the effective interest method, in selling and administrative expenses on the Consolidated Statements of Income. The changes to the amounts of our environmental liabilities for the thirty-nine weeks ended May 25, 2013 are as follows (in thousands):

| | May 25, 2013 |
|----------------------------------------------------|-----------------------------|
| Beginning balance as of August 25, 2012 | \$20,020 |
| Payments made for which reserves had been provided | (1,478) |
| Insurance proceeds received | 163 |
| Interest accretion | 407 |
| Change in discount rates | (702) |
| Balance as of May 25, 2013 | \$18,410 |

Anticipated payments and insurance proceeds relating to currently identified environmental remediation liabilities as of May 25, 2013, for the next five fiscal years and thereafter, as measured in current dollars, are reflected below.

| (In thousands) | 2013 | 2014 | 2015 | 2016 | 2017 | Thereafter | Total |
|-----------------------------------|-------------|-------------|-------------|-------------|-------------|-------------------|--------------|
| Estimated costs – current dollars | \$3,785 | \$2,470 | \$1,437 | \$950 | \$752 | \$ 11,861 | \$21,255 |
| Estimated insurance proceeds | — | (173) | (159) | (173) | (159) | (1,743) | (2,407) |
| Net anticipated costs | \$3,785 | \$2,297 | \$1,278 | \$777 | \$593 | \$ 10,118 | \$18,848 |
| Effect of inflation | | | | | | | 7,109 |
| Effect of discounting | | | | | | | (7,547) |
| Balance as of May 25, 2013 | | | | | | | \$18,410 |

Estimated insurance proceeds are primarily received from an annuity received as part of our legal settlement with an insurance company. Annual proceeds of approximately \$0.3 million are deposited into an escrow account which funds remediation and monitoring costs for three sites related to our former operations in Williamstown, Vermont. Annual proceeds received but not expended in the current year accumulate in this account and may be used in future years for costs related to this site through the year 2027. As of May 25, 2013, the balance in this escrow account, which is held in a trust and is not recorded in our Consolidated Balance Sheet, was approximately \$3.4 million. Also included in estimated insurance proceeds are amounts we are entitled to receive pursuant to legal settlements as reimbursements from three insurance companies for estimated costs at the site in Uvalde, Texas.

Our nuclear garment decontamination facilities are licensed by the Nuclear Regulatory Commission (“NRC”), or, in certain cases, by the applicable state agency, and are subject to regulation by federal, state and local authorities. There can be no assurance that such regulation will not lead to material disruptions in our garment decontamination business.

From time to time, we are also subject to legal proceedings and claims arising from the conduct of our business operations, including litigation related to charges for certain ancillary services on invoices, personal injury claims, customer contract matters, employment claims and environmental matters as described above.

While it is impossible for us to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits and environmental contingencies, we believe that the aggregate amount of such liabilities, if any, in excess of amounts covered by insurance have been properly accrued in accordance with accounting principles generally accepted in the United States. It is possible, however, that the future financial position and/or results of operations for any particular future period could be materially affected by changes in our assumptions or strategies related to these contingencies or changes out of our control.

In addition, on December 31, 2012, we received a letter from counsel for New England Compounding Center (“NECC”) demanding, among other things, that we indemnify NECC regarding claims made against NECC, including those

related to NECC's highly-publicized compounding and sale of tainted methylprednisolone acetate. This demand relates to the limited, once-a-month cleaning services we provided to portions of NECC's clean room facilities. Based on our preliminary review of this matter, we believe that NECC's claims are without merit. We have notified our insurers of this claim and preliminary discussions concerning coverage have begun. In June 2013, we received a subpoena from the Plaintiffs' Steering Committee appointed in conjunction with the NECC multi-district litigation proceeding seeking information relating to the NECC matter. While we are unable to ascertain the ultimate outcome of this matter, based on the information currently available, we believe that a loss with respect to this matter is neither probable nor remote, and we are unable to reasonably assess an estimate or range of estimates of any potential losses.

Off-Balance Sheet Arrangements

As of May 25, 2013, we did not have any off-balance-sheet arrangements, as defined in Item 303(a)(4)(ii) of Securities and Exchange Commission Regulation S-K.

Seasonality

Historically, our revenues and operating results have varied from quarter to quarter and are expected to continue to fluctuate in the future. These fluctuations have been due to a number of factors, including: general economic conditions in our markets; the timing of acquisitions and of commencing start-up operations and related costs; our effectiveness in integrating acquired businesses and start-up operations; the timing of nuclear plant outages; capital expenditures; seasonal rental and purchasing patterns of our customers; and price changes in response to competitive factors. In addition, our operating results historically have been lower during the second and fourth fiscal quarters than during the other quarters of the fiscal year. The operating results for any historical quarter are not necessarily indicative of the results to be expected for an entire fiscal year or any other interim periods.

Effects of Inflation

In general, we believe that our results of operations are not dependent on moderate changes in the inflation rate. Historically, we have been able to manage the impacts of more significant changes in inflation rates through our customer relationships, customer agreements that generally provide for price increases consistent with the rate of inflation, and continued focus on improvements of operational productivity.

Energy Costs

Significant increases in energy costs, specifically with respect to natural gas and gasoline, can materially affect our results of operations and financial condition.

Contractual Obligations and Other Commercial Commitments

As of May 25, 2013, there were no material changes in our contractual obligations that were disclosed in our Annual Report on Form 10-K for the year ended August 25, 2012.

Recent Accounting Pronouncements

In May 2011, the FASB issued updated accounting guidance to amend existing requirements for fair value measurements and disclosures. The guidance expands the disclosure requirements around fair value measurements categorized in Level 3 of the fair value hierarchy and requires disclosure of the level in the fair value hierarchy of items that are not measured at fair value but whose fair value must be disclosed. It also clarifies and expands upon existing requirements for fair value measurements of financial assets and liabilities as well as instruments classified in shareholders' equity. The guidance was effective for interim and annual financial periods beginning after December 15, 2011. We adopted this revised guidance on August 26, 2012 and the adoption did not have a material impact on our financial statements.

In June 2011, the FASB issued updated accounting guidance that improves the comparability, consistency, and transparency of financial reporting and increases the prominence of items reported in other comprehensive income by eliminating the option to present components of other comprehensive income as part of the statement of changes in shareholders' equity. The amendments to the existing standard require that all nonowner changes in shareholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The amendments to the existing standard do not change the current option for presenting components of other comprehensive income ("OCI") gross or net of the effect of income taxes, provided that such tax effects are presented in the statement in which OCI is presented or disclosed in the notes to the financial statements. Additionally, the standard does not affect the calculation or reporting of earnings per share. This guidance was effective for annual reporting periods, and any interim periods within those annual periods, that begin after December 15, 2011 and is to be applied retrospectively, with early adoption permitted. We adopted this revised guidance on August 26, 2012 and the adoption did not have a material impact on our financial statements.

In September 2011, the FASB issued updated guidance intended to simplify how entities, both public and nonpublic, test for goodwill impairment. This guidance permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. Also, the guidance improves the examples of events and circumstances that an entity having a reporting unit with a zero or negative carrying amount should consider in determining whether to measure an impairment loss, if any, under the second step of the goodwill impairment test. This guidance was effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. We adopted this revised guidance on August 26, 2012 and the adoption did not have a material impact on our financial statements.

In February 2013, the FASB issued updated accounting guidance that improves the reporting of reclassifications out of accumulated other comprehensive income. The amendments in this updated guidance require an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under US GAAP to be reclassified in its entirety to net income. For other amounts that are not required under US GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under US GAAP that provide additional detail about those amounts. The guidance is effective for interim and annual financial periods beginning after December 15, 2012, with early adoption permitted. We do not expect this guidance to have a material impact on our financial statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Risk

We have determined that all of our foreign subsidiaries operate primarily in local currencies that represent the functional currencies of such subsidiaries. All assets and liabilities of our foreign subsidiaries are translated into U.S. dollars using the exchange rate prevailing at the balance sheet date. The effects of exchange rate fluctuations on the translation of assets and liabilities are recorded as a component of shareholders' equity. Revenues and expenses are translated at the average exchange rates in effect during each month of the fiscal year. As such, our financial condition and operating results are affected by fluctuations in the value of the U.S. dollar as compared to currencies in foreign countries. Revenues denominated in currencies other than the U.S. dollar represented approximately 8.9% and 8.8% of total consolidated revenues for the thirteen and thirty-nine weeks ended May 25, 2013, respectively, and total assets denominated in currencies other than the U.S. dollar represented approximately 10.6% and 11.1% of total consolidated assets at May 25, 2013 and August 25, 2012, respectively. If exchange rates had increased or decreased by 10% from the actual rates in effect during the thirteen and thirty-nine weeks ended and as of May 25, 2013, our revenues would have increased or decreased by approximately \$3.0 million and \$8.8 million, respectively, and assets as of May 25, 2013 would have increased or decreased by approximately \$14.1 million.

We do not operate a hedging program to mitigate the effect of a significant change in the value of our foreign subsidiaries functional currencies, which include the Canadian Dollar, Euro, British Pound, and Mexican Peso, as compared to the U.S. dollar. Any gains or losses resulting from foreign currency transactions, including exchange rate fluctuations on intercompany accounts are reported as transaction (gains) losses in our other (income) expense. The intercompany payables and receivables are denominated in Canadian Dollars, Euros, British Pounds and Mexican Pesos. During the thirteen and thirty-nine weeks ended May 25, 2013, transaction losses included in other (income) expense was approximately \$0.3 million for both periods. If the exchange rates had increased or decreased by 10% during the thirteen and thirty-nine weeks ended May 25, 2013, we would have recognized exchange gains or losses of approximately \$0.9 million and \$1.0 million, respectively.

Interest Rate Sensitivity

We are exposed to market risk from changes in interest rates which may adversely affect our financial position, results of operations and cash flows. In seeking to minimize the risks from interest rate fluctuations, we manage these exposures through our regular operating and financing activities. We are exposed to interest rate risk primarily through our borrowings under our Credit Agreement with a syndicate of banks and our Floating Rate Notes which were purchased by a group of insurance companies pursuant to the 2006 Note Agreement. Under both agreements, we borrow funds at variable interest rates based on the Eurodollar rate or LIBOR rates. If the LIBOR and Eurodollar rates fluctuated by 10% from the actual rates in effect during the thirteen and thirty-nine weeks ended May 25, 2013, our interest expense would have fluctuated by less than \$0.1 million from the interest expense recognized for both periods.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), we carried out an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based upon their evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective to ensure that material information relating to the Company required to be disclosed by the Company in reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and to ensure that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, our management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurances of achieving the desired control objectives, and management necessarily was required to apply its judgment in designing and evaluating the controls and procedures. We continue to review our disclosure controls and procedures, and our internal control over financial reporting, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that our systems evolve with our business.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the third quarter of fiscal year 2013 that have materially affected, or that are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we are subject to legal proceedings and claims arising from the current conduct of our business operations, including personal injury, customer contract, employment claims and environmental matters as described in our Consolidated Financial Statements. We maintain insurance coverage providing indemnification against many of such claims, and we do not expect that we will sustain any material loss as a result thereof. Refer to Note 8, “Commitments and Contingencies,” to the Consolidated Financial Statements for further discussion.

ITEM 1A. RISK FACTORS

To our knowledge, except as set forth below under this “Item 1A. Risk Factors,” there have been no material changes in the risk factors described in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended August 25, 2012. In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended August 25, 2012, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business, financial condition and/or operating results.

In addition to contingencies and claims relating to environmental compliance matters, we may from time to time be subject to legal proceedings and claims related to our business operations which may adversely affect our financial condition and operating results.

In addition to contingencies and claims relating to environmental compliance matters, we are subject from time to time to legal proceedings and claims arising from the conduct of our business operations, including personal injury claims, customer contract matters and employment claims. Certain of these claims are typically not covered by our available insurance. In addition, claims occasionally result in significant investigation and litigation expenses and, if successful, may result in material losses to us. Certain claims may also result in significant adverse publicity against us. As a consequence, successful claims against us not covered by our available insurance coverage could have a material adverse effect on our business, financial condition and results of operation.

In particular, on December 31, 2012, we received a letter from counsel for New England Compounding Center (“NECC”) demanding, among other things, that we indemnify NECC regarding claims made against NECC, including those related to NECC’s highly-publicized compounding and sale of tainted methylprednisolone acetate. This demand relates to the limited, once-a-month cleaning services we provided to portions of NECC’s clean room facilities. Based on our preliminary review of this matter, we believe that NECC’s claims are without merit. We have notified our insurers of this claim and preliminary discussions concerning coverage have begun. In June 2013, we received a subpoena from the Plaintiffs’ Steering Committee appointed in conjunction with the NECC multi-district litigation proceeding seeking information relating to the NECC matter. While we are unable to ascertain the ultimate outcome of this matter, based on the information currently available, we believe that a loss with respect to this matter is neither probable nor remote, and we are unable to reasonably assess an estimate or range of estimates of any potential losses. If we are found to be liable with respect to claims brought against us relating to NECC that are not covered by our available insurance, we may incur liabilities that are material to our financial condition and operating results.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) Not Applicable.

(b) Not Applicable.

(c) Issuer Purchases of Equity Securities

| Period | (a) Total Number of Shares of Common Stock Purchased | (b) Average Price Paid per Common Share | (c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | (d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet be Purchased Under the Plan or Program |
|------------------------------------|------------------------------------------------------|-----------------------------------------|--------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------|
| February 24, 2013 – March 23, 2013 | – | – | N/A | N/A |
| March 24, 2013 – April 20, 2013 | 35,938 (1) | 88.98 | N/A | N/A |
| April 21, 2013 – May 25, 2013 | – | – | N/A | N/A |
| | 35,938 | \$ 88.98 | N/A | N/A |

(1) Represents shares of Common Stock surrendered by the Company’s CEO to the Company to satisfy such tax withholding obligations in connection with the vesting of restricted stock.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

* 31.1 Rule 13a-14(a)/15d-14(a) Certification of Ronald D. Croatti

* 31.2 Rule 13a-14(a)/15d-14(a) Certification of Steven S. Sintros

** 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

** 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101 The following materials from UniFirst Corporation's Quarterly Report on Form 10-Q for the quarter ended May 25, 2013, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Statements of Income, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Balance Sheets, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Consolidated Financial Statements.

* *Filed herewith*

*** Furnished herewith*

SIGNATURES

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

UniFirst Corporation

July 3, 2013 By: /s/ Ronald D. Croatti
Ronald D. Croatti
President and Chief Executive Officer

July 3, 2013 By: /s/ Steven S. Sintros
Steven S. Sintros
Vice President and Chief Financial Officer

EXHIBIT INDEX

- * 31.1 Rule 13a-14(a)/15d-14(a) Certification of Ronald D. Croatti
- * 31.2 Rule 13a-14(a)/15d-14(a) Certification of Steven S. Sintros
- ** 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- ** 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101 The following materials from UniFirst Corporation's Quarterly Report on Form 10-Q for the quarter ended May 25, 2013, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Statements of Income, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Balance Sheets, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Consolidated Financial Statements.

* *Filed herewith*

** *Furnished herewith*