

G&K SERVICES INC  
Form 10-Q  
November 01, 2013  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

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FORM 10-Q

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QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended September 28, 2013  
Commission file number 0-4063

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G&K SERVICES, INC.  
(Exact name of registrant as specified in its charter)

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MINNESOTA (State or other jurisdiction of incorporation or organization) 5995 OPUS PARKWAY MINNETONKA, MINNESOTA 55343 (Address of principal executive offices and zip code) Registrant's telephone number, including area code (952) 912-5500	41-0449530 (I.R.S. Employer Identification No.)
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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  (do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined 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.

Common Stock, par value \$0.50 per share, outstanding  
October 28, 2013 was 19,808,601 shares

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## PART I

## FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## CONDENSED CONSOLIDATED BALANCE SHEETS

## G&amp;K Services, Inc. and Subsidiaries

(In thousands)	September 28, 2013 (Unaudited)	June 29, 2013
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$35,587	\$38,590
Accounts receivable, less allowance for doubtful accounts of \$3,538 and \$3,135	95,681	90,989
Inventories, net	170,795	165,006
Other current assets	13,774	13,810
Total current assets	315,837	308,395
Property, Plant and Equipment, net	194,060	194,156
Goodwill	335,633	334,393
Other Assets	62,712	60,342
Total assets	\$908,242	\$897,286
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities		
Accounts payable	\$43,271	\$41,655
Accrued expenses	69,441	81,902
Deferred income taxes	6,800	6,729
Current maturities of long-term debt	—	18
Total current liabilities	119,512	130,304
Long-Term Debt, net of Current Maturities	181,600	175,000
Deferred Income Taxes	17,899	19,894
Accrued Income Taxes	10,083	9,726
Pension Withdrawal Liability	24,236	22,059
Other Noncurrent Liabilities	74,486	73,295
Total liabilities	427,816	430,278
Stockholders' Equity		
Common stock, \$0.50 par value	9,886	9,842
Additional paid-in capital	48,964	44,872
Retained earnings	409,248	402,905
Accumulated other comprehensive income	12,328	9,389
Total stockholders' equity	480,426	467,008
Total liabilities and stockholders' equity	\$908,242	\$897,286

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

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## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

G&amp;K Services, Inc. and Subsidiaries

(Unaudited)

(In thousands, except per share data)	For the Three Months Ended	
	September 28, 2013	September 29, 2012
Revenues		
Rental operations	\$213,040	\$203,459
Direct sales	16,253	18,969
Total revenues	229,293	222,428
Operating Expenses		
Cost of rental operations	139,746	138,672
Cost of direct sales	11,695	14,333
Selling and administrative	53,920	49,875
Total operating expenses	205,361	202,880
Income from Operations	23,932	19,548
Interest expense	1,581	1,036
Income before Income Taxes	22,351	18,512
Provision for income taxes	8,530	6,618
Net Income	\$13,821	\$11,894
Basic Earnings per Common Share	\$0.70	\$0.63
Diluted Earnings per Common Share	\$0.69	\$0.62
Weighted average number of shares outstanding, basic	19,429	18,681
Weighted average number of shares outstanding, diluted	19,836	18,949
Dividends Declared per Share	\$0.270	\$0.195

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

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## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

G&amp;K Services, Inc. and Subsidiaries

(Unaudited)

(In thousands)	For the Three Months Ended	
	September 28, 2013	September 29, 2012
Net income	\$13,821	\$11,894
Other comprehensive income (loss)		
Foreign currency translation adjustments, net of tax \$126 and \$0, respectively	2,684	1,183
Pension benefit liabilities, net of tax \$170 and \$363, respectively	283	581
Derivative financial instruments loss recognized, net of tax \$(65) and \$(146), respectively	(109)	(273)
Derivative financial instruments loss reclassified, net of tax \$48 and \$49, respectively	81	80
Total other comprehensive income, net of tax	2,939	1,571
Total comprehensive income	\$16,760	\$13,465

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

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## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

G&amp;K Services, Inc. and Subsidiaries

(Unaudited)

	For the Three Months Ended	
	September 28, 2013	September 29, 2012
(In thousands)		
Operating Activities:		
Net income	\$13,821	\$11,894
Adjustments to reconcile net income to net cash provided by operating activities -		
Depreciation and amortization	7,631	8,056
Deferred income taxes	(2,022	) (187
Share-based compensation	1,851	1,554
Changes in current operating items, exclusive of acquisitions -		
Accounts receivable and prepaid expenses	(4,112	) 246
Inventories	(5,249	) 4,152
Accounts payable and other accrued expenses	(11,259	) (1,568
Other	793	(4,367
Net cash provided by operating activities	1,454	19,780
Investing Activities:		
Property, plant and equipment additions, net	(6,390	) (10,200
Acquisition of business, net of cash	—	(101
Net cash used for investing activities	(6,390	) (10,301
Financing Activities:		
Repayments of long-term debt	(18	) (133
Proceeds from (Repayments of) revolving credit facilities, net	6,600	(12,400
Cash dividends paid	(5,312	) —
Net issuance of common stock, under stock option plans	2,453	3,999
Repurchase of common stock	(2,183	) —
Shares associated with tax withholdings under our equity incentive plans	(1,287	) (730
Excess tax benefit from share-based compensation	1,141	—
Net cash provided by (used for) financing activities	1,394	(9,264
(Decrease) Increase in Cash and Cash Equivalents	(3,542	) 215
Effect of Exchange Rates on Cash	539	411
Cash and Cash Equivalents:		
Beginning of period	38,590	19,604
End of period	\$35,587	\$20,230

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

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G&K SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

1. Basis of Presentation for Interim Financial Statements

The Condensed Consolidated Financial Statements of G&K Services, Inc. (the "Company" or "G&K") as set forth in this quarterly report have been prepared pursuant to the rules and regulations of the U. S. Securities and Exchange Commission for interim reporting. As permitted under those rules, certain footnotes and other financial information that are normally required by accounting principles generally accepted in the United States can be condensed or omitted. Our accounting policies are described in the Notes to the Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended June 29, 2013 ("fiscal 2013"). Management is responsible for the unaudited Condensed Consolidated Financial Statements included in this document. The Condensed Consolidated Financial Statements included in this document are unaudited but, in the opinion of management, include all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of our financial position as of September 28, 2013, and the results of our operations for the three months ended September 28, 2013 and September 29, 2012 and our cash flows for the three months ended September 28, 2013 and September 29, 2012. The results of operations for the three month periods ended September 28, 2013 and September 29, 2012 are not necessarily indicative of the results to be expected for the full year. We have evaluated subsequent events and have found none that require recognition or disclosure.

This Quarterly Report on Form 10-Q should be read in conjunction with our Consolidated Financial Statements and notes included in our fiscal 2013 Annual Report on Form 10-K.

2. Contingent Liabilities

Environmental Matters

We are currently involved in several environmental-related proceedings by certain governmental agencies, which relate primarily to allegedly operating certain facilities in noncompliance with required permits. In addition to these proceedings, in the normal course of our business, we are subject to, among other things, periodic inspections by regulatory agencies, and we are involved in the remediation of various properties which we own. As of September 28, 2013 and June 29, 2013, we had reserves of approximately \$1,800 and \$1,700, respectively, related to these matters. There was \$283 of expense for these matters for the three months ended September 28, 2013. There was no expense for these matters for the three month period ended September 29, 2012.

Legal Matters

The United States Office of Federal Contract Compliance Programs, or OFCCP, is, as part of routine audits, conducting a review of certain of our employment practices. The OFCCP has issued a Notice of Violations to one of our facilities and audits of nine other facilities, where the OFCCP may claim there are similar alleged violations, are ongoing. We have been engaged in conversations with the OFCCP and believe that our practices are lawful and without bias. We have signed a Conciliation Agreement resolving the Notice of Violations mentioned above. Beyond that, no proceedings with respect to these matters have been commenced. While we cannot predict the ultimate outcome of these matters with certainty and it is possible that we may incur additional losses in excess of established reserves, we believe the possibility of a material adverse effect on our results of operations or financial position is remote.

See Note 13, "Employee Benefit Plans" of the Notes to the Consolidated Condensed Financial Statements for information regarding disputed amounts related to our withdrawal from the Central States Southeast and Southwest Areas Pension Fund.

3. New Accounting Pronouncements

In February 2013, the FASB issued updated guidance to improve the reporting of reclassifications out of accumulated other comprehensive income. The guidance requires an entity to present, either on the face of the statement of income or in the notes, separately for each component of comprehensive income, the current period reclassifications out of accumulated other comprehensive income by the respective line items of net income affected by the reclassification. The updated guidance is effective prospectively for fiscal years, and interim periods within those years, beginning

after December 15, 2012. The Company's adoption of this guidance in the first quarter of fiscal 2014 resulted in a change in the presentation of the Notes to the Consolidated Condensed Financial Statements and did not have any effect on the Company's results of operations or financial position.



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## 4. Fair Value Measurements

Generally accepted accounting principles (GAAP) defines fair value, 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. We considered non-performance risk when determining fair value of our derivative financial instruments. The fair value hierarchy prescribed under GAAP contains the following three levels:

Level 1 — unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 — other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets in non-active markets;
- inputs other than quoted prices that are observable for the asset or liability; and
- inputs that are derived principally from or corroborated by other observable market data.

Level 3 — unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

We do not have any level 3 assets or liabilities and we have not transferred any items between fair value levels during the first quarter of fiscal years 2013 or 2014.

The following tables summarize the assets and liabilities measured at fair value on a recurring basis as of September 28, 2013 and June 29, 2013:

	As of September 28, 2013		
	Fair Value Measurements Using Inputs Considered as		
	Level 1	Level 2	Total
Other assets:			
Money market mutual funds	\$ 3,283	\$ —	\$ 3,283
Equity and fixed income mutual funds	26,247	—	26,247
Cash surrender value of life insurance policies	—	13,660	13,660
Total assets	\$ 29,530	\$ 13,660	\$ 43,190
Accrued expenses:			
Derivative financial instruments	\$ —	\$ 1,310	\$ 1,310
Total liabilities	\$ —	\$ 1,310	\$ 1,310
	As of June 29, 2013		
	Fair Value Measurements Using Inputs Considered as		
	Level 1	Level 2	Total
Other assets:			
Money market mutual funds	\$ 2,964	\$ —	\$ 2,964
Equity and fixed income mutual funds	23,811	—	23,811
Cash surrender value of life insurance policies	—	13,377	13,377
Total assets	\$ 26,775	\$ 13,377	\$ 40,152
Accrued expenses:			
Derivative financial instruments	\$ —	\$ 1,136	\$ 1,136
Total liabilities	\$ —	\$ 1,136	\$ 1,136

The cash surrender value of life insurance policies are primarily investments established to fund the obligations of the company's non-qualified, non-contributory supplemental executive retirement plan (SERP). The money market, equity

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and fixed income mutual funds are investments established to fund the obligations of the company's non-qualified deferred compensation plan.

The following tables summarize the fair values of assets and liabilities that are recorded at historical cost as of September 28, 2013 and June 29, 2013:

	As of September 28, 2013		
	Fair Value Measurements Using Inputs Considered as		
	Level 1	Level 2	Total
Cash and cash equivalents	\$ 35,587	\$ —	\$ 35,587
Total assets	\$ 35,587	\$ —	\$ 35,587
Current maturities of long-term debt	\$ —	\$ —	\$ —
Long-term debt, net of current maturities	—	181,600	181,600
Total liabilities	\$ —	\$ 181,600	\$ 181,600

	As of June 29, 2013		
	Fair Value Measurements Using Inputs Considered as		
	Level 1	Level 2	Total
Cash and cash equivalents	\$ 38,590	\$ —	\$ 38,590
Total assets	\$ 38,590	\$ —	\$ 38,590
Current maturities of long-term debt	\$ —	\$ 18	\$ 18
Long-term debt, net of current maturities	—	175,000	175,000
Total liabilities	\$ —		