TASTY BAKING CO
Form 10-Q
May 04, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the thirteen weeks ended March 28, 2009

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

For the transition period from _______to _______

Commission File Number 1-5084

TASTY BAKING COMPANY
(Exact name of Company as specified in its charter)

Pennsylvania (State of Incorporation)	23-1145880 (IRS Employer Identification Number)

Navy Yard Corporate Center, Three Crescent Drive, Suite 200, Philadelphia, Pennsylvania 19112
(Address of principal executive offices including Zip Code)

215-221-8500
(Company's telephone number, including area code)

2801 Hunting Park Avenue, Philadelphia, Pennsylvania 19129
(Former Name or Former Address, if Changed Since Last Report)

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

YES x NO o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 o NO o

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

Large accelerated filer	o	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	x

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

YES o NO x

There were 8,576,448 shares of Common Stock outstanding as of May 4, 2009.

TASTY BAKING COMPANY AND SUBSIDIARIES

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Part I. FINANCIAL INFORMATION
Item 1. Financial Statements

TASTY BAKING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(000's)

	March 28, 2009	December 27, 2008
Assets		
Current assets:		
Cash and cash equivalents	$ 76	$ 58
Receivables, less allowance of $2,815 and $2,862, respectively	22,915	21,519
Inventories	7,883	7,190
Deferred income taxes	2,707	2,707
Prepayments and other	3,983	3,200
Total current assets	37,564	34,674
Property, plant and equipment:		
Land	1,433	1,433
Buildings and improvements	52,092	52,052
Machinery and equipment	133,768	132,609
Construction in progress	50,419	37,412
	237,712	223,506
Less accumulated depreciation and amortization	128,390	125,218
	109,322	98,288
Other assets:		
Long-term receivables from independent sales distributors	9,924	9,817
Deferred income taxes	13,358	13,088
Miscellaneous	3,199	3,330
	26,481	26,235
Total Assets	$ 173,367	$ 159,197
Liabilities		
Current liabilities:		
Accounts payable	$ 12,692	$ 7,641
Accrued payroll and employee benefits	5,890	5,182
Cash overdraft	3,161	2,770
Current obligations under capital leases	772	720
Notes payable, banks and current portion of long-term debt	1,000	1,000
Other accrued liabilities	4,964	6,419
Reserve for restructure	1,652	-
Total current liabilities	30,131	23,732
Accrued other liabilities	5,415	5,256
Accrued pension	27,446	27,921
Asset retirement obligation	7,146	7,050

Long-term debt		67,561		57,194
Long-term obligations under capital leases, less current portion		1,234		1,199
Postretirement benefits other than pensions		2,134		2,226
Reserve for restructure		-		1,652
Total liabilities		141,067		126,230
Shareholders' equity				
Accumulated other comprehensive income (loss)		(5,920)		(5,599)
Capital in excess of par value of stock		28,557		28,699
Common stock, par value $0.50 per share, and entitled to one		4,558		4,558
vote per share: Authorized 30,000 shares, issued 9,116 shares				
Retained earnings		16,160		16,653
Treasury stock, at cost		(11,055)		(11,344)
Total shareholders' equity		32,300		32,967
Total Liabilities and Shareholders' Equity	$	173,367	$	159,197

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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TASTY BAKING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(000's, except per share amounts)

	For the Thirteen Weeks Ended March 28, 2009	March 29, 2008
Gross sales	$ 76,930	$ 69,294
Less discounts and allowances	(30,767)	(26,472)
Net sales	46,163	42,822
Costs and expenses:		
Cost of sales, exclusive of depreciation shown below	29,921	28,794
Depreciation	3,240	3,030
Selling, general and administrative	12,695	12,012
Interest expense	604	456
Other income, net	(208)	(199)
	46,252	44,093
Income (loss) before provision for income taxes	(89)	(1,271)
Provision (benefit) for income taxes	(19)	(312)
Net income (loss)	$ (70)	$ (959)
Average common shares outstanding:		
Basic	8,059	8,034
Diluted	8,059	8,034
Per share of common stock:		
Net income (loss):		
Basic	$ (0.01)	$ (0.12)
Diluted	$ (0.01)	$ (0.12)
Cash dividend	$ 0.05	$ 0.05

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

TASTY BAKING COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(000's)

	For the Thirteen Weeks Ended March 28, 2009	March 29, 2008
Cash flows from (used for) operating activities		
Net income (loss)	$ (70)	$ (959)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	3,240	3,030
Amortization	91	76
Asset retirement obligation interest	97	92
Defined benefit pension expense (benefit)	209	(146)
Pension contributions	(630)	-
(Increase) deferred taxes	(270)	(690)
Post retirement medical	(156)	(425)
Other	125	(261)
Changes in assets and liabilities:		
Increase in receivables	(1,379)	(836)
(Increase) decrease in inventories	(693)	474
Increase in prepayments, deferred taxes and other	(875)	(704)
Increase in accrued taxes	-	207
Increase (decrease) in accounts payable, accrued payroll and other current liabilities	4,303	(2,779)
Net cash from (used for) operating activities	3,992	(2,921)
Cash flows from (used for) investing activities		
Purchase of property, plant and equipment	(14,274)	(8,877)
Independent sales distributor loan repayments	666	813
Loans to independent sales distributors	(790)	(989)
Other	2	(106)
Net cash used for investing activities	(14,396)	(9,159)
Cash flows from (used for) financing activities		
Dividends paid	(423)	(413)
Increase in long-term debt	41,750	39,790
Payment on long-term debt	(31,295)	(28,819)
Net increase in cash overdraft	390	1,538
Net cash from financing activities	10,422	12,096
Net increase in cash	18	16

Cash, beginning of year		58		57
Cash, end of period	$	76	$	73
Supplemental Cash Flow Information				
Cash paid during the period for:				
Interest	$	798	$	386
Income taxes	$	-	$	23

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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Notes to Condensed Consolidated Financial Statements
All disclosures are pre-tax, unless otherwise noted.

1. Summary of Significant Accounting Policies

Nature of the Business
Tasty Baking Company (the "Company") is a leading producer of sweet baked goods and one of the nation's oldest and largest independent baking companies, in operation since 1914. It has two manufacturing facilities, one in Philadelphia, PA, and a second in Oxford, PA.

Fiscal Year
The Company and its subsidiaries operate on a 52-53 week fiscal year, ending on the last Saturday of December. Fiscal year 2009 is a 52-week year. Fiscal year 2008 was a 52-week year.

Basis of Presentation
The condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated.

The condensed consolidated financial statements included herein have been prepared by the Company 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 generally accepted accounting principles in the United States of America ("GAAP") have been condensed or omitted pursuant to such rules and regulations. In the opinion of the Company, the accompanying unaudited condensed consolidated interim financial statements reflect all adjustments, consisting of only normal recurring items, which are necessary for a fair statement of the results of operations for the periods shown. The results of operations for such periods are not necessarily indicative of the results expected for the full year or for any future period.

The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to customer sales, discounts and allowances, long-lived asset impairment, indefinite-lived asset impairment, pension and postretirement plan assumptions, workers' compensation expense and income taxes. Actual results may differ from these estimates.

Concentration of Credit
The Company encounters, in the normal course of business, exposure to concentrations of credit risk with respect to trade receivables. Ongoing credit evaluations of customers' financial conditions are performed and, generally, no collateral is required. The Company maintains reserves for potential credit losses and such losses have not exceeded management's expectations.

Revenue Recognition
Revenue is recognized when title and risk of loss pass, which is upon receipt of goods by the independent sales distributors, retailers or third-party distributors. For route area sales, the Company sells to independent sales distributors who, in turn, sell to retailers. Revenue for sales to independent sales distributors is recognized upon receipt of the product by the distributor. For sales made directly to a customer or a third-party distributor, revenue is recognized upon receipt of the products by the retailer or third-party distributor.

Sale of Routes

Sales distribution routes are primarily owned by independent sales distributors who purchase the exclusive right to sell and distribute Tastykake® products in defined geographical territories. When the Company sells routes to independent sales distributors, it recognizes a gain or loss on the sale. Routes sold by the Company are either existing routes that the Company has previously purchased from an independent sales distributor or newly established routes in new geographies. Any gain or loss recorded by the Company is based on the difference between the sales price and the carrying value of the route. The Company recognizes gains or losses on sales of routes because all material services or conditions related to the sale have been substantially performed or satisfied by the Company as of the date of the sale. In most cases, the Company will finance a portion of the purchase price with interest bearing notes, which are required to be repaid in full. Interest rates on the notes are based on Treasury or LIBOR yields plus a spread. The Company has no obligation to later repurchase a route but may choose to do so to facilitate a change in route ownership.

Sales distribution routes owned by the Company are considered to have an indefinite life and are reviewed for impairment at least annually or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Any potential impairment of the net carrying value is fully reserved when identified. As of March 28, 2009 and December 27, 2008, the net carrying value of sales distribution routes owned by the Company was $1.9 million.

Cash and Cash Equivalents

The Company considers all investments with an original maturity of three months or less on their acquisition date to be cash equivalents. Cash overdrafts are recorded within current liabilities. Cash flows associated with cash overdrafts are classified as financing activities.

Inventory Valuation

Inventories, which include material, labor and manufacturing overhead, are stated at the lower of cost or market, cost being determined using the first-in, first-out ("FIFO") method. Inventory balances for raw materials, work in progress and finished goods are regularly analyzed and provisions for excess and obsolete inventory are recorded, as necessary, based on the forecast of product demand and production requirements.

Property and Depreciation

Property, plant and equipment are carried at cost. Depreciation is computed by the straight-line method over the estimated useful lives of the assets. Buildings and improvements, machinery and equipment, and vehicles are depreciated over thirty-nine years, seven to fifteen years, and five to ten years, respectively, except where a shorter useful life is necessitated by the Company's decision to relocate its Philadelphia operations. Spare parts are capitalized as part of machinery and equipment and are expensed as utilized or capitalized as part of the relevant fixed asset. Spare parts are valued using a moving average method and are reviewed for potential obsolescence on a regular basis. Reserves are established for all spare parts that are no longer usable and have no fair market value. Capitalized computer hardware and software is depreciated over five years.

Costs of major additions, replacements and betterments are capitalized, while maintenance and repairs, which do not improve or extend the life of the respective assets, are expensed as incurred. For significant projects, the Company capitalizes interest and labor costs associated with the construction and installation of plant and equipment and significant information technology development projects.

In accordance with Statement of Financial Accounting Standards No.144, Accounting for the Impairment or Disposal of Long-Lived Assets ("FAS 144"), long-lived assets are reviewed for impairment at least annually or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In instances where the carrying amount may not be recoverable, the review for potential impairment utilizes estimates and assumptions of future cash flows directly related to the asset. For assets where there is no plan for future use, the review for impairment includes estimates and assumptions of the fair value of the asset, which is based on the best information available. These assets are recorded at the lower of their book value or fair value.

The Company has a conditional asset retirement obligation related to asbestos in its Philadelphia manufacturing facility. As a result of the Company's decision in May 2007 to relocate its Philadelphia operations, it was able to estimate a settlement date for the asset retirement obligation and in accordance with FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations, recorded an obligation of $6.6 million which was the present value of the future obligation. This obligation will continue to accrete to the full value of the future obligation over the remaining period until settlement of the obligation which is expected to occur in June 2010, while the capitalized asset retirement cost is depreciated through December 2044, the remaining useful life of the Philadelphia manufacturing facility. During the quarter ended March 28, 2009 and March 29, 2008, the Company recorded $0.1 million in interest associated with the asset retirement obligation and as of March 28, 2009 and December 27, 2008, the asset retirement obligation totaled $7.1 million and $7.0 million, respectively.

Grants

The Company receives grants from various government agencies for employee training purposes. Expenses for the training are recognized in the Company's Statement of Operations at the time the training takes place. When the proper approvals are given and funds are received from the government agencies, the Company records an offset to the training expense already recognized.

In 2007, in connection with the decision to relocate its Philadelphia manufacturing operations, the Company received a $0.6 million grant from the Department of Community and Economic Development of the Commonwealth of Pennsylvania ("DCED"). The opportunity grant has certain spending, job retention and nondiscrimination conditions with which the Company must comply. The Company accounted for this grant under the deferred income approach and will amortize the deferred income over the same period as the useful life of the asset acquired with the grant. The asset acquired with the grant is expected to be placed into service when the new manufacturing facility becomes fully operational in 2010.

In addition, in 2006, in conjunction with The Reinvestment Funds, Allegheny West Foundation and the DCED, the Company activated Project Fresh Start (the "Project"). The Project is an entrepreneurial development program that provides an opportunity for qualified minority entrepreneurs to purchase routes from independent sales distributors. The source of grant monies for this program is the DCED. The grants are used by minority applicants to partially fund their purchase of an independent sales distribution route.

Because the Project's grant funds merely pass through the Company in its role as an intermediary, the Company records an offsetting asset and liability for the total amount of grants as they relate to the Project. There is no Statement of Operations impact related to the establishment of, or subsequent change to, the asset and liability amounts.

Marketing Costs
The Company expenses marketing costs, which include advertising and consumer promotions, as incurred or as required in accordance with Statement of Position 93-7, Reporting on Advertising Costs. Marketing costs are included as a part of selling, general and administrative expense.

Computer Software Costs
The Company capitalizes certain costs, such as software coding, installation and testing that are incurred to purchase or create and implement internal use computer software in accordance with Statement of Position 98-1, Accounting for Costs of Computer Software Development or Obtained for Internal Use. The majority of the Company's capitalized software relates to the implementation of the enterprise resource planning and handheld computer systems.

Freight, Shipping and Handling Costs
Outbound freight, shipping and handling costs are included as a part of selling, general and administrative expense. Inbound freight, shipping and handling costs are capitalized with inventory and expensed with cost of sales.

Pension Plan
The Company's funding policy for the pension plan is to contribute amounts deductible for federal income tax purposes plus such additional amounts, if any, as the Company's actuarial consultants advise to be appropriate. Effective January 1, 2008, the Company is required to make quarterly contributions under the Pension Protection Act of 2006. The Company will make four quarterly contributions in 2009 totaling $2.4 million. As of March 28, 2009, the Company had made one of the four required contributions. In 1987 the Company elected to immediately recognize all gains and losses in excess of the pension corridor, which is equal to the greater of ten percent of the accumulated pension benefit obligation or ten percent of the market-related value of plan assets.

The Company accrues normal periodic pension expense or income during the year based upon certain assumptions and estimates from its actuarial consultants. These estimates and assumptions include discount rate, rate of return on plan assets, compensation increases, mortality and employee turnover. In addition, the rate of return on plan assets is directly related to changes in the equity and credit markets, which can be and have recently been very volatile. The use of the above estimates and assumptions, market volatility and the Company's election to immediately recognize all gains and losses in excess of its pension corridor in the current year may cause the Company to experience significant changes in its pension expense or income from year to year. Expense or income that falls outside the corridor is recognized only in the fourth quarter of each year.

In accordance with Financial Accounting Standards Board ("FASB") Statement No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, the Company maintains a liability on its Balance Sheet equal to the under-funded status of its defined benefit and other postretirement benefit plans.

Accounting for Derivative Instruments

The Company has entered into certain variable-to-fixed interest rate swap contracts and foreign currency forward contracts denominated in Australian Dollars ("AUD"), primarily to hedge against fluctuations in interest rates or foreign currency exchange rates. The Company accounts for derivative instruments in accordance with FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities ("FAS 133") and FASB Statement No. 161, Disclosures about Derivative Instruments and Hedging Activities An Amendment of FASB Statement No. 133.

Treasury Stock
Treasury stock is stated at cost. Cost is determined by the FIFO method.

Accounting for Income Taxes
The Company accounts for income taxes under the asset and liability method, in accordance with FASB Statement No. 109, Accounting for Income Taxes. Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates in effect when the differences are expected to be recovered or settled.

Net Income (Loss) Per Common Share
Net income (loss) per common share is presented as basic and diluted earnings per share. Net income (loss) per common share – basic is based on the weighted average number of common shares outstanding during the period. Net income (loss) per common share – diluted is based on the weighted average number of common shares and dilutive potential common shares outstanding during the period. Dilution is the result of outstanding stock options and restricted shares. For the thirteen weeks ended March 28, 2009 and March 29, 2008, 499,798 and 575,928 options to purchase common stock and restricted shares, respectively, were excluded from the net income (loss) per common share – basic calculation, as they were anti-dilutive.

Share-based Compensation
The Company accounts for share-based compensation in accordance with FASB Statement No. 123(R), Share-Based Payment ("FAS 123(R)"). Share-based compensation expense recognized during the current period is based on the value of the portion of share-based payment awards that is ultimately expected to vest. The total value of compensation expense for restricted stock is equal to the closing market price of Tasty Baking Company shares on the date of grant. FAS 123(R) requires forfeitures to be estimated at the time of grant in order to estimate the amount of share-based awards that will ultimately vest. The forfeiture rate is based on the Company's historical forfeiture experience. The Company calculated its historical pool of windfall tax benefits.

Recent Accounting Statements
In September 2006, the FASB issued Statement No. 157, Fair Value Measurements ("FAS 157"), which creates a single definition of fair value, along with a conceptual framework to measure fair value and to increase the consistency and the comparability in fair value measurements and in financial statement disclosure. The Company adopted the required provisions of FAS 157, effective December 30, 2007. The required provisions did not have a material impact on the Company's condensed consolidated financial statements.

In February 2008, the FASB issued FASB Staff Position ("FSP") No. FAS 157-2, Effective Date of FASB Statement No. 157. This FSP permits a delay in the effective date of FAS 157 to fiscal years beginning after November 15, 2008, for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). The delay was intended to allow the Board and constituents additional time to consider the effect of various implementation issues that had arisen from the application of FAS 157. The FASB also issued FSP FAS 157-1, Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13("FAS 157-1"), to exclude SFAS 13, Accounting for Leases, and its related interpretive accounting pronouncements from the scope of FAS 157 in February 2008. The Company adopted the provisions of FSP FAS 157-1 and FSP FAS 157-2 in the quarter ended March 28, 2009. The required provisions did not have a material impact on the Company's condensed consolidated financial statements.

In October 2008, the FASB issued FSP No. FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active. This FSP clarifies the application of FAS 157 in determining the fair values of assets or liabilities in a market that is not active. This FSP became effective upon issuance, including prior periods for which financial statements have not been issued. The Company adopted this FSP in the fourth quarter of 2008. The required provisions did not have a material impact on the Company's condensed consolidated financial statements.

In February 2007, the FASB issued Statement No. 159, The Fair Value Option for Financial Assets and Financial Liabilities – Including an Amendment of FASB Statement No. 115 ("FAS 159"). This statement permits, but does not require entities to measure certain financial instruments and other assets and liabilities at fair value on an instrument-by-instrument basis and is irrevocable. At the adoption date, unrealized gains and losses on financial assets and liabilities for which the fair value option has been elected would be reported as a cumulative adjustment to beginning retained earnings. Unrealized gains and losses due to changes in their fair value must be recognized in earnings at each subsequent reporting date. This statement is effective for fiscal years beginning after November 15, 2007. Although FAS 159 was adopted December 30, 2007, the Company has not yet elected the fair value option for any items permitted under FAS 159.

In December 2007, the FASB issued Statement No. 141 (Revised 2007), Business Combinations (“FAS 141(R)”). FAS 141(R) significantly changes the accounting for business combinations in a number of areas including the treatment of contingent consideration, acquired contingencies, transaction costs, in-process research and development and restructuring costs. In addition, under FAS 141(R), changes in an acquired entity's deferred tax assets and uncertain tax positions after the measurement period impact income tax expense. FAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning after December 15, 2008. Earlier adoption was prohibited. The Company adopted FAS 141 (R) in the quarter ended March 28, 2009. The required provisions did not have an impact on the Company’s condensed consolidated financial statements.

In December 2007, the FASB issued Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements—An Amendment of ARB No. 51 (“FAS 160”), which establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary, changes in a parent's ownership interest in a subsidiary and the deconsolidation of a subsidiary. FAS 160 is effective for fiscal years beginning after December 15, 2008. Earlier adoption was prohibited. The Company adopted FAS 160 for the quarter ended March 28, 2009. The required provisions did not have an impact on the Company’s condensed consolidated financial statements.

In March 2008, the FASB issued Statement No. 161, Disclosures about Derivative Instruments and Hedging Activities—An Amendment of FASB Statement No. 133 (“FAS 161”). FAS 161 applies to all derivative instruments and related hedged items accounted for under FAS 133, Accounting for Derivative Instruments and Hedging Activities. It requires entities to provide greater transparency about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under FAS 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity’s financial position, results of operations, and cash flows. FAS 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company adopted FAS 161 in the quarter ended March 28, 2009. Because FAS 161 applies only to financial statement disclosures, it did not have a material impact on the Company’s condensed consolidated financial statements.

In June 2008, the FASB issued FSP No. EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities (“FSP 03-6-1”), which classifies unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents as participating securities and requires them to be included in the computation of earnings per share pursuant to the two-class method described in SFAS No. 128, Earnings per Share. FSP 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those years and requires all prior period earnings per share data presented to be adjusted retrospectively. The Company adopted FSP 03-6-1 for the quarter ended March 28, 2009. The required provisions did not have a material impact on the Company’s condensed consolidated financial statements.

In April 2009, the FASB issued FSP No. FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments (“FAS 107-1 and APB 28-1”). This FSP requires disclosure about fair value of financial instruments for interim reporting periods and annual financial statements of publicly traded companies. FAS 107-1 and APB 28-1 is effective for interim reporting periods ending after June 15, 2009. Because FAS 107-1 and APB 18-1 applies only to financial statement disclosures, it will not have a material impact on the Company’s condensed consolidated financial statements.

In April 2009, the FASB issued FSP No. FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Indentifying Transactions That Are Not Orderly (“FAS 157-4”). This FSP provides additional guidance for estimating fair value in accordance with FASB Statement No. 157 when the volume and level of activity for the asset or liability have significantly decreased and provides guidance on identifying circumstances that indicate a transaction is not orderly. FAS 157-4 is effective for interim reporting periods ending after June 15, 2009. The Company does not expect the adoption of FAS 157-4 to have a material impact on its condensed consolidated financial statements.

In April 2009, the FASB issued FSP No. FAS 115-2, Recognition and Presentation of Other-Than-Temporary Impairments ("FAS 115-2"). This FSP provides a framework to perform an other-than-temporary impairment analysis, in compliance with GAAP, which determines whether the holder of an investment in a debt or equity security, for which changes in fair value are not regularly recognized in earnings, should recognize a loss in earnings when the investment is impaired. Additionally this FSP amends the other-than-temporary impairment guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements. FAS 115-2 is effective for interim reporting periods ending after June 15, 2009. The Company does not expect the adoption of FAS 115-2 to have a material impact on its condensed consolidated financial statements.

2. New Facilities

In May 2007, the Company announced that as part of its comprehensive operational review of strategic manufacturing alternatives, it entered into an agreement to relocate its Philadelphia operations to the Philadelphia Navy Yard. The bakery lease agreement provides for a 26-year lease for a 345,500 square foot bakery, warehouse and distribution center located on approximately 25 acres. Construction of the facility is underway and is expected to be substantially complete by the end of 2009. The Company expects the new facility to be fully operational in 2010. The lease provides for no rent payments in the first year of occupancy. Rental payments increase from $3.5 million in the second year of occupancy to $7.2 million in the final year of the lease. In accordance with FASB Statement No. 13, Accounting for Leases ("FAS 13"), the Company will recognize the rental expenses associated with the agreement on a straight-line basis over the term of the agreement.

As part of this initiative, the Company also entered into a 16-year agreement for $9.5 million in financing at a fixed rate of 8.54% to be used for leasehold improvements. This agreement provides for no principal or interest payments in the first year of occupancy and then requires equal monthly payments of principal and interest aggregating to $1.2 million annually over the remainder of the term.

The Company also entered into an agreement to relocate its corporate headquarters to the Philadelphia Navy Yard. This lease agreement provides for approximately 36,000 square feet of office space. Construction of the office space is complete and during mid-April 2009, the Company relocated its corporate headquarters to the Philadelphia Navy Yard. The lease, which commenced in April 2009, will end at the same time as the new bakery lease. The lease provides for no rent payments in the first six months of occupancy. Rental payments increase from approximately $0.9 million in the second year of occupancy to approximately $1.5 million in the final year of the lease. In accordance with FAS 13, the Company will recognize the rental expenses associated with the agreement on a straight-line basis over the term of the agreement.

In connection with these agreements, the Company provided a $1.1 million letter of credit, which increased to $8.1 million in the beginning of 2009. The outstanding amount of the letter of credit will be reduced starting in 2026 and will be eliminated by the end of the lease term. As of March 28, 2009, the outstanding letter of credit under this arrangement totaled $8.1 million.

In connection with these agreements and the related construction of the new facilities, the Company provided an additional $0.5 million letter of credit, which increased to $5.6 million in the first quarter of 2009. The outstanding amount of the letter of credit will be eliminated in August 2009. As of March 28, 2009, the outstanding letter of credit under this arrangement totaled $5.6 million.

In addition to the facility leases, the Company is purchasing high-tech, modern baking equipment. This equipment is designed to increase product development flexibility and efficiency, while maintaining existing taste and quality standards. The investment for this project, in addition to any costs associated with the agreements described above, is projected to be approximately $75.0 million through 2010. In September 2007, the Company closed on a multi-bank credit facility and low-interest development loans provided in part by the Commonwealth of Pennsylvania and the Philadelphia Industrial Development Corporation to finance this investment and refinance the Company's existing revolving credit facilities, as well as to provide for financial flexibility in running the ongoing operations and working capital needs.

The Company accounts for disposal and exit activities in accordance with FASB Statement No. 146, Accounting for Costs Associated with Exit or Disposal Activities ("FAS 146") and FAS 144. To date, the Company has not incurred any material obligations related to one-time termination benefits, contract termination costs or other associated costs as described in FAS 146.

The Company has evaluated the long-lived assets utilized in its Philadelphia operations for potential impairment or other treatment in accordance with FAS 144. Based on the commitment to the planned relocation, neither the assets to be relocated nor the assets to be left in place at the Philadelphia operations have suffered impairment. Therefore the estimated fair value of the asset groups continues to exceed the carrying amount of such asset groups. The Company anticipates that long-lived assets utilized in the Philadelphia operations with an aggregate net book value of approximately $20.0 million at June 30, 2007 will not be relocated to the new facilities or sold as a result of the relocation. With respect to the group of assets not expected to be relocated or sold, certain of the assets included in the group had previously estimated useful lives that extended beyond the expected project completion in 2010. As such, in the quarter ended June 30, 2007, the Company changed its estimate of the remaining useful lives of such assets to be consistent with the time remaining until the end of the project, and accounted for such change in estimate in accordance with FASB Statement No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3. For the thirteen week periods ended March 28, 2009 and March 29, 2008, the change in estimated useful lives of these assets resulted in incremental depreciation of $1.3 million. The after-tax impact of the incremental depreciation on net income, net income per common share-basic and net income per common share-diluted was $0.8 million, $0.10 per share, and $0.10 per share, respectively, for the thirteen week periods ended March 28, 2009 and March 29, 2008. The Company expects that the future pre-tax impact of incremental depreciation resulting from the change in useful lives will be approximately $1.3 million per quarter through June 2010, when the new bakery is expected to be fully operational.

As part of the relocation of its Philadelphia operations, the Company expects to eliminate approximately 215 positions. While the Company hopes to achieve this result through normal attrition and the reduction of contract labor, it is probable that the Company will incur obligations related to postemployment benefits accounted for under FASB Statement No. 112, Employers' Accounting for Postemployment Benefits, an amendment of FASB Statements No. 5 and 43. During the quarter ended September 27, 2008, the Company recorded a reserve of $1.7 million for estimated future obligations related to postemployment benefits associated with the relocation of its Philadelphia operations. The cost associated with this reserve was recorded in other income.

3. Inventories

Inventories are classified as follows (in thousands):

	March 28, 2009	Dec. 27, 2008
Finished goods	$ 3,173	$ 2,275
Work in progress	125	109
Raw materials and supplies	4,585	4,806
	$ 7,883	$ 7,190

The inventory balance has been reduced by reserves for obsolete and slow-moving inventories of $35,000 as of March 28, 2009. At December 27, 2008, there were no reserves established.

4. Credit Facilities

On September 6, 2007, the Company entered into a 5 year, $100.0 million secured credit facility with 4 banks, consisting of a $55.0 million fixed asset line of credit, a $35.0 million working capital revolver and a $10.0 million low-interest loan from the agent bank with the Commonwealth of Pennsylvania (the “Bank Credit Facility”). The Bank Credit Facility is secured by a blanket lien on the Company’s assets and contains various non-financial and financial covenants, including a fixed charge coverage covenant, a maximum operating leverage ratio covenant, a minimum liquidity ratio covenant and minimum level of earnings before interest, taxes, depreciation and amortization

(“EBITDA”) covenant. Interest rates for the fixed asset line of credit and working capital revolver are indexed to LIBOR and include a spread above that index from 125 to 325 basis points based upon the Company’s ratio of debt to EBITDA. The fixed asset line of credit and the working capital revolver include commitment fees from 20 to 50 basis points based upon the Company’s ratio of debt to EBITDA. The $10.0 million low-interest loan bears interest at a fixed rate of 5.5% per annum. In October 2008, the Company amended its Bank Credit Facility to provide for additional flexibility and to change certain financial covenants, including the minimum EBITDA requirement as of December 27, 2008 and the maximum operating leverage ratio as of September 27, 2008 and December 27, 2008 which was necessary to eliminate an instance of non-compliance. As of March 28, 2009 and December 27, 2008, the outstanding balances under the Bank Credit Facility were $46.6 million and $45.2 million, respectively.

On September 6, 2007, the Company entered into a 10 year, $12.0 million secured credit agreement with the PIDC Local Development Corporation ("PIDC Credit Facility"). This credit facility bears interest at a blended fixed rate of 4.5% per annum, participates in the blanket lien on the Company's assets and contains customary representations and warranties as well as customary affirmative and negative covenants essentially similar to those in the Bank Credit Facility, as amended in October 2008. Negative covenants include, among others, limitations on incurrence of liens and secured indebtedness by the Company and/or its subsidiaries, other than in connection with the Bank Credit Facility and the MELF Loan 1 and the MELF Loan 2, as defined below. As of March 28, 2009 and December 27, 2008, the outstanding balances under the PIDC Credit Facility were $12.0 million and $3.0 million, respectively.

On September 6, 2007, the Company entered into a 10 year, $5.0 million Machinery and Equipment Loan Fund secured loan with the Commonwealth of Pennsylvania ("MELF Loan 1"). This loan bears interest at a fixed rate of 5.0% per annum and contains customary representations and warranties as well as customary affirmative and negative covenants similar to those in the Bank Credit Facility, as amended in October 2008. Negative covenants include, among others, limitations on incurrence of liens and secured indebtedness by the Company, other than in connection with the Bank Credit Facility and the PIDC Credit Facility. In September 2008, the Company entered into a second 10 year, $5.0 million Machinery and Equipment Loan Fund secured loan with the Commonwealth of Pennsylvania ("MELF Loan 2"). The terms and conditions of MELF Loan 2 are substantially the same as MELF Loan 1. The Company borrowed $5.0 million under MELF Loan 1 in September 2008 and $5.0 million under MELF Loan 2 in October 2008. As of March 28, 2009 and December 27, 2008, the aggregate outstanding balance under the MELF Loan 1 and MELF Loan 2 was $10.0 million. As of March 28, 2009, the Company was in compliance with the various non-financial and financial covenants included in the Bank Credit Facility, the PIDC Credit Facility, the MELF Loan 1 and the MELF Loan 2.

On September 6, 2007, the Company entered into an agreement which governs the shared collateral positions under the Bank Credit Facility, the PIDC Credit Facility, the MELF Loan 1 and the MELF Loan 2 (the "Intercreditor Agreement"), and establishes the priorities and procedures that each lender has in enforcing the terms and conditions of each of their respective agreements. The Intercreditor Agreement permits the group of banks and their agent bank in the Bank Credit Facility to have the initial responsibility to enforce the terms and conditions of the various credit agreements, subject to certain specific limitations, and allows such bank group to negotiate amendments and waivers on behalf of all lenders, subject to the approval of each lender.

The Company has used and expects to continue to utilize proceeds from the Bank Credit Facility, the PIDC Credit Facility, the MELF Loan 1 and the MELF Loan 2 to finance the Company's mid-April 2009 move to its corporate headquarters to the Philadelphia Navy Yard and its planned move of the Philadelphia manufacturing facility to new facilities to be constructed at the Philadelphia Navy Yard, along with working capital needs.

5. Derivative Instruments

In order to hedge a portion of the Company's exposure to changes in interest rates on debt incurred under its Bank Credit Facility, the Company enters into variable-to-fixed interest rate swap contracts to fix the interest rates on a portion of its variable interest rate debt. These contracts are accounted for as cash flow hedges in accordance with FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities ("FAS 133"). Accordingly, these derivatives are marked to market and the resulting gains or losses are recorded in other comprehensive income as an offset to the related hedged asset or liability. The actual interest expense incurred, inclusive of the effect of the hedge in the current period, is recorded in the Statement of Operations.

In January 2008, the Company entered into an $8.5 million notional value interest rate swap contract that increases to $35.0 million by April 2010 with a fixed LIBOR rate of 3.835% that expires on September 5, 2012. As of March 28, 2009, the notional value of the swap was $8.5 million. As of March 28, 2009, the LIBOR rates were subject to an additional credit spread which could range from 125 basis points to 325 basis points and was equal to 325 basis points as of that date. The Company records as an asset or a liability the cumulative change in the fair market value of the derivative instrument, and as of March 28, 2009 and December 27, 2008, the Company recorded a liability of $1.9 million and $1.8 million, respectively.