LANCASTER COLONY CORP
Form 10-Q
April 30, 2019

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
Form 10-Q

(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2019
or
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number 000-04065

Lancaster Colony Corporation
(Exact name of registrant as specified in its charter)

Ohio	13-1955943
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
380 Polaris Parkway, Suite 400 Westerville, Ohio	43082
(Address of principal executive offices)	(Zip Code)

614-224-7141
(Registrant’s telephone number, including area code)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨
Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes ý No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.
Large accelerated filer ý Accelerated filer ¨

Non-accelerated filer	o	Smaller reporting company	¨
		Emerging growth company	¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes ¨ No ý

As of April 18, 2019, there were approximately 27,505,000 shares of Common Stock, without par value, outstanding.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
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PART I – FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements
LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(Amounts in thousands, except share data)	March 31, 2019	June 30, 2018
ASSETS		
Current Assets:		
Cash and equivalents	$187,389	$205,752
Receivables	81,156	72,960
Inventories:		
Raw materials	36,407	32,673
Finished goods	56,713	58,188
Total inventories	93,120	90,861
Other current assets	5,640	9,304
Total current assets	367,305	378,877
Property, Plant and Equipment:		
Land, buildings and improvements	147,497	132,318
Machinery and equipment	326,061	293,409
Total cost	473,558	425,727
Less accumulated depreciation	249,060	234,914
Property, plant and equipment-net	224,498	190,813
Other Assets:		
Goodwill	210,429	168,030
Other intangible assets-net	71,551	56,176
Other noncurrent assets	12,502	10,595
Total	$886,285	$804,491
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current Liabilities:		
Accounts payable	$70,390	$57,978
Accrued liabilities	38,407	35,789
Total current liabilities	108,797	93,767
Other Noncurrent Liabilities	42,464	41,638
Deferred Income Taxes	20,016	16,804
Commitments and Contingencies		
Shareholders’ Equity:		
Preferred stock-authorized 3,050,000 shares; outstanding-none		
Common stock-authorized 75,000,000 shares; outstanding-March-27,504,669 shares; June-27,487,989 shares	121,565	119,232
Retained earnings	1,344,638	1,279,343
Accumulated other comprehensive loss	(8,129)	(8,259)
Common stock in treasury, at cost	(743,066)	(738,034)
Total shareholders’ equity	715,008	652,282
Total	$886,285	$804,491

See accompanying notes to condensed consolidated financial statements.

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

	Three Months Ended March 31,		Nine Months Ended March 31,	
(Amounts in thousands, except per share data)	2019	2018	2019	2018
Net Sales	$317,882	$296,174	$984,117	$914,755
Cost of Sales	242,485	228,263	736,129	687,430
Gross Profit	75,397	67,911	247,988	227,325
Selling, General and Administrative Expenses	37,981	29,875	109,902	97,005
Change in Contingent Consideration	88	521	(9,517)	1,514
Operating Income	37,328	37,515	147,603	128,806
Other, Net	1,329	525	3,682	1,595
Income Before Income Taxes	38,657	38,040	151,285	130,401
Taxes Based on Income	8,053	10,419	33,746	27,474
Net Income	$30,604	$27,621	$117,539	$102,927
Net Income Per Common Share:				
Basic	$1.11	$1.01	$4.28	$3.75
Diluted	$1.11	$1.00	$4.26	$3.74
Weighted Average Common Shares Outstanding:				
Basic	27,448	27,405	27,436	27,399
Diluted	27,549	27,458	27,543	27,456

See accompanying notes to condensed consolidated financial statements.

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

	Three Months Ended March 31,		Nine Months Ended March 31,	
(Amounts in thousands)	2019	2018	2019	2018
Net Income	$30,604	$27,621	$117,539	$102,927
Other Comprehensive Income:				
Defined Benefit Pension and Postretirement Benefit Plans:				
Amortization of loss, before tax	102	134	307	402
Amortization of prior service credit, before tax	(46)	(45)	(137)	(136)
Total Other Comprehensive Income, Before Tax	56	89	170	266
Tax Attributes of Items in Other Comprehensive Income:				
Amortization of loss, tax	(24)	(41)	(72)	(140)
Amortization of prior service credit, tax	11	14	32	47
Total Tax Expense	(13)	(27)	(40)	(93)
Other Comprehensive Income, Net of Tax	43	62	130	173
Comprehensive Income	$30,647	$27,683	$117,669	$103,100

See accompanying notes to condensed consolidated financial statements.

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

	Nine Months Ended March 31,					
(Amounts in thousands)	2019			2018		
Cash Flows From Operating Activities:						
Net income	$	117,539		$	102,927	
Adjustments to reconcile net income to net cash provided by operating activities:						
Impacts of noncash items:						
Depreciation and amortization	22,677			19,899		
Change in contingent consideration	(9,517		)	1,514		
Deferred income taxes and other changes	3,910			(8,633		)
Stock-based compensation expense	4,542			3,484		
Pension plan activity	(602		)	(362		)
Changes in operating assets and liabilities:						
Receivables	(6,220		)	(6,828		)
Inventories	(766		)	(11,738		)
Other current assets	3,080			(303		)
Accounts payable and accrued liabilities	8,780			16,879		
Net cash provided by operating activities	143,423			116,839		
Cash Flows From Investing Activities:						
Cash paid for acquisitions, net of cash acquired	(57,540		)	(318		)
Payments for property additions	(43,966		)	(22,561		)
Other-net	(592		)	(36		)
Net cash used in investing activities	(102,098		)	(22,915		)
Cash Flows From Financing Activities:						
Payment of dividends	(52,244		)	(48,044		)

Purchase of treasury stock	(5,032	)	(1,102	)
Tax withholdings for stock-based compensation	(2,209	)	(552	)
Other-net	(203	)	—	
Net cash used in financing activities	(59,688	)	(49,698	)
Net change in cash and equivalents	(18,363	)	44,226	
Cash and equivalents at beginning of year	205,752		143,104	
Cash and equivalents at end of period	$ 187,389		$ 187,330	
Supplemental Disclosure of Operating Cash Flows:				
Net cash payments for income taxes	$ 25,373		$ 37,196	

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(UNAUDITED)

(Amounts in thousands, except per share data)	Nine Months Ended March 31, 2019 Common Stock Outstanding		Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total Shareholders' Equity
	Shares	Amount				
Balance, June 30, 2018	27,488	$119,232	$1,279,343	$ (8,259)	$(738,034)	$652,282
Net income			39,028			39,028
Net pension and postretirement benefit gains, net of $13 tax effect				44		44
Cash dividends - common stock ($0.60 per share)			(16,495)			(16,495)
Purchase of treasury stock	(10)				(1,593)	(1,593)
Stock-based plans	12	(778)				(778)
Stock-based compensation expense		1,531				1,531
Balance, September 30, 2018	27,490	119,985	1,301,876	(8,215)	(739,627)	674,019
Net income			47,907			47,907
Net pension and postretirement benefit gains, net of $14 tax effect				43		43
Cash dividends - common stock ($0.65 per share)			(17,875)			(17,875)
Purchase of treasury stock	(1)				(166)	(166)
Stock-based plans	16	(988)				(988)
Stock-based compensation expense		1,831				1,831
Balance, December 31, 2018	27,505	120,828	1,331,908	(8,172)	(739,793)	704,771
Net income			30,604			30,604
Net pension and postretirement benefit gains, net of $13 tax effect				43		43
Cash dividends - common stock ($0.65 per share)			(17,874)			(17,874)
Purchase of treasury stock	(21)				(3,273)	(3,273)
Stock-based plans	21	(443)				(443)
Stock-based compensation expense		1,180				1,180
Balance, March 31, 2019	27,505	$121,565	$1,344,638	$ (8,129)	$(743,066)	$715,008

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (continued)
(UNAUDITED)

	Nine Months Ended March 31, 2018					
(Amounts in thousands, except per share data)	Common Stock Outstanding		Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total Shareholders' Equity
	Shares	Amount				
Balance, June 30, 2017	27,448	$115,174	$1,206,671	$ (8,936)	$(736,932)	$ 575,977
Net income			29,386			29,386
Net pension and postretirement benefit gains, net of $33 tax effect				56		56
Cash dividends - common stock ($0.55 per share)			(15,092)			(15,092)
Purchase of treasury stock	(7)				(849)	(849)
Stock-based plans	1	(95)				(95)
Stock-based compensation expense		1,163				1,163
Balance, September 30, 2017	27,442	116,242	1,220,965	(8,880)	(737,781)	590,546
Net income			45,920			45,920
Net pension and postretirement benefit gains, net of $33 tax effect				55		55
Cash dividends - common stock ($0.60 per share)			(16,469)			(16,469)
Purchase of treasury stock	—				(4)	(4)
Stock-based plans	9	(189)				(189)
Stock-based compensation expense		1,150				1,150
Balance, December 31, 2017	27,451	117,203	1,250,416	(8,825)	(737,785)	621,009
Net income			27,621			27,621
Net pension and postretirement benefit gains, net of $27 tax effect				62		62
Tax Cuts and Jobs Act of 2017, Reclassification from accumulated other comprehensive loss to retained earnings			1,889	(1,889)		—
Cash dividends - common stock ($0.60 per share)			(16,483)			(16,483)
Purchase of treasury stock	(2)				(249)	(249)
Stock-based plans	29	(268)				(268)
Stock-based compensation expense		1,171				1,171
Balance, March 31, 2018	27,478	$118,106	$1,263,443	$ (10,652)	$(738,034)	$ 632,863

See accompanying notes to condensed consolidated financial statements.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Note 1 – Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Lancaster Colony Corporation and our wholly-owned subsidiaries, collectively referred to as “we,” “us,” “our,” “registrant” or the “Company” ar have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and SEC Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, the interim condensed consolidated financial statements reflect all adjustments necessary for a fair presentation of the results of operations and financial position for such periods. All such adjustments reflected in the interim condensed consolidated financial statements are considered to be of a normal recurring nature. Intercompany transactions and accounts have been eliminated in consolidation. The results of operations for any interim period are not necessarily indicative of results for the full year. Accordingly, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in our 2018 Annual Report on Form 10-K. Unless otherwise noted, the term “year” and references to a particular year pertain to our fiscal year, which begins on July 1 and ends on June 30; for example, 2019 refers to fiscal 2019, which is the period from July 1, 2018 to June 30, 2019.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost, except for those acquired as part of a business combination, which are recorded at fair value at the time of purchase. We use the straight-line method of computing depreciation for financial reporting purposes based on the estimated useful lives of the corresponding assets. Purchases of property, plant and equipment included in Accounts Payable and excluded from the property additions and the change in accounts payable in the Condensed Consolidated Statements of Cash Flows were as follows:

	March 31,	
	2019	2018
Construction in progress in Accounts Payable	$3,131	$1,279

Earnings Per Share

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

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

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

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Net income	$30,604	$27,621	$117,539	$102,927
Net income available to participating securities	(52)	(58)	(212)	(206)
Net income available to common shareholders	$30,552	$27,563	$117,327	$102,721
Weighted average common shares outstanding – basic	27,448	27,405	27,436	27,399
Incremental share effect from:				
Nonparticipating restricted stock	1	2	3	3
Stock-settled stock appreciation rights	100	51	104	54
Weighted average common shares outstanding – diluted	27,549	27,458	27,543	27,456
Net income per common share – basic	$1.11	$1.01	$4.28	$3.75
Net income per common share – diluted	$1.11	$1.00	$4.26	$3.74

Accumulated Other Comprehensive Loss

The following table presents the amounts reclassified out of accumulated other comprehensive loss by component:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Accumulated other comprehensive loss at beginning of period	$(8,172)	$(8,825)	$(8,259)	$(8,936)
Defined Benefit Pension Plan Items:				
Amortization of unrecognized net loss	111	143	335	429
Postretirement Benefit Plan Items:				
Amortization of unrecognized net gain	(9)	(9)	(28)	(27)
Amortization of prior service credit	(46)	(45)	(137)	(136)
Total other comprehensive income, before tax	56	89	170	266
Total tax expense	(13)	(27)	(40)	(93)
Other comprehensive income, net of tax	43	62	130	173
Tax Cuts and Jobs Act of 2017, Reclassification from accumulated other comprehensive loss to retained earnings	—	(1,889)	—	(1,889)
Accumulated other comprehensive loss at end of period	$(8,129)	$(10,652)	$(8,129)	$(10,652)

Significant Accounting Policies

There were no changes to our Significant Accounting Policies from those disclosed in our 2018 Annual Report on Form 10-K. See expanded disclosure of revenue recognition policies in Note 3.

Recently Issued Accounting Standards

In February 2016, the Financial Accounting Standards Board ("FASB") issued new accounting guidance to require lessees to recognize a right-of-use asset and a lease liability for leases with terms of more than 12 months and issued subsequent clarifications of this new guidance. This guidance retains the two classifications of a lease as either an operating or finance lease (previously referred to as a capital lease). Both lease classifications require the lessee to record a right-of-use asset and a lease liability based upon the present value of the lease payments. Finance leases will reflect the financial arrangement by recognizing interest expense on the lease liability separately from the amortization expense of the right-of-use asset. Operating leases will recognize lease expense (with no separate recognition of interest expense) on a straight-line basis over the term of the lease. The guidance requires expanded qualitative and quantitative disclosures, including additional information about the amounts recorded in the consolidated financial statements. The guidance will be effective for us in fiscal 2020, including interim periods. In July 2018, the FASB issued guidance that allows for an alternate transition method whereby companies can recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption rather than restating comparative periods. We expect to elect this alternate transition method. While the adoption of this guidance will result in a significant increase in the balances of right-of-use assets and lease liabilities on our Consolidated Balance Sheet, we do not expect the adoption to impact our results of operations or cash flows. We are currently assessing the impact that this standard will have on our accounting policies, processes, system requirements, internal controls and disclosures. We have completed an initial review of our leases and have implemented lease accounting software, and we are preparing to calculate the adoption impact on our financial statements.

In August 2018, the FASB issued new accounting guidance related to the disclosure requirements for fair value measurements. The guidance removes, modifies and adds disclosures related to fair value. The amendments on changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements, and the narrative description of measurement uncertainty should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. This guidance will be effective for us in fiscal 2021, including interim periods. As the guidance only relates to disclosures, there will be no impact on our financial position or results of operations.

Recently Adopted Accounting Standards

In May 2014, the FASB issued new accounting guidance for the recognition of revenue and issued subsequent clarifications of this new guidance in 2016 and 2017. The core principle of the new guidance states that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This model is based on a control approach. We completed a review of customer contracts and evaluated the impact of the new standard on certain common practices employed by us. We also finalized our assessment of the impact on our accounting policies, processes, system requirements, internal controls and disclosures using internal resources and the assistance of a qualified third party expert. We adopted the new guidance on July 1, 2018 using a modified retrospective approach; however, we did not record a cumulative-effect adjustment from initially applying the standard as the adoption did not have a material impact on our financial position or results of operations. See additional revenue recognition disclosures in Note 3.

In March 2017, the FASB issued new accounting guidance to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost by disaggregating the service cost component from the other components of net periodic benefit cost. The amendments require an employer to present service cost in the same line item(s) as compensation costs for the pertinent employees whereas the other components of net periodic benefit cost must be reported separately from service cost and outside of income from operations. The amendments also allow only the service cost component to be eligible for capitalization. The amendments require retrospective application for the income statement presentation provisions and prospective application for the capitalization of the service cost component. However, as a result of prior years' restructuring activities, we no longer have any active employees continuing to accrue service cost. Therefore, the service cost provisions are not applicable to us. We adopted the new guidance on July 1, 2018, and this adoption resulted in changes in classification on the income statement for all periods presented. The changes were not material.

In August 2018, the FASB issued new accounting guidance to align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. Costs for implementation activities in the application development stage are capitalized depending on the nature of the costs, while costs incurred during the preliminary project and postimplementation stages are expensed as the activities are performed. The guidance also requires such capitalized implementation costs to be expensed over the term of the hosting arrangement and advises on related presentation within the statement of financial position, the statement of income and statement of cash flows. The guidance will be effective for fiscal years, and interim periods within those years, beginning after December 15, 2019 and should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. Early adoption is permitted. We adopted this guidance in the first quarter of fiscal 2019 on a prospective basis. The adoption resulted in a change in accounting principle, to capitalize certain costs instead of expensing them immediately. The costs capitalized under this new guidance were not material to our condensed consolidated financial statements.

In August 2018, the FASB issued new accounting guidance related to the disclosure requirements for defined benefit plans. The guidance removes, adds and clarifies disclosure requirements related to defined benefit pension or other postretirement plans. The guidance will be effective for fiscal years ending after December 15, 2020 and should be applied on a retrospective basis to all periods presented. Early adoption is permitted. We adopted this guidance in the first quarter of fiscal 2019. As the guidance only relates to disclosures, there was no impact on our financial position or results of operations. Changes to our annual disclosures for defined benefit pension plans will be included in our 2019 Annual Report on Form 10-K.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Note 2 – Acquisitions
Bantam Bagels, LLC
On October 19, 2018, we acquired all the assets of Bantam Bagels, LLC ("Bantam"). Bantam, a producer and marketer of frozen mini stuffed bagels and mini stuffed pancakes sold to both the retail and foodservice channels, is based in New York, New York. The base purchase price of $33.1 million, which includes the post-closing working capital adjustment, was funded with cash on hand. This purchase price excludes contingent consideration relating to an additional earn-out payment which is tied to performance-based conditions. In general, the terms of the acquisition specify that the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Bantam for the twelve months ending December 31, 2023. We are unable to provide a range for the amount of this earn-out because it is based on the future adjusted EBITDA of Bantam, and the earn-out does not contain a minimum or maximum value. See further discussion of the earn-out in Note 4. Bantam's results of operations are allocated between our Retail and Foodservice segments in a manner consistent with our current segment allocations. These results have been included in our condensed consolidated financial statements from the date of acquisition. This acquisition is not significant to our financial position or results of operations.
The following table summarizes the consideration related to the acquisition and the purchase price allocation based on the fair value of the net assets acquired. The initial fair value of the contingent consideration is a noncash investing activity.

Consideration	
Cash paid for acquisition	$33,111
Contingent consideration - fair value of earn-out at date of closing	8,000
Fair value of total consideration	$41,111
Purchase Price Allocation	
Receivables	$1,937
Inventories	684
Other current assets	95
Machinery and equipment	1,896
Goodwill (tax deductible)	20,677
Other intangible assets	18,700
Current liabilities	(2,256)
Other noncurrent liabilities	(622)
Net assets acquired	$41,111

Further adjustments are not expected to the allocation above.
The goodwill recognized above arose because the purchase price for Bantam reflects a number of factors including the future earnings and cash flow potential of Bantam, as well as the impact of the inclusion of the initial fair value of the earn-out associated with the acquisition. Bantam is a fast growing, on-trend business with distribution in traditional grocery, club stores, e-commerce and foodservice. Notably, in the foodservice channel, Bantam Bagels® bagel bites are available at corporate-owned Starbucks® cafes nationwide. Bantam also provides innovation opportunities within and beyond our present product lines. A small amount of goodwill also resulted from the workforce acquired with Bantam.
We have determined values and lives of the other intangible assets listed in the allocation above as: $12.8 million for the tradename with a 20-year life; $3.3 million for the customer relationships with a 10-year life and $2.6 million for the technology / know-how with a 10-year life.
Pro forma results of operations have not been presented herein as the acquisition was not material to our results of operations.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Omni Baking Company LLC

On November 16, 2018, we acquired all the assets of Omni Baking Company LLC ("Omni"). Omni has been a long-time supplier of products to our frozen garlic bread operations and is based in Vineland, New Jersey. The purchase price of $24.4 million, which is subject to post-closing adjustments, was funded with cash on hand. Omni's results of operations are allocated between our Retail and Foodservice segments in a manner consistent with our current segment allocations. These results have been included in our condensed consolidated financial statements from the date of acquisition. This acquisition is not significant to our financial position or results of operations.

The following table summarizes the preliminary purchase price allocation based on the fair value of the net assets acquired.

Preliminary Purchase Price Allocation	
Inventories	$809
Other current assets	180
Machinery and equipment	4,777
Goodwill (tax deductible)	21,722
Current liabilities	(3,059)
Net assets acquired	$24,429

Further adjustments may occur to the allocation above as certain aspects of the transaction are finalized during the measurement period, including the post-closing working capital adjustment. In addition to the machinery and equipment acquired, we also assumed an operating lease for Omni's production facility with future minimum rental commitments totaling $7.2 million as of the date of acquisition. This lease continues through December 2026.

The goodwill recognized above arose because the purchase price for Omni reflects a number of factors including the production capabilities of the leased facility and the ability to expand production in the future. Goodwill also resulted from the workforce acquired with Omni. Due to the transitional nature of the foodservice operations, which are related to an interim supply agreement, no goodwill was allocated to the Foodservice segment.

Due to the unique nature of this acquisition, we did not identify any intangible assets apart from goodwill.

Pro forma results of operations have not been presented herein as the acquisition was not material to our results of operations.

Note 3 – Revenue Recognition

We adopted the new revenue recognition guidance on July 1, 2018 using a modified retrospective approach; however, we did not record a cumulative-effect adjustment from initially applying the standard as the adoption did not have a material impact on our financial position or results of operations. We completed a review of customer contracts and evaluated the impact of the new standard on certain common practices employed by us. We also finalized our assessment of the impact on our accounting policies, processes, system requirements, internal controls and disclosures using internal resources and the assistance of a qualified third party expert.

When Performance Obligations Are Satisfied

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer and is the unit of account for revenue recognition. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. The singular performance obligation of our customer contracts is determined by each individual purchase order and the respective food products ordered, with revenue being recognized at a point-in-time when the obligation under the terms of the agreement is satisfied and product control is transferred to our customer. Specifically, control transfers to our customers when the product is delivered to or picked up by our customers based upon applicable shipping terms, as our customers can direct the use and obtain substantially all of the remaining benefits from the asset at this point in time. The performance obligations in our customer contracts are generally satisfied within 30 days. As such, we have not disclosed the transaction price allocated to remaining performance obligations as of March 31, 2019.

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Significant Payment Terms

In general, within our customer contracts, the purchase order identifies the product, quantity, price, pick-up allowances, payment terms and final delivery terms. Payment terms usually include early pay discounts. We grant payment terms consistent with industry standards. Although some payment terms may be more extended, presently the majority of our payment terms are less than 60 days. As a result, we have used the available practical expedient and, consequently, do not adjust our revenues for the effects of a significant financing component.

Shipping

All shipping and handling costs associated with outbound freight are accounted for as fulfillment costs and are included in our cost of sales; this includes shipping and handling costs incurred after control over a product has transferred to a customer, as we have chosen to use the available practical expedient to account for these costs within our cost of sales.

Variable Consideration

In addition to fixed contract consideration, our contracts include some form of variable consideration, including sales discounts, returns, trade promotions and certain other sales and consumer incentives, including rebates and coupon redemptions. In general, variable consideration is treated as a reduction in revenue when the related revenue is recognized. Depending on the specific type of variable consideration, we use either the expected value or most likely amount method to determine the variable consideration. We believe there will be no significant changes to our estimates of variable consideration when any related uncertainties are resolved with our customers. We review and update our estimates and related accruals of variable consideration each period based on historical experience and any recent changes in the market.

Warranties & Returns

We provide all customers with a standard or assurance type warranty. Either stated or implied, we provide assurance the related products will comply with all agreed-upon specifications and other warranties provided under the law. No services beyond an assurance warranty are provided to our customers.

We do not grant a general right of return. However, customers may return defective or non-conforming products. Customer remedies may include either a cash refund or an exchange of the product. As a result, the right of return and related refund liability is estimated and recorded as a reduction in revenue. This return estimate is reviewed and updated each period and is based on historical sales and return experience.

Contract Balances

We do not have deferred revenue or unbilled receivable balances and thus do not have any related contract asset and liability balances as of March 31, 2019.

Contract Costs

We have identified sales commissions as an incremental cost incurred to obtain a customer contract. These costs are required to be capitalized under the new revenue recognition standard. We have chosen to use the available practical expedient to continue to expense these costs as incurred as the amortization period for such costs is one year or less. We do not incur significant fulfillment costs related to customer contracts which would require capitalization.

Disaggregation of Revenue

See Note 9 for disaggregation of our net sales by class of similar product and type of customer.

Note 4 – Fair Value

Fair value is defined as the exit price, or the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. GAAP sets forth a three-level fair value hierarchy, which prioritizes the inputs used in measuring fair value. The three levels are as follows:

Level 1 – defined as observable inputs, such as quoted market prices in active markets.

Level 2 – defined as inputs other than quoted prices in active markets that are either directly or indirectly observable.

Level 3 – defined as unobservable inputs in which little or no market data exists, therefore, requiring an entity to develop its own assumptions.

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Our financial assets and liabilities subject to the three-level fair value hierarchy consist principally of cash and equivalents, accounts receivable, accounts payable, contingent consideration payable and defined benefit pension plan assets. The estimated fair value of cash and equivalents, accounts receivable and accounts payable approximates their carrying value.

Our contingent consideration, which resulted from the earn-outs associated with our acquisitions of Bantam and Angelic Bakehouse, Inc. (“Angelic”), is measured at fair value on a recurring basis and is included in Other Noncurrent Liabilities on the Condensed Consolidated Balance Sheets. The following table summarizes our contingent consideration:

	Fair Value Measurements at March 31, 2019			
	Level 1	Level 2	Level 3	Total
Contingent consideration - Bantam	$—	$—	$8,183	$8,183
Contingent consideration - Angelic	—	—	7,380	7,380
Total contingent consideration	$—	$—	$15,563	$15,563

	Fair Value Measurements at June 30, 2018			
	Level 1	Level 2	Level 3	Total
Contingent consideration - Bantam	$—	$—	$—	$—
Contingent consideration - Angelic	—	—	17,080	17,080
Total contingent consideration	$—	$—	$17,080	$17,080

Bantam Contingent Consideration

This contingent consideration resulted from the earn-out associated with our October 19, 2018 acquisition of Bantam. In general, the terms of the acquisition specify the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Bantam for the twelve months ending December 31, 2023. The initial fair value of the contingent consideration was determined to be $8.0 million, which includes a refinement to the purchase price allocation in the current quarter related to a change in assumptions. The fair value is measured on a recurring basis using a Monte Carlo simulation that randomly changes revenue, EBITDA and other uncertain variables to estimate an expected value. This fair value measurement is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy.

The following table represents our Level 3 fair value measurements using significant other unobservable inputs for Bantam’s contingent consideration:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Contingent consideration at beginning of period	$8,995	$—	$—	$—
Initial fair value - (reductions)/additions	(900)	—	8,000	—
Change in contingent consideration included in operating income	88	—	183	—
Contingent consideration at end of period	$8,183	$—	$8,183	$—

Angelic Contingent Consideration

This contingent consideration resulted from the earn-out associated with our November 17, 2016 acquisition of Angelic. In general, the terms of the acquisition specify the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Angelic for fiscal 2021. The initial fair value of the contingent consideration was determined to be $13.9 million. The fair value is measured on a recurring basis using a present value approach, which incorporates factors such as business risks and projections, to estimate an expected value. This fair value measurement is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy. Our December 31, 2018 fair value measurement resulted in a $9.7 million reduction in the fair value of Angelic's contingent consideration based on a change in Angelic's forecasted adjusted EBITDA for fiscal 2021. This adjustment was recorded in our Retail segment.

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The following table represents our Level 3 fair value measurements using significant other unobservable inputs for Angelic's contingent consideration:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Contingent consideration at beginning of period	$7,380	$16,021	$17,080	$15,028
Change in contingent consideration included in operating income	—	521	(9,700)	1,514
Contingent consideration at end of period	$7,380	$16,542	$7,380	$16,542

Note 5 – Long-Term Debt

At March 31, 2019 and June 30, 2018, we had an unsecured credit facility ("Facility") under which we could borrow, on a revolving credit basis, up to a maximum of $150 million at any one time, with potential to expand the total credit availability to $225 million subject to us obtaining consent of the issuing banks and certain other conditions. The Facility expires on April 8, 2021, and all outstanding amounts are then due and payable. Interest is variable based upon formulas tied to LIBOR or an alternative base rate defined in the Facility, at our option. We must also pay facility fees that are tied to our then-applicable consolidated leverage ratio. Loans may be used for general corporate purposes. Due to the nature of its terms, when we have outstanding borrowings under the Facility, they will be classified as long-term debt.

At March 31, 2019 and June 30, 2018, we had no borrowings outstanding under the Facility. At March 31, 2019 and June 30, 2018, we had $5.1 million of standby letters of credit outstanding, which reduced the amount available for borrowing on the Facility. We paid no interest for the three and nine months ended March 31, 2019 and 2018.

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

Note 6 – Commitments and Contingencies

At March 31, 2019, we were a party to various claims and litigation matters arising in the ordinary course of business. Such matters did not have a material effect on the current-year results of operations and, in our opinion, their ultimate disposition will not have a material effect on our consolidated financial statements.

We have a significant commitment of approximately $40 million related to a capacity expansion project at our frozen dinner roll facility in Horse Cave, Kentucky.

With our acquisitions of Angelic and Bantam, we have contingent liabilities recorded for the earn-outs associated with these transactions. See further discussion in Note 4.

Note 7 – Goodwill and Other Intangible Assets

Goodwill attributable to the Retail and Foodservice segments was $159.5 million and $51.0 million, respectively, at March 31, 2019 compared to $119.3 million and $48.7 million, respectively, at June 30, 2018. The increase in goodwill is the result of the acquisitions of Bantam in October 2018 and Omni in November 2018. See further discussion in Note 2.

The following table is a rollforward of goodwill by reportable segment from June 30, 2018 to March 31, 2019:

	Retail	Foodservice	Total
Goodwill at beginning of year	$119,301	$ 48,729	$168,030
Goodwill acquired during the period - Bantam	18,431	2,246	20,677

Goodwill acquired during the period - Omni	21,722	—	21,722
Goodwill at end of period	$159,454	$ 50,975	$210,429

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The following table summarizes our identifiable other intangible assets. The intangible asset values and lives related to the acquisition of Bantam are included in the table below. See further discussion in Note 2.

	March 31, 2019	June 30, 2018
Tradenames (20 to 30-year life)		
Gross carrying value	$63,121	$50,321
Accumulated amortization	(6,688)	(5,071)
Net carrying value	$56,433	$45,250
Customer Relationships (10 to 15-year life)		
Gross carrying value	$17,507	$14,207
Accumulated amortization	(9,277)	(8,283)
Net carrying value	$8,230	$5,924
Technology / Know-how (10-year life)		
Gross carrying value	$8,950	$6,350
Accumulated amortization	(2,277)	(1,682)
Net carrying value	$6,673	$4,668
Non-compete Agreements (5-year life)		
Gross carrying value	$791	$791
Accumulated amortization	(576)	(457)
Net carrying value	$215	$334
Total net carrying value	$71,551	$56,176

Amortization expense for our other intangible assets, which is reflected in Selling, General and Administrative Expenses, was as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Amortization expense	$1,273	$1,007	$3,325	$2,980

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

2020	$5,061
2021	$4,976
2022	$4,902
2023	$4,343
2024	$4,343

Note 8 – Income Taxes

The Tax Cuts and Jobs Act of 2017 (“Tax Act”) was signed into law on December 22, 2017 with an effective date of January 1, 2018. Most notably, the Tax Act reduced the statutory federal income tax rate for corporations from 35% to 21%. The statutory federal income tax rate for our 2019 tax return will be 21%.

The SEC issued Staff Accounting Bulletin No. 118 (“SAB 118”) on December 22, 2017. SAB 118 allowed for a measurement period in which companies can either use provisional estimates for changes resulting from the Tax Act or apply the tax laws that were in effect immediately prior to the Tax Act being enacted if estimates cannot be determined at the time of the preparation of the financial statements until the actual impacts can be determined. We recorded an initial estimate of the impact of the Tax Act within our December 31, 2017 financial statements, and the

adjustments recorded in the second half of 2018 were not material. The measurement period has ended, and we have completed the accounting for all the impacts of the Tax Act.
Accrued federal income taxes of $1.1 million were included in Accrued Liabilities at March 31, 2019. Prepaid federal income taxes of $3.6 million and prepaid state and local income taxes of $0.9 million were included in Other Current Assets at June 30, 2018. Prepaid state and local income taxes were an immaterial amount at March 31, 2019.

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Note 9 – Business Segment Information

Our financial results are presented as two reportable segments: Retail and Foodservice. Costs that are directly attributable to either Retail or Foodservice are charged directly to the appropriate segment. Costs that are deemed to be indirect, excluding corporate expenses and other unusual significant transactions, are allocated to the two reportable segments using a reasonable methodology that is consistently applied.

Retail - The vast majority of the products we sell in the Retail segment are sold through sales personnel, food brokers and distributors in the United States. We have placement of products in grocery produce departments through our refrigerated salad dressings, vegetable dips and fruit dips. Our flatbread products and sprouted grain bakery products are generally placed in the specialty bakery/deli section of the grocery store. We also have products typically marketed in the shelf-stable section of the grocery store, which include salad dressing, slaw dressing and croutons. Within the frozen food section of the grocery store, we sell yeast rolls, garlic breads and mini stuffed bagels.

Foodservice - The vast majority of the products we sell in the Foodservice segment are sold through sales personnel, food brokers and distributors in the United States. Most of the products we sell in the Foodservice segment are custom-formulated and include salad dressings, sandwich and dipping sauces, frozen breads and yeast rolls. The majority of our Foodservice sales are products sold under private label to restaurants. We also manufacture and sell various branded Foodservice products to distributors. Finally, within this segment, we sell other roll products under a transitional co-packing arrangement resulting from the Omni acquisition.

As many of our products are similar between our two segments, our procurement, manufacturing, warehousing and distribution activities are substantially integrated across our operations in order to maximize efficiency and productivity. Consequently, we do not prepare, and our Chief Operating Decision Maker does not review, separate balance sheets for the reportable segments. As such, our external reporting does not include the presentation of identifiable assets by reportable segment. The composition of our identifiable assets at March 31, 2019 is generally consistent with that of June 30, 2018. However, due to the acquisitions of Bantam in October 2018 and Omni in November 2018, the amount of Retail and Foodservice assets increased as compared to June 30, 2018.

We continue to evaluate our Retail and Foodservice segments based on net sales and operating income which follow:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Net Sales				
Retail	$153,038	$152,011	$502,088	$493,441
Foodservice	164,844	144,163	482,029	421,314
Total	$317,882	$296,174	$984,117	$914,755
Operating Income				
Retail	$24,082	$26,324	$102,815	$96,511
Foodservice	17,124	14,297	55,390	42,398
Corporate Expenses	(3,878)	(3,106)	(10,602)	(10,103)
Total	$37,328	$37,515	$147,603	$128,806

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The following table sets forth net sales disaggregated by class of similar products for the Retail and Foodservice segments:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Retail				
Frozen breads	$59,846	$56,360	$207,256	$202,843
Refrigerated dressings, dips and other	47,900	50,327	164,973	164,785
Shelf-stable dressings and croutons	45,292	45,324	129,859	125,813
Total Retail net sales	$153,038	$152,011	$502,088	$493,441
Foodservice				
Dressings and sauces	$115,746	$108,757	$347,583	$316,202
Frozen breads and other	41,230	35,406	122,742	105,112
Other roll products	7,868	—	11,704	—
Total Foodservice net sales	$164,844	$144,163	$482,029	$421,314
Total net sales	$317,882	$296,174	$984,117	$914,755

The following table provides an additional disaggregation of Foodservice net sales by type of customer:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
Foodservice				