UNIFIRST CORP
Form 10-Q
April 05, 2012

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

FORM 10-Q

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

For the quarterly period ended February 25, 2012

OR

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

For the transition period from ________________ to ________________

Commission file number: 001-08504

UNIFIRST CORPORATION
(Exact name of Registrant as Specified in Its Charter)

Massachusetts (State or Other Jurisdiction of Incorporation or Organization)	04-2103460 (I.R.S. Employer Identification No.)
68 Jonspin Road, Wilmington, MA (Address of Principal Executive Offices)	01887 (Zip Code)

(978) 658-8888
(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 ü No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ü No

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

Large accelerated filer ü Accelerated filer Smaller Reporting Company Non-accelerated filer

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

Yes No ü

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date.

The number of outstanding shares of UniFirst Corporation Common Stock and Class B Common Stock at March 30, 2012 were 15,051,774 and 4,885,277, respectively.

UniFirst Corporation
Quarterly Report on Form 10-Q
For the Quarter ended February 25, 2012

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PART I – FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

UniFirst Corporation and Subsidiaries
Consolidated Statements of Income
(Unaudited)

(In thousands, except per share data)	Thirteen weeks ended February 25, 2012	Thirteen weeks ended February 26, 2011	Twenty-six weeks ended February 25, 2012	Twenty-six weeks ended February 26, 2011
Revenues	$ 309,959	$ 278,595	$ 622,984	$ 551,685
Operating expenses:				
Cost of revenues (1)	201,437	176,233	396,576	339,468
Selling and administrative expenses (1)	61,197	58,614	120,321	113,797
Depreciation and amortization	16,489	16,075	32,897	31,577
Total operating expenses	279,123	250,922	549,794	484,842
Income from operations	30,836	27,673	73,190	66,843
Other (income) expense:				
Interest expense	555	2,202	1,128	4,405
Interest income	(749)	(654)	(1,380)	(1,236)
Exchange rate (gain) loss	(56)	(219)	571	(391)
Total other (income) expense	(250)	1,329	319	2,778
Income before income taxes	31,086	26,344	72,871	64,065
Provision for income taxes	11,890	10,067	27,873	24,024
Net income	$ 19,196	$ 16,277	$ 44,998	$ 40,041
Income per share – Basic:				
Common Stock	$ 1.01	$ 0.86	$ 2.38	$ 2.12
Class B Common Stock	$ 0.81	$ 0.69	$ 1.90	$ 1.70
Income per share – Diluted:				
Common Stock	$ 0.96	$ 0.82	$ 2.26	$ 2.02
Income allocated to – Basic:				
Common Stock	$ 15,081	$ 12,750	$ 35,341	$ 31,356
Class B Common Stock	$ 3,765	$ 3,218	$ 8,832	$ 7,921
Income allocated to – Diluted:				
Common Stock	$ 18,863	$ 15,983	$ 44,213	$ 39,314
Weighted average number of shares outstanding – Basic:				
Common Stock	14,873	14,778	14,856	14,766

Class B Common Stock	4,640	4,661	4,640	4,662
Weighted average number of shares outstanding – Diluted:				
Common Stock	19,605	19,528	19,575	19,503
Dividends per share:				
Common Stock	$ 0.0375	$ 0.0375	$ 0.0750	$ 0.0750
Class B Common Stock	$ 0.0300	$ 0.0300	$ 0.0600	$ 0.0600

(1) Exclusive of depreciation on the Company’s property, plant and equipment and amortization of its intangible assets.

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

UniFirst Corporation and Subsidiaries
Consolidated Balance Sheets
(Unaudited)

(In thousands, except share data)	February 25, 2012	August 27, 2011(a)
Assets		
Current Assets:		
Cash and cash equivalents	$59,346	$48,812
Receivables, less reserves of $6,658 and $4,201, respectively	139,563	128,377
Inventories	77,539	76,460
Rental merchandise in service	136,523	126,536
Prepaid and deferred income taxes	7,298	11,358
Prepaid expenses	6,812	3,647
Total current assets	427,081	395,190
Property, plant and equipment:		
Land, buildings and leasehold improvements	349,672	346,738
Machinery and equipment	408,275	393,530
Motor vehicles	136,075	129,762
Total property, plant and equipment	894,022	870,030
Less -- accumulated depreciation	493,313	474,963
Total property, plant and equipment, net	400,709	395,067
Goodwill	288,119	288,249
Customer contracts, net	53,079	57,890
Other intangible assets, net	2,439	3,015
Other assets	2,246	2,109
Total assets	$1,173,673	$1,141,520
Liabilities and shareholders' equity		
Current liabilities:		
Current maturities of long-term debt	$4,565	$20,133
Accounts payable	54,198	56,064
Accrued liabilities	76,741	76,630
Total current liabilities	135,504	152,827
Long-term liabilities:		
Long-term debt, net of current maturities	100,164	100,163
Accrued liabilities	42,011	39,698
Accrued and deferred income taxes	51,169	50,890
Total long-term liabilities	193,344	190,751

Commitments and contingencies (Note 9)		
Shareholders' equity:		
Preferred stock, $1.00 par value; 2,000,000 shares authorized; no shares issued and outstanding	—	—
Common Stock, $0.10 par value; 30,000,000 shares authorized; 15,050,524 and 14,987,371 issued and outstanding, respectively	1,505	1,499
Class B Common Stock, $0.10 par value; 20,000,000 shares authorized; 4,885,277 and 4,887,777 issued and outstanding, respectively	488	488
Capital surplus	39,197	33,588
Retained earnings	796,108	752,530
Accumulated other comprehensive income	7,527	9,837
Total shareholders' equity	844,825	797,942
Total liabilities and shareholders’ equity	$1,173,673	$1,141,520

(a) Derived from audited financial statements

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

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

Twenty-six weeks ended (In thousands)	February 25, 2012	February 26, 2011
Cash flows from operating activities:		
Net income	$44,998	$40,041
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation	27,550	26,574
Amortization of intangible assets	5,347	5,003
Amortization of deferred financing costs	119	133
Share-based compensation	3,701	3,492
Accretion on environmental contingencies	316	341
Accretion on asset retirement obligations	316	295
Deferred income taxes	362	5,620
Changes in assets and liabilities, net of acquisitions:		
Receivables	(11,698)	(17,538)
Inventories	(1,348)	(10,602)
Rental merchandise in service	(10,246)	(10,165)
Prepaid expenses	(3,169)	(1,292)
Accounts payable	(1,699)	(2,138)
Accrued liabilities	1,891	3,798
Prepaid and accrued income taxes	4,006	(10,941)
Net cash provided by operating activities	60,446	32,621
Cash flows from investing activities:		
Acquisition of businesses, net of cash acquired	—	(16,326)
Capital expenditures	(34,275)	(31,191)
Other	(464)	35
Net cash used in investing activities	(34,739)	(47,482)
Cash flows from financing activities:		
Proceeds from long-term debt	38,910	—
Payments on long-term debt	(54,325)	(1,102)
Proceeds from exercise of Common Stock options	1,914	1,009
Payment of cash dividends	(1,418)	(1,414)
Net cash used in financing activities	(14,919)	(1,507)
Effect of exchange rate changes	(254)	2,597
Net increase (decrease) in cash and cash equivalents	10,534	(13,771)
Cash and cash equivalents at beginning of period	48,812	121,258
Cash and cash equivalents at end of period	$59,346	$107,487

The accompanying notes are an integral part of these

Consolidated Financial Statements.

UniFirst Corporation and Subsidiaries
Notes to Consolidated Financial Statements

1. Basis of Presentation

These Consolidated Financial Statements of UniFirst Corporation (the "Company") have been prepared, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States ("US GAAP") have been condensed or omitted pursuant to such rules and regulations; however, the Company believes that the information furnished reflects all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair statement of results for the interim period.

It is suggested that these Consolidated Financial Statements be read in conjunction with the financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended August 27, 2011. There have been no material changes in the accounting policies followed by the Company during the current fiscal year. Results for an interim period are not indicative of any future interim periods or for an entire fiscal year.

2. Recent Accounting Pronouncements

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

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

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

In September 2011, the FASB issued updated guidance applicable to nongovernmental employers that participate in multiemployer pension and other postretirement benefit plans. The revised accounting rules will require enhanced disclosures relating to an employer's participation in a multiemployer pension plan, but more limited disclosures for multiemployer plans that provide postretirement benefits other than pensions. This guidance is effective for fiscal years ending after December 15, 2011, with early adoption permitted. The Company does not expect the adoption of this guidance to have a material impact on its Consolidated Financial Statements.

In December 2011, the FASB issued updated guidance that requires companies with financial instruments and derivative instruments that are offset on the balance sheet or subject to a master netting arrangement to provide additional disclosures regarding the instrument's impact on a company's financial position. This guidance is effective for interim and annual fiscal periods beginning on or after January 1, 2013. The Company does not expect the adoption of this guidance to have a material impact on its Consolidated Financial Statements.

3. Acquisitions

During the twenty-six weeks ended February 25, 2012, the Company acquired no businesses. Whenever the Company acquires a business, consistent with current accounting guidance, the results of operations of the acquisition are included in the Company's consolidated financial results from the date of the acquisition.

4. Fair Value Measurements

US GAAP establishes a framework for measuring fair value and establishes disclosure requirements about fair value measurements. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

The fair value hierarchy prescribed under US GAAP contains three levels as follows:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

All financial assets or liabilities that are measured at fair value on a recurring basis (at least annually) have been segregated into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date. The assets or liabilities measured at fair value on a recurring basis are summarized in the table below (in thousands):

	As of February 25, 2012			
	Level 1	Level 2	Level 3	Fair Value
Assets:				
Cash equivalents	$ 40,563	$ —	$ —	$ 40,563

Total	$ 40,563	$ —	$ —	$ 40,563

The Company's cash equivalents listed above represent money market securities and are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices. The Company does not adjust the quoted market price for such financial instruments.

5. Derivative Instruments and Hedging Activities

In January 2008, the Company entered into an interest rate swap agreement to manage its exposure to interest rate movements and the related effect on its variable rate debt. The Company concluded that the interest rate swap met the criteria to qualify as a cash flow hedge under US GAAP. Accordingly, the Company reflected all changes in the fair value of the swap agreement in accumulated other comprehensive income, a component of shareholders' equity. The swap agreement, with a notional amount of $100.0 million, matured on March 14, 2011. The Company paid a fixed rate of 3.51% and received a variable rate tied to the three month LIBOR rate.

As of February 25, 2012 and August 27, 2011, there were no fair value amounts recorded by the Company related to this agreement as it matured on March 14, 2011. As of February 25, 2012, we had no outstanding derivative instruments.

The Company recorded any realized gains or losses from its interest rate swap as an adjustment to interest expense in its Consolidated Statements of Income. For the thirteen weeks ended February 26, 2011, the Company reclassified a loss from accumulated other comprehensive income into interest expense totaling $0.8 million. For the twenty-six weeks ended February 26, 2011, the Company reclassified a loss from accumulated other comprehensive income into interest expense totaling $1.6 million.

6. Employee Benefit Plans

Defined Contribution Retirement Savings Plan

The Company has a defined contribution retirement savings plan with a 401(k) feature for all eligible employees not under collective bargaining agreements. The Company matches a portion of the employee's contribution and can make an additional contribution at its discretion. Contributions charged to expense under the plan for the thirteen weeks ended February 25, 2012 and February 26, 2011 were $2.9 million and $2.6 million, respectively. Contributions charged to expense under the plan for the twenty-six weeks ended February 25, 2012 and February 26, 2011 were $5.8 million and $5.2 million, respectively.

Pension Plans and Supplemental Executive Retirement Plans

The Company maintains an unfunded Supplemental Executive Retirement Plan for certain eligible employees of the Company, a non-contributory defined benefit pension plan covering union employees at one of its locations, and a frozen pension plan the Company assumed in connection with its acquisition of Textilease Corporation in fiscal 2004. The amount charged to expense related to these plans for both the thirteen weeks ended February 25, 2012 and February 26, 2011 was $0.5 million. The amounts charged to expense related to these plans for the twenty-six weeks ended February 25, 2012 and February 26, 2011 were $1.1 million and $1.0 million, respectively.

7. Net Income Per Share

The Company calculates net income per share in accordance with US GAAP, which requires the Company to allocate income to its unvested participating securities as part of its earnings per share ("EPS") calculations. The following table sets forth the computation of basic earnings per share using the two-class method for amounts attributable to the Company's shares of Common Stock and Class B Common Stock (in thousands, except per share data):

	Thirteen weeks ended February 25, 2012	Thirteen weeks ended February 26, 2011	Twenty-six weeks ended February 25, 2012	Twenty-six weeks ended February 26, 2011
Net income	$19,196	$16,277	$44,998	$40,041
Allocation of net income for Basic:				
Common Stock	$15,081	$12,750	$35,341	$31,356
Class B Common Stock	3,765	3,218	8,832	7,921
Unvested participating shares	350	309	825	764
	$19,196	$16,277	$44,998	$40,041
Weighted average number of shares for Basic:				
Common Stock	14,873	14,778	14,856	14,766
Class B Common Stock	4,640	4,661	4,640	4,662
Unvested participating shares	394	408	396	410
	19,907	19,847	19,892	19,838
Earnings per share for Basic:				
Common Stock	$1.01	$0.86	$2.38	$2.12
Class B Common Stock	$0.81	$0.69	$1.90	$1.70

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

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

For the thirteen and twenty-six weeks ended February 25, 2012, the Company's diluted EPS assumes the conversion of all vested Class B Common Stock into Common Stock and uses the two-class method for its unvested participating shares as follows (in thousands, except per share data):

	Thirteen weeks ended February 25, 2012			Twenty-six weeks ended February 25, 2012		
	Earnings to Common shareholders	Common Shares	EPS	Earnings to Common shareholders	Common Shares	EPS
As reported - Basic	$ 15,081	14,873	$ 1.01	$ 35,341	14,856	$ 2.38
Add: effect of dilutive potential common shares						
Share-based awards	—	92		—	79	
Class B Common Stock	3,765	4,640		8,832	4,640	

Add: Undistributed earnings allocated to unvested participating shares	337	—		799	—	
Less: Undistributed earnings reallocated to unvested participating shares	(320)	—		(759)	—	
Diluted EPS – Common Stock	$ 18,863	19,605	$ 0.96	$ 44,213	19,575	$ 2.26

Share-based awards that would result in the issuance of 17,454 and 16,369 shares of Common Stock were excluded from the calculation of diluted earnings per share for the thirteen and twenty-six weeks ended February 25, 2012, respectively, because they were anti-dilutive.

For the thirteen and twenty-six weeks ended February 26, 2011, the Company's diluted EPS assumes the conversion of all vested Class B Common Stock into Common Stock and uses the two-class method for its unvested participating shares as follows (in thousands, except per share data):

	Thirteen weeks ended February 26, 2011			Twenty-six weeks ended February 26, 2011		
	Earnings to Common shareholders	Common Shares	EPS	Earnings to Common shareholders	Common Shares	EPS
As reported - Basic	$ 12,750	14,778	$ 0.86	$ 31,356	14,766	$ 2.12
Add: effect of dilutive potential common shares						
Share-based awards	—	89		—	75	
Class B Common Stock	3,218	4,661		7,921	4,662	
Add: Undistributed earnings allocated to unvested participating shares	295	—		737	—	
Less: Undistributed earnings reallocated to unvested participating shares	(280)	—		(700)	—	
Diluted EPS – Common Stock	$ 15,983	19,528	$ 0.82	$ 39,314	19,503	$ 2.02

Share-based awards that would result in the issuance of 19,197 and 127,780 shares of Common Stock were excluded from the calculation of diluted earnings per share for the thirteen and twenty-six weeks ended February 26, 2011, respectively, because they were anti-dilutive.

8. Asset Retirement Obligations

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

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

	February 25, 2012
Beginning balance as of August 27, 2011	$ 9,488
Accretion expense	316
Ending balance as of February 25, 2012	$ 9,804

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

9. Commitments and Contingencies

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

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

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

The Company has accrued certain costs related to the sites described above as it has been determined that the costs are probable and can be reasonably estimated. The Company continues to implement mitigation measures and to monitor environmental conditions at the Somerville, Massachusetts site. The Company also has potential exposure related to an additional parcel of land (the "Central Area") related to the Woburn, Massachusetts site discussed above. Currently, the consent decree for the Woburn site does not define or require any remediation work in the Central Area. The United States Environmental Protection Agency (the "EPA") has provided the Company and other signatories to the consent decree with comments on the design and implementation of groundwater and soil remedies at the Woburn site and investigation of environmental conditions in the Central Area. The Company, and other signatories, have implemented and proposed to do additional work at the Woburn site but many of the EPA’s comments remain to be resolved. The Company has accrued costs to perform certain work responsive to EPA's comments. In addition, in April 2011, the Company received a request from the EPA under the Clean Air Act for information regarding its handling of and operations with respect to the laundering of soiled towels. The Company has responded to this request.

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

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

There is usually a range of reasonable estimates of the costs associated with each site. The Company’s accruals reflect the amount within the range that constitutes its best estimate. Where it believes that both the amount of a particular liability and the timing of the payments are reliably determinable, the Company adjusts the cost in current dollars using a rate of 3% for inflation until the time of expected payment and discounts the cost to present value using current risk-free interest rates. As of February 25, 2012, the risk-free interest rates utilized by the Company ranged from 2.0% to 3.1%.

For environmental liabilities that have been discounted, the Company includes interest accretion, based on the effective interest method, in selling and administrative expenses on the Consolidated Statements of Income. The changes to the Company’s environmental liabilities for the twenty-six weeks ended February 25, 2012 are as follows (in thousands):

	February 25, 2012
Beginning balance as of August 27, 2011	$ 18,368
Costs incurred for which reserves have been provided	(694)
Insurance proceeds received	137
Interest accretion	316
Change in discount rates	760

Balance as of February 25, 2012	$ 18,887

Anticipated payments and insurance proceeds of currently identified environmental remediation liabilities as of February 25, 2012, for the next five fiscal years and thereafter, as measured in current dollars, are reflected below.

(In thousands)	2012	2013	2014	2015	2016	Thereafter	Total
Estimated costs – current dollars	$ 3,641	$ 2,366	$ 1,766	$ 919	$ 766	$ 12,386	$ 21,844
Estimated insurance proceeds	(22)	(173)	(159)	(173)	(159)	(1,893)	(2,579)
Net anticipated costs	$ 3,619	$ 2,193	$ 1,607	$ 746	$ 607	$ 10,493	$ 19,265
Effect of inflation							7,301
Effect of discounting							(7,679)
Balance as of February 25, 2012							$ 18,887

Estimated insurance proceeds are primarily received from an annuity received as part of a legal settlement with an insurance company. Annual proceeds of approximately $0.3 million are deposited into an escrow account which funds remediation and monitoring costs for three sites related to former operations in Williamstown, Vermont. Annual proceeds received but not expended in the current year accumulate in this account and may be used in future years for costs related to this site through the year 2027. As of February 25, 2012, the balance in this escrow account, which is held in a trust and is not recorded in the Company's Consolidated Balance Sheet, was approximately $3.0 million. Also included in estimated insurance proceeds are amounts the Company is entitled to receive pursuant to legal settlements as reimbursements from three insurance companies for estimated costs at the site in Uvalde, Texas.

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

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

While it is impossible to ascertain the ultimate legal and financial liability with respect to contingent liabilities, including lawsuits and environmental contingencies, the Company believes that the aggregate amount of such liabilities, if any, in excess of amounts accrued or covered by insurance, will not have a material adverse effect on the consolidated financial position and/or results of operations of the Company. It is possible, however, that future financial position or results of operations for any particular period could be materially affected by changes in the Company's assumptions or strategies related to these contingencies or changes out of the Company's control.

10. Income Taxes

The Company's effective income tax rate was 38.3% for both the thirteen and twenty-six weeks ended February 25, 2012 as compared to 38.2% and 37.5% for the thirteen and twenty-six weeks ended February 26, 2011, respectively. The increase in the effective income tax rate for the twenty-six weeks ended February 25, 2012 was due to the fact that the 2011 rate benefited from the reversal of tax contingency reserves related to the resolution of certain state tax audits. The Company recognizes interest and penalties related to uncertain tax positions as a component of income tax expense which is consistent with the recognition of these items in prior reporting periods. During the twenty-six weeks ended February 25, 2012, there were no material changes in the amount of unrecognized tax benefits or the amount accrued for interest and penalties.

U.S. and Canadian federal income tax statutes have lapsed for filings up to and including fiscal years 2007 and 2004, respectively. With a few exceptions, the Company is no longer subject to state and local income tax examinations for periods prior to fiscal 2006. The Company is not aware of any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will change significantly in the next 12 months.

11. Long-Term Debt

On May 5, 2011, the Company entered into a $250.0 million unsecured revolving credit agreement (the “Credit Agreement”) with a syndicate of banks, which matures on May 4, 2016. Under the Credit Agreement, the Company is able to borrow funds at variable interest rates based on, at the Company’s election, the Eurodollar rate or a base rate, plus in each case a spread based on the Company’s consolidated funded debt ratio. Availability of credit requires compliance with certain financial and other covenants, including a maximum consolidated funded debt ratio and minimum consolidated interest coverage ratio as defined in the Credit Agreement. The Company tests its compliance with these financial covenants on a fiscal quarterly basis. At February 25, 2012, the interest rates applicable to the Company’s borrowings under the Credit Agreement would be calculated as LIBOR plus 100 basis points at the time of the respective borrowing. As of February 25, 2012, the Company had no outstanding borrowings, letters of credit amounting to $43.2 million and $206.8 million available for borrowing under the Credit Agreement.

Prior to May 5, 2011, the Company had a $225.0 million unsecured revolving credit agreement (the “Prior Credit Agreement”) with a syndicate of banks, which was scheduled to mature on September 13, 2011. In connection with the Company's entry into the Credit Agreement, the Company terminated the Prior Credit Agreement.

On September 14, 2006, the Company issued $100.0 million of floating rates notes (“Floating Rate Notes”) pursuant to a Note Purchase Agreement (“2006 Note Agreement”). The Floating Rate Notes mature on September 14, 2013, bear interest at LIBOR plus 50 basis points and may be repaid at face value two years from the date of issuance.

As of February 25, 2012, the Company was in compliance with all covenants under the Credit Agreement and the 2006 Note Agreement.

12. Other Comprehensive Income

The components of other comprehensive income are as follows (in thousands):

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