LIFEWAY FOODS INC
Form 10-K/A
April 10, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K/A

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015

Commission file number: 000-17363

LIFEWAY FOODS, INC.

(Name of registrant as specified in its charter)

Illinois	**36-3442829**
(State or other jurisdiction of incorporation or organization)	*(IRS Employer Identification No.)*

6431 West Oakton St., Morton Grove, Illinois 60053

(Address of principal executive offices) (Zip Code)

(847) 967-1010

(Registrant's telephone number, including area code)

Securities registered under Section 12(b) of the Exchange Act:

Title of Each Class	**Name of each exchange on which registered**
Common Stock, No Par Value	**Nasdaq Global Market**

Securities registered under Section 12(g) of the Exchange Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

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

Large accelerated filer ¨ Accelerated filer þ Non-accelerated filer o Smaller reporting company o

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the stock was last sold as of June 30, 2015 ($19.19 per share as quoted on the Nasdaq Global Market) was $91,167,353.

As of March 1, 2016 16,188,376 shares of the registrant's common stock, no par value, were outstanding.

Portions of the Registrant's Proxy Statement for the Annual Meeting of Shareholders to be held on June 17, 2016, are incorporated by reference into Part III.

Table of Contents

EXPLANATORY NOTE

On November 4, 2016, the Audit Committee of the Board of Directors (the "Board") of Lifeway Foods, Inc. (the "Company"), upon the recommendation of management, determined that the consolidated financial statements (the "Previously Issued Financial Statements") presented in the Company's reports for the annual period ended December 31, 2015, and the reports of the independent registered public accounting firm thereon, and related quarterly periods for the annual period ended December 31, 2015 as set forth in the Company's previous filings with the Securities and Exchange Commission (the "SEC") (the "Revised Periods") should no longer be relied upon as a result of the following classification errors:

- During fiscal year 2015 certain indirect manufacturing overhead costs were classified as an element of General and Administrative (G&A) expenses in our Statements of Income and Comprehensive Income. These indirect manufacturing overhead costs are more appropriately classified as an element of Cost of Goods Sold.

A description of the restatement is presented in Note 1, under the caption Restatements of prior period financial statements. The classification errors described above have no impact on the Company's previously-reported net sales, income from operations, net income, or basic and diluted earnings per common share presented in its Consolidated Statements of Income and Comprehensive Income, nor does it have a material effect on the Company's previously-reported Consolidated Balance Sheets, Consolidated Statements of Cash Flows, or Consolidated Statements of Changes in Stockholders' Equity.

Additionally, during the first quarter of 2015 certain executive compensation was classified in Selling expenses that management determined should be classified as G&A expenses. Management has determined that these compensation reclassifications are not material.

This Form 10-K/A reflects changes to the Company’s consolidated financial statements and certain notes to the consolidated financial statements including Note 1, Basis of presentation, out of period adjustments and restatements of prior periods. In addition, in connection with the restatement this Form 10-K/A reflects the revisions to Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7 of Part II and revisions to the disclosures regarding controls and procedures in Item 9A of Part II.

FORWARD LOOKING STATEMENTS

In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, readers of this document and any document incorporated by reference herein, are advised that this document and documents incorporated by reference into this document contain both statements of historical facts and forward looking statements. Forward looking statements are subject to certain risks and uncertainties, which could cause actual results to differ materially from those indicated by the forward looking statements. Examples of forward looking statements include, but are not limited to, (i) projections of revenues, income or loss, earnings or losses per share, capital expenditures, dividends, capital structure and other financial items, (ii) statements of Lifeway Foods, Inc.'s ("Lifeway" or the "Company") plans and objectives, including the introduction of new products, or estimates or predictions of actions by customers, suppliers, competitors or regulatory authorities, (iii) statements of future economic performance, and (iv) statements of assumptions underlying other statements and statements about Lifeway or its business.

This document and any documents incorporated by reference herein also identify important factors which could cause actual results to differ materially from those indicated by forward looking statements. These risks and uncertainties include

price competition;

the decisions of customers or consumers;

the actions of competitors;

changes in the pricing of commodities;

the effects of government regulation;

possible delays in the introduction of new products;

customer acceptance of products and services; and

the other risks and uncertainties that are set forth in Item 1, "Business", Item 1A "Risk Factors" and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations".

These factors are not necessarily all of the important factors that could cause actual results to differ materially from those expressed in any of our forward-looking statements. Other unknown or unpredictable factors could also have material adverse effects on future results. Except as otherwise required to be disclosed in periodic reports required to be filed by public companies with the Securities and Exchange Commission ("SEC") pursuant to the SEC's rules, we have no duty to update these statements, and we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

PART I

ITEM 1 BUSINESS

OVERVIEW

Lifeway Foods, Inc. (the "Company" or "Lifeway") was co-founded in 1986 by Michael and Ludmila Smolyansky shortly after their emigration from Russia to the United States. Mr. and Mrs. Smolyansky were the first to successfully introduce Kefir to the U.S. consumer on a commercial scale, initially catering to ethnic consumers in the Chicago metropolitan area. In the thirty years that have followed, Lifeway has grown to become the largest producer and marketer of Kefir in the U.S. and an important player in the broader market spaces of probiotic-based products and natural, "better for you" foods.

PRODUCTS

Lifeway's primary product is drinkable kefir, a fermented dairy product. Kefir has a tart and tangy taste similar to yogurt and the consistency of a smoothie. Kefir also has a slightly effervescent quality all its own. Unlike yogurt though, Lifeway incorporates a unique blend of probiotic kefir cultures in the fermentation process. The probiotic feature, in concert with the base-line nutritional value of a staple beverage that is high in protein, calcium and vitamin D, and low in calories, presents a unique and differentiated taste profile that we believe appeals to a broad and growing demographic.

Because of its drinkable feature, kefir requires no spoon and is ideal for on-the-go consumption … straight from the bottle. Lifeway's Kefir is commonly consumed as part of a healthy breakfast or as an "any-time, better for you" snack in its native form or as a smoothie input. Kefir also serves as a base for lower-calorie dressings, dips, marinades, soups or sauces and as a basic ingredient in other healthy, home-prepared foods. Recipes are made available through the company's website.

In addition to the drinkable kefir that we broadly market to consumers of all ages, we also market and sell our ProBugs line of drinkable kefir which is delivered in our proprietary non-spill pouches (and in 3.5 oz. bottles) intended for children with caring, health-conscious parents. Our frozen kefir offers a nutritional profile similar to our drinkable kefir but in a frozen bar and pint size container conventionally thought of as an indulgent treat. In addition to kefir, Lifeway produces a variety of Kefir-based Eastern European style soft cheeses.

Gross sales of products by category were as follows for the years ended December 31:

	2015		2014		2013	
In thousands	$	%	$	%	$	%
Drinkable Kefir other than ProBugs	118,090	86.0%	110,297	84.7%	90,441	83.0%
ProBugs drinkable Kefir	7,936	5.8%	7,868	6.0%	7,127	6.5%
Lifeway cheese products	9,725	7.1%	10,266	7.9%	9,388	8.6%
Frozen Kefir	1,493	1.1%	1,785	1.4%	2,010	1.9%
Gross Sales	137,244	100%	130,216	100%	108,966	100%

Product innovation and new product development

The company is committed to maintaining its position as the leading producer of Kefir and routinely evaluates opportunities for new product flavors and formulations, improved package design, new product configurations and other forms of routine innovation. As of December 31, 2015 the company offered over 50 unique varieties of its Kefir product including more than 20 unique flavors delivered to consumers on three different milk platforms (fat- free, 1% and whole milk) as well as in both organic and conventional ingredient profiles. During 2015 our routine innovations led to the introduction of several new items, including our new 16 ounce protein enhanced Kefir aimed at the fitness-oriented consumer looking to incorporate more protein into their diets.

Beyond routine innovation, the company has an on-going effort to extend the strength of the Lifeway brand and leverage the capabilities of the Lifeway organization into categories outside of the dairy aisle including into non-food categories. Though we have not yet delivered a product to the market place that has clear commercial viability, our efforts will continue.

The company's innovation, research and development efforts are largely accomplished leveraging an intuitive entrepreneurial, unstructured approach; not a highly formalized, distinct "R&D" function commonly found with large food processors. Research and development costs are not significant.

Product Quality Assurance

The Company employs many skilled production managers across its three Kefir producing facilities who closely monitor our kefir-production process. The production managers have a complement of deep capabilities that spans from traditional dairy operations to the artisan, old-world practices first introduced by Michael and Ludmila Smolyansky at the inception of the Company. We conduct routine tests, tastings and evaluations to ensure that each batch of kefir conforms to the Company's product quality and safety standards. The Company leverages both on-site and third party quality control labs.

The Company includes a clearly legible "freshness" code on every Kefir product in order to ensure that our customers enjoy only the freshest products. To maintain the best of product freshness in the channel, we expect our channel customers (a) to ensure that our products are delivered directly to the retailer's dairy cooler and (b) to rotate such product in a routine and timely way. Due to the perishable nature of our products and the costs associated with moving product back through the channel, the Company does not offer return privileges to any of its channel customers; however, from time to time we do provide our customers with allowances for non-saleable product.

DISTRIBUTION

Lifeway's products reach the consumer through three primary "route-to-market" pathways:

- Direct store delivery ("DSD");
- Retail-direct; and,
- Distributor.

Under the direct store delivery (DSD) route to market, we distribute our products directly to the grocer's dairy cooler using a fleet of company-owned vehicles and a team of seasoned Lifeway merchandisers who engage face-to-face with store management to ensure optimal product assortments and presentation. We operate our DSD model in the Chicago metropolitan area only. Sales to our DSD customers represents less than10% of total company net sales.

Under the retail-direct channel, our products are sold to the retailer and shipped to that retailer's distribution center. In turn our retail customer then delivers the product to their respective stores within their chain. Customers in this route-to-market grouping include among others Kroger, Wal Mart and Costco. Under the retail direct model, optimal product merchandising, assortments and product presentation are attended to by the retailer with support from Lifeway's broker network. Sales to our retail-direct customers represents about 50% of total company net sales.

Under the distributor channel, our products are sold to distributors and shipped to that distributors designated warehouse. In turn, our distributor customers then sell the product to their retail customers and ship the products to their retail customers. Our distributors often use a DSD model of their own to make deliveries directly to individual stores but also make deliveries to the retailer's warehouse. Our distributor customers include among others United Natural Foods, Kehe Foods and C&S Wholesale. Optimal product merchandising, assortments and product presentation at the retail end of the channel are attended to by the distributor with support from Lifeway's broker network. Sales to our distributor customers represents about 40% of total company net sales.

Distribution outside of the U.S.

Substantially all of Lifeway's products are distributed within the United States; however, certain of our distributors sell our products to retailers in Mexico, Costa Rica, Dubai, Hong Kong, China, and the Caribbean. Additionally, the company's products reach a small number of consumers across Canada and in London, England under third party co-manufacturing agreements and in-country distributor arrangements.

Distribution arrangements

Beyond the customer's purchase order, we do not have written agreements with our distributors. Consequently we believe that our arrangements with distributors allow us the latitude to establish new relationships with distributors as the need arises. Lifeway does not offer exclusive territories to any of its distributors.

Distributors are provided Lifeway products at wholesale prices for distribution to their retail accounts. Lifeway believes that the price at which its products are sold to its distributors is competitive with the prices generally paid by distributors for similar products in the markets served. Each distributor carries a line of Lifeway's products on its trucks, checks the retail stores for space allocated to Lifeway's products, determines inventory requirements of the store and places Lifeway products directly into the retailers' dairy cases. Lifeway believes this method of distribution best serves the needs of each retail store, and is the best available means to ensure consistency and quality of product handling, quality control, flavor selection and favorable retail display.

MARKETING

The Company engages in an on-going and wide variety marketing and media campaigns - primarily digital and social media, print advertising in some newspapers and magazines and to a lesser extent television advertising. These marketing and media efforts are complemented by participation in sponsorships of cultural and community events, various festivals, industry-related trade shows and in-store promotional events. Our marketing efforts also include co-op advertising programs with our retail customers and various couponing campaigns.

Our marketing efforts are aimed at stimulating demand with our existing consumers and at driving trial with new consumers by elevating Kefir awareness. Our Kefir awareness marketing seeks to promote the verifiable nutritional profile, purity and good taste of our Kefir and to promote the common perception that our products may have a particular health benefit, such as promoting digestion.

COMPETITION

Lifeway competes with a limited number of other domestic kefir producers and consequently faces a small amount of direct competition for kefir products; however, Lifeway's kefir-based products compete with other dairy products, notably yogurt. Many producers of yogurt and other dairy products are well-established and have significantly greater financial resources than Lifeway to promote their products.

SUPPLIERS

We purchase our ingredients such as raw milk, cane and other forms of sugar and packaging materials from unaffiliated suppliers. Lifeway is not limited or contractually bound to any supplier beyond the terms of our purchase orders, which generally do not exceed our expected demand for periods more than one year. Lifeway has ready access to multiple suppliers for all of its ingredients and packaging requirements.

MAJOR CUSTOMERS

During the year ended December 31, 2015 one distributor, United Natural Foods, Inc., represented approximately 19% of the Company's total sales and one retail customer, Kroger, represented approximately 7% of the Company's total sales. These customers collectively accounted for approximately 19% of accounts receivable as of December 31, 2015.

SEGMENTS

The Company has determined that it has one reportable segment based on how the Company's chief operating decision maker manages the business and in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing company performance, has been identified collectively as the Chief Financial Officer, the Chief Executive Officer and Chairman of the board of directors. Substantially all of the consolidated revenues of the Company relate to the sale of fermented dairy products which are produced using the same processes and materials and are sold to consumers through a network of distributors and retailers in the United States.

GROUPE DANONE SA

Since October, 1999 Groupe Danone SA has been the beneficial owner of approximately 20% of the outstanding common stock of Lifeway. Lifeway and Danone are parties to a Stockholders' Agreement dated October 1, 1999, which as amended provides Danone the right to nominate one director, provides Danone with anti-dilutive rights relating to future offerings and grants Danone limited registration rights.

Danone's interest as of December 31, 2015 was approximately 21%.

PATENTS, TRADEMARKS, LICENSES, ROYALTY AGREEMENTS

The Company has obtained United States trademark registrations for over 20 trademarks, including ProBug Design 1, ProBug Design 2, Penelope ProBug Design, BA3APHBIII (a Stylized presentation of "bazarny" in Cyrillic characters), Bambino, Bazarny, Bio Kefir, Goo-Berry Pie, Helios Nutrition, Korovka, KPECTBRHCKNN (a Stylized presentation of "krestyanskiy" in Cyrillic characters-means "peasant"), Kwashenka, La Fruta, Lifeway, Orange Creamy Crawler, Phytoboost, Playgroup Pack, Pride of Main Street, PRO2O, ProBugs, Starfruit, Sublime Slime Lime and Sweet Kiss.

Lifeway also claims common law rights to, the following unregistered trademarks: "Elita," "Healthy Foods Today for a Better Life Tomorrow," "Milkshake Smoothie," "White Cheese," "Drink It to Be Beautiful Inside and Out," "Golden Zesta" and "Pride of Main Street."

The Company regards its Lifeway family of trademarks and other trademarks as having substantial value and as being an important factor in the marketing of its products. The Company is not aware of any trademark infringements that could materially affect its current business or any prior claim to the trademarks that would prevent the Company from using such trademarks in its business. The Company's policy is to pursue registration of its marks whenever appropriate and to vigorously oppose any infringements of its marks.

REGULATION

Lifeway is subject to regulation by federal, state and local governmental authorities regarding the distribution and sale of food products. Although Lifeway believes that it currently has all material government permits, licenses, qualifications and approvals for its operations, there can be no assurance that Lifeway will be able to maintain its existing licenses and permits or to obtain any future licenses, permits, qualifications or approvals which may be required for the operation of Lifeway's business.

Lifeway believes that it is currently in compliance with all applicable environmental laws and that the cost of such compliance was not material to the financial position of Lifeway.

SEASONALITY

The Company's business is not seasonal.

EMPLOYEES

As of December 31, 2015 the Company employed approximately 370 employees.

AVAILABLE INFORMATION

The Company maintains a corporate website for investors at www.lifeway.net and it makes available, free of charge, through this website its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports that the Company files with or furnishes to the Securities and Exchange Commission (the "SEC"), as soon as reasonably practicable after it electronically files such material with, or furnishes it to, the SEC.

ITEM 1A RISK FACTORS

In evaluating and understanding us and our business, you should carefully consider the risks described below, in conjunction with all of the other information included in this Annual Report on Form 10-K, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" contained in Part II, Item 7 and "Quantitative and Qualitative Disclosures About Market Risk" contained in Part II, Item 7A. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may become important factors that adversely affect our business. If any of the events or circumstances described in the following risk factors actually occurs, our business, financial condition, results of operations, and future prospects could be materially and adversely affected.

Our product categories face a high level of competition, which could negatively impact our sales and results of operations.

We face significant competition in each of our product categories. Competition in our product categories is based on product innovation, product quality, price, brand recognition and loyalty, effectiveness of marketing, promotional activity, and our ability to identify and satisfy consumer tastes and preferences. We believe that our brands have benefited in many cases from being the first to introduce products in their categories, and their success has attracted competition from other food and beverage companies that produce branded products, as well as from private label competitors. Some of our competitors, such as Groupe Danone, General Mills, Inc., Dean Foods, WhiteWave Foods, Hain Celestial Group, and Nestle S.A., have substantial financial and marketing resources. These competitors and others may be able to introduce innovative products more quickly or market their products more successfully than we can, which could cause our growth rate to be slower than we anticipate and could cause sales to decline.

We also compete with producers of non-organic products, which have lower ingredient and production-related costs. As a result, these non-organic producers may be able to offer conventional products to customers at a lower price point. This could cause us to lower our prices, resulting in lower profitability or, in the alternative, cause us to lose market share if we fail to lower prices. Furthermore, private label competitors are generally able to sell their products at lower prices because private label products typically have lower marketing costs than their branded counterparts. If our products fail to compete successfully with other branded or private label offerings, demand for our products and our sales volumes could be negatively impacted.

Additionally, due to high levels of competition, certain of our key retailers may demand price concessions on our products or may become more resistant to price increases for our products. Increased price competition and resistance to price increases have had, and may continue to have, a negative effect on our results of operations.

We may not be able to successfully implement our growth strategy for our brands on a timely basis or at all.

We believe that our future success depends, in part, on our ability to implement our growth strategy of leveraging our existing brands and products to drive increased sales. Our ability to implement this strategy depends, among other things, on our ability to:

- enter into distribution and other strategic arrangements with third-party retailers and other potential distributors of our products;
- compete successfully in the product categories in which we choose to operate;
- introduce new and appealing products and innovate successfully on our existing products;
- develop and maintain consumer interest in our brands;
- increase our brand recognition and loyalty; and
- enter into strategic arrangements with third-party growers and other providers to supply our necessary raw materials.

We may not be able to implement this growth strategy successfully, and our sales and income growth rates may not be sustainable over time. Our sales and results of operations will be negatively affected if we fail to implement our growth strategy or if we invest resources in a growth strategy that ultimately proves unsuccessful.

If we fail to anticipate and respond to changes in consumer preferences, demand for our products could decline.

Consumer tastes and preferences are difficult to predict and they evolve over time. Demand for our products depends on our ability to identify and offer products that appeal to these shifting preferences. Factors that may affect consumer tastes and preferences include:

- dietary trends and increased attention to nutritional values, such as the sugar, fat, protein, fiber or calorie content of different foods and beverages;
- concerns regarding the health effects of specific ingredients and nutrients, such as sugar, other sweeteners, dairy, soybeans, nuts, oils, vitamins, fiber and minerals;
- concerns regarding the public health consequences associated with obesity, particularly among young people; and
- increasing awareness of the environmental and social effects of food processing .

If consumer demand for our products declines, our sales volumes and our business could be negatively affected.

We are subject to the risk of product contamination and product liability claims, which could harm our reputation, force us to recall products and incur substantial costs.

The sale of food products for human consumption involves the risk of injury to consumers. Such injuries may result from tampering by unauthorized third parties, misbranding, product contamination or spoilage including the presence of foreign objects, substances, chemicals, other agents, or residues introduced during the growing, storage, processing, handling or transportation phases. We also may be subject to liability if our products or production processes violate applicable laws or regulations, including environmental, health, and safety requirements, or in the event our products cause injury, illness, or death.

In addition, our product advertising could make us the target of claims relating to false or deceptive advertising under U.S. federal and state laws, including the consumer protection statutes of some states, or laws of other jurisdictions in which we operate. Lifeway is from time to time engaged in such litigation matters none of which presently is expected to have a material adverse effect on its business results or operations.

A significant product liability, consumer fraud, or other legal judgment against us or a widespread product recall would negatively impact our profitability. Moreover, claims or liabilities of this sort might not be covered by insurance or by any rights of indemnity or contribution that we may have against others. Even if a product liability, consumer fraud, or other claim is found to be without merit or is otherwise unsuccessful, the negative publicity surrounding such assertions regarding our products or processes could materially and adversely affect our reputation and brand image, particularly in categories that are promoted as having strong health and wellness credentials. Any loss of consumer confidence in our brand, our products and the ingredients we use or in the safety and quality of our products would be costly and might not be overcome.

The loss of any of our largest customers could negatively impact our sales and results of operations.

Two of our customers together accounted for 26% of our net sales in the fiscal year ended December 31, 2015. We do not generally enter into written agreements with our customers, and where such agreements exist, they are generally terminable at will by the customer. In addition, our customers sometimes award contracts based on competitive bidding, which could result in lower profits for contracts we win and the loss of business for contracts we lose. The loss of any large customer for an extended period of time could negatively affect our sales and results of operations.

We may not be able to successfully complete strategic acquisitions, establish joint ventures, or integrate brands that we acquire.

We intend to continue to grow our business in part through the acquisition of new brands and through the establishment of strategic alliances including potential joint ventures .. We cannot be certain that we will successfully be able to:

- identify suitable acquisition candidates or joint venture partners and accurately assess their value, growth potential, strengths, weaknesses, contingent and other liabilities, and potential profitability;
- secure regulatory clearance for our acquisitions and joint ventures;
- negotiate acquisitions and joint ventures on terms acceptable to us; or
- integrate any acquisitions that we complete.

Acquired companies or brands may not achieve the level of sales or profitability that justify our investment in them, or an acquired company may have unidentified liabilities for which we, as a successor owner, may be responsible. These transactions typically involve a number of risks and present financial and other challenges, including the existence of unknown disputes, liabilities, or contingencies and changes in the industry, location, or regulatory or political environment in which these investments are located, that may arise after entering into such arrangements.

The success of any acquisitions we complete will depend on our ability to effectively integrate the acquired brands or products into our existing operations. We may experience difficulty entering new categories or geographies, integrating new products into our product mix, integrating an acquired brand's distribution channels and sales force, achieving anticipated cost savings, or retaining key personnel and customers of the acquired business. Integrating an acquired brand into our existing operations requires management resources and may divert management's attention from our day-to-day operations. If we are not successful in integrating the operations of acquired brands, or in executing strategies and business plans related to our joint ventures, our business could be negatively affected.

We may have to pay cash, incur debt, or issue equity, equity-linked, or debt securities to pay for any such acquisition, any of which could adversely affect our financial results.

Our continued success depends on our ability to innovate successfully and to innovate on a cost-effective basis.

A key element of our growth strategy is to introduce new and appealing products and to successfully innovate on our existing products. Success in product development is affected by our ability to anticipate consumer preferences, and to utilize our management's ability to launch new or improved products successfully and on a cost-effective basis. Furthermore, the development and introduction of new products requires substantial marketing expenditures, which we may not be able to finance or which we may be unable to recover if the new products do not achieve commercial success and gain widespread market acceptance. If we are unsuccessful in our product innovation efforts, our business could be negatively affected.

Reduced availability of raw materials and other inputs, as well as increased costs for our raw materials and other inputs, could adversely affect us.

Our business depends heavily on raw materials, such as conventional and organic raw milk, used in the production of our products. Our raw materials are generally sourced from third-party suppliers, and we are not assured of continued supply, pricing, or exclusive access to raw materials from any of these suppliers. In addition, a substantial portion of our raw materials are agricultural products, which are vulnerable to adverse weather conditions and natural disasters, such as floods, droughts, frost, earthquakes, and pestilence. Adverse weather conditions and natural disasters also can lower dairy and crop yields and reduce supplies of these ingredients or increase their prices. Other events that adversely affect our third-party suppliers and that are out of our control could also impair our ability to obtain the raw materials and other inputs that we need in the quantities and at the prices that we desire. Such events include problems with our suppliers' businesses, finances, labor relations, costs, production, insurance, and reputation.

The organic ingredients (including milk) we use in some of our products are less plentiful and available from a fewer number of suppliers than their conventional counterparts. Competition with other manufacturers in the procurement of organic product ingredients may increase in the future if consumer demand for organic products increases. In addition, the dairy industry continues to experience periodic imbalances between supply and demand for organic raw milk. Industry regulation and the costs of organic farming compared to costs of conventional farming can impact the supply of organic raw milk in the market. Oversupply levels of organic raw milk can increase competitive pressure on our products and pricing, while supply shortages can cause higher input costs and reduce our ability to deliver product to our customers. Cost increases in raw materials and other inputs could cause our profits to decrease significantly compared to prior periods, as we may be unable to increase our prices to offset the increased cost of these raw materials and other inputs. If we are unable to obtain raw materials and other inputs for our products or offset any increased costs for such raw materials and inputs, our business could be negatively affected.

Failure to maintain sufficient internal production capacity may result in our inability to meet customer demand and/or increase our operating costs and capital expenditures.

The success of our business depends, in part, on maintaining a strong production platform and we rely primarily on internal production resources to fulfill our manufacturing needs. Certain of our manufacturing plants are operating at high rates of utilization, and we may need to expand our production facilities or increase our reliance on third parties to provide manufacturing and supply services, commonly referred to as "co-packing" agreements, for a number of our products. A failure by any future co-packers to comply with food safety, environmental, or other laws and regulations may disrupt our supply of products. In addition, we have experienced, and expect to continue to experience, increased distribution and warehousing costs due to capacity constraints resulting from our growth.

If we need to enter into co-packing, warehousing or distribution agreements in the future, we can provide no assurance that we would be able to find acceptable third party providers or enter into agreements on satisfactory terms or at all. Our inability to maintain sufficient internal capacity or establish satisfactory co-packing, warehousing and distribution arrangements could limit our ability to operate our business or implement our strategic growth plan, and could negatively affect our sales volumes and results of operations.

In addition, our recent initiatives to expand our production platform and our productive capacity, could fail to achieve such objectives and in any case could increase our operating costs beyond our expectations and could require significant additional capital expenditures. If we cannot maintain sufficient production, warehousing and distribution capacity, either internally or through third party agreements, we may be unable to meet customer demand and/or our manufacturing, distribution and warehousing costs may increase, which could negatively affect our business.

Disruption of our supply or distribution chains could adversely affect our business.

Damage or disruption to our manufacturing or distribution capabilities due to weather, natural disaster, fire, environmental incident, terrorism, pandemic, strikes, the financial or operational instability of key suppliers, distributors, warehousing, and transportation providers, or other reasons could impair our ability to manufacture or distribute our products. In addition, most of our products are processed in a single facility, and damage or disruption to this facility could impair our ability to process and sell those products. If we are unable or it is not financially feasible to mitigate the likelihood or potential impact of such events, our business and results of operations could be negatively affected and additional resources could be required to restore our supply chain.

Our substantial debt and financial obligations could adversely affect our financial condition and ability to operate our business.

As of December 31, 2015, we had outstanding borrowings of approximately $8 million substantially all of which consists of term loan borrowings. We also had additional borrowing capacity of approximately $5 million under our line of credit, of which none was outstanding as of December 31, 2015.

Our loan agreements contain certain restrictions and requirements that among other things:

- require us to maintain a minimum fixed charged ratio and a tangible net worth thresholds;
- limit our ability to obtain additional financing in the future for working capital, capital expenditures and acquisitions, to fund growth or for general corporate purposes;
- limit our future ability to refinance our indebtedness on terms acceptable to us or at all;
- limit our flexibility in planning for or reacting to changes in our business and market conditions or in funding our strategic growth plan; and
- impose on us financial and operational restrictions.

Our debt level and the terms of our financing arrangements could adversely affect our financial condition and limit our ability to successfully implement our growth strategy.

Our ability to meet our debt service obligations will depend on our future performance, which will be affected by the other risk factors described in this Annual Report on Form 10-K. If we do not generate enough cash flow to pay our debt service obligations, we may be required to refinance all or part of our existing debt, sell our assets, borrow more money or raise equity. There is no guarantee that we will be able to take any of these actions on a timely basis, on terms satisfactory to us, or at all.

Our notes bear interest at variable rates. If market interest rates increase, it will increase our debt service requirements, which could adversely affect our cash flow.

Our loan agreements also contain provisions that restrict our ability to:

- borrow money or guarantee debt;
- create liens;
- make specified types of investments and acquisitions;
- pay dividends on or redeem or repurchase stock;
- enter into new lines of business;
- enter into transactions with affiliates; and
- sell assets or merge with other companies.

These restrictions on the operation of our business could harm us by, among other things, limiting our ability to take advantage of financing, merger and acquisition opportunities, and other corporate opportunities. Various risks, uncertainties, and events beyond our control could affect our ability to comply with these covenants. Unless cured or waived, a default would permit lenders to accelerate the maturity of the debt under the credit agreement and to foreclose upon the collateral securing the debt.

We may need additional financing in the future, and we may not be able to obtain that financing.

From time to time, we may need additional financing to support our business and pursue our growth strategy, including strategic acquisitions. Our ability to obtain additional financing, if and when required, will depend on investor demand, our operating performance, the condition of the capital markets, and other factors. We cannot assure you that additional financing will be available to us on favorable terms when required, or at all. If we raise additional funds through the issuance of equity, equity-linked, or debt securities, those securities may have rights, preferences, or privileges senior to those of our common stock, and, in the case of equity and equity-linked securities, our existing stockholders may experience dilution.

Our international operations subject us to business risks that could cause our revenue and profitability to decline.

We intend to expand distribution of our products worldwide. Risks associated with our operations as we expand outside of the United States may include, among other things:

- legal and regulatory requirements in multiple jurisdictions that differ from those in the United States and change from time to time, such as tax, labor, and trade laws, as well as laws that affect our ability to manufacture, market, or sell our products;
- foreign currency exposures;
- political and economic instability, such as the recent debt crisis in Europe;
- trade protection measures and price controls; and
- diminished protection of intellectual property in some countries.

If one or more of these business risks occur, our business and results of operations could be negatively affected.

Loss of our key management or other personnel, or an inability to attract such management and other personnel, could negatively impact our business.

We depend on the skills, working relationships, and continued services of key personnel, including our experienced senior management team. We also depend on our ability to attract and retain qualified personnel to operate and expand our business. If we lose one or more members of our senior management team, or if we fail to attract talented new employees, our business and results of operations could be negatively affected.

Our workforce could become unionized in the future, which could materially and adversely affect the stability of our production and materially reduce our profitability.

Our employees have the right at any time under the National Labor Relations Act to form or affiliate with a union and certain of our employees have undertaken the process of forming a union. If our employees form or affiliate with a union and the terms of a union collective bargaining agreement are significantly different from our current compensation and job assignment arrangements with our employees, these arrangements could materially and adversely affect the stability of our operations and materially reduce our profitability.

Our intellectual property rights are valuable, and any inability to protect them could reduce the value of our products and brands.

We consider our intellectual property rights, particularly our trademarks, but also our trade secrets, copyrights, and licenses, to be a significant and valuable aspect of our business. We attempt to protect our intellectual property rights through a combination of trademark, copyright, and trade secret laws, as well as licensing agreements, third-party confidentiality, nondisclosure, and assignment agreements, and by policing third-party misuses of our intellectual property. Our failure to obtain or maintain adequate protection of our intellectual property rights, or any change in law or other changes that serve to lessen or remove the current legal protections of our intellectual property, may diminish our competitiveness and could materially harm our business.

We also face the risk of claims that we have infringed third parties' intellectual property rights. Any claims of intellectual property infringement, even those without merit, could be expensive and time consuming to defend, cause us to cease making, licensing, or using products that incorporate the challenged intellectual property, require us to redesign or rebrand our products or packaging, divert management's attention and resources, or require us to enter into royalty or licensing agreements to obtain the right to use a third party's intellectual property. Any royalty or licensing agreements, if required, may not be available to us on acceptable terms or at all. Additionally, a successful claim of infringement against us could result in our being required to pay significant damages, enter into costly license or royalty agreements, or stop the sale of certain products, any of which could have a negative effect on our results of operations.

Litigation or legal proceedings could expose us to significant liabilities and have a negative impact on our reputation.

We are party to various litigation claims and legal proceedings in the ordinary course of our business. In the opinion of management, the resolution of current litigation claims and legal proceedings will not have a material adverse effect on the Company's consolidated statements of financial condition. We evaluate these litigation claims and legal proceedings to assess the likelihood of unfavorable outcomes and to estimate, if possible, the amount of potential losses. Based on these assessments and estimates, we establish reserves or disclose the relevant litigation claims or legal proceedings, as appropriate. These assessments and estimates are based on the information available to management at the time and involve a significant amount of management judgment. Actual outcomes or losses may differ materially from our current assessments and estimates. If actual outcomes or losses differ materially from our current assessments and estimates or additional litigation or legal proceedings are initiated, we could be exposed to significant liabilities.

Our business is subject to various environmental and health and safety laws and regulations, which may increase our compliance costs or subject us to liabilities.

Our business operations are subject to numerous requirements in the United States relating to the protection of the environment and health and safety matters, including the Clean Air Act, the Clean Water Act, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, and the National Organic Standards of the U.S. Department of Agriculture, as well as similar state and local statutes and regulations in the United States and in each of the countries in which we do business in Europe. These laws and regulations govern, among other things, air emissions and the discharge of wastewater and other pollutants, the use of refrigerants, the handling and disposal of hazardous materials, and the cleanup of contamination in the environment.

We could incur significant costs, including fines, penalties and other sanctions, cleanup costs, and third-party claims for property damage or personal injury as a result of the failure to comply with, or liabilities under, environmental, health, and safety requirements. New legislation, as well as current federal and other state regulatory initiatives relating to these environmental matters, could require us to replace equipment, install additional pollution controls, purchase various emission allowances, or curtail operations. These costs could negatively affect our results of operations and financial condition.

Violations of laws or regulations related to the food industry, as well as new laws or regulations or changes to existing laws or regulations related to the food industry, could adversely affect our business.

The food production and marketing industry is subject to a variety of federal, state, local, and foreign laws and regulations, including food safety requirements related to the ingredients, manufacture, processing, storage, marketing, advertising, labeling, and distribution of our products, as well as those related to worker health and workplace safety. Our activities, both in and outside of the United States, are subject to extensive regulation. We are regulated by, among other federal and state authorities, the U.S. FDA, the U.S. Federal Trade Commission ("FTC"), and the U.S. Departments of Agriculture, Commerce, and Labor, as well as by similar authorities abroad within the regulatory framework of the European Union and its members. Governmental regulations also affect taxes and levies, healthcare costs, energy usage, immigration, and other labor issues, all of which may have a direct or indirect effect on our business or those of our customers or suppliers.

In addition, the marketing and advertising of our products could make us the target of claims relating to alleged false or deceptive advertising under federal, state, and foreign laws and regulations, and we may be subject to initiatives that limit or prohibit the marketing and advertising of our products to children.

We are also subject to federal laws and regulations relating to our organic products and production. For example, as required by the National Organic Program ("NOP"), we rely on third parties to certify certain of our products and production locations as organic. Because the Organic Foods Production Act of 1990, which created the NOP, was so recently adopted, many regulations and informal positions taken by the NOP are subject to continued review and scrutiny.

Changes in these laws or regulations or the introduction of new laws or regulations could increase our compliance costs, increase other costs of doing business for us, our customers, or our suppliers, or restrict our actions, which could adversely affect our results of operations. In some cases, increased regulatory scrutiny could interrupt distribution of our products, as could be the case in the United States as the FDA enacts the Food Safety Modernization Act of 2011, or force changes in our production processes and our products. Further, if we are found to be in violation of applicable laws and regulations in these areas, we could be subject to civil remedies, including fines, injunctions, or recalls, as well as potential criminal sanctions, any of which could have a material adverse effect on our business.

Three of our directors and executive officers control a significant portion of our common stock and their interests may not align with the interests of our other shareholders.

Ludmila Smolyansky, the chairman of our board, Julie Smolyansky, our chief executive officer, president and director and Edward Smolyansky, our chief financial and accounting officer, chief operating officer, treasurer and secretary (together, the "Smolyansky Family") own approximately 49.6% of our issued and outstanding common stock. This significant concentration of share ownership may adversely affect the trading price of our common stock because investors often perceive a disadvantage in owning shares in a company with one or several controlling shareholders.

Furthermore, our directors and officers, as a group, which own in excess of 49.8% of our issued and outstanding common stock have the ability to significantly influence or control the outcome of all matters requiring shareholder approval, including the election of directors and approval of significant corporate transactions, such as mergers, consolidations or the sale of substantially all of our assets.

This concentration of ownership may have the effect of delaying or preventing a change in control of our company which could deprive our shareholders of an opportunity to receive a premium for their shares as part of a sale of our company and might reduce the price of our common stock. In addition, without the consent of the Smolyansky Family, we could be prevented from entering into transactions that could be beneficial to us. The Smolyansky Family may cause us to take actions that are opposed by other shareholders as their interests may differ from those of other shareholders.

We have identified material weaknesses in our internal control over financial reporting. Our failure to establish and maintain effective internal control over financial reporting could result in material misstatements in our financial statements, our failure to meet our reporting obligations and cause investors to lose confidence in our reported financial information, which in turn could cause the trading price of our securities to decline.

We have identified material weaknesses in our internal control over financial reporting. A description of the material weaknesses can be found in Item 9A of this report. As a result of such weaknesses, our management concluded that our disclosure controls and procedures and internal control over financial reporting were not effective as of December 31, 2015.

Unless and until these material weaknesses have been remediated, or should new material weaknesses arise or be discovered in the future material misstatements could occur and go undetected in the Company's interim or annual consolidated financial statements and we may be required to restate our financial statements. In addition, we may experience delays in satisfying our reporting obligations or to comply with SEC rules and regulations, which could result in investigations and sanctions by regulatory authorities. Any of these results could adversely affect our business and the value of our common stock.

ITEM 1B UNRESOLVED STAFF COMMENTS

None

ITEM 2 PROPERTIES

We operate the following facilities:

Location	Owned / Leased	Principal Use
Morton Grove, Illinois	Owned	Production of kefir and cheese, principal executive offices
Waukesha, Wisconsin	Owned	Production of kefir, administrative offices
Niles, Illinois	Owned	Distribution center, administrative offices
Philadelphia, Pennsylvania	Owned	Production of kefir and cheese, administrative offices
Skokie, Illinois	Owned	Production of cheese
Sauk Centre, Minnesota	Owned	Administrative offices

The Company believes that its facilities are adequate for its current needs and that suitable additional space will be available on commercially acceptable terms as required. The Company believes that Lifeway has adequate insurance coverage for all of its properties.

ITEM 3 LEGAL PROCEEDINGS

From time to time we are engaged in litigation matters arising in the ordinary course of business none of which presently is reasonably likely to have a material adverse effect on our financial position or results of operations.

ITEM 4 MINE SAFETY DISCLOSURES

None

PART II

ITEM 5 MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is listed on The Nasdaq Global Market under the symbol "LWAY." Trading commenced on March 29, 1988.

As of February 29, 2016, there were approximately 65 holders of record of Lifeway's Common Stock. The Company has no information regarding beneficial owners whose shares are held in street name.

Common stock price

The following table shows the high and low sale prices per share of our common stock as reported on The Nasdaq Global Market for each quarter during the two most recent fiscal years is set forth in the following table:

	Common Stock Price Range	
	2014	
	Low	High
First Quarter	$13.35	$15.99
Second Quarter	$12.59	$15.50
Third Quarter	$12.34	$14.78
Fourth Quarter	$15.00	$20.33
	2015	
First Quarter	$16.79	$22.38
Second Quarter	$17.20	$21.90
Third Quarter	$10.16	$20.00
Fourth Quarter	$9.88	$12.56

Stock Performance Graph

The following graph compares the cumulative total stockholder return on Lifeway's common stock over the last five fiscal years based on the market price of the common shares and assumes reinvestment of dividends, with the cumulative total return of companies in the Russell 2000 Stock Index and the S&P Packaged Foods group.

The table below assumes an investment of $100 on December 31, 2011 in our common stock, the Russell 2000 Index and the S&P Packaged Foods group.

17

	2010	2011	2012	2013	2014	2015
Lifeway	100	101	92	167	194	116
Russell 2000 Index	100	95	108	148	153	144
S&P Packaged Foods group	100	114	122	156	170	195

Dividend Policy

Lifeway does not routinely declare and pay dividends. From time to time however our Board of Directors may declare and pay dividends depending on the Company's operating cash flow, financial condition, capital requirements and such other factors as the Board of Directors may deem relevant.

There were no dividends declared or paid in fiscal 2015 and 2014.

Issuer Purchases of Equity Securities

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of a publicly announced program (a)		Approximate Dollar Value of Shares that may yet be Purchased Under the Plans or Programs ($ in thousands)
10/1/2015 to 10/31/2015	41,607	$ 11.56	41,607		$ 3,019
11/1/2015 to 11/302015	35,054	$ 10.63	35,054		$ 2,647
12/1/2015 to 12/31/2015	59,526	$ 11.56	59,526	(b)	$ 1,958
Total	136,187	$ 11.32	136,187		$ 1,958

(a) During the fourth quarter of 2015, the company had a publicly announced share repurchase program. Under this program, which was announced on September 24, 2015, the company's Board of Directors authorized the purchase of up to $3.5 million of company stock. The program has no expiration date.

(b) Includes 30,000 shares purchased by the company in privately negotiated transactions, in accordance with all applicable securities laws and regulations.

ITEM 6 SELECTED FINANCIAL DATA

The following table sets forth selected financial data for each of the fiscal years in the five-year period ended December 31, 2015:

Thousands except per share information	2015	2014	2013	2012	2011
Net Sales	$118,587	$118,960	$97,524	$81,351	$69,970
Income from Operations	4,403	4,235	8,031	8,845	5,076
Net Income	1,972	1,956	4,990	5,620	2,855
Total assets	64,918	63,424	63,674	53,507	51,473

Notes payable	7,119	8,125	8,999	4,956	5,540
Total equity	45,256	44,700	42,950	39,313	35,357
Basic and diluted earnings per common share	0.12	0.12	0.31	0.34	0.17
Dividends per share	–	–	0.08	0.07	–

19

ITEM 7 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of the financial condition and results of operations for the twelve-months ended December 31, 2015, 2014 and 2013 should be read in conjunction with the audited consolidated financial statements and the notes to those statements that are included elsewhere in this report on Form 10-K. In addition to historical information, the following discussion contains certain forward-looking statements within the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. These statements relate to our future plans, objectives, expectations and intentions. These statements may be identified by the use of words such as "may", "will", "could", "expect", "anticipate", "intend", "believe", "estimate", "plan", "predict", and similar terms or terminology, or the negative of such terms or other comparable terminology. Although we believe the expectations expressed in these forward-looking statements are based on reasonable assumptions within the bounds of our knowledge of our business, our actual results could differ materially from those discussed in these statements. Factors that could contribute to such differences include, but are not limited to, those discussed in the "Risk Factors" section in Part I, Item 1A. We undertake no obligation to update publicly any forward-looking statements for any reason even if new information becomes available or other events occur in the future.

Results of Operation

Comparison of Year Ended December 31, 2015 to Year Ended December 31, 2014

Net sales

The following table summarizes our net sales:

	Year ended December 31,		Change	
	2015	2014	$	%
Gross Sales	$137,244	$130,216	$7,028	5.4 %
Less: Discounts & promotional allowances	(18,657)	(11,256)	(7,401)	65.8%
Net Sales	$118,587	$118,960	$(373)	-0.3 %
Discounts & promotional allowances % to gross sales	13.6 %	8.6 %		

Net sales declined by $373 or 0.3% during the year ended December 31, 2015 from $118,960 during the same period in 2014. The decrease in net sales reflects a 5.4% increase in gross sales reflecting higher volumes of drinkable Kefir, higher cream sales, and increased private label sales offset by lower sales of cheese and frozen product and significantly higher discounts and promotional allowances given to customers.

Cost of goods sold & gross profit

The following table summarizes our cost of goods sold and gross profit:

	Year ended December 31,		Change	
	2015	2014	$	%
Purchases, net	$ 51,776	$ 59,378	$ (7,602)	-12.8 %
Testing	113	51	62	121.6 %
Supplies	2,026	1,414	612	43.3 %
Salaries production	12,078	9,465	2,613	27.6 %
Contract work	145	158	(13)	-8.2 %
Freight	13,206	12,790	416	3.3 %
Labor and overhead	6,948	4,305	2,643	61.4 %
Cost of Goods Sold, excluding depreciation	86,292	87,561	(1,269)	-1.4 %
Depreciation expense	2,413	2,536	(123)	-4.9 %
Cost of Goods Sold	$ 88,705	$ 90,097	$ (1,392)	-1.5 %
Gross profit	$ 29,882	$ 28,863	$ 1,019	3.5 %
Gross Profit % to net sales	25.2 %	24.3 %		

20

Gross profit as a percent of net sales increased to 25.2% during the year ended December 31, 2015 from 24.3% during the same period in 2014. The increase in the gross profit percent reflects lower input costs, primarily lower milk prices, partially offset by higher labor and overhead costs and the elevated level of promotional allowances and discounts given to customers. During the second quarter of 2015, our Waukesha facility began producing kefir, requiring the classification of certain of the facility's labor and overhead costs as Cost of Goods Sold, versus their classification as G&A in 2014 (before production had begun). The higher labor and overhead costs in 2015 reflects the Waukesha production and its relatively low capacity utilization.

Selling Expenses

The following table summarizes our selling expenses:

	Year ended December 31,		Change	
	2015	2014	$	%
Salesperson commissions	$ 2,285	$ 2,259	$ 26	1.2 %
Advertising	5,006	3,875	1,131	29.2 %
Salaries	3,627	3,331	296	8.9 %
Other marketing & promotion costs	216	403	(187)	-46.4%
Travel	758	1,743	(985)	-56.5%
Selling expense	$ 11,892	$ 11,611	$ 281	2.4 %
% to net sales	10.0 %	9.8 %		

Selling expenses increased by $281 or 2.4% to $11,892 during the year ended December 31, 2015 from $11,611 during the same period in 2014 reflecting an increase in advertising and higher salaries and partially offset by lower travel related costs. The lower travel related costs reflects a concerted effort to contain these costs in 2015. Selling expenses as a percentage of sales were 10.0% for the year ended December 31, 2015 compared to 9.8% for the same period in 2014.

General and administrative expenses

The following table summarizes our general and administrative expenses:

	Year ended December 31,		Change	
	2015	2014	$	%
Salaries	$ 6,671	$ 6,177	$ 494	8.0 %
Rent	265	298	(33)	-11.1 %
Equipment lease	12	8	4	50 %
Auto expense	135	93	42	45.2 %
Office supplies	167	325	(158)	-48.6 %
Professional fees	4,768	3,086	1,682	54.5 %
Telephone expense	165	99	66	66.7 %
Facilities	211	1,515	(1,304)	-86.1 %
Miscellaneous	477	700	(223)	-31.8 %
General & administrative expense	$ 12,871	$ 12,301	$ 570	4.6 %
% to net sales	10.9 %	10.3 %		

General and administrative expenses increased $570 or 4.6% to $12,871 during the year ended December 31, 2015 from $12,301 during the same period in 2014. The increase is primarily a result of increases in professional fees and salaries partially offset by lower facilities costs. Professional fees, which consists primarily of legal and accounting fees increased by $1,682 or 54.5% to $4,768 during the year ended December 31, 2015 from $3,086 during the same period in 2014. The higher professional fees primarily arise from our process improvement initiatives aimed at remediating internal control deficiencies, redundancies and inefficiencies associated with retaining a new audit firm, elevated legal fees associated the company's delayed SEC filings and related matters, and fees paid to executive search firms. During the second quarter of 2015, our Waukesha facility began producing kefir, requiring the classification of certain of the facility’s 2015 labor and overhead costs as Cost of Goods Sold, versus their classification as G&A in 2014 (before production had begun). The lower facilities costs in 2015 were primarily driven by this change in classification.

Income from operations and net income

The company reported income from operations of $4,403 during the year ended December 31, 2015, compared to $4,235 during the same period in 2014. The provision for income taxes was $2,020, or a 50.6% effective rate for the year ended December 31, 2015 compared to a provision for income taxes of $2,242 or a 53.4% effective tax rate during the same period in 2014. Income taxes are discussed in Note 10 to the Notes to the Consolidated Financial Statements.

Net income was $1,972 or $0.12 per basic and diluted common share for the year ended December 31, 2015 compared to $1,956 or $0.12 per basic and diluted common share in the same period in 2014.

Comparison of Year Ended December 31, 2014 to Year Ended December 31, 2013

Net sales

The following table summarizes our net sales:

	Year ended December 31,		Change	
	2014	2013	$	%
Gross Sales	$130,216	$108,966	$21,250	19.5%
Less: Discounts & promotional allowances	(11,256)	(11,442)	186	-1.6%
Net Sales	$118,960	$97,524	$21,436	22.0%
Discounts & promotional allowances % to gross sales	8.6%	10.5%		

Total consolidated net sales increased by $21,436 (approximately 22%) to $118,960 during the year ended December 31, 2014 from $97,524 during the year ended December 31, 2013, primarily as a result of a $21,250 (approximately 19.5%) increase in total consolidated gross sales to $130,216 during the year ended December 31, 2014 from $108,966 during the year ended December 31, 2013, offset by a decrease in discounts and allowances in fiscal year 2014 as compared to fiscal year 2013. The increase in total consolidated gross sales resulted primarily from an increase in volume of products sold. The increase included $18,062 from an increase in volume of products sold and

$3,188 from increases in prices of products sold.

Cost of goods sold & gross profit

The following table summarizes our cost of goods sold and gross profit:

	Year ended December 31,		Change	
	2014	2013	$	%
Purchases, net	$59,379	$47,145	$12,234	25.9 %
Testing	51	37	14	37.8 %
Supplies	1,414	780	634	81.3 %
Salaries production	9,465	7,981	1,484	18.6 %
Contract work	158	69	89	129.0 %
Freight	12,790	9,560	3,230	33.8 %
Labor and overhead	4,304	2,703	1,601	59.2 %
Cost of Goods Sold, excluding depreciation	87,561	68,275	19,286	28.2 %
Depreciation expense	2,536	1,626	910	56.0 %
Cost of Goods Sold	$90,097	$69,901	$20,196	28.9 %
Gross profit	$28,863	$27,623	$1,240	4.5 %
Gross Profit % to net sales	24.3 %	28.3 %		

Total cost of goods sold, increased by $20,196 (approximately 28.9%) to $90,097 during the year ended December 31, 2014 from $69,901 during the year ended December 31, 2013. This increase is a result of increases in cost of goods sold, excluding depreciation expense, and depreciation expense.

Cost of goods sold, excluding depreciation expense, increased by $19,286 (approximately 28.2%) to $87,561 during the year ended December 31, 2014 from $68,275 during the year ended December 31, 2013. This increase is primarily a result of increases in purchases, supplies, salaries, freight and labor and overhead.

Purchases increased by $12,233 (approximately 25.9%) to $59,378 during the year ended December 31, 2014 from $47,145 during the year ended December 31, 2013 primarily as a result of the increase in volume of goods produced. The increase in purchases included approximately $9,196 from an increase in volume of purchases and approximately $3,065 from increases in prices of products purchased.

Supplies increased $634 (approximately 81.3%) to $1,414 during the year ended December 31, 2014 from $780 during the year ended December 31, 2013. The increase is primarily a result of increased purchases related to the Company's Wisconsin facility purchased in July, 2013.

Salaries increased $1,484 (approximately 18.6%) to $9,465 during the year ended December 31, 2014 from $7,981 during the year ended December 31, 2013. The increase was a result of additional employees hired in connection with the purchase of the Wisconsin facility in July 2013.

Freight increased $3,230 (approximately 33.8%) to $12,790 during the year ended December 31, 2014 from $9,560 during the year ended December 31, 2013. The increase was primarily as a result of an increase in the volume of our products sold and shipped.

Labor and overhead increased $1,601 (approximately 59.2%) to $4,304 during the year ended December 31, 2014 from $2,703 during the year ended December 31, 2013. The increase was primarily as a result of increased costs related to the Company's Wisconsin facility purchased in July 2013.

Depreciation expense increased by $910 (approximately 56.0%) to $2,536 during the year ended December 31, 2014 from $1,627 during the year ended December 31, 2013. The increase is partially attributable to an increase in depreciation expense of $470 during 2014 related to an adjustment to the useful lives of the Starfruit leasehold improvements and the depreciation expense of $320 associated with assets placed in service at the Lifeway Wisconsin location since July 2013.

Selling Expenses

The following table summarizes our selling expenses:

	Year ended December 31,		Change
	2014	2013	
Basic and Diluted	39,029,822	39,350,611	

See notes to the condensed consolidated financial statements.

5

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the Six Months Ended January 23, 2010	January 24, 2009
	(Dollars in thousands)	
OPERATING ACTIVITIES:		
Net loss	$(442)	$(67,405)
Adjustments to reconcile net loss to net cash inflow from operating activities:		
Depreciation and amortization	30,707	33,429
Bad debts expense (recovery), net	(6)	23
Gain on sale of fixed assets, net	(1,835)	(1,520)
Gain on extinguishment of debt, net	-	(1,300)
Write-off of deferred financing costs	-	551
Deferred income tax provision	2,428	(12,077)
Stock-based compensation	1,676	1,877
Amortization of debt issuance costs	523	472
Goodwill impairment charge	-	94,429
Excess tax benefit from share-based awards	(69)	-
Change in operating assets and liabilities:		
Accounts receivable, net	24,843	31,252
Costs and estimated earnings in excess of billings, net	24,513	36,072
Other current assets and inventory	(7,717)	(6,165)
Other assets	(445)	572
Income taxes receivable	(2,106)	(4,902)
Accounts payable	(5,413)	(7,141)
Accrued liabilities and insurance claims	(9,784)	(22,957)
Net cash provided by operating activities	56,873	75,210
INVESTING ACTIVITIES:		
Changes in restricted cash	-	(233)
Capital expenditures	(27,275)	(18,313)
Proceeds from sale of assets	2,529	1,840
Net cash used in investing activities	(24,746)	(16,706)
FINANCING ACTIVITIES:		
Proceeds from long-term debt	-	30,000
Principal payments on long-term debt	(722)	(31,268)
Purchase of senior subordinated notes	-	(3,242)
Debt issuance costs	-	(1,795)
Restricted stock tax withholdings	(269)	(246)
Exercise of stock options and other	16	16
Excess tax benefit from share based awards	69	-
Net cash used in financing activities	(906)	(6,535)
Net increase in cash and equivalents	31,221	51,969

CASH AND EQUIVALENTS AT BEGINNING OF PERIOD	104,707	22,068
CASH AND EQUIVALENTS AT END OF PERIOD	$135,928	$74,037
SUPPLEMENTAL DISCLOSURE OF OTHER CASH FLOW ACTIVITIES		
AND NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Cash paid during the period for:		
Interest	$6,518	$7,119
Income taxes	$5,752	$6,581
Purchases of capital assets included in accounts payable or other accrued liabilities at period end	$4,858	$1,221

See notes to the condensed consolidated financial statements.

6

Table of Contents

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Accounting Policies

Basis of Presentation – Dycom Industries, Inc. ("Dycom" or the "Company") is a leading provider of specialty contracting services. These services are provided throughout the United States and include engineering, construction, maintenance and installation services to telecommunications providers, underground facility locating services to various utilities including telecommunications providers, and other construction and maintenance services to electric utilities and others. Additionally, Dycom provides services on a limited basis in Canada.

The condensed consolidated financial statements include the results of Dycom and its subsidiaries, all of which are wholly-owned. All intercompany accounts and transactions have been eliminated. The accompanying condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). The condensed consolidated financial statements do not include all of the financial information and footnotes required by GAAP for complete financial statements. The condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring accruals which are, in the opinion of management, necessary for a fair presentation of such statements. The results of operations for the three and six months ended January 23, 2010 are not necessarily indicative of the results that may be expected for the entire year. These unaudited condensed consolidated financial statements should be read in conjunction with the Company's audited financial statements for the year ended July 25, 2009 included in the Company's 2009 Annual Report on Form 10-K, filed with the SEC on September 3, 2009.

Discontinued Operations – During fiscal 2007, a wholly-owned subsidiary of the Company, Apex Digital, LLC ("Apex") notified its primary customer of its intention to cease performing installation services in accordance with its contractual rights. Effective December 2006, this customer, a satellite broadcast provider, transitioned its installation service requirements to others and Apex ceased providing these services. As a result, the Company discontinued the operations of Apex. The results of Apex were not material in fiscal 2009 or 2010.

Use of Estimates – The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. For the Company, key estimates include: recognition of revenue for costs and estimated earnings in excess of billings, the fair value of goodwill and intangible assets, income taxes, accrued insurance claims, asset lives used in computing depreciation and amortization, allowance for doubtful accounts, stock-based compensation expense for performance-based stock awards, and accruals for contingencies, including legal matters. At the time they are made, the Company believes that such estimates are fair when considered in conjunction with the condensed consolidated financial position and results of operations taken as a whole. However, actual results could differ from those estimates and such differences may be material to the financial statements.

Restricted Cash — As of January 23, 2010 and July 25, 2009, the Company had approximately $4.9 million in restricted cash which is held as collateral in support of the Company's insurance obligations. Restricted cash is included in other current assets and other assets in the condensed consolidated balance sheets and changes in restricted cash are reported in cash flows used in investing activities in the condensed consolidated statements of cash flows.

Comprehensive Loss – During the three and six months ended January 23, 2010 and January 24, 2009, the Company did not have any material changes in its equity resulting from non-owner sources. Accordingly, comprehensive loss approximated the net loss amounts presented for the respective period's operations.

Multiemployer Defined Benefit Pension Plan – A wholly-owned subsidiary of the Company participates in a multiemployer defined benefit pension plan that covers certain of its employees. This subsidiary makes periodic contributions to the plan to meet its benefit obligations. During the three months ended January 23, 2010 and January 24, 2009, the subsidiary contributed approximately $1.4 million and $1.8 million to the plan, respectively. During the six months ended January 23, 2010 and January 24, 2009, the subsidiary contributed approximately $2.6 million and $3.0 million to the plan, respectively.

Table of Contents

Fair Value of Financial Instruments — Accounting Standard Codification ("ASC") Topic 825 requires certain disclosures regarding the fair value of financial instruments. The Company's financial instruments consist primarily of cash and equivalents, restricted cash, accounts receivable, income taxes receivable and payable, accounts payable and accrued expenses, and long-term debt. The carrying amounts of these instruments approximate their fair value due to the short maturity of these items, except for the Company's 8.125% senior subordinated notes due October 2015 (the "Notes"). The Company determined that the fair value of the Notes at January 23, 2010 was $125.4 million based on quoted market prices compared to a carrying value of $135.35 million.

Segment Information — The Company operates in one reportable segment as a specialty contractor, providing engineering, construction, maintenance and installation services to telecommunications providers, underground facility locating services to various utilities including telecommunications providers, and other construction and maintenance services to electric utilities and others. All of the Company's operating segments have been aggregated into one reporting segment due to their similar economic characteristics, products and production methods, and distribution methods. The Company's services are provided by its various subsidiaries throughout the United States and, on a limited basis, in Canada. One of the Company's operating segments earned revenues from contracts in Canada of approximately $1.9 million and $3.5 million during the three and six months ended January 23, 2010, respectively, and $0.8 million and $1.9 million during the three and six months ended January 24, 2009, respectively. The Company had no material long-lived assets in the Canadian operations at January 23, 2010 or July 25, 2009.

Recently Issued Accounting Pronouncements – ASC Topic 860, "Accounting for Transfers of Financial Assets", eliminates the concept of a qualifying special-purpose entity, creates more stringent conditions for reporting a transfer of a portion of a financial asset as a sale, clarifies other sale-accounting criteria, and changes the initial measurement of a transferor's interest in transferred financial assets. This pronouncement is effective for the Company in fiscal 2011. The adoption of ASC Topic 860 is not expected to have a material effect on the Company's condensed consolidated financial statements.

ASC Topic 810, "Amendments to FASB Interpretation: Consolidation of Variable Interest Entities", requires an analysis to determine whether a variable interest gives an enterprise a controlling financial interest in a variable interest entity. This pronouncement requires an ongoing reassessment of whether an enterprise is the primary beneficiary of a variable interest entity. This pronouncement is effective for the Company in fiscal 2011. The adoption of ASC Topic 810 is not expected to have a material effect on the Company's condensed consolidated financial statements.

2. Computation of Earnings (Loss) Per Common Share

FASB Staff Position No. EITF 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities" (ASC Topic 260) addresses whether unvested share-based payment awards with rights to receive dividends or dividend equivalents should be considered as participating securities for the purposes of applying the two-class method of calculating earnings (loss) per share. Unvested share-based payment awards that contain rights to receive non-forfeitable dividends or dividend equivalents are participating securities, and thus, should be included in the two-class method of computing earnings (loss) per share. The Company adopted this standard in the first quarter of fiscal 2010 and the adoption did not change the Company's earnings (loss) per share calculation for any prior period presented.

Basic earnings (loss) per common share is computed based on the weighted average number of shares outstanding during the period, excluding unvested restricted shares and restricted share units. Diluted earnings per common share includes the weighted average common shares outstanding for the period plus dilutive potential common shares, including unvested time vesting and certain performance vesting restricted shares and restricted share units. Performance vesting restricted shares and restricted share units are only included in diluted earnings per common share calculations for the period if all the necessary performance conditions are satisfied and their impact is not anti-dilutive. Common stock equivalents related to stock options are excluded from diluted earnings (loss) per common share calculations if their effect would be anti-dilutive. For the three months and six months ended January 23, 2010 and January 24, 2009, all common stock equivalents related to stock options and unvested restricted shares and restricted share units were excluded from the diluted loss per share calculation as their effect would be anti-dilutive due to the Company's net loss for the periods. The following is a reconciliation of the numerator and denominator of the basic and diluted earnings (loss) per common share computation as required by ASC Topic 260.

8

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
	(Dollars in thousands, except per share amounts)			
Numerator:				
Loss from continuing operations	$(3,965)	$(77,953)	$(442)	$(67,368)
Loss from discontinued operations, net of tax	-	-	-	(37)
Net loss	$(3,965)	$(77,953)	$(442)	$(67,405)
Denominator:				
Basic & Diluted				
Weighted-average number of common shares	39,069,364	39,379,470	39,029,822	39,350,611
Antidilutive weighted shares excluded from the calculation of earnings per common share	3,553,522	3,145,042	3,408,514	2,901,314
LOSS PER COMMON SHARE - BASIC AND DILUTED:				
Loss from continuing operations	$(0.10)	$(1.98)	$(0.01)	$(1.71)
Loss from discontinued operations, net of tax	-	-	-	-
Net loss	$(0.10)	$(1.98)	$(0.01)	$(1.71)

3. Accounts Receivable

Accounts receivable consists of the following:

	January 23, 2010	July 25, 2009
	(Dollars in thousands)	
Contract billings	$89,330	$113,275
Retainage and other receivables	2,061	4,501
Total	91,391	117,776
Less: allowance for doubtful accounts	605	808
Accounts receivable, net	$90,786	$116,968

The allowance for doubtful accounts changed as follows:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009

	(Dollars in thousands)			
Allowance for doubtful accounts at beginning of period	$820	$474	$808	$769
Bad debt expense (recovery), net	(30)	161	(6)	23
Amounts charged against the allowance	(185)	(34)	(197)	(191)
Allowance for doubtful accounts at end of period	$605	$601	$605	$601

As of January 23, 2010, the Company expected to collect all retainage balances within the next twelve months.

9

Table of Contents

4. Costs and Estimated Earnings on Contracts in Excess of Billings

Costs and estimated earnings in excess of billings, net, consists of the following:

	January 23, 2010	July 25, 2009
	(Dollars in thousands)	
Costs incurred on contracts in progress	$ 35,415	$ 53,823
Estimated to date earnings	7,440	13,288
Total costs and estimated earnings	42,855	67,111
Less: billings to date	408	151
	$ 42,447	$ 66,960
Included in the accompanying consolidated balance sheets under the captions:		
Costs and estimated earnings in excess of billings	$ 42,855	$ 67,111
Billings in excess of costs and estimated earnings	(408)	(151)
	$ 42,447	$ 66,960

The above amounts include revenue for services from contracts based both on the units of delivery and the cost-to-cost measures of the percentage of completion method.

5. Property and Equipment

Property and equipment, including amounts for assets subject to capital leases, consists of the following:

	January 23, 2010	July 25, 2009
	(Dollars in thousands)	
Land	$ 3,165	$ 2,974
Buildings	11,625	9,875
Leasehold improvements	4,392	4,361
Vehicles	206,430	199,372
Computer hardware and software	49,026	42,323
Office furniture and equipment	5,210	5,030
Equipment and machinery	125,890	123,709
Total	405,738	387,644
Less: accumulated depreciation	263,179	245,512
Property and equipment, net	$ 142,559	$ 142,132

Depreciation expense and repairs and maintenance, including amounts for assets subject to capital leases, were as follows:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
	(Dollars in thousands)			
Depreciation expense	$13,951	$15,116	$27,526	$29,904
Repairs and maintenance expense	$3,452	$3,836	$7,368	$8,315

Table of Contents

6. Goodwill and Intangible Assets

The Company's goodwill and intangible assets consist of the following:

	Useful Life In Years	January 23, 2010	July 25, 2009
		(Dollars in thousands)	
Goodwill	N/A	$ 157,851	$ 157,851
Intangible Assets:			
Carrying amount			
UtiliQuest tradename	Indefinite	4,700	4,700
Tradenames	4-15	2,600	2,925
Customer relationships	5-15	77,555	77,555
		84,855	85,180
Accumulated amortization:			
Tradenames		659	897
Customer relationships		31,321	28,227
		31,980	29,124
Net Intangible Assets		$ 52,875	$ 56,056

For finite-lived intangible assets, amortization expense for the three months ended January 23, 2010 and January 24, 2009 was $1.6 million and $1.7 million, respectively. For finite-lived intangible assets, amortization expense for the six months ended January 23, 2010 and January 24, 2009 was $3.2 million and $3.5 million, respectively. Amortization of the Company's customer relationships is recognized on an accelerated basis related to the expected economic benefit of the intangible asset, while amortization of other finite-lived intangibles is recognized on a straight-line basis over the estimated useful life.

The Company's goodwill resides in multiple reporting units. The profitability of individual reporting units may periodically suffer from downturns in customer demand and other factors resulting from the cyclical nature of the Company's business, the high level of competition existing within the Company's industry, the concentration of the Company's revenues within a limited number of customers, and the level of overall economic activity. During times of economic slowdown, the Company's customers may reduce their capital expenditures and defer or cancel pending projects. Individual reporting units may be relatively more impacted by these factors than the Company as a whole. As a result, demand for the services of one or more of the Company's reporting units could decline resulting in an impairment of goodwill or intangible assets.

During the second quarter of fiscal 2009, the Company's market capitalization was significantly impacted by the extreme volatility in the U.S. equity and credit markets and was below the book value of shareholders' equity by a substantial margin. As a result, the Company evaluated whether the decrease in its market capitalization reflected factors that would more likely than not reduce the fair value of the Company's reporting units below their carrying value. Based on a combination of factors, including the economic environment, the sustained period of decline in the Company's market capitalization, and the implied valuation and discount rate assumptions in the Company's industry, the Company concluded there were sufficient indicators to perform an interim impairment test of the reporting units and related intangible assets as of January 24, 2009, and, as a result, recognized a preliminary goodwill impairment charge of $94.4 million during the second quarter of fiscal 2009. The Company's interim impairment analysis was finalized during the third quarter of fiscal 2009 and no further charges were incurred. The Company performed its annual impairment test in the fourth quarter of fiscal 2009 and there was no impairment of goodwill or indefinite-lived intangible assets. However, the estimated fair value of the Prince Telecom ("Prince") reporting unit exceeded its carrying value by a margin of less than 25%. There were also smaller margins of fair value over carrying value for the Broadband Installations Services, Ervin Cable Construction ("Ervin"), and UtiliQuest reporting units, as their carrying values were written down to their estimated fair values during fiscal 2009. Broadband Installation Services, Ervin, Prince, and UtiliQuest have remaining goodwill balances of $19.7 million, $7.4 million, $39.7 million, and $35.6 million, respectively, as of January 23, 2010.

Except for the goodwill impairment charges described above, none of the Company's reporting units with remaining goodwill balances incurred material losses in fiscal 2009 or 2010. The estimates and assumptions used in assessing the fair value of the Company's reporting units and the valuation of the underlying assets and liabilities are inherently subject to significant uncertainties. Changes in the Company's judgments and estimates could result in a significantly different estimate of the fair value of the reporting units and could result in impairments of goodwill or intangible assets at additional reporting units. A change in the estimated discount

Table of Contents

rate used would have impacted the amount of the goodwill impairment charges recorded during fiscal 2009. Additionally, continued adverse conditions in the economy and future volatility in the equity and credit markets could further impact the valuation of the Company's reporting units. The Company can provide no assurances that, if such conditions continue, they will not trigger additional impairments of goodwill and other intangible assets in future periods.

The Company continually monitors the economic environment and the impact on its reporting units and market capitalization. When determining the fair value of its reporting units, the Company estimates a premium associated with the control of such reporting unit. The premium is market based and the Company believes it is reasonable based on the industry in which it operates. The Company does not believe that conditions presently exist which would require testing goodwill or intangible assets for impairment in advance of the tests it performs annually in the fourth fiscal quarter of each year. However, future adverse changes in general economic and market conditions and future volatility in the equity and credit markets could trigger an impairment test and impact the Company's valuation of its reporting units.

As of January 23, 2010, the Company believes the carrying value of its goodwill and other indefinite-lived intangible asset is recoverable; however, there can be no assurances that they will not be impaired in future periods. Certain of the Company's reporting units also have other intangible assets including tradenames and customer relationship intangibles. As of January 23, 2010, management believes that the carrying amounts of the intangible assets are recoverable. However, if adverse events were to occur or circumstances were to change indicating that the carrying amount of such assets may not be fully recoverable, the assets would be reviewed for impairment and the assets may become impaired.

7. Accrued Insurance Claims

The Company retains the risk of loss, up to certain limits, for claims relating to automobile liability, general liability (including locate damages), workers' compensation, employee group health. With regard to losses occurring in fiscal 2010, the Company has retained the risk of loss up to $1.0 million on a per occurrence basis for automobile liability, general liability and workers' compensation. These retention amounts are applicable to all of the states in which the Company operates, except with respect to workers' compensation insurance in three states in which the Company participates in a state sponsored insurance fund. Aggregate stop loss coverage for automobile liability, general liability and workers' compensation claims is $43.8 million for fiscal 2010. For losses under the Company's employee health plan occurring during fiscal 2010, it has retained the risk of loss, on an annual basis, of $250,000 per participant.

Accrued insurance claims consist of the following:

	January 23, 2010	July 25, 2009
	(Dollars in thousands)	
Amounts expected to be paid within one year:		
Accrued auto, general liability and workers' compensation	$ 14,183	$ 15,559
Accrued employee group health	3,534	3,698
Accrued damage claims	8,194	8,129
	25,911	27,386
Amounts expected to be paid beyond one year:		
Accrued auto, general liability and workers' compensation	23,854	23,866

Accrued damage claims		5,597		5,893
		29,451		29,759
Total accrued insurance claims	$	55,362	$	57,145

12

Table of Contents

8. Other Accrued Liabilities

Other accrued liabilities consist of the following:

	January 23, 2010	July 25, 2009
	(Dollars in thousands)	
Accrued payroll and related taxes	$ 19,211	$ 22,041
Accrued employee benefit and incentive plan costs	2,384	7,195
Accrued construction costs	8,109	8,083
Accrued interest and related bank fees	3,208	3,228
Current liabilities of discontinued operations	344	528
Other	11,754	11,515
Total other accrued liabilities	$ 45,010	$ 52,590

9. Debt

The Company's outstanding indebtedness consists of the following:

	January 23, 2010	July 25, 2009
	(Dollars in thousands)	
Senior subordinated notes	$ 135,350	$ 135,350
Capital leases	348	953
	135,698	136,303
Less: current portion	348	926
Long-term debt	$ 135,350	$ 135,377

During the first quarter of fiscal 2009, the Company entered into a new three-year $195.0 million revolving Credit Agreement (the "Credit Agreement") with a syndicate of banks. The Credit Agreement was subsequently amended to add an additional bank to the syndicate of banks and increase the maximum borrowing available under the Credit Agreement from $195.0 million to $210.0 million. The Credit Agreement has an expiration date of September 12, 2011 and includes a sublimit of $100.0 million for the issuance of letters of credit. Subject to certain conditions, the Credit Agreement provides for two one-year extensions and, after giving affect to the amendment, also provides the ability to borrow an incremental $85.0 million (the "Incremental Revolving Facility").

Borrowings under the Credit Agreement bear interest, at the Company's option, at either (a) the administrative agent's base rate, described in the Credit Agreement as the higher of the administrative agent's prime rate or the federal funds rate plus 0.50%, or (b) LIBOR (a publicly published rate) plus, in either instance, a spread determined by the Company's condensed consolidated leverage ratio. Since the Credit Agreement has been in place, the spread above the administrative agent's base rate ranged from 0.75% to 1.00% and the spread above LIBOR ranged from 1.75% to 2.00%. The Credit Agreement requires the payment of fees for outstanding letters of credit and unutilized commitments, in each case based on the Company's consolidated leverage ratio. Since inception of the Credit Agreement, fees for outstanding letters of credit ranged from 1.875% to 2.125% per annum and fees for unutilized commitments ranged from 0.625% to 0.75% per annum. The payments under the Credit Agreement are guaranteed by certain subsidiaries and secured by a pledge of (i) 100% of the equity of the Company's material domestic subsidiaries, as defined, and (ii) 100% of the non-voting equity and 65% of the voting equity of first tier material foreign subsidiaries, if any, in each case excluding certain unrestricted subsidiaries.

The Credit Agreement contains certain affirmative and negative covenants, including limitations with respect to indebtedness, liens, investments, distributions, mergers and acquisitions, disposition of assets, sale-leaseback transactions and transactions with affiliates. It also contains defined financial covenants which require the Company to (i) maintain a leverage ratio of not greater than 3.00 to 1.00, as measured at the end of each fiscal quarter, (ii) maintain an interest coverage ratio of not less than 2.75 to 1.00, as measured at the end of each fiscal quarter and (iii) maintain condensed consolidated total tangible net worth, as measured at the end of each fiscal quarter, of not less than $50.0 million plus (A) 50% of condensed consolidated net income (if positive) from September 12, 2008 to the date of computation plus (B) 75% of equity issuances made from September 12, 2008 to the date of computation.

Table of Contents

As of January 23, 2010, the Company had no outstanding borrowings and $43.9 million of outstanding letters of credit issued under the Credit Agreement. The outstanding letters of credit are issued as part of the Company's insurance program. At January 23, 2010, the Company had additional borrowing availability of $153.4 million as determined by the most restrictive covenants of the Credit Agreement and was in compliance with the financial covenants.

In October 2005, Dycom Investments, Inc., a wholly-owned subsidiary of the Company, issued $150.0 million in aggregate principal amount of 8.125% senior subordinated notes due October 2015 ("Notes"). Interest on the Notes is due on April 15th and October 15th of each year. The Company purchased $14.65 million principal amount of the Notes during fiscal 2009 for $11.3 million. As of January 23, 2010, the principal amount outstanding under the Notes was $135.35 million. The indenture governing the Notes contains covenants that restrict the Company's ability to, among other things:

- make certain payments, including the payment of dividends;
- redeem or repurchase capital stock;
- incur additional indebtedness and issue preferred stock;
- make investments or create liens;
- enter into sale and leaseback transactions;
- merge or consolidate with another entity;
- sell certain assets; and
- enter into transactions with affiliates.

10. Income Taxes

The Company accounts for income taxes under the asset and liability method. This approach requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Prior to fiscal 2009, the Company incurred non-cash impairment charges on an investment for financial statement purposes and recorded a deferred tax asset reflecting the tax benefits of those impairment charges. During the first quarter of fiscal 2010, the investment became impaired for tax purposes and the Company determined that it was more likely than not that the associated tax benefit would not be realized prior to its eventual expiration. Accordingly, the Company recognized a non-cash income tax charge of $1.1 million for a valuation allowance of the associated deferred tax asset during the first quarter of fiscal 2010.

As of January 23, 2010, the Company has total unrecognized tax benefits of $2.9 million, which would reduce the Company's effective tax rate during future periods if it is subsequently determined that those liabilities are not required. The Company recognizes interest related to unrecognized tax benefits in interest expense and penalties in general and administrative expenses. Interest expense related to unrecognized tax benefit was immaterial for the three and six months ended January 23, 2010 and January 24, 2009.

11. Other Income, net

The components of other income, net, are as follows:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009

	(Dollars in thousands)			
Gain on sale of fixed assets	$809	$499	$1,835	$1,520
Miscellaneous (loss) income	94	33	173	(35)
Gain on extinguishment of debt, net	-	1,300	-	1,300
Write-off of deferred financing costs	-	-	-	(551)
Total other income, net	$903	$1,832	$2,008	$2,234

12. Capital Stock

On February 23, 2010, the Board of Directors authorized the repurchase of up to $20.0 million of its common stock to be made over the next eighteen months in open market or private transactions. This repurchase program replaces the Company's existing program, scheduled to expire in February 2010, under which there was a remaining authorization of $16.9 million.

Table of Contents

13. Stock-Based Awards

Stock-based awards are granted by the Company under its 2003 Long-term Incentive Plan ("2003 Plan") and the 2007 Non-Employee Directors Equity Plan ("2007 Directors Plan"), (collectively, "the Plans"). The Company also has several other plans under which no further awards will be granted, including expired plans. The Company's policy is to issue new shares to satisfy equity awards under the Plans. Under the terms of the Plans, stock options are granted at the closing price on the date of the grant and are exercisable over a period of up to ten years. The Plans also provide for the grants of time based restricted share units ("RSUs"), that currently vest ratably over a four year period from the date of grant. Additionally, the 2003 Plan provides for the grants of performance based restricted share units ("Performance RSUs"). Outstanding Performance RSUs vest over a three year period from the grant date if certain Company performance goals are achieved.

The following table summarizes the stock-based awards activity during the six months ended January 23, 2010:

	Stock Options		RSUs		Performance RSUs	
	Shares	Weighted Average Exercise Price	Shares/Units	Weighted Average Grant Price	Shares/Units	Weighted Average Grant Price
Outstanding as of July 25, 2009	2,866,675	$23.36	177,400	$13.78	680,342	$21.34
Granted	1,034,248	$8.55	112,436	$8.56	55,746	$12.25
Options Exercised/Shares and Units Vested	(2,375)	$6.83	(83,617)	$13.66	(82,428)	$22.55
Forfeited or cancelled	(210,130)	$25.62	(9,300)	$8.49	(349,468)	$20.93
Outstanding as of January 23, 2010	3,688,418	$19.09	196,919	$11.10	304,192	$19.40
Exercisable options as of January 23, 2010	2,045,723	$27.87				

The Performance RSUs in the above table represent the maximum number of awards which may vest under the outstanding grants assuming that all performance criteria are met. Approximately 310,000 Performance RSUs were cancelled during 2010 related to fiscal 2009 performance criteria not being achieved.

Compensation expense for stock-based awards is based on the fair value at the measurement date and is included in general and administrative expenses in the condensed consolidated statements of operations. The compensation expense and the related tax benefit recognized related to stock options, restricted share and restricted share units for the three and six months ended January 23, 2010 and January 24, 2009 is as follows:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
	(Dollars in thousands)			
Stock-based compensation expense	$705	$330	$1,676	$1,877
Tax benefit recognized	(172)	(89)	(486)	(685)

The Company evaluates compensation expense quarterly and only recognizes expense for performance based awards if management determines it is probable that the performance criteria for the awards will be met. The total amount of expense ultimately recognized is based on the number of awards that actually vest. Accordingly, the amount recognized during current and prior periods may not be representative of future stock-based compensation expense.

Table of Contents

Under the Plans, the maximum total unrecognized compensation expense and weighted-average period over which the expense would be recognized subsequent to January 23, 2010 is as follows:

	Unrecognized Compensation Expense (In thousands)	Weighted-Average Period (In years)
Stock options	$ 7,470	3.5
Unvested RSUs	$ 2,028	2.9
Unvested Performance RSUs	$ 5,900	1.1

For Performance RSUs, the unrecognized compensation cost above is based upon the maximum amount of restricted units that can be earned under outstanding awards. If performance goals are not met related to future performance periods, no compensation expense will be recognized for these units and compensation expense previously recognized on the unvested awards will be reversed.

14. Related Party Transactions

The Company leases administrative offices from entities related to officers of the Company's subsidiaries. The total expense under these arrangements was $0.3 million for both the three month periods ended January 23, 2010 and January 24, 2009, and $0.6 million and $0.7 million the six month periods ended January 23, 2010 and January 24, 2009, respectively.

15. Commitments and Contingencies

Legal Proceedings.

In May 2009, the Company and one of its subsidiaries were named as defendants in a lawsuit in the U.S. District Court for the Western District of Washington. The plaintiffs, all former employees of the subsidiary, allege various wage and hour claims, including that employees were not paid for all hours worked and were subject to improper wage deductions. Plaintiffs seek to certify as a class current and former employees of the subsidiary who worked in the State of Washington. In November 2009, the plaintiffs' attorneys, the Company and the subsidiary entered into a memorandum of understanding pursuant to which the parties agreed to the terms of a proposed settlement with respect to the lawsuit. The proposed settlement provides for the resolution of all claims against the Company and the subsidiary in exchange for an aggregate payment of not more than $2.2 million. In January 2010, the Court granted preliminary approval of the proposed settlement. Notice of the terms of the proposed settlement and claim forms were mailed to members of the plaintiffs' class in February 2010. The settlement is contingent upon final Court approval. The Company estimated the liability of this proposed settlement at $2.0 million and recorded a pre-tax charge for this amount during the first quarter of fiscal 2010. The actual amount of the settlement to be paid will depend on the number of class members that participate in the settlement, and could differ from the estimated amount.

From time to time, the Company and its subsidiaries are also party to various other claims and legal proceedings. Additionally, as part of the Company's insurance program, the Company retains the risk of loss, up to certain limits, for claims related to automobile liability, general liability, workers' compensation, employee group health, and locate damages. For these claims, the effect on the Company’s financial statements is generally limited to the amount of the Company’s insurance deductible or insurance retention. It is the opinion of the Company’s management, based on information available at this time, that none of such other pending claims or proceedings will have a material effect on its condensed consolidated financial statements.

Table of Contents

Performance Bonds and Guarantees.

The Company has obligations under performance bonds related to certain of its customer contracts. Performance bonds generally provide the Company's customer with the right to obtain payment and/or performance from the issuer of the bond if the Company fails to perform its contractual obligations. As of January 23, 2010, the Company had $35.5 million of outstanding performance bonds and no events have occurred in which the customers have exercised their rights under the performance bonds.

The Company has periodically guaranteed certain obligations of its subsidiaries, including obligations in connection with obtaining state contractor licenses and leasing real property.

16. Customer Concentrations

The Company provides specialty contracting services to telecommunications providers, utilities and others. Revenue information by type of customer is as follows:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
	(Dollars in thousands)			
Telecommunications	$173,716	$191,301	$378,613	$454,504
Underground facility locating	37,322	39,659	84,262	91,176
Electric utilities and other construction and maintenance	5,293	14,562	12,572	33,809
Total contract revenues	$216,331	$245,522	$475,447	$579,489

The Company's customer base is highly concentrated, with the top five customers accounting for approximately 65.3% and 64.6% of total contract revenues for the six months ended January 23, 2010 and January 24, 2009, respectively. AT&T, Inc. ("AT&T"), Comcast Cable Corporation ("Comcast"), Verizon Communications, Inc. ("Verizon"), and CenturyTel, Inc. ("Century Link") represent a significant portion of the Company's customer base and were over 10% or more of total revenue for the three months or six months ended January 23, 2010 and January 24, 2009. For the three and six month periods ended January 23, 2010 and January 24, 2009 as follows:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
AT&T	19.8%	19.7%	18.9%	17.4%
Comcast	13.3%	15.4%	14.6%	15.8%
Verizon	12.5%	14.8%	13.7%	17.4%
CenturyLink*	11.1%	6.2%	9.6%	6.0%

*For comparison purposes, CenturyTel, Inc. and Embarq Corporation revenues have been combined for periods prior to their July 2009 merger.

The Company believes that none of its significant customers were experiencing financial difficulties that would impact the collectability of the Company's trade accounts receivable and costs in excess of billings as of January 23, 2010. Customers representing 10% or more of revenue had the following combined amounts of trade accounts receivable and costs and estimated earnings in excess of billings outstanding and the related percentage of the Company's total outstanding balances:

	January 23, 2010		July 25, 2009	
	Amount	% of Total	Amount	% of Total
	(Dollars in millions)			
AT&T	$22.8	17.0 %	$28.5	15.6 %
Comcast	$14.3	10.6 %	$21.6	11.8 %
Verizon	$19.8	14.7 %	$48.0	26.2 %
CenturyLink*	$15.3	11.4 %	$8.8	4.8 %

Table of Contents

17. Supplemental Consolidating Financial Statements

As of January 23, 2010, the principal amount outstanding of the Company's Notes was $135.35 million. The Notes were issued in fiscal 2006 by Dycom Investments, Inc. ("Issuer"), a wholly-owned subsidiary of the Company. The following condensed consolidating financial statements present, in separate columns, financial information for (i) Dycom Industries, Inc. ("Parent") on a parent only basis, (ii) the Issuer, (iii) the guarantor subsidiaries for the Notes on a combined basis, (iv) other non-guarantor subsidiaries on a combined basis, (v) the eliminations and reclassifications necessary to arrive at the information for the Company on a consolidated basis, and (vi) the Company on a consolidated basis. The condensed consolidating financial statements are presented in accordance with the equity method. Under this method, the investments in subsidiaries are recorded at cost and adjusted for the Company's share of subsidiaries' cumulative results of operations, capital contributions, distributions and other equity changes. Intercompany charges (income) between the Parent and subsidiaries are recognized in the condensed consolidating financial statements during the period incurred and the settlement of intercompany balances is reflected in the condensed consolidating statement of cash flows based on the nature of the underlying transactions.

Each guarantor and non-guarantor subsidiary is wholly-owned, directly or indirectly, by the Issuer and the Parent. The Notes are fully and unconditionally guaranteed on a joint and several basis by each guarantor subsidiary and Parent. There are no contractual restrictions limiting transfers of cash from guarantor and non-guarantor subsidiaries to Issuer or Parent, within the meaning of Rule 3-10 of Regulation S-X.

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING BALANCE SHEET (UNAUDITED)
JANUARY 23, 2010

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
ASSETS						
CURRENT ASSETS:						
Cash and equivalents	$-	$-	$135,400	$ 528	$ -	$ 135,928
Accounts receivable, net	-	-	89,475	1,311	-	90,786
Costs and estimated earnings in excess of billings	-	-	42,218	637	-	42,855
Deferred tax assets, net	470	-	13,019	48	(112)	13,425
Income taxes receivable	9,122	-	-	-	-	9,122
Inventories	-	-	10,714	100	-	10,814
Other current assets	6,937	36	5,221	1,322	-	13,516
Total current assets	16,529	36	296,047	3,946	(112)	316,446
Property and equipment, net	13,364	-	112,676	17,126	(607)	142,559
Goodwill	-	-	157,851	-	-	157,851
Intangible assets, net	-	-	52,875	-	-	52,875
Deferred tax assets, net non-current	-	-	14,652	-	(14,652)	-
Investment in subsidiaries	672,674	1,226,700	-	-	(1,899,374)	-
Intercompany receivables	-	-	732,822	-	(732,822)	-
Other	4,518	2,728	2,267	565	-	10,078
Total non-current assets	690,556	1,229,428	1,073,143	17,691	(2,647,455)	363,363
TOTAL	$707,085	$1,229,464	$1,369,190	$ 21,637	$ (2,647,567)	$ 679,809
LIABILITIES AND STOCKHOLDERS' EQUITY						
CURRENT LIABILITIES:						
Accounts payable	$264	$-	$22,982	$ 734	$ -	$ 23,980
Current portion of debt	-	-	348	-	-	348
Billings in excess of costs and estimated earnings	-	-	408	-	-	408
Accrued insurance claims	552	-	25,313	46	-	25,911
Income taxes payable	-	-	-	-	-	-
Deferred tax liabilities	-	112	-	-	(112)	-
Other accrued liabilities	2,170	3,058	38,373	1,409	-	45,010
Total current liabilities	2,986	3,170	87,424	2,189	(112)	95,657
LONG-TERM DEBT	-	135,350	-	-	-	135,350
ACCRUED INSURANCE CLAIMS	806	-	28,584	61	-	29,451

DEFERRED TAX LIABILITIES, net non-current	1,363	390	33,410	3,070	(14,652)	23,581
INTERCOMPANY PAYABLES	307,047	417,880	-	7,905	(732,832)	-
OTHER LIABILITIES	3,865	-	879	8	-	4,752
Total liabilities	316,067	556,790	150,297	13,233	(747,596)	288,791
Total stockholders' equity	391,018	672,674	1,218,893	8,404	(1,899,971)	391,018
TOTAL	$707,085	$1,229,464	$1,369,190	$ 21,637	$ (2,647,567)	$ 679,809

19

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING BALANCE SHEET
JULY 25, 2009

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
ASSETS						
CURRENT ASSETS:						
Cash and equivalents	$-	$-	$104,582	$ 125	$ -	$ 104,707
Accounts receivable, net	3	-	115,631	1,334	-	116,968
Costs and estimated earnings in excess of billings	-	-	66,780	331	-	67,111
Deferred tax assets, net	1,275	-	14,562	112	(170)	15,779
Income taxes receivable	7,028	-	-	-	(12)	7,016
Inventories	-	-	8,189	114	-	8,303
Other current assets	2,202	8	4,454	659	-	7,323
Total current assets	10,508	8	314,198	2,675	(182)	327,207
Property and equipment, net	13,114	-	113,032	16,615	(629)	142,132
Goodwill	-	-	157,851	-	-	157,851
Intangible assets, net	-	-	56,056	-	-	56,056
Deferred tax assets, net non-current	-	-	15,576	113	(15,689)	-
Investment in subsidiaries	672,026	1,216,440	-	2	(1,888,468)	-
Intercompany receivables	-	-	716,687	-	(716,687)	-
Other	4,796	2,906	1,875	634	-	10,211
Total non-current assets	689,936	1,219,346	1,061,077	17,364	(2,621,473)	366,250
TOTAL	$700,444	$1,219,354	$1,375,275	$ 20,039	$ (2,621,655)	$ 693,457
LIABILITIES AND STOCKHOLDERS' EQUITY						
CURRENT LIABILITIES:						
Accounts payable	$258	$-	$28,019	$ 700	$ -	$ 28,977
Current portion of debt	-	-	926	-	-	926
Billings in excess of costs and estimated earnings	-	-	151	-	-	151
Accrued insurance claims	670	-	26,641	75	-	27,386
Deferred tax liabilities	-	105	10	55	(170)	-
Other accrued liabilities	4,937	3,073	43,026	1,566	(12)	52,590
Total current liabilities	5,865	3,178	98,773	2,396	(182)	110,030
LONG-TERM DEBT	-	135,350	27	-	-	135,377
ACCRUED INSURANCE CLAIMS	970	-	28,676	113	-	29,759
DEFERRED TAX LIABILITIES, net	491	428	34,413	3,267	(15,689)	22,910

non-current						
INTERCOMPANY PAYABLES	298,713	408,372	-	9,614	(716,699)	-
OTHER LIABILITIES	3,782	-	964	12	-	4,758
Total liabilities	309,821	547,328	162,853	15,402	(732,570)	302,834
Total stockholders' equity	390,623	672,026	1,212,422	4,637	(1,889,085)	390,623
TOTAL	$700,444	$1,219,354	$1,375,275	$ 20,039	$ (2,621,655)	$ 693,457

20

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)
FOR THE THREE MONTHS ENDED JANUARY 23, 2010

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
REVENUES:						
Contract revenues	$ -	$ -	$ 213,936	$ 2,395	$ -	$ 216,331
EXPENSES:						
Costs of earned revenues, excluding depreciation and amortization	-	-	178,800	2,136	-	180,936
General and administrative	5,285	-	15,544	3,069	-	23,898
Depreciation and amortization	826	-	13,740	962	(12)	15,516
Intercompany charges (income) , net	(6,801)	-	6,557	244	-	-
Total	(690)	-	214,641	6,411	(12)	220,350
Interest income	6	-	16	-	-	22
Interest expense	(696)	(2,832)	(13)	-	-	(3,541)
Other income, net	-	-	940	(37)	-	903
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF SUBSIDIARIES	-	(2,832)	238	(4,053)	12	(6,635)
PROVISION (BENEFIT) FOR INCOME TAXES	-	(1,872)	1,748	(2,546)	-	(2,670)
LOSS FROM CONTINUING OPERATIONS BEFORE EQUITY IN LOSSES OF SUBSIDIARIES	-	(960)	(1,510)	(1,507)	12	(3,965)
LOSS FROM DISCONTINUED OPERATIONS, NET OF TAX	-	-	-	-	-	-
NET LOSS BEFORE EQUITY IN LOSSES OF SUBSIDIARIES	-	(960)	(1,510)	(1,507)	12	(3,965)

EQUITY IN LOSSES OF SUBSIDIARIES	(3,965)	(3,005)	-	-	6,970	-
NET LOSS	$ (3,965)	$ (3,965)	$ (1,510)	$ (1,507)	$ 6,982	$ (3,965)

21

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)
FOR THE SIX MONTHS ENDED JANUARY 23, 2010

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
REVENUES:						
Contract revenues	$ -	$ -	$ 470,953	$ 4,494	$ -	$ 475,447
EXPENSES:						
Costs of earned revenues, excluding depreciation and amortization	-	-	386,739	4,169	-	390,908
General and administrative	10,858	124	31,330	5,089	-	47,401
Depreciation and amortization	1,563	-	27,273	1,893	(22)	30,707
Intercompany charges (income) , net	(13,799)	-	13,369	430	-	-
Total	(1,378)	124	458,711	11,581	(22)	469,016
Interest income	12	-	46	-	-	58
Interest expense	(1,391)	(5,662)	(31)	-	-	(7,084)
Other income, net	1	-	2,037	(30)	-	2,008
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN EARNINGS (LOSSES) OF SUBSIDIARIES	-	(5,786)	14,294	(7,117)	22	1,413
PROVISION (BENEFIT) FOR INCOME TAXES	1,090	(3,133)	7,751	(3,853)	-	1,855
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE EQUITY IN EARNINGS (LOSSES) OF SUBSIDIARIES	(1,090)	(2,653)	6,543	(3,264)	22	(442)
LOSS FROM DISCONTINUED OPERATIONS, NET OF TAX	-	-	-	-	-	-
NET INCOME (LOSS) BEFORE EQUITY						

IN EARNINGS (LOSSES) OF SUBSIDIARIES	(1,090)	(2,653)	6,543	(3,264)	22	(442)
EQUITY IN EARNINGS (LOSSES) OF SUBSIDIARIES	645	3,301	-	-	(3,946)	-
NET INCOME (LOSS)	$ (445)	$ 648	$ 6,543	$ (3,264)	$ (3,924)	$ (442)

22

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)
FOR THE THREE MONTHS ENDED JANUARY 24, 2009

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
REVENUES:						
Contract revenues	$ -	$ -	$ 244,246	$ 1,276	$ -	$ 245,522
EXPENSES:						
Costs of earned revenues, excluding depreciation and amortization	-	-	203,958	1,902	-	205,860
General and administrative	4,918	-	14,862	1,755	-	21,535
Depreciation and amortization	694	-	15,250	884	(11)	16,817
Goodwill impairment charge	-	-	94,429	-	-	94,429
Intercompany charges (income) , net	(6,603)	(23)	7,273	(647)	-	-
Total	(991)	(23)	335,772	3,894	(11)	338,641
Interest income	-	-	40	-	-	40
Interest expense	(989)	(3,064)	(46)	-	-	(4,099)
Other income (expense), net	(2)	1,300	528	6	-	1,832
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN LOSSES OF SUBSIDIARIES	-	(1,741)	(91,004)	(2,612)	11	(95,346)
BENEFIT FOR INCOME TAXES	-	(809)	(15,420)	(1,164)	-	(17,393)
LOSS FROM CONTINUING OPERATIONS BEFORE EQUITY IN LOSSES OF SUBSIDIARIES	-	(932)	(75,584)	(1,448)	11	(77,953)
LOSS FROM DISCONTINUED OPERATIONS, NET OF TAX	-	-	-	-	-	-

NET LOSS BEFORE EQUITY IN LOSSES OF SUBSIDIARIES	-	(932)	(75,584)	(1,448)	11	(77,953)
EQUITY IN LOSSES OF SUBSIDIARIES	(77,953)	(77,021)	-	-	154,974	-
NET LOSS	$ (77,953)	$ (77,953)	$ (75,584)	$ (1,448)	$ 154,985	$ (77,953)

23

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)
FOR THE SIX MONTHS ENDED JANUARY 24, 2009

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
REVENUES:						
Contract revenues	$ -	$ -	$ 576,743	$ 2,746	$ -	$ 579,489
EXPENSES:						
Costs of earned revenues, excluding depreciation and amortization	-	-	470,893	3,829	(216)	474,506
General and administrative	12,067	125	33,215	3,667	-	49,074
Depreciation and amortization	1,329	-	30,483	1,628	(11)	33,429
Goodwill impairment charge	-	-	94,429	-	-	94,429
Intercompany charges (income) , net	(15,807)	(23)	16,776	(1,227)	281	-
Total	(2,411)	102	645,796	7,897	54	651,438
Interest income	-	-	174	-	-	174
Interest expense	(1,858)	(6,203)	(90)	-	-	(8,151)
Other income (expense), net	(553)	1,300	1,616	(129)	-	2,234
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN LOSSES OF SUBSIDIARIES	-	(5,005)	(67,353)	(5,280)	(54)	(77,692)
BENEFIT FOR INCOME TAXES	-	(2,116)	(5,976)	(2,232)	-	(10,324)
LOSS FROM CONTINUING OPERATIONS BEFORE EQUITY IN LOSSES OF SUBSIDIARIES	-	(2,889)	(61,377)	(3,048)	(54)	(67,368)
LOSS FROM DISCONTINUED OPERATIONS, NET OF TAX	-	-	(37)	-	-	(37)

NET LOSS BEFORE EQUITY IN LOSSES OF SUBSIDIARIES	-	(2,889)	(61,414)	(3,048)	(54)	(67,405)
EQUITY IN LOSSES OF SUBSIDIARIES	(67,405)	(64,516)	-	-	131,921	-
NET LOSS	$ (67,405)	$ (67,405)	$ (61,414)	$ (3,048)	$ 131,867	$ (67,405)

24

Table of Contents

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JANUARY 23, 2010

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
Net cash provided by (used in) operating activities	$ (5,090)	$ (2,548)	$ 66,803	$ (2,292)	$ -	$ 56,873
Cash flows from investing activities:						
Capital expenditures	(1,809)	-	(23,032)	(2,434)	-	(27,275)
Proceeds from sale of assets	-	-	2,525	4	-	2,529
Capital contributions to subsidiaries	-	(6,960)	-	-	6,960	-
Net used in investing activities	(1,809)	(6,960)	(20,507)	(2,430)	6,960	(24,746)
Cash flows from financing activities:						
Principal payments on long-term debt	-	-	(722)	-	-	(722)
Restricted stock tax withholdings	(269)	-	-	-	-	(269)
Intercompany funding and financing activities	7,083	9,508	(14,756)	5,125	(6,960)	-
Exercise of stock options and other	16	-	-	-	-	16
Excess tax benefit from share based awards	69	-	-	-	-	69
Net cash (used in) provided by financing activities	6,899	9,508	(15,478)	5,125	(6,960)	(906)
Net increase in cash and equivalents	-	-	30,818	403	-	31,221
CASH AND EQUIVALENTS AT BEGINNING OF PERIOD	-	-	104,582	125	-	104,707
CASH AND EQUIVALENTS AT END OF PERIOD	$ -	$ -	$ 135,400	$ 528	$ -	$ 135,928

25

Table of Contents

DYCOM INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS (UNAUDITED)
FOR THE SIX MONTHS ENDED JANUARY 24, 2009

	Parent	Issuer	Subsidiary Guarantors	Non-Guarantor Subsidiaries	Eliminations and Reclassifications	Dycom Consolidated
			(Dollars in thousands)			
Net cash provided by (used in) operating activities	$ (3,197)	$ (4,127)	$ 83,830	$ (1,232)	$ (64)	$ 75,210
Cash flows from investing activities:						
Restricted cash	(233)	-	-	-	-	(233)
Capital expenditures	(3,556)	-	(9,606)	(5,151)	-	(18,313)
Proceeds from sale of assets	-	-	1,840	-	-	1,840
Net cash used in investing activities	(3,789)	-	(7,766)	(5,151)	-	(16,706)
Cash flows from financing activities:						
Proceeds from long-term debt	30,000	-	-	-	-	30,000
Principal payments on long-term debt	(30,000)	-	(1,268)	-	-	(31,268)
Purchase of senior subordinated notes	-	(3,242)	-	-	-	(3,242)
Debt issuance costs	(1,795)	-	-	-	-	(1,795)
Restricted stock tax withholdings	(246)	-	-	-	-	(246)
Exercise of stock options and other	16	-	-	-	-	16
Intercompany funding and financing activities	9,011	7,369	(22,736)	6,292	64	-
Net cash provided by (used in) financing activities	6,986	4,127	(24,004)	6,292	64	(6,535)
Net increase (decrease) in cash and equivalents	-	-	52,060	(91)	-	51,969
CASH AND EQUIVALENTS AT BEGINNING OF PERIOD	-	-	21,568	500	-	22,068
CASH AND EQUIVALENTS AT END	$ -	$ -	$ 73,628	$ 409	$ -	$ 74,037

OF PERIOD

26

Table of Contents

18. Subsequent Events

On February 23, 2010, the Board of Directors authorized the repurchase of up to $20.0 million of its common stock to be made over the next eighteen months in open market or private transactions. This repurchase program replaces the Company's existing program, scheduled to expire in February 2010, under which there was a remaining authorization of $16.9 million.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and with our Annual Report on Form 10-K for the year ended July 25, 2009. Our Annual Report on Form 10-K for the year ended July 25, 2009 was filed with the Securities and Exchange Commission ("SEC") on September 3, 2009 and is available on the SEC's website at www.sec.gov and on our website, which is www.dycomind.com.

Cautionary Note Concerning Forward-Looking Statements and Information

In this Quarterly Report on Form 10-Q, Dycom Industries, Inc. and its subsidiaries (referred to as "the Company," "we," "us," or "our") have made forward-looking statements. The words "believe," "expect," "anticipate," "estimate," "intend," "fore "may," "should," "could," "project" and similar expressions identify forward-looking statements. Such statements may include, but are not limited to:

- anticipated outcomes of contingent events, including litigation;
- projections of revenues, income or loss, or capital expenditures;
- whether the carrying value of our assets are impaired;
- plans for future operations, growth and acquisitions, dispositions, or financial needs;
- liquidity and availability of financing;
- plans relating to our services, including our contract backlog;
- current economic conditions and trends in the industries we serve; and
- assumptions relating to any of foregoing.

These forward-looking statements are based on management's current expectations, estimates and projections and are subject to known and unknown risks and uncertainties that may cause actual results in the future to differ materially from the results projected or implied in any forward-looking statements contained in this report. The factors that could affect future results and cause these results to differ materially from those expressed in the forward-looking statements include, but are not limited to, those described under Item 1A, "Risk Factors" included in the Company's 2009 Annual Report on Form 10-K, filed with the SEC on September 3, 2009 and other risks outlined in our periodic filings with the SEC. Except as required by law, we may not update forward-looking statements, although our circumstances may change in the future. With respect to forward-looking statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

Overview

We are a leading provider of specialty contracting services. These services are provided throughout the United States and include engineering, construction, maintenance and installation services to telecommunications providers, underground facility locating services to various utilities including telecommunications providers, and other construction and maintenance services to electric utilities and others. Additionally, we provide services on a limited basis in Canada. For the six months ended January 23, 2010, the percentage of our revenue by customer type from telecommunications, underground facility locating, and electric utilities and other customers, was approximately 79.6%, 17.7%, and 2.7%, respectively.

Table of Contents

We conduct operations through our subsidiaries. Our revenues may fluctuate as a result of changes in the capital expenditure and maintenance budgets of our customers, as well as changes in the general level of construction activity. The capital expenditures and maintenance budgets of our telecommunications customers may be impacted by consumer demands on telecommunication providers, the introduction of new communication technologies, the physical maintenance needs of their infrastructure, the actions of the Federal Communications Commission, and general economic conditions.

A significant portion of our services are performed under master service agreements and other arrangements with customers that extend for periods of one or more years. We are currently a party to approximately 200 of these agreements. Master service agreements generally contain customer specified service requirements, such as discrete pricing for individual tasks. To the extent that such contracts specify exclusivity, there are often a number of exceptions, including the ability of the customer to issue work orders valued above a specified dollar amount to other service providers, perform work with the customer's own employees, and use other service providers when jointly placing facilities with another utility. In most cases, a customer may terminate these agreements for convenience with written notice.

The remainder of our services are provided pursuant to contracts for specific projects. Long-term contracts relate to specific projects with terms in excess of one year from the contract date. Short-term contracts for specific projects are generally of three to four months in duration. A portion of our contracts include retainage provisions under which 5% to 10% of the contract invoicing may be withheld by the customer pending project completion.

We recognize revenues under the percentage of completion method of accounting using the units of delivery or cost-to-cost measures. A significant majority of our contracts are based on units of delivery and revenue is recognized as each unit is completed. Revenues from contracts using the cost-to-cost measures of completion are recognized based on the ratio of contract costs incurred to date to total estimated contract costs. Revenues from services provided under time and materials based contracts are recognized as the services are performed.

The following table summarizes our revenues from multi-year master service agreements and other long-term contracts, as a percentage of contract revenues from continuing operations:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
Multi-year master service agreements	76.4%	69.8%	75.5%	66.2%
Other long-term contracts	14.2%	15.8%	15.1%	18.9%
Total long-term contracts	90.6%	85.6%	90.6%	85.1%

The percentage of revenue from long-term contracts varies between periods depending on the volume of work performed under the Company's contracts. During the three and six months ended January 23, 2010, revenue from total long-term contracts increased compared to the comparable prior period as more work was performed for contracts with original terms greater than one year. Revenue during the three and six months ended January 24, 2009 included revenue for services performed under short-term contracts related to the hurricanes that impacted the Southern United States during September 2008.

28

Table of Contents

A significant portion of our revenue comes from several large customers. The following table reflects the percentage of total revenue from those customers who contributed at least 2.5% of our total revenue from continuing operations in the three or six month periods ended January 23, 2010 or January 24, 2009:

	For the Three Months Ended	
	January 23, 2010	January 24, 2009
AT&T, Inc.	19.8%	19.7%
Comcast Corporation	13.3%	15.4%
Verizon Communications, Inc.	12.5%	14.8%
CenturyLink (CenturyTel, Inc.)*	11.1%	6.2%
Time Warner Cable, Inc.	8.4%	8.2%
Charter Communications, Inc.	6.2%	4.7%
Windstream Corporation	3.2%	3.6%

	For the Six Months Ended	
	January 23, 2010	January 24, 2009
AT&T, Inc.	18.9%	17.4%
Comcast Corporation	14.6%	15.8%
Verizon Communications, Inc.	13.7%	17.4%
CenturyLink (CenturyTel, Inc.)*	9.6%	6.0%
Time Warner Cable, Inc.	8.5%	8.0%
Charter Communications, Inc.	5.8%	4.8%
Windstream Corporation	3.3%	3.4%
Qwest Communications International, Inc.	1.9%	2.6%

*For comparison purposes, CenturyTel, Inc. and Embarq Corporation revenues have been combined for periods prior to their July 2009 merger.

Cost of earned revenues includes all direct costs of providing services under our contracts, including costs for direct labor provided by employees, services by subcontractors, operation of capital equipment (excluding depreciation and amortization), and insurance claims and other related costs. We retain the risk of loss, up to certain limits, for claims related to automobile liability, general liability, workers' compensation, employee group health, and underground facility locate damages. Locate damage claims result from property and other damages arising in connection with services for our customers. A change in claims experience or actuarial assumptions related to these risks could materially affect our results of operations. For a majority of the contract services we perform, our customers provide all necessary materials and we provide the personnel, tools, and equipment necessary to perform installation and maintenance services. Materials supplied by our customers, for which the customer retains financial and performance risk, are not included in our revenue or costs of sales. In addition, cost of earned revenues for the six months ended January 23, 2010 includes a $2.0 million charge related to the pending settlement of a legal matter, see "Legal Proceedings" below.

General and administrative costs include all of our corporate costs, as well as costs of our subsidiaries' management personnel and administrative overhead. These costs primarily consist of employee compensation and related expenses, including stock-based compensation, legal and professional fees, information technology and development costs, provision for or recoveries of bad debt expense, and other costs that are not directly related to our services under customer contracts. Our senior management, including the senior managers of our subsidiaries, perform substantially all of our sales and marketing functions as part of their management responsibilities and, accordingly, we have not incurred material sales and marketing expenses. Information technology and development costs included in general and administrative expenses are primarily incurred to support and enhance our operating efficiency. To protect our rights, we have filed for patents on certain of our innovations. In December 2009, the United States Patent and Trademark Office granted our first patent as a result of these efforts.

We are subject to concentrations of credit risk relating primarily to our cash and equivalents, trade accounts receivable and costs and estimated earnings in excess of billings. Cash and equivalents primarily include balances on deposit in banks. We maintain substantially all of our cash and equivalents at financial institutions we believe to be of high credit quality. To date we have not experienced any loss or lack of access to cash in our operating accounts.

We grant credit under normal payment terms, generally without collateral, to our customers. These customers primarily consist of telephone companies, cable television multiple system operators and electric utilities. With respect to a portion of the services provided to these customers, we have certain statutory lien rights which may in certain circumstances enhance our collection efforts. Adverse changes in overall business and economic factors may impact our customers and increase potential credit risks. These risks may be heightened as a result of the current economic climate and market volatility. In the past, some of our customers have experienced significant financial difficulties and likewise, some may experience financial difficulties in the future. These difficulties expose us to increased risks related to the collectability of amounts due for services performed. We believe that none of our significant customers were experiencing financial difficulties that would impact the collectability of our trade accounts receivable and costs in excess of billings as of January 23, 2010.

Growth in economic activity slowed substantially beginning in fiscal 2009. The duration of the current economic weakness and the impact that it will have on our customers remain uncertain. The economic slowdown, when combined with developments in the financial and credit markets, has created a challenging business environment for us and our customers. We are closely monitoring the effects that changes in economic and market conditions may have on our customers and our business, including rising fuel costs, and we continue to manage the areas of the business that we can control. These areas include, but are not limited to, deploying appropriate workforce levels and supervisory employees, practicing sound safety procedures, managing fuel consumption levels and maintaining the investment in our fleet of vehicles and equipment to support current and future business opportunities.

Legal Proceedings

In May 2009, the Company and one of our subsidiaries were named as defendants in a lawsuit in the U.S. District Court for the Western District of Washington. The plaintiffs, former employees of the subsidiary, allege various wage and hour claims, including that employees were not paid for all hours worked and were subject to improper wage deductions. Plaintiffs seek to certify as a class current and former employees of the subsidiary who worked in the State of Washington. In November 2009, the plaintiffs' attorneys, the Company and the subsidiary entered into a memorandum of understanding pursuant to which the parties agreed to the terms of a proposed settlement with respect to the lawsuit. The proposed settlement provides for the resolution of all claims against us and the subsidiary in exchange for an aggregate payment of not more than $2.2 million. In January 2010, the Court granted preliminary approval of the proposed settlement. Notice of the terms of the proposed settlement and claim forms were mailed to members of the plaintiffs' class in February 2010. The settlement is contingent upon final Court approval. The Company has estimated the liability of this proposed settlement at $2.0 million and recorded a pre-tax charge for this amount during the first quarter of fiscal 2010. The actual amount of the settlement to be paid will depend on the number of class members that participate in the settlement, and could differ from the estimated amount.

From time to time, the Company and our subsidiaries are parties to various other claims and legal proceedings. Additionally, as part of our insurance program, we retain the risk of loss, up to certain limits, for claims related to automobile liability, general liability, workers' compensation, employee group health, and locate damages. For these claims, the effect on our financial statements is generally limited to the amount needed to satisfy our insurance deductibles or retentions. It is the opinion of management, based on information available at this time, that none of such other pending claims or proceedings will have a material effect on our condensed consolidated financial statements.

Acquisitions

As part of our growth strategy, we may acquire companies that expand, complement, or diversify our business. We regularly review opportunities and periodically engage in discussions regarding possible acquisitions. Our ability to sustain our growth and maintain our competitive position may be affected by our ability to identify, acquire, and successfully integrate companies.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based on our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these condensed consolidated financial statements requires management to make certain estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. On an ongoing basis, we evaluate these estimates and assumptions, including those related to recognition of revenue for costs and estimated earnings in excess of billings, the fair value of goodwill and intangible assets, income taxes, accrued insurance claims, asset lives used in determining depreciation and amortization, allowance for doubtful accounts, stock-based compensation expense for performance awards, and the outcome of contingencies,

Table of Contents

including legal matters. These estimates and assumptions require the use of judgment as to the likelihood of various future outcomes and, as a result, actual results could differ materially from these estimates. Please refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations-Critical Accounting Policies and Estimates" included in our Annual Report on Form 10-K for the year ended July 25, 2009 for further information regarding our critical accounting policies and estimates.

Results of Operations

The following table sets forth, as a percentage of revenues earned, our condensed consolidated statements of operations for the periods indicated (totals may not add due to rounding):

	For the Three Months Ended			
	January 23, 2010		January 24, 2009	
	(Dollars in millions)			
Revenues	$216.3	100.0 %	$245.5	100.0 %
Expenses:				
Cost of earned revenue, excluding depreciation and amortization	180.9	83.6	205.9	83.8
General and administrative	23.9	11.0	21.5	8.8
Depreciation and amortization	15.5	7.2	16.8	6.8
Goodwill impairment charge	-	-	94.4	38.5
Total	220.4	101.9	338.6	137.9
Interest income	-	-	-	-
Interest expense	(3.5)	(1.6)	(4.1)	(1.7)
Other income, net	0.9	0.4	1.8	0.7
Loss from continuing operations before income taxes	(6.6)	(3.1)	(95.3)	(38.8)
Benefit for income taxes	(2.7)	(1.2)	(17.4)	(7.1)
Loss from continuing operations	(4.0)	(1.8)	(78.0)	(31.7)
Loss from discontinued operations, net of tax	-	-	-	-
Net loss	$(4.0)	(1.8)%	$(78.0)	(31.7)%

	For the Six Months Ended			
	January 23, 2010		January 24, 2009	
	(Dollars in millions)			
Revenues	$475.4	100.0 %	$579.5	100.0 %
Expenses:				
Cost of earned revenue, excluding depreciation and amortization	390.9	82.2	474.5	81.9
General and administrative	47.4	10.0	49.1	8.5
Depreciation and amortization	30.7	6.5	33.4	5.8
Goodwill impairment charge	-	-	94.4	16.3
Total	469.0	98.7	651.4	112.4
Interest income	0.1	0.0	0.2	0.0
Interest expense	(7.1)	(1.5)	(8.2)	(1.4)
Other income, net	2.0	0.4	2.2	0.4
Income (loss) from continuing operations before income taxes	1.4	0.3	(77.7)	(13.4)

Provision (benefit) for income taxes	1.9	0.4	(10.3)	(1.8)
Loss from continuing operations	(0.4)	(0.1)	(67.4)	(11.6)
Loss from discontinued operations, net of tax	-	-	-	-
Net loss	$(0.4)	(0.1)%	$(67.4)	(11.6)%

31

Revenues. The following table presents information regarding total revenues by type of customer for the three months ended January 23, 2010 and January 24, 2009 (totals may not add due to rounding):

	For the Three Months Ended					
	January 23, 2010		January 24, 2009			
	Revenue	% of Total	Revenue	% of Total	Decrease	Decrease
	(Dollars in millions)					
Telecommunications	$ 173.7	80.3 %	$ 191.3	77.9 %	$ (17.6)	(9.2)%
Underground facility locating	37.3	17.3 %	39.7	16.2 %	(2.3)	(5.9)%
Electric utilities and other customers	5.3	2.4 %	14.6	5.9 %	(9.3)	(63.7)%
Total contract revenues	$ 216.3	100.0 %	$ 245.5	100.0 %	$ (29.2)	(11.9)%

Revenues decreased $29.2 million, or 11.9%, during the three months ended January 23, 2010 as compared to the three months ended January 24, 2009. The decrease was the result of a $17.6 million decrease in specialty contracting services provided to telecommunications customers, a $9.3 million decrease in revenues from construction and maintenance services provided to electric utilities and other customers, and a $2.3 million decrease in underground facility locating services revenue.

Specialty construction services provided to telecommunications companies were $173.7 million during the three months ended January 23, 2010, compared to $191.3 million during the three months ended January 24, 2009, a decrease of 9.2%. We experienced decreases from significant customers as a result of their reductions in spending, including a $10.1 million decrease for a customer engaged in a fiber deployment project, a $9.9 million net decrease for installation, maintenance and construction services provided to leading cable multiple system operators, and a $3.1 million decline in work performed for two significant telephone customers. Additionally, during the three months ended January 24, 2009, we performed restoration services totaling $3.2 million related to the hurricanes that impacted the Southern United States. There were no services for storm work during the quarter ended January 23, 2010. Partially offsetting these decreases was a $8.7 million increase in services to a significant telephone customer that merged with another telephone customer in July 2009. Net revenues from remaining customers were consistent during each period.

Total revenues from underground facility locating during the three months ended January 23, 2010 were $37.3 million compared to $39.7 million during the three months ended January 24, 2009, a decrease of 5.9%. The decrease resulted from declines in customer demand levels as general economic weakness continued during the current period resulting in a lower level of construction activity.

Our total revenues from electric utilities and other construction and maintenance services decreased $9.3 million, or 63.7%, during the three months ended January 23, 2010 as compared to the three months ended January 24, 2009. The decrease was primarily attributable to a decline in construction work performed for gas customers, including a gas pipeline project for a customer that was completed during fiscal 2009.

Table of Contents

The following table presents information regarding total revenues by type of customer for the six months ended January 23, 2010 and January 24, 2009 (totals may not add due to rounding):

	For the Six Months Ended					
	January 23, 2010		January 24, 2009			
	Revenue	% of Total	Revenue	% of Total	Decrease	Decrease
	(Dollars in millions)					
Telecommunications	$ 378.6	79.6 %	$ 454.5	78.4 %	$ (75.9)	(16.7)%
Underground facility locating	84.3	17.7 %	91.2	15.7 %	(6.9)	(7.6)%
Electric utilities and other customers	12.6	2.7 %	33.8	5.9 %	(21.2)	(62.8)%
Total contract revenues	$ 475.4	100.0 %	$ 579.5	100.0 %	$ (104.0)	(18.0)%

Revenues decreased $104.0 million, or 18.0%, during the six months ended January 23, 2010 as compared to the six months ended January 24, 2009. The decrease was the result of a $75.9 million decrease in specialty contracting services provided to telecommunications customers, a $21.2 million decrease in revenues from construction and maintenance services provided to electric utilities and other customers, and a $6.9 million decrease in underground facility locating services revenue.

Specialty construction services provided to telecommunications companies were $378.6 million during the six months ended January 23, 2010, compared to $454.5 million during the six months ended January 24, 2009, a decrease of 16.7%. During the six months ended January 24, 2009, we performed restoration services totaling $17.1 million related to the hurricanes that impacted the Southern United States. There were no services for storm work during fiscal 2010. We also experienced other decreases from significant customers as a result of their reductions in spending, including a $37.7 million decrease for a customer engaged in a fiber deployment project, a $17.2 million net decrease for installation, maintenance and construction services provided to leading cable multiple system operators, and a $8.9 million decline in work performed for two significant telephone customers. Other customers had net decreases of $5.9 million during the six months ended January 23, 2010 as compared to the six months ended January 24, 2009. Partially offsetting these decreases was a $10.9 million increase in services to a significant telephone customer that merged with another telephone customer in July 2009.

Total revenues from underground facility locating during the six months ended January 23, 2010 were $84.3 million compared to $91.2 million during the six months ended January 24, 2009, a decrease of 7.6%. The decrease resulted from declines in customer demand levels as general economic weakness continued during the six month period. Additionally, the six months ended January 24, 2009 included $0.9 million of restoration work related to the hurricanes that impacted the Southern United States compared to none during 2010.

Our total revenues from electric utilities and other construction and maintenance services decreased $21.2 million, or 62.8%, during the six months ended January 23, 2010 as compared to the six months ended January 24, 2009. The decrease was primarily attributable to a decline in construction work performed for gas customers, including gas pipeline projects for two customers that were completed during fiscal 2009. Additionally, the six months ended January 24, 2009 included $0.4 million of restoration work related to the hurricanes that impacted the Southern United States compared to none during 2010.

Costs of Earned Revenues. Costs of earned revenues decreased $25.0 million to $180.9 million for the three months ended January 23, 2010 compared to $205.9 million for the three months ended January 24, 2009. The primary components of the decrease in cost of earned revenues were direct labor and subcontractor costs taken together, other direct costs, and direct materials, which decreased $18.5 million, $4.5 million, and $1.9 million, respectively. The decrease in costs of earned revenues was primarily due to lower levels of operations during the three months ended January 23, 2010 as compared to the period ended January 24, 2009.

Costs of earned revenues as a percentage of contract revenues decreased 0.2% for the three months ended January 23, 2010 as compared to the three months ended January 24, 2009. Other direct costs decreased 0.8% as a percentage of contract revenues, primarily from reduced costs related to insurance claims and from lower equipment costs. We also experienced a 0.1% decrease in direct materials as a percentage of contract revenues. Offsetting these decreases, fuel costs increased 0.75% as a percentage of contract revenues as compared to the same period last year primarily due to increases in the price of gasoline and diesel fuel. Labor and subcontractor costs remained consistent as a percentage of contract revenues during the three months ended January 23, 2010 and January 24, 2009.

33

Costs of earned revenues decreased $83.6 million to $390.9 million for the six months ended January 23, 2010 compared to $474.5 million for the six months ended January 24, 2009. Included in costs of earned revenues for the six months ended January 23, 2010 is a $2.0 million charge recorded in the first quarter of fiscal 2010 in connection with the pending settlement of a legal matter described under “Legal Proceedings” above. The primary components of the remaining $85.6 million net decrease in costs of earned revenues were direct labor and subcontractor costs taken together, other direct costs, and direct materials, which decreased $64.4 million, $15.8 million, and $5.4 million, respectively. The decrease in costs of earned revenues was primarily due to lower levels of operations during the six months ended January 23, 2010 as compared to the six month period ended January 24, 2009.

Costs of earned revenues as a percentage of contract revenues increased 0.3% for the six months ended January 23, 2010 as compared to the same period last year due in part to the $2.0 million charge related to the pending legal settlement referred to above, or 0.4% of contract revenues. Excluding this legal settlement charge, costs of earned revenues as a percentage of contract revenues decreased 0.1% for the six months ended January 23, 2010 as compared to the six months ended January 24, 2009. Fuel costs decreased 0.2% as a percentage of contract revenues as compared to the same period last year primarily due to declines in the price of gasoline and diesel fuel during the first quarter of fiscal 2010. Offsetting this decrease was an increase in other direct costs of 0.1% as a percentage of contract revenues, primarily from lower absorption of costs for support and field offices in relation to reduced operating levels during the current year period. Labor and subcontractor costs and direct materials as a percentage of contract revenues was consistent for the six months ended January 23, 2010 and January 24, 2009.

General and Administrative Expenses. General and administrative expenses increased $2.4 million to $23.9 million during the three months ended January 23, 2010 as compared to $21.5 million for the three months ended January 24, 2009. The change resulted from increased payroll costs, higher incentive compensation for subsidiaries that outperformed the prior year results, and higher legal and software-related costs. Additionally, stock-based compensation expense increased to $0.7 million during the three months ended January 23, 2010 from $0.3 million during the three months ended January 24, 2009. General and administrative expenses decreased $1.7 million to $47.4 million during the six months ended January 23, 2010 as compared to $49.1 million for the six months ended January 24, 2009. The decrease in total general and administrative expenses for the six months ended January 23, 2010 compared to the prior year period resulted from a reduction of payroll and incentive pay expense due to lower operating levels and reduced legal and professional fees and other expenses. Additionally, stock-based compensation expense decreased to $1.7 million during the six months ended January 23, 2010 from $1.9 million during the six months ended January 24, 2009.

General and administrative expenses as a percentage of contract revenues were 11.0% and 8.8% for the three months ended January 23, 2010 and January 24, 2009, respectively. General and administrative expenses as a percentage of contract revenues were 10.0% and 8.5% for the six months ended January 23, 2010 and January 24, 2009, respectively. The increase in general and administrative expenses as a percentage of contract revenues for the three and six months ended January 23, 2010 as compared to the same periods in fiscal 2009 reflects lower absorption of a portion of our expenses, such as certain office and support costs and certain payroll costs, as a result of lower revenues.

Depreciation and Amortization. Depreciation and amortization decreased to $15.5 million during the three months ended January 23, 2010 from $16.8 million during the three months ended January 24, 2009 and increased as a percentage of contract revenues to 7.2% compared to 6.8% from the same period in the prior year. For the six months ended January 23, 2010, depreciation and amortization decreased to $30.7 million from $33.4 million during the six months ended January 24, 2009 and increased as a percentage of contract revenues to 6.5% compared to 5.8% from the six months ended January 24, 2009. The decrease in amount was primarily a result of certain assets becoming fully depreciated or sold during fiscal 2009 and fiscal 2010. Amortization expense also decreased during the three and six months ended January 23, 2010 as compared to the prior year periods. This reduction related to customer relationship intangible assets of certain prior acquisitions that became fully amortized.

Goodwill Impairment Charge. During the second quarter of fiscal 2009, we recognized a goodwill impairment charge of $94.4 million that included impairments at the following reporting units: Broadband Installation Services for $14.8 million, C-2 Utility Contractors for $9.2 million, Ervin Cable Construction for $15.7 million, Nichols Communications for $2.0 million, Stevens Communications for $2.4 million and UtiliQuest for $50.5 million. This charge was the result of an interim test for impairment reflecting valuation assumptions as of the end of our second quarter of fiscal 2009. Our interim analysis was finalized in the third quarter of fiscal 2009 and no further charges were incurred during the fiscal year.

Table of Contents

We continually monitor the economic environment and the impact on our reporting units and market capitalization. When determining the fair value of our reporting units, we estimate a premium associated with the control of such reporting unit. The premium is market based and we believe it is reasonable based on the industry in which we operate. We do not believe that conditions presently exist which would require testing goodwill or intangible assets for impairment in advance of the tests we perform annually in the fourth fiscal quarter of each year. However, future adverse changes in general economic and market conditions and future volatility in the equity and credit markets could trigger an impairment test and impact the valuation of our reporting units.

Interest Income and Expense. Interest income was less than $0.1 million during each of the three months ended January 23, 2010 and January 24, 2009. Interest income decreased to less than $0.1 million during the six months ended January 23, 2010 as compared to $0.2 million during the six months ended January 24, 2009. The decrease for the six months ended January 23, 2010 is the result of lower interest yield earned on cash balances during the periods.

Interest expense was $3.5 million during the three months ended January 23, 2010 as compared to $4.1 million during the three months ended January 24, 2009. Interest expense decreased to $7.1 million during the six months ended January 23, 2010 as compared to $8.2 million during the six months ended January 24, 2009. The decrease for the three and six month periods ended January 23, 2010 reflects reduced interest expense on our 8.125% senior subordinated notes (“Notes”) as a result of the buyback of $14.65 million principal amount of the Notes during fiscal 2009 and reduced balances for letters of credit. Additionally, we had no borrowings under our revolving credit agreement ("Credit Agreement") during 2010 compared to $30.0 million which was borrowed and repaid during 2009.

Other Income, Net. Other income decreased to $0.9 million during the three months ended January 23, 2010 from $1.8 million during the three months ended January 24, 2009, and decreased to $2.0 million during the six months ended January 23, 2010 from $2.2 million during the six months ended January 24, 2009. During the three and six months ended January 24, 2009 other income included a gain of $1.3 million on extinguishment of debt related to the buyback of $4.65 million principal amount of Notes during the second quarter of fiscal 2009. Additionally, other income for the six months ended January 24, 2009 includes a charge of $0.6 million for the write-off of deferred financing costs when we replaced our existing credit agreement during the first quarter of fiscal 2009.

Income Taxes. The following table presents our income tax expense and effective income tax rate for continuing operations during the three and six months ended January 23, 2010 and January 24, 2009:

	For the Three Months Ended		For the Six Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
	(dollars in millions)			
Income tax provision (benefit)	$ (2.7)	$ (17.4)	$ 1.9	$ (10.3)
Effective income tax rate	40.2 %	18.2 %	131.3 %	13.3 %

Our effective income tax rate differs from the statutory rate for the tax jurisdictions where we operate as a result of several factors. In the first quarter of fiscal 2010, we recognized a non-cash income tax charge of $1.1 million for a valuation allowance on a deferred tax asset associated with an investment that became impaired for tax purposes. During the second quarter of fiscal 2009, we incurred a non-cash goodwill impairment charge of $94.4 million, of which only $17.4 million was deductible for income tax purposes. Other variations in our tax rate for the three and six months ended January 23, 2010 and January 24, 2009 are attributable to the impact of non-deductible and non-taxable items in relation to our pre-tax results during the period. As of January 23, 2010, we had total unrecognized tax benefits of approximately $2.9 million, which would reduce the Company's effective tax rate during the periods recognized if it is subsequently determined that those liabilities are not required.

Loss from Continuing Operations. Loss from continuing operations was $4.0 million during the three months ended January 23, 2010 as compared to $78.0 million during the three months ended January 24, 2009. Loss from continuing operations was $0.4 million during the six months ended January 23, 2010 as compared to $67.4 million during the six months ended January 24, 2009.

Table of Contents

Discontinued Operations. During fiscal 2007, a wholly-owned subsidiary of the Company, Apex Digital, LLC ("Apex") notified its primary customer of its intention to cease performing installation services in accordance with its contractual rights. Effective December 2006, this customer, a satellite broadcast provider, transitioned its installation service requirements to others and Apex ceased providing these services. As a result, we discontinued the operations of Apex. Apex did not have material operations in fiscal 2009 or 2010.

Net Loss. Net loss was $4.0 million during the three months ended January 23, 2010 as compared to $78.0 million during the three months ended January 24, 2009. Net loss was $0.4 million during the six months ended January 23, 2010 as compared to $67.4 million during the six months ended January 24, 2009.

Liquidity and Capital Resources

Capital requirements. Historically, our sources of cash have been operating activities, long-term debt, equity offerings, bank borrowings, and proceeds from the sale of idle and surplus equipment and real property. Our working capital needs vary based upon our level of operations and generally increase with higher levels of revenues. They are also impacted by the time it takes us to collect our accounts receivable for work performed for customers. Cash and cash equivalents totaled $135.9 million at January 23, 2010 compared to $104.7 million at July 25, 2009. Cash increased for the six months ended January 23, 2010 as a result of cash collected from operations offset by capital expenditures. Working capital (total current assets less total current liabilities) increased by $3.6 million to $220.8 million at January 23, 2010 compared to $217.2 million at July 25, 2009.

Capital resources are primarily used to purchase equipment and maintain sufficient levels of working capital in order to support our contractual commitments to customers. We periodically borrow from and repay our Credit Agreement based on our cash requirements. Additionally, to the extent we make acquisitions that involve consideration other than our stock, buyback our common stock or repurchase or call our senior subordinated notes, our capital requirements may increase. In the normal course of business, we may hedge our anticipated fuel purchases with the use of financial instruments. For the six months ended January 23, 2010, we were not party to any such financial instruments. We believe that none of our major customers are experiencing significant financial difficulty as of January 23, 2010 that will materially affect our cash flows or liquidity.

	For the Six Months Ended	
	January 23, 2010	January 24, 2009
	(Dollars in millions)	
Net cash flows:		
Provided by operating activities	$56.9	$75.2
Used in investing activities	$(24.7)	$(16.7)
Used in financing activities	$(0.9)	$(6.5)

Cash from operating activities. During the six months ended January 23, 2010, net cash provided by operating activities was $56.9 million. Non-cash items during the six months ended January 23, 2010 were primarily depreciation and amortization, gain on disposal of assets, stock-based compensation, and deferred income taxes. Changes in working capital (excluding cash) and changes in other long term assets and liabilities contributed $23.9 million of operating cash flow during the six months ended January 23, 2010. The primary working capital sources during the six months ended January 23, 2010 were decreases in accounts receivable and net costs and estimated earnings in excess of billings of $24.8 million and $24.5 million, respectively. During the three months ended January

23, 2010, the timing of our billing and the collection activity improved compared to the prior year period. Based on average daily revenue during the applicable quarter, days sales outstanding calculated for accounts receivable, net was 38.2 days as of January 23, 2010 compared to 42.7 days as of January 24, 2009. Days sales outstanding calculated for costs and estimated earnings in excess of billings, net of billings in excess of costs and estimated earnings, were 17.9 days as of January 23, 2010 compared to 21.4 days as of January 24, 2009.

Working capital changes that used operating cash flow during the six months ended January 23, 2010 were decreases in other accrued liabilities and accrued insurance claims of $11.6 million due to the reduced level of operations during the quarter ended January 23, 2010. Offsetting these decreases was a $2.0 million increase in other accrued liabilities related to the proposed settlement of the legal matter described in “Legal Proceedings” above. Other working capital changes that used operating cash flow during the six months ended January 23, 2010 were net increases in other current and other non-current assets of $8.2 million primarily for prepaid insurance and other prepaid costs that were incurred near the beginning of our fiscal year. Additionally, accounts payable decreased $5.4 million during the six months ended January 23, 2010 due to the timing of receipt and payment of invoices and an increase in income taxes receivable, net of $2.2 million due to the timing of applicable tax payments.

Table of Contents

For the six months ended January 24, 2009, changes in working capital and changes in other long term assets and liabilities contributed $26.7 million of operating cash flow. Working capital changes that contributed operating cash flow during the six months ended January 24, 2009 included decreases in accounts receivable and net costs and estimated earnings in excess of billings of $31.3 million and $36.1 million, respectively. Other working capital changes that used operating cash flow during the six months ended January 24, 2009 were decreases in other liabilities of $23.0 million primarily attributable to payments of approximately $8.6 million in connection with a wage and hour class action settlement in fiscal 2009, payments for fiscal 2008 incentive pay, and overall decreases in other accrued liabilities due to the reduced level of operations during the latter part of the quarter ended January 24, 2009. Additionally, there were decreases in accounts payable of $7.1 million during the six months ended January 24, 2009 due to the timing of the receipt and payment of invoices and an increase in income taxes receivable of $4.9 million due to the timing of applicable tax payments. We had net increases in other current and other non-current assets of $5.6 million during the six months ended January 24, 2009 primarily as a result of increased prepaid insurance and other prepaid costs.

Cash used in investing activities. For the six months ended January 23, 2010 and January 24, 2009, net cash used in investing activities was $24.7 million and $16.7 million, respectively. Capital expenditures of $27.3 million and $18.3 million during the six months ended January 23, 2010 and January 24, 2009, respectively, were offset in part by proceeds from the sale of assets of $2.5 million and $1.8 million, respectively. Capital expenditures increased during the six months ended January 23, 2010 as compared to the prior period due to the replacement cycle of our assets and for new work opportunities. Restricted cash, primarily related to funding provisions of our insurance claims program, increased $0.2 million during the six months ended January 24, 2009.

Cash used in financing activities. For the six months ended January 23, 2010, net cash used in financing activities was $0.9 million as compared to $6.5 million for the six months ended January 24, 2009. During the six months ended January 23, 2010, we paid $0.7 million for principal payments on capital leases compared to $1.3 million for the six months ended January 24, 2009. During the six months ended January 24, 2009 we borrowed and repaid $30 million under our Credit Agreement and paid $1.8 million in debt issuance costs related to entering into the Credit Agreement in September 2008. In addition, we purchased $4.65 million principal amount of Notes during the six months ended January 24, 2009 for $3.2 million.

During the six months ended January 23, 2010 and January 24, 2009, we withheld shares of restricted units and paid $0.3 million and $0.2 million, respectively, to tax authorities in order to meet payroll tax withholdings obligations on restricted units that vested to certain officers and employees during those periods. Additionally, during the six months ended January 23, 2010, we received excess tax benefits of $0.1 million from the vesting of restricted stock units.

Compliance with Notes and Credit Agreement

The indenture governing the Notes contains covenants that restrict our ability to, among other things:

- make certain payments, including the payment of dividends;
- redeem or repurchase our capital stock;
- incur additional indebtedness and issue preferred stock;
- make investments or create liens;
- enter into sale and leaseback transactions;
- merge or consolidate with another entity;

- sell certain assets; and
- enter into transactions with affiliates.

As of January 23, 2010, the principal amount outstanding under the Notes was $135.35 million and we were in compliance with the covenants and conditions under the indenture governing the Notes.

Table of Contents

The Company's $210.0 million Credit Agreement, which expires in September 2011, contains certain affirmative and negative covenants, including limitations with respect to indebtedness, liens, investments, distributions, mergers and acquisitions, disposition of assets, sale-leaseback transactions and transactions with affiliates. It also contains defined financial covenants which require us to (i) maintain a leverage ratio of not greater than 3.00 to 1.00, as measured at the end of each fiscal quarter, (ii) maintain an interest coverage ratio of not less than 2.75 to 1.00, as measured at the end of each fiscal quarter and (iii) maintain consolidated total tangible net worth, as measured at the end of each fiscal quarter, of not less than $50.0 million plus (A) 50% of consolidated net income (if positive) from September 12, 2008 to the date of computation plus (B) 75% of equity issuances made from September 12, 2008 to the date of computation. The Credit Agreement has a sublimit of $100.0 million for the issuance of letters of credit. As of January 23, 2010, we had no outstanding borrowings and $43.9 million of outstanding letters of credit issued under the Credit Agreement. The outstanding letters of credit are issued as part of our insurance program. At January 23, 2010, we had additional borrowing availability of up to $153.4 million, as determined by the most restrictive covenants of the Credit Agreement, and were in compliance with the financial covenants.

Contractual Obligations. The following tables set forth our outstanding contractual obligations, including related party leases, as of January 23, 2010:

	Less than 1 Year	Years 1-3	Years 3 - 5	Greater than 5 Years	Total
			(Dollars in thousands)		
Notes	$-	$-	$-	$135,350	$135,350
Interest payments on debt (excluding capital leases)	10,997	21,994	21,994	10,998	65,983
Capital lease obligations (including interest and executory costs)	432	-	-	-	432
Operating leases	8,212	9,474	5,301	4,892	27,879
Employment agreements	2,645	2,639	-	-	5,284
Purchase and other contractual obligations	2,264	-	-	-	2,264
Total	$24,550	$34,107	$27,295	$151,240	$237,192

Our condensed consolidated balance sheet as of January 23, 2010 includes a long term liability of approximately $29.5 million for Accrued Insurance Claims. This liability has been excluded from the above table as the timing of any cash payments is uncertain. See Note 7 of the notes to our condensed consolidated financial statements for additional information regarding our accrued insurance claims liability.

The liability for unrecognized tax benefits for uncertain tax positions at January 23, 2010 was $2.9 million and is included in other liabilities in our condensed consolidated balance sheet. This entire amount has been excluded from the contractual obligations table because we are unable to reasonably estimate the timing of the resolutions of the underlying tax positions with the relevant tax authorities.

Off-Balance Sheet Arrangements. We have obligations under performance bonds related to certain of our customer contracts. Performance bonds generally provide a customer with the right to obtain payment and/or performance from the issuer of the bond if we fail to perform our obligations under a contract. As of January 23, 2010, we had $35.5 million of outstanding performance bonds and no events have occurred in which customers have exercised their rights under the performance bonds.

Sufficiency of Capital Resources. We believe that our capital resources, including existing cash balances and amounts available under our Credit Agreement, are sufficient to meet our financial obligations. These obligations include interest payments required on our Notes and borrowings, working capital requirements, and the normal replacement of equipment at our current level of operations for at least the next twelve months. Our future operating results and cash flows may be affected by a number of factors including our success in bidding on future contracts and our ability to manage costs effectively. To the extent we seek to grow by acquisitions that involve consideration other than our stock, or to the extent we buyback our common stock or repurchase or call our senior subordinated notes, our capital requirements may increase.

Although the distress in the financial markets has not significantly impacted our financial position or our cash flow as of and for the six month period ending January 23, 2010, management continues to monitor the financial markets and assess general economic conditions. If further changes in financial markets or other areas of the economy adversely impact our ability to access capital markets,

38

Table of Contents

we would expect to rely on a combination of available cash and the existing committed credit facility to provide short-term funding. We believe that our cash investment policies are conservative and we expect that the current volatility in the capital markets will not have a material impact on our cash investments.

Backlog. Our backlog consists of the uncompleted portion of services to be performed under job-specific contracts and the estimated value of future services that we expect to provide under master service agreements and other long-term requirements contracts. Many of our contracts are multi-year agreements, and we include in our backlog the amount of services projected to be performed over the terms of the contracts based on our historical experience with customers and, more generally our experience in procurements of this type. In many instances, our customers are not contractually committed to procure specific volumes of services under a contract. Our estimates of a customer’s requirements during a particular future period may not prove to be accurate, particularly in light of the current economic conditions and the uncertainty that imposes on changes in our customer’s requirements for our services.

Our backlog totaled $1.078 billion and $935.4 million at January 23, 2010 and July 25, 2009, respectively. We expect to complete 63.4% of the January 23, 2010 backlog during the next twelve months.

Seasonality and Quarterly Fluctuations

Our revenues are affected by seasonality as a significant portion of the work we perform is outdoors. Consequently, our operations are impacted by extended periods of inclement weather. Generally, inclement weather is more likely to occur during the winter season which falls during our second and third fiscal quarters. Also, a disproportionate percentage of total paid holidays fall within our second quarter, which decreases the number of available workdays. Additionally, our customer premise equipment installation activities for cable providers historically decrease around calendar year end holidays as their customers generally require less activity during this period.

In addition, we have experienced and expect to continue to experience quarterly variations in revenues and net income as a result of other factors, including:

- the timing and volume of customers’ construction and maintenance projects;
- seasonal budgetary spending patterns of customers and the timing of budget approvals;
- the commencement or termination of master service agreements and other long-term agreements with customers;
- costs incurred to support growth internally or through acquisitions;
- fluctuations in results of operations caused by acquisitions;
- fluctuation in the employer portion of payroll taxes as a result of reaching the limitation on social security withholdings and unemployment obligations;
- changes in mix of customers, contracts, and business activities;
- fluctuations in insurance expense due to changes in claims experience and actuarial assumptions;
- fluctuations in stock-based compensation expense as a result of performance criteria in performance-based share awards, as well as the timing and vesting period of all stock-based awards;
- fluctuations in performance cash awards as a result of operating results;
- fluctuations in interest expense due to levels of debt and related borrowing costs;
- fluctuations in other income as a result of the timing and levels of capital assets sold during the period, and
- fluctuations in income tax expense due to levels of taxable earnings.

Accordingly, operating results for any fiscal period are not necessarily indicative of results that may be achieved for any subsequent fiscal period.

39

Table of Contents

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risks related to interest rates on our cash and equivalents and our debt obligations. We monitor the effects of market changes on interest rates and manage interest rate risks by investing in short-term cash equivalents with market rates of interest and by maintaining a mix of fixed and variable rate debt. A hypothetical 100 basis point increase in interest rates would result in an increase to annual earnings of approximately $1.4 million if our cash and equivalents held as of January 23, 2010 were to be fully invested in interest bearing financial instruments.

Our revolving credit facility permits borrowings at a variable rate of interest; however, we had no outstanding borrowings as of January 23, 2010. Outstanding long-term debt at January 23, 2010 included $135.35 million of our senior subordinated notes due in 2015 (“Notes”), which bear a fixed rate of interest of 8.125%. Due to the fixed rate of interest on the Notes, changes in interest rates would not have an impact on the related interest expense. The fair value of the outstanding Notes totaled approximately $125.4 million as of January 23, 2010, based on quoted market prices. There exists market risk sensitivity on the fair value of the fixed rate Notes with respect to changes in interest rates. A hypothetical 50 basis point change in the market interest rates in effect would result in an increase or decrease in the fair value of the Notes of approximately $3.2 million, calculated on a discounted cash flow basis.

We had $0.3 million of capital leases outstanding at January 23, 2010 with varying rates of interest due through fiscal 2011 under separate lease agreements. A hypothetical 100 basis point change in interest rates in effect at January 23, 2010 on these capital leases would not have a material impact on the fair value of the leases or on our annual interest cost.

We also have market risk for foreign currency exchange rates related to our operations in Canada. As of January 23, 2010, the market risk for foreign currency exchange rates was not significant as our operations in Canada have not been material.

Item 4. Controls and Procedures

The Company, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of the Company’s disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this report on Form 10-Q. Based on that evaluation, our Chief Executive Officer and our Chief Financial Officer each concluded that the Company’s disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and (2) accumulated and communicated to the Company’s management, including our Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosure.

There were no changes in the Company’s internal control over financial reporting that occurred during the Company’s most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In May 2009, the Company and one of our subsidiaries were named as defendants in a lawsuit in the U.S. District Court for the Western District of Washington. The plaintiffs, former employees of the subsidiary, allege various wage and hour claims, including that employees were not paid for all hours worked and were subject to improper wage deductions. Plaintiffs seek to certify as a class current and former employees of the subsidiary who worked in the State of Washington. In November 2009, the plaintiffs' attorneys, the Company and the subsidiary entered into a memorandum of understanding pursuant to which the parties agreed to the terms of a proposed settlement with respect to the lawsuit. The proposed settlement provides for the resolution of all claims against the Company and the subsidiary in exchange for an aggregate payment of not more than $2.2 million. In January 2010, the Court granted preliminary approval of the proposed settlement. Notice of the terms of the proposed settlement and claim forms were mailed to members of the plaintiffs' class in February 2010. The settlement is contingent upon final Court approval. The Company has estimated the liability of this proposed settlement at $2.0 million and recorded a pre-tax charge for this amount during the first quarter of fiscal 2010. The actual amount of the settlement to be paid will depend on the number of class members that participate in the settlement, and could differ from the estimated amount.

From time to time, the Company and its subsidiaries are parties to various other claims and legal proceedings. Additionally, as part of our insurance program, we retain the risk of loss, up to certain limits, for claims related to automobile liability, general liability, workers' compensation, employee group health, and locate damages. For these claims, the effect on our financial statements is generally limited to the amount needed to satisfy our insurance deductibles or retentions. It is the opinion of management, based on information available at this time, that none of such other pending claims or proceedings will have a material effect on our consolidated financial statements.

Item 1A. Risk Factors

There have been no material changes from the risk factors disclosed in our fiscal 2009 Form 10-K under the heading "Risk Factors" in Part I, Item 1A of Form 10-K.

Table of Contents

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

(a) During the six months ended January 23, 2010, we did not sell any of our equity securities that were not registered under the Securities Act of 1933.

(b) Not applicable.

(c) The following table summarizes the Company’s purchases of its common stock:

ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased		Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
October 25, 2009 - November 21, 2009	-		$-	-	(b)
November 22, 2009 - December 19, 2009	28,726	(a)	$8.37	-	(b)
December 20, 2009 - January 23, 2010	-		$-	-	(b)

(a) Shares were withheld to satisfy tax withholding obligations that arose on the vesting of restricted stock units.

(b) On February 23, 2010, the Company’s Board of Directors authorized the repurchase of up to $20.0 million of its common stock to be made over the next eighteen months in open market or private transactions. This repurchase program replaces the Company’s existing program, scheduled to expire in February 2010, under which there was a remaining authorization of $16.9 million.

Item 4. Submission of Matters to a Vote of Security Holders

An annual meeting of shareholders of the Company was held on November 24, 2009 to consider and take action on the election of three directors and to ratify the appointment of Deloitte & Touche LLP as the Company’s independent auditor for fiscal 2010. The Company’s nominee, Stephen C. Coley, was elected as a director of the Company. Mr. Coley received 33,537,532 votes for and 2,561,558 votes withheld. The Company’s nominee, Patricia L. Higgins, was elected a director of the Company. Ms. Higgins received 20,430,364 votes for and 15,668,726 votes withheld. The Company’s nominee, Steven E. Nielsen, was elected as a director of the Company. Mr. Nielsen received 32,873,531 votes for and 3,225,559 votes withheld. Each of the following directors’ term of office as a director of the Company continued after the annual meeting: Thomas G. Baxter, Charles M. Brennan III, James A. Chiddix, and Charles B. Coe. The proposal to ratify the appointment of Deloitte & Touche LLP as the Company’s independent auditor for fiscal 2010 was approved with 35,616,092 votes for, 472,932 against, and 10,066 abstaining.

42

Table of Contents

Item 6. Exhibits

Exhibits furnished pursuant to the requirements of Form 10-Q:

Exhibit number	
10.1 +	Credit Agreement and related Schedules, dated September 12, 2008, by and among Dycom Industries, Inc. and the Wachovia Bank, National Association, as Administrative Agent for the Lenders and Bank of America, N.A., as Syndication Agent.
10.2 +	First Amendment and related Schedule, dated as of April 10, 2009, to Credit Agreement dated as of September 12, 2008 with Wachovia Bank, National Association, as Administrative Agent, Bank of America, N.A., as Syndication Agent.
11	Statement re computation of per share earnings; All information required by Exhibit 11 is presented within Note 2 of the Company's condensed consolidated financial statements in accordance with the provisions of ASC 260, Earnings Per Share.
31.1+	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2+	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1+	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2+	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

+ Filed herewith

Table of Contents

SIGNATURES

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

DYCOM INDUSTRIES, INC.
Registrant

Date:	February 26, 2010	/s/ Steven E. Nielsen Name: Steven E. Nielsen Title: President and Chief Executive Officer
Date:	February 26, 2010	/s/ H. Andrew DeFerrari Name: H. Andrew DeFerrari Title: Senior Vice President and Chief Financial Officer

44