LANCASTER COLONY CORP
Form 10-Q
February 07, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

Form 10-Q

(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 31, 2016
or
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number 000-04065

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

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

614-224-7141
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨

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

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

Large Accelerated filer	ý	Accelerated filer	¨
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller Reporting Company	¨

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

As of January 19, 2017, there were 27,431,138 shares of Common Stock, without par value, outstanding.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
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PART I – FINANCIAL INFORMATION

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

(Amounts in thousands, except share data)	December 31, 2016	June 30, 2016
ASSETS		
Current Assets:		
Cash and equivalents	$118,507	$118,080
Receivables (less allowance for doubtful accounts, December-$31; June-$125)	71,438	66,006
Inventories:		
Raw materials	32,160	26,153
Finished goods	47,955	49,944
Total inventories	80,115	76,097
Other current assets	6,899	7,644
Total current assets	276,959	267,827
Property, Plant and Equipment:		
Land, buildings and improvements	120,864	116,858
Machinery and equipment	274,907	263,336
Total cost	395,771	380,194
Less accumulated depreciation	218,846	210,599
Property, plant and equipment-net	176,925	169,595
Other Assets:		
Goodwill	164,908	143,788
Other intangible assets-net	64,820	44,866
Other noncurrent assets	7,846	8,656
Total	$691,458	$634,732
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$39,420	$39,931
Accrued liabilities	30,425	33,072
Total current liabilities	69,845	73,003
Other Noncurrent Liabilities	41,292	26,698
Deferred Income Taxes	20,838	21,433
Commitments and Contingencies		
Shareholders' Equity:		
Preferred stock-authorized 3,050,000 shares; outstanding-none		
Common stock-authorized 75,000,000 shares; outstanding-December-27,430,232 shares; June-27,423,550 shares	112,852	110,677
Retained earnings	1,193,899	1,150,337
Accumulated other comprehensive loss	(11,194)	(11,350)
Common stock in treasury, at cost	(736,074)	(736,066)
Total shareholders' equity	559,483	513,598
Total	$691,458	$634,732

See accompanying notes to condensed consolidated financial statements.

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

	Three Months Ended December 31,		Six Months Ended December 31,	
(Amounts in thousands, except per share data)	2016	2015	2016	2015
Net Sales	$326,773	$324,769	$618,134	$618,854
Cost of Sales	233,034	241,175	443,761	467,293
Gross Profit	93,739	83,594	174,373	151,561
Selling, General and Administrative Expenses	34,381	31,479	64,261	57,558
Operating Income	59,358	52,115	110,112	94,003
Other, Net	206	(205)	293	(83)
Income Before Income Taxes	59,564	51,910	110,405	93,920
Taxes Based on Income	20,608	17,399	38,049	31,781
Net Income	$38,956	$34,511	$72,356	$62,139
Net Income Per Common Share:				
Basic	$1.42	$1.26	$2.64	$2.27
Diluted	$1.42	$1.25	$2.63	$2.26
Cash Dividends Per Common Share	$0.55	$5.50	$1.05	$5.96
Weighted Average Common Shares Outstanding:				
Basic	27,366	27,328	27,364	27,324
Diluted	27,441	27,374	27,435	27,359

See accompanying notes to condensed consolidated financial statements.

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

	Three Months Ended December 31,		Six Months Ended December 31,	
(Amounts in thousands)	2016	2015	2016	2015
Net Income	$38,956	$34,511	$72,356	$62,139
Other Comprehensive Income:				
Defined Benefit Pension and Postretirement Benefit Plans:				
Prior service credit arising during the period, before tax	—	2,038	—	2,038
Amortization of loss, before tax	168	127	338	258
Amortization of prior service credit, before tax	(45)	(31)	(90)	(32)
Total Other Comprehensive Income, Before Tax	123	2,134	248	2,264
Tax Attributes of Items in Other Comprehensive Income:				
Prior service credit arising during the period, tax	—	(753)	—	(753)
Amortization of loss, tax	(62)	(48)	(125)	(97)
Amortization of prior service credit, tax	17	12	33	12
Total Tax Expense	(45)	(789)	(92)	(838)
Other Comprehensive Income, Net of Tax	78	1,345	156	1,426
Comprehensive Income	$39,034	$35,856	$72,512	$63,565

See accompanying notes to condensed consolidated financial statements.

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

	Six Months Ended December 31,	
(Amounts in thousands)	2016	2015
Cash Flows From Operating Activities:		
Net income	$72,356	$62,139
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	11,943	12,149
Deferred income taxes and other noncash changes	71	269
Stock-based compensation expense	2,155	1,353
Excess tax benefit from stock-based compensation	(154)	(411)
Pension plan activity	(122)	(148)
Changes in operating assets and liabilities:		
Receivables	(3,931)	1,731
Inventories	(3,589)	(2,572)
Other current assets	918	51
Accounts payable and accrued liabilities	(3,831)	(115)
Net cash provided by operating activities	75,816	74,446
Cash Flows From Investing Activities:		
Cash paid for acquisitions, net of cash acquired	(34,997)	(12)
Payments for property additions	(11,838)	(7,362)
Other-net	94	(379)
Net cash used in investing activities	(46,741)	(7,753)
Cash Flows From Financing Activities:		
Payment of dividends (including special dividend payment, 2017-$0; 2016-$136,677)	(28,794)	(163,139)
Purchase of treasury stock	(8)	—
Excess tax benefit from stock-based compensation	154	411
Increase in cash overdraft balance	—	974
Net cash used in financing activities	(28,648)	(161,754)
Net change in cash and equivalents	427	(95,061)
Cash and equivalents at beginning of year	118,080	182,202
Cash and equivalents at end of period	$118,507	$87,141
Supplemental Disclosure of Operating Cash Flows:		
Cash paid during the period for income taxes	$37,383	$33,600

See accompanying notes to condensed consolidated financial statements.

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

Note 1 – Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Lancaster Colony Corporation and our wholly-owned subsidiaries, collectively referred to as “we,” “us,” “our,” “registrant” or the “Company” ar have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and SEC Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In our opinion, the interim condensed consolidated financial statements reflect all adjustments necessary for a fair presentation of the results of operations and financial position for such periods. All such adjustments reflected in the interim condensed consolidated financial statements are considered to be of a normal recurring nature. Intercompany transactions and accounts have been eliminated in consolidation. The results of operations for any interim period are not necessarily indicative of results for the full year. Accordingly, these financial statements should be read in conjunction with the financial statements and notes thereto contained in our 2016 Annual Report on Form 10-K. Unless otherwise noted, the term “year” and references to a particular year pertain to our fiscal year, which begins on July 1 and ends on June 30; for example, 2017 refers to fiscal 2017, which is the period from July 1, 2016 to June 30, 2017.

Subsequent Event

On January 21, 2017 the employees at our Bedford Heights, Ohio plant voted to ratify a new collective bargaining agreement to replace the agreement that expired on April 30, 2016. The new collective bargaining agreement will expire on April 30, 2020. Among other terms, the new agreement provides for our complete withdrawal from the Cleveland Bakers and Teamsters Pension Fund, a multiemployer pension fund. In lieu of contributions to the pension fund, we will make non-elective contributions for the employees at the Bedford Heights, Ohio plant into a union-sponsored 401(k) plan. We have agreed to initially fund the new 401(k) plan and pay a withdrawal liability as settlement of our portion of underfunded pension benefits of the multiemployer plan. The recording of these charges is predicated upon when the liability is probable in occurrence. Due to the fact that the new collective bargaining agreement was contingent upon ratification by the employees, the probability of occurrence was not satisfied until the vote on January 21, 2017. Therefore, we will record a one-time charge of $17.7 million for the multiemployer pension settlement and other benefit-related costs in the quarter ended March 31, 2017.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation, except for those acquired as part of a business combination, which are stated at fair value at the time of purchase. Purchases of property, plant and equipment included in Accounts Payable and excluded from the property additions and the change in accounts payable in the Condensed Consolidated Statements of Cash Flows were as follows:

	December 31,	
	2016	2015
Construction in progress in Accounts Payable	$1,298	$476

Accrued Distribution

Accrued distribution costs included in Accrued Liabilities were $7.1 million and $4.5 million at December 31, 2016 and June 30, 2016, respectively.

Earnings Per Share

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

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(Tabular amounts in thousands, except per share data)

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

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Net income	$38,956	$34,511	$72,356	$62,139
Net income available to participating securities	(77)	(177)	(142)	(192)
Net income available to common shareholders	$38,879	$34,334	$72,214	$61,947
Weighted average common shares outstanding – basic	27,366	27,328	27,364	27,324
Incremental share effect from:				
Nonparticipating restricted stock	3	3	4	4
Stock-settled stock appreciation rights	72	43	67	31
Weighted average common shares outstanding – diluted	27,441	27,374	27,435	27,359
Net income per common share – basic	$1.42	$1.26	$2.64	$2.27
Net income per common share – diluted	$1.42	$1.25	$2.63	$2.26

Accumulated Other Comprehensive Loss

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

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Accumulated other comprehensive loss at beginning of period	$(11,272)	$(9,976)	$(11,350)	$(10,057)
Defined Benefit Pension Plan Items:				
Amortization of unrecognized net loss	178	135	357	270
Postretirement Benefit Plan Items:				
Prior service credit arising during the period	—	2,038	—	2,038
Amortization of unrecognized net gain	(10)	(8)	(19)	(12)
Amortization of prior service credit	(45)	(31)	(90)	(32)
Total other comprehensive income, before tax	123	2,134	248	2,264
Total tax expense	(45)	(789)	(92)	(838)
Other comprehensive income, net of tax	78	1,345	156	1,426
Accumulated other comprehensive loss at end of period	$(11,194)	$(8,631)	$(11,194)	$(8,631)

Significant Accounting Policies

There were no changes to our Significant Accounting Policies from those disclosed in our 2016 Annual Report on Form 10-K.

Recently Issued Accounting Standards

In March 2016, the Financial Accounting Standards Board (“FASB”) issued new accounting guidance to simplify the accounting for stock-based compensation. The amendments include changes to the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. The guidance will be effective for us in fiscal 2018 including interim periods. The transition method that will be applied on adoption varies for each of the amendments. We are currently evaluating the impact of this guidance.

In May 2014, the FASB issued new accounting guidance for the recognition of revenue and issued subsequent clarifications of this new guidance in 2016 and 2017. The core principle of the new guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This model is based on a control approach rather than

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the current risks and rewards model. The new guidance would also require expanded disclosures. Since we do not plan to early adopt this standard, the guidance will be effective for us in fiscal 2019 including interim periods and will require either retrospective application to each prior period presented or modified retrospective application with the cumulative effect of initially applying the standard recognized at the date of adoption. We are currently evaluating the impact of this guidance.

In February 2016, the FASB issued new accounting guidance to require lessees to recognize a right-of-use asset and a lease liability for leases with terms of more than 12 months. The updated guidance retains the two classifications of a lease as either an operating or finance lease (previously referred to as a capital lease). Both lease classifications require the lessee to record a right-of-use asset and a lease liability based upon the present value of the lease payments. Finance leases will reflect the financial arrangement by recognizing interest expense on the lease liability separately from the amortization expense of the right-of-use asset. Operating leases will recognize lease expense (with no separate recognition of interest expense) on a straight-line basis over the term of the lease. The updated guidance requires expanded qualitative and quantitative disclosures, including additional information about the amounts recorded in the consolidated financial statements. The guidance will be effective for us in fiscal 2020 including interim periods using a modified retrospective approach. We are currently evaluating the impact of this guidance.

Recently Adopted Accounting Standards

In July 2015, the FASB issued new accounting guidance which requires entities to measure most inventory “at the lower of cost or net realizable value,” thereby simplifying current guidance. Under current guidance an entity must measure inventory at the lower of cost or market, where market is defined as one of three different measures, one of which is net realizable value. We adopted this guidance effective July 1, 2016 on a prospective basis, and it did not have a material impact on our condensed consolidated financial statements.

In August 2016, the FASB issued new accounting guidance to reduce diversity in practice in how certain cash receipts and cash payments are presented in the statement of cash flows. Current guidance is either unclear or does not include specific requirements for the classification of these transactions. The majority of the new provisions are not currently applicable to us, and those that are applicable are consistent with our current practice. The guidance will be effective for fiscal years, and interim periods within those years, beginning after December 15, 2017 using a retrospective transition method for all periods presented. Early adoption is permitted provided that all amendments are adopted in the same period. We adopted this guidance effective July 1, 2016, and it did not have an impact on our Condensed Consolidated Statements of Cash Flows.

Note 2 – Acquisition

On November 17, 2016, we acquired substantially all of the assets of Angelic Bakehouse, Inc. (“Angelic”). Angelic, a privately owned manufacturer and marketer of premium sprouted grain bakery products, is based near Milwaukee, Wisconsin. The initial purchase price of $35.0 million was funded by cash on hand and excludes contingent consideration relating to an additional earn-out payment which is tied to performance-based conditions. In general, the terms of the acquisition specify that the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Angelic in fiscal 2021. We are unable to provide a range for the amount of this earn-out because it is based on the future adjusted EBITDA of Angelic, and the earn-out does not contain a minimum or maximum value. See further discussion of the earn-out in Note 3.

Angelic is reported in our Specialty Foods segment, and its results of operations have been included in our condensed consolidated financial statements from the date of acquisition. Such results were not material.

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The following table summarizes the consideration related to the acquisition and the preliminary purchase price allocation based on the fair value of the net assets acquired, as adjusted for the preliminary net working capital adjustment recorded as of December 31, 2016. The initial fair value of the contingent consideration is a noncash investing activity.

Consideration	
Cash paid for acquisition	$34,997
Contingent consideration - fair value of earn-out at date of closing	13,872
Working capital adjustment receivable	(63)
Fair value of total consideration	$48,806

Preliminary Purchase Price Allocation	
Trade receivables	$831
Other receivables	550
Inventories	430
Other current assets	19
Property, plant and equipment	5,083
Goodwill (tax deductible)	21,120
Other intangible assets	21,491
Current liabilities	(718)
Net assets acquired	$48,806

Further adjustments may occur to the allocation above as certain aspects of the transaction are finalized during the measurement period.

The goodwill recognized above arose because the purchase price for Angelic reflects a number of factors including the future earnings and cash flow potential of Angelic, as well as the impact of the inclusion of the initial fair value of the earn-out associated with the acquisition. Angelic is a fast growing, on-trend business with placement in the specialty deli/bakery section of the grocery store and provides innovation opportunities within and beyond our present product lines. Goodwill also resulted from the workforce acquired with Angelic.

We have determined preliminary values and lives of the other intangible assets listed in the allocation above as: $18.6 million for the tradename with a 20-year life; $0.3 million for the customer relationships with a 10-year life; $2.4 million for the technology / know-how with a 10-year life and $0.2 million for the non-compete agreements with a 5-year life.

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

Note 3 – Fair Value

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

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

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

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

Our financial assets and liabilities consist principally of cash, accounts receivable, accounts payable and contingent consideration payable. The estimated fair value of cash, accounts receivable and accounts payable approximates their carrying value. Contingent consideration payable is recorded at fair value.

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(Tabular amounts in thousands, except per share data)

Our contingent consideration, which is measured at fair value on a recurring basis and did not have a balance at June 30, 2016, is included in Other Noncurrent Liabilities on the Condensed Consolidated Balance Sheets. The following table summarizes our contingent consideration as of December 31, 2016:

	Fair Value Measurements at December 31, 2016			
	Level 1	Level 2	Level 3	Total
Acquisition-related contingent consideration	$—	$—	$14,096	$14,096

The contingent consideration resulted from the earn-out associated with our November 17, 2016 acquisition of Angelic. The initial purchase price of $35.0 million did not include the future earn-out payment which is tied to performance-based conditions. In general, the terms of the acquisition specify that the sellers will receive an earn-out based upon a pre-determined multiple of the defined adjusted EBITDA of Angelic in fiscal 2021. The fair value of the contingent consideration was estimated using a present value approach, which incorporates factors such as business risks and projections, to estimate an expected value. This fair value measurement is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy. Using this valuation technique, the fair value of the contingent consideration was determined to be $13.9 million at November 17, 2016.

The following table represents our Level 3 fair value measurements using significant other unobservable inputs for acquisition-related contingent consideration as of December 31, 2016:

Change in acquisition-related contingent consideration	
Acquisition-related contingent consideration at beginning of year	$—
Additions	13,872
Changes in fair value included in Selling, General and Administrative Expenses	224
Acquisition-related contingent consideration at end of period	$14,096

Note 4 – Long-Term Debt

At December 31, 2016 and June 30, 2016, we had an unsecured credit facility (“Facility”) under which we could borrow, on a revolving credit basis, up to a maximum of $150 million at any one time, with potential to expand the total credit availability to $225 million subject to us obtaining consent of the issuing banks and certain other conditions. The Facility expires on April 8, 2021, and all outstanding amounts are then due and payable. Interest is variable based upon formulas tied to LIBOR or an alternative base rate defined in the Facility, at our option. We must also pay facility fees that are tied to our then-applicable consolidated leverage ratio. Loans may be used for general corporate purposes. Due to the nature of its terms, when we have outstanding borrowings under the Facility, they will be classified as long-term debt.

At December 31, 2016 and June 30, 2016, we had no borrowings outstanding under the Facility. At December 31, 2016, we had $5.1 million of standby letters of credit outstanding, which reduced the amount available for borrowing on the Facility. We paid no interest for the three and six months ended December 31, 2016 and 2015.

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

Note 5 – Commitments and Contingencies

At December 31, 2016, we were a party to various claims and litigation matters arising in the ordinary course of business. Such matters did not have a material effect on the current-year results of operations and, in our opinion, their ultimate disposition will not have a material effect on our consolidated financial statements.

With our recent acquisition of Angelic, we have a contingent liability recorded for the earn-out associated with the transaction. See further discussion in Note 3.

Note 6 – Goodwill and Other Intangible Assets

Goodwill attributable to the Specialty Foods segment was $164.9 million and $143.8 million at December 31, 2016 and June 30, 2016, respectively. The increase in goodwill is the result of the acquisition of Angelic in November 2016. See further discussion in Note 2.

LANCASTER COLONY CORPORATION AND SUBSIDIARIES
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(Tabular amounts in thousands, except per share data)

The following table is a rollforward of goodwill from June 30, 2016 to December 31, 2016:

	Carrying Value
Goodwill at beginning of year	$143,788
Goodwill acquired during the period	21,120
Goodwill at end of period	$164,908

The following table summarizes our identifiable other intangible assets, all included in the Specialty Foods segment. The intangible asset values and lives related to the Angelic acquisition, which are included in the table below, are preliminary and subject to further review over the measurement period. See further discussion in Note 2.

	December 31, 2016	June 30, 2016
Tradenames (20 to 30-year life)		
Gross carrying value	$53,063	$34,500
Accumulated amortization	(2,177)	(1,485)
Net carrying value	$50,886	$33,015
Trademarks (40-year life)		
Gross carrying value	$370	$370
Accumulated amortization	(237)	(232)
Net carrying value	$133	$138
Customer Relationships (10 to 15-year life)		
Gross carrying value	$14,207	$13,920
Accumulated amortization	(6,598)	(6,048)
Net carrying value	$7,609	$7,872
Technology / Know-how (10-year life)		
Gross carrying value	$6,350	$3,900
Accumulated amortization	(729)	(504)
Net carrying value	$5,621	$3,396
Non-compete Agreements (5-year life)		
Gross carrying value	$791	$600
Accumulated amortization	(220)	(155)
Net carrying value	$571	$445
Total net carrying value	$64,820	$44,866

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

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Amortization expense	$846	$777	$1,537	$1,523

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

2018	$4,004

2019	$4,004
2020	$3,969
2021	$3,884
2022	$3,811

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in thousands, except per share data)

Note 7 – Income Taxes

Prepaid federal income taxes of $2.3 million and $4.3 million were included in Other Current Assets at December 31, 2016 and June 30, 2016, respectively. Prepaid state and local income taxes of $1.1 million and $0.5 million were included in Other Current Assets at December 31, 2016 and June 30, 2016, respectively.

Note 8 – Business Segment Information

The December 31, 2016 identifiable assets by reportable segment are generally consistent with that of June 30, 2016. However, due to the acquisition of Angelic in November 2016, the amount of Specialty Foods assets increased as compared to June 30, 2016. The following summary of financial information is consistent with the basis of segmentation and measurement of segment profit or loss presented in our June 30, 2016 consolidated financial statements:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2016	2015	2016	2015
Net Sales	$326,773	$324,769	$618,134	$618,854
Operating Income				
Specialty Foods	$62,052	$55,429	$116,877	$100,390
Corporate Expenses	(2,694)	(3,314)	(6,765)	(6,387)
Total	$59,358	$52,115	$110,112	$94,003

Note 9 – Stock-Based Compensation

There have been no changes to our stock-based compensation plans from those disclosed in our 2016 Annual Report on Form 10-K.

Our stock-settled stock appreciation rights ("SSSARs") compensation expense was $0.4 million and $0.2 million for the three months ended December 31, 2016 and 2015, respectively. Year-to-date SSSARs compensation expense was $0.9 million for the current-year period compared to $0.5 million for the prior-year period. At December 31, 2016, there was $2.3 million of unrecognized compensation expense related to SSSARs that we will recognize over a weighted-average period of 2 years.

Our restricted stock compensation expense was $0.6 million and $0.4 million for the three months ended December 31, 2016 and 2015, respectively. Year-to-date restricted stock compensation expense was $1.2 million for the current-year period compared to $0.8 million for the prior-year period. At December 31, 2016, there was $3.1 million of unrecognized compensation expense related to restricted stock that we will recognize over a weighted-average period of 2 years.

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

Our fiscal year begins on July 1 and ends on June 30. Unless otherwise noted, references to "year" pertain to our fiscal year; for example, 2017 refers to fiscal 2017, which is the period from July 1, 2016 to June 30, 2017.

The following discussion should be read in conjunction with our condensed consolidated financial statements and the notes thereto, all included elsewhere in this report. The forward-looking statements in this section and other parts of this report involve risks, uncertainties and other factors, including statements regarding our plans, objectives, goals, strategies, and financial performance. Our actual results could differ materially from the results anticipated in these forward-looking statements due to these factors. For more information, see the section below entitled "Forward-Looking Statements."

OVERVIEW

Business Overview

Lancaster Colony Corporation is a manufacturer and marketer of specialty food products for the retail and foodservice channels.

Part of our future growth may result from acquisitions. We continue to review potential acquisitions that we believe will complement our existing product lines, enhance our profitability and/or offer good expansion opportunities in a manner that fits our overall strategic goals.

Our operations are organized into one reportable segment: "Specialty Foods." Our sales are predominately domestic.

Our business has the potential to achieve future growth in sales and profitability due to attributes such as:

- leading retail market positions in several product categories with a high-quality perception;
- recognized innovation in retail products;
- a broad customer base in both retail and foodservice accounts;
- well-regarded culinary expertise among foodservice customers;
- recognized leadership in foodservice product development;
- experience in integrating complementary business acquisitions; and
- historically strong cash flow generation that supports growth opportunities.

Our goal is to grow both retail and foodservice sales over time by:

- leveraging the strength of our retail brands to increase current product sales;
- introducing new retail products and expanding distribution;
- growing our foodservice sales through the strength of our reputation in product development and quality; and
- pursuing acquisitions that meet our strategic criteria.

Consistent with our current acquisition strategy, in November 2016 we acquired substantially all of the assets of Angelic Bakehouse, Inc. ("Angelic"), a manufacturer and marketer of premium sprouted grain bakery products based near Milwaukee, Wisconsin. This transaction is discussed in further detail in Note 2 to the condensed consolidated financial statements.

We have made substantial capital investments to support our existing food operations and future growth opportunities. For example, in 2015 we completed a significant processing capacity expansion at our Horse Cave, Kentucky dressing facility to help meet demand for our dressing products. Based on our current plans and expectations, we believe our capital expenditures for 2017 could total approximately $20 to $25 million. We anticipate we will be able to fund all of our capital needs in 2017 with cash generated from operations.

RESULTS OF CONSOLIDATED OPERATIONS

Net Sales and Gross Profit

	Three Months Ended December 31,				Six Months Ended December 31,			
(Dollars in thousands)	2016	2015	Change		2016	2015	Change	
Net Sales	$326,773	$324,769	$2,004	1 %	$618,134	$618,854	$(720)	— %
Gross Profit	$93,739	$83,594	$10,145	12%	$174,373	$151,561	$22,812	15 %
Gross Margin	28.7 %	25.7 %			28.2 %	24.5 %		

In November 2016, we acquired Angelic and its results of operations have been included in our condensed consolidated financial statements from the date of acquisition. Such results were not material.

Net sales for the three months ended December 31, 2016 increased 1% as an increase in retail net sales was partially offset by a decline in foodservice net sales. Net sales for the six months ended December 31, 2016 were essentially flat as an increase in retail net sales was offset by a decline in foodservice net sales. Our overall sales volume, as measured by pounds shipped, increased by 2% and 1% for the three and six months ended December 31, 2016, respectively. Pricing had a net deflationary impact of 1% of net sales for the quarter and year-to-date periods.

Retail net sales increased 3% during both the three and six months ended December 31, 2016, due to higher sales of certain product lines including Olive Garden® retail dressings, New York BRAND® Bakery frozen garlic bread products and Sister Schubert's® frozen dinner rolls. Higher trade promotions and increased new product placement costs combined to limit the retail sales growth. Foodservice net sales declined 2% and 3% for the quarter and year-to-date periods, respectively, as influenced by our targeted customer rationalization efforts that began in the third quarter of last year. Also contributing to the foodservice sales decline was deflationary pricing from lower egg costs.

Gross margin improved for the three months ended December 31, 2016 due to the influence of overall lower raw-material costs, primarily for eggs, but also for flour, honey, dairy and soybean oil. Margins also benefited from a more favorable sales mix, partially offset by higher retail trade spending and product placement costs. Excluding any pricing actions, total raw-material costs positively affected our gross margins by 4% of net sales for the quarter.

Gross margin also improved for the six months ended December 31, 2016 due to the influence of overall lower raw-material costs, again primarily for eggs, but also for soybean oil, flour, honey and resin packaging. Margins also benefited from a more favorable sales mix, partially offset by higher retail trade spending, product placement costs and coupon redemptions. Excluding any pricing actions, total raw-material costs positively affected our gross margins by 4% of net sales for the year-to-date period.

Selling, General and Administrative Expenses

	Three Months Ended December 31,				Six Months Ended December 31,			
(Dollars in thousands)	2016	2015	Change		2016	2015	Change	
SG&A Expenses	$34,381	$31,479	$2,902	9%	$64,261	$57,558	$6,703	12%
SG&A Expenses as a Percentage of Net Sales	10.5 %	9.7 %			10.4 %	9.3 %		

Selling, general and administrative expenses increased 9% and 12% for the three and six months ended December 31, 2016, respectively, and were higher as a percentage of net sales for the comparative second quarter and first half periods. The increase in these costs reflects the influence of higher levels of investment in marketing and promotions for our key retail product lines and new product introductions. Increased salary expenses attributed to some recent staffing additions in marketing and operations, combined with higher consulting fees, and professional fees also contributed to the increased selling, general and administrative expenses.

Operating Income

The foregoing factors contributed to consolidated operating income totaling $59.4 million and $110.1 million for the three and six months ended December 31, 2016, respectively. Our operating income can be summarized as follows:

	Three Months Ended December 31,				Six Months Ended December 31,			
(Dollars in thousands)	2016	2015	Change		2016	2015	Change	
Operating Income								
Specialty Foods	$62,052	$55,429	$6,623	12 %	$116,877	$100,390	$16,487	16%
Corporate Expenses	(2,694)	(3,314)	620	(19)%	(6,765)	(6,387)	(378)	6 %
Total	$59,358	$52,115	$7,243	14 %	$110,112	$94,003	$16,109	17%
Operating Income as a Percentage of Net Sales								
Specialty Foods	19.0 %	17.1 %			18.9 %	16.2 %		
Total	18.2 %	16.0 %			17.8 %	15.2 %		

Looking ahead, the fiscal third quarter will reflect the impact of a pre-tax charge of $17.7 million in settlement costs and related expenses resulting from our withdrawal from an underfunded multiemployer pension plan as discussed in more detail in “Subsequent Event” in Note 1 to the condensed consolidated financial statements. Given this year’s later Easter holiday, we anticipate a shift in some of our retail net sales and related consumer activities into our fiscal fourth quarter. We expect volume-driven growth in our retail sales channel for the balance of 2017 with continued support from recent new product introductions along with increased sales from Flatout and the incremental sales contribution from Angelic. In our foodservice channel, we expect volume-driven growth from continuing customers will again be largely offset by the influence of deflationary pricing (due to lower commodity costs, particularly eggs) and the impact of our customer rationalization initiative that was implemented beginning in the third quarter of 2016. Ongoing softness in the foodservice industry, particularly the casual dining segment, may also impact sales volumes in the foodservice channel. Based on current market conditions, in the second half of 2017, we anticipate an overall more neutral cost environment for ingredients in the third quarter then turning slightly unfavorable in the fourth quarter.

Income Before Income Taxes

As impacted by the factors discussed above, income before income taxes for the three months ended December 31, 2016 increased by $7.7 million to $59.6 million from the prior-year total of $51.9 million. Income before income taxes for the six months ended December 31, 2016 and 2015 was $110.4 million and $93.9 million, respectively.

Taxes Based on Income

Our effective tax rate was 34.5% and 33.8% for the six months ended December 31, 2016 and 2015, respectively. Given the nature of our operations (predominately U.S. based for both sales and manufacturing), our effective tax rates typically stay within a fairly narrow range.

Net Income

Second quarter net income for 2017 of $39.0 million increased from the preceding year's net income for the quarter of $34.5 million, as influenced by the factors noted above. Year-to-date net income of $72.4 million was higher than the prior year-to-date total of $62.1 million. Diluted weighted average common shares outstanding have remained relatively stable. As a result, and due to the change in net income for each year, net income per share for the second quarter of 2017 totaled $1.42 per diluted share, as compared to net income of $1.25 per diluted share in the prior year. Year-to-date net income per share was $2.63 per diluted share, as compared to $2.26 per diluted share for the prior-year period.

FINANCIAL CONDITION

For the six months ended December 31, 2016, net cash provided by operating activities totaled $75.8 million, as compared to $74.4 million in the prior-year period. The increase was due to an increase in net income, which was largely offset by higher working capital requirements, primarily in accounts receivable, which can vary depending on the timing of monthly sales, and accounts payable.

Cash used in investing activities for the six months ended December 31, 2016 was $46.7 million, as compared to $7.8 million in the prior year. This increase primarily reflects cash paid for the acquisition of Angelic in November 2016, as well as a higher level of capital expenditures in 2017, with the largest amounts spent on packaging equipment to accommodate growth and build-out costs related to our planned corporate office relocation.

Cash used in financing activities for the six months ended December 31, 2016 of $28.6 million decreased from the prior-year total of $161.8 million. This decrease was primarily due to lower dividend payments in the current year. Prior-year dividend payments included a $5.00 per share special dividend that was paid in December 2015. The special dividend payment totaled $136.7 million. The share repurchases in the six months ended December 31, 2016 were for shares repurchased in satisfaction of tax withholding obligations arising from the vesting of restricted stock granted to employees. At December 31, 2016, 1,418,088 shares remained authorized for future buyback under the existing share repurchase program.

Under our unsecured revolving credit facility ("Facility"), we may borrow up to a maximum of $150 million at any one time. We had no borrowings outstanding under the Facility at December 31, 2016. At December 31, 2016, we had $5.1 million of standby letters of credit outstanding, which reduced the amount available for borrowing on the Facility. The Facility expires in April 2021, and all outstanding amounts are then due and payable. Interest is variable based upon formulas tied to LIBOR or an alternative base rate defined in the Facility, at our option. We must also pay facility fees that are tied to our then-applicable consolidated leverage ratio. Loans may be used for general corporate purposes. Due to the nature of its terms, when we have outstanding borrowings under the Facility, they will be classified as long-term debt.

The Facility contains certain restrictive covenants, including limitations on indebtedness, asset sales and acquisitions, and financial covenants relating to interest coverage and leverage. At December 31, 2016, we were in compliance with all applicable provisions and covenants of this facility, and we exceeded the requirements of the financial covenants by substantial margins. At December 31, 2016, we were not aware of any event that would constitute a default under this facility.

We currently expect to remain in compliance with the Facility’s covenants for the foreseeable future. However, a default under the Facility could accelerate the repayment of any outstanding indebtedness and limit our access to $75 million of additional credit available under the Facility. Such an event could require a reduction in or curtailment of cash dividends or share repurchases, reduce or delay beneficial expansion or investment plans, or otherwise impact our ability to meet our obligations when due.

We believe that cash provided by operating activities and our existing balances in cash and equivalents, in addition to that available under the Facility, should be adequate to meet our cash requirements through 2017. If we were to borrow outside of the Facility under current market terms, our average interest rate may increase significantly and have an adverse effect on our results of operations.

CONTRACTUAL OBLIGATIONS

We have various contractual obligations that are appropriately recorded as liabilities in our condensed consolidated financial statements. Certain other items are not recognized as liabilities in our condensed consolidated financial statements. Examples of such items are commitments to purchase raw materials or packaging inventory that has not yet been received as of December 31, 2016 and future minimum lease payments for the use of property and equipment under operating lease agreements. Aside from expected changes in raw-material needs due to changes in product demand and the impact of commodity prices, there have been no significant changes to the contractual obligations disclosed in our 2016 Annual Report on Form 10-K.

CRITICAL ACCOUNTING POLICIES

There have been no changes in critical accounting policies from those policies disclosed in our 2016 Annual Report on Form 10-K.

RECENT ACCOUNTING PRONOUNCEMENTS

Recent accounting pronouncements and their impact on our consolidated financial statements are disclosed in Note 1 to the condensed consolidated financial statements.

FORWARD-LOOKING STATEMENTS

We desire to take advantage of the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995 (the “PSLRA”). This Quarterly Report on Form 10-Q contains various “forward-looking statements” within the meaning of the PSLRA and other applicable securities laws. Such statements can be identified by the use of the forward-looking words “anticipate,” “estimate,” “project,” “believe,” “intend,” “plan,” “expect,” “hope” or similar words. These statements disc future expectations; contain projections regarding future developments, operations or financial conditions; or state other forward-looking information. Such statements are based upon assumptions and assessments made by us in light of our experience and perception of historical trends, current conditions, expected future developments and other factors we believe to be appropriate. These forward-looking statements involve various important risks, uncertainties and other factors that could cause our actual results to differ materially from those expressed in the forward-looking statements. Actual results may differ as a result of factors over which we have no, or limited, control including, without limitation, the specific influences outlined below. Management believes these forward-looking statements to be reasonable; however, one should not place undue reliance on such statements that are based on current expectations. Forward-looking statements speak only as of the date they are made, and we undertake no obligation to update such forward-looking statements, except as required by law.

Items which could impact these forward-looking statements include, but are not limited to:

- the ability to successfully integrate the acquisition of Angelic and subsequently grow the business;
- price and product competition;
- the impact of any regulatory matters affecting our food business, including any required labeling changes and their impact on consumer demand;
- the potential for loss of larger programs or key customer relationships;
- the impact of customer store brands on our branded retail volumes;
- fluctuations in the cost and availability of ingredients and packaging;
- the reaction of customers or consumers to the effect of price increases we may implement;
- the effect of consolidation of customers within key market channels;
- the success and cost of new product development efforts;
- the lack of market acceptance of new products;

- the possible occurrence of product recalls or other defective or mislabeled product costs;
- changes in demand for our products, which may result from loss of brand reputation or customer goodwill;
- maintenance of competitive position with respect to other manufacturers;
- adverse changes in freight, energy or other costs of producing, distributing or transporting our products;
- capacity constraints that may affect our ability to meet demand or may increase our costs;

- dependence on contract manufacturers;
- efficiencies in plant operations;
- stability of labor relations, including the impact of contract negotiations with collective bargaining units;
- the outcome of any litigation or arbitration;
- the impact, if any, of certain contingent liabilities associated with our withdrawal from a multiemployer pension plan;
- the impact of fluctuations in our pension plan asset values on funding levels, contributions required and benefit costs;
- the extent to which future business acquisitions are completed and acceptably integrated;
- dependence on key personnel and changes in key personnel;
- changes in estimates in critical accounting judgments; and
- certain other factors, including the information disclosed in our discussion of risk factors under Item 1A of our 2016 Annual Report on Form 10-K.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our market risks have not changed materially from those disclosed in our 2016 Annual Report on Form 10-K.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures. As of the end of the period covered by this Quarterly Report on Form 10-Q, our Chief Executive Officer and Chief Financial Officer evaluated, with the participation of management, the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”)). Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of December 31, 2016 to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is 1) recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms and 2) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, in a manner that allows timely decisions regarding required disclosure.

(b) Changes in Internal Control Over Financial Reporting. No changes were made to our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION
Item 1A. Risk Factors
There have been no material changes to the risk factors disclosed under Item 1A in our 2016 Annual Report on Form 10-K other than the risk described below.
We may incur liabilities related to multiemployer pension plans which could adversely affect our financial results.
Until recently, we contributed to two multiemployer pension plans under certain collective bargaining agreements that provide pension benefits to employees and retired employees who are part of the plans. On January 21, 2017, the employees at our Bedford Heights, Ohio plant voted to ratify a new collective bargaining agreement that provided for our complete withdrawal from the multiemployer pension plan associated with that facility. At this time, we still contribute to a multiemployer pension plan related to our facility in Milpitas, California.
Because we have withdrawn from the multiemployer pension plan associated with our Bedford Heights plant, we are no longer subject to risks associated with increased contributions with respect to this pension fund. Nonetheless, certain future events related to this pension fund could result in incremental pension-related costs; however, the likelihood of these events occurring is indeterminate at this time.
As a contributor to the multiemployer pension plan associated with our Milpitas, California facility, we are responsible for making periodic contributions to this plan. Our required contributions to this plan could increase, however any increase would be dependent upon a number of factors, including our ability to renegotiate the collective bargaining contract successfully, current and future regulatory requirements, the performance of the pension plan's investments, the number of participants who are entitled to receive benefits from the plan, the contribution base as a result of the insolvency or withdrawal of other companies that currently contribute to this plan, the inability or failure of withdrawing companies to pay their withdrawal liability, low interest rates and other funding deficiencies. We may also be required to pay a withdrawal liability if we exit from this plan. While we cannot determine whether and to what extent our contributions may increase or what our withdrawal liability may be, we do not expect any payments related to this plan to have a material adverse effect on our business, financial condition, results of operations and cash flows.
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
(c) In November 2010, our Board of Directors approved a share repurchase authorization of 2,000,000 shares, of which 1,418,088 shares remained authorized for future repurchases at December 31, 2016. This share repurchase authorization does not have a stated expiration date. In the second quarter, we did not repurchase any of our common stock.

Period	Total Number of Shares Purchased	Average Price Paid Per Share		Total Number of Shares Purchased as Part of Publicly Announced Plans	Maximum Number of Shares that May Yet be Purchased Under the Plans
October 1-31, 2016	—	$	——		1,418,088
November 1-30, 2016	—	$	——		1,418,088
December 1-31, 2016	—	$	——		1,418,088
Total	—	$	——		1,418,088

Item 6. Exhibits
See Index to Exhibits following Signatures.

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.

		LANCASTER COLONY CORPORATION	
			(Registrant)
Date:	February 7, 2017	By:	/s/ JOHN B. GERLACH, JR. John B. Gerlach, Jr. Chairman, Chief Executive Officer and Director (Principal Executive Officer)
Date:	February 7, 2017	By:	/s/ DOUGLAS A. FELL Douglas A. Fell Treasurer, Vice President, Assistant Secretary and Chief Financial Officer (Principal Financial and Accounting Officer)

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LANCASTER COLONY CORPORATION AND SUBSIDIARIES
FORM 10-Q
DECEMBER 31, 2016
INDEX TO EXHIBITS

Exhibit Number	Description	Located at
31.1	Certification of CEO under Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
31.2	Certification of CFO under Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
32	Certification of CEO and CFO under Section 906 of the Sarbanes-Oxley Act of 2002	Furnished herewith
101.INS	XBRL Instance Document	Filed herewith
101.SCH	XBRL Taxonomy Extension Schema Document	Filed herewith
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	Filed herewith
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	Filed herewith
101.LAB	XBRL Taxonomy Extension Label Linkbase Document	Filed herewith
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document	Filed herewith