

G&K SERVICES INC  
Form 10-Q  
April 30, 2015  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended March 28, 2015  
Commission file number 0-4063

G&K SERVICES, INC.  
(Exact name of registrant as specified in its charter)

MINNESOTA 41-0449530  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)  
5995 OPUS PARKWAY  
MINNETONKA, MINNESOTA 55343  
(Address of principal executive offices and zip code)  
Registrant's telephone number, including area code (952) 912-5500

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  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  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  Accelerated filer

Non-accelerated filer  (do not check if a smaller reporting company) Smaller reporting company

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

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

Common Stock, par value \$0.50 per share, outstanding  
April 27, 2015 was 19,992,070 shares

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## PART I

## FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## CONDENSED CONSOLIDATED BALANCE SHEETS

## G&amp;K Services, Inc. and Subsidiaries

| (In thousands)  | March 28,<br>2015<br>(Unaudited) | June 28,<br>2014 |
|---|----------------------------------|------------------|
| <b>ASSETS</b>   |                                  |                  |
| Current Assets  |                                  |                  |
| Cash and cash equivalents   | \$ 13,328                        | \$ 37,118        |
| Accounts receivable, less allowance for doubtful accounts of \$3,745 and \$3,697        | 96,934                           | 100,193          |
| Inventory   | 40,102                           | 38,423           |
| Merchandise in service  | 129,643                          | 124,111          |
| Other current assets  | 18,671                           | 27,250           |
| Total current assets  | 298,678                          | 327,095          |
| Property, plant and equipment, less accumulated depreciation of \$377,138 and \$368,672 | 213,239                          | 201,382          |
| Goodwill  | 324,289                          | 333,214          |
| Other assets  | 63,026                           | 61,828           |
| Total assets  | \$ 899,232                       | \$ 923,519       |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                  |                  |
| Current Liabilities   |                                  |                  |
| Accounts payable  | \$ 49,775                        | \$ 44,600        |
| Accrued expenses and other current liabilities  | 69,275                           | 72,640           |
| Deferred income taxes   | 26,088                           | 26,306           |
| Current maturities of long-term debt  | 337                              | 792              |
| Total current liabilities   | 145,475                          | 144,338          |
| Long-term debt, net of current maturities   | 229,000                          | 266,230          |
| Deferred income taxes   | 16,824                           | 17,214           |
| Other noncurrent liabilities  | 121,321                          | 121,693          |
| Total liabilities   | 512,620                          | 549,475          |
| Stockholders' Equity  |                                  |                  |
| Common stock, \$0.50 par value  | 9,985                            | 9,956            |
| Additional paid-in capital  | 74,251                           | 62,864           |
| Retained earnings   | 313,219                          | 297,237          |
| Accumulated other comprehensive income (loss)   | (10,843)                         | ) 3,987          |
| Total stockholders' equity  | 386,612                          | 374,044          |
| Total liabilities and stockholders' equity  | \$ 899,232                       | \$ 923,519       |

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

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## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

G&amp;K Services, Inc. and Subsidiaries

(Unaudited)

| (In thousands, except per share data)                  | For the Three Months Ended |                   | For the Nine Months Ended |                   |
|--|----------------------------|-------------------|---------------------------|-------------------|
|  | March 28,<br>2015          | March 29,<br>2014 | March 28,<br>2015         | March 29,<br>2014 |
| Rental and direct sale revenue                         | \$233,514                  | \$225,046         | \$701,065                 | \$671,188         |
| Operating Expenses                                     |                            |                   |                           |                   |
| Cost of rental and direct sale revenue                 | 154,573                    | 150,284           | 463,018                   | 443,109           |
| Pension withdrawal and associated expenses             | 6,500                      | 8,167             | 6,500                     | 9,854             |
| Selling and administrative                             | 50,840                     | 48,521            | 154,472                   | 148,886           |
| Total operating expenses                               | 211,913                    | 206,972           | 623,990                   | 601,849           |
| Income from Continuing Operations                      | 21,601                     | 18,074            | 77,075                    | 69,339            |
| Interest expense                                       | 1,745                      | 1,560             | 5,463                     | 4,707             |
| Income from Continuing Operations before Income Taxes  | 19,856                     | 16,514            | 71,612                    | 64,632            |
| Provision for income taxes                             | 7,427                      | 6,123             | 25,862                    | 24,288            |
| Net Income from Continuing Operations                  | 12,429                     | 10,391            | 45,750                    | 40,344            |
| Net loss from discontinued operations                  | —                          | (181)             | —                         | (8,393)           |
| Net Income   | \$12,429                   | \$10,210          | \$45,750                  | \$31,951          |
| Basic Earnings (Loss) per Common Share:                |                            |                   |                           |                   |
| From continuing operations                             | \$0.62                     | \$0.52            | \$2.29                    | \$2.04            |
| From discontinued operations                           | \$—                        | \$(0.01)          | \$—                       | \$(0.43)          |
| Basic earnings per share                               | \$0.62                     | \$0.51            | \$2.29                    | \$1.61            |
| Diluted Earnings (Loss) per Common Share:              |                            |                   |                           |                   |
| From continuing operations                             | \$0.61                     | \$0.51            | \$2.24                    | \$2.00            |
| From discontinued operations                           | \$—                        | \$(0.01)          | \$—                       | \$(0.42)          |
| Diluted earnings per share                             | \$0.61                     | \$0.50            | \$2.24                    | \$1.58            |
| Weighted average number of shares outstanding, basic   | 19,679                     | 19,657            | 19,653                    | 19,545            |
| Weighted average number of shares outstanding, diluted | 20,074                     | 19,996            | 20,037                    | 19,924            |
| Dividends Declared per Share                           | \$0.31                     | \$0.27            | \$0.93                    | \$0.81            |

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

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## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

G&amp;K Services, Inc. and Subsidiaries

(Unaudited)

|   | For the Three Months Ended |                   | For the Nine Months Ended |                   |
|---|----------------------------|-------------------|---------------------------|-------------------|
|   | March 28,<br>2015          | March 29,<br>2014 | March 28,<br>2015         | March 29,<br>2014 |
| (In thousands)  |                            |                   |                           |                   |
| Net income  | \$ 12,429                  | \$ 10,210         | \$45,750                  | \$31,951          |
| Other comprehensive income (loss):                            |                            |                   |                           |                   |
| Foreign currency translation adjustments                      | (8,427 )                   | (4,453 )          | (20,475 )                 | (6,632 )          |
| Amortization of actuarial loss on pension benefit obligations | 608                        | 453               | 1,825                     | 1,359             |
| Derivative financial instruments loss recognized              | (6 )                       | (78 )             | (27 )                     | (324 )            |
| Derivative financial instruments loss reclassified            | 132                        | 134               | 405                       | 397               |
| Other comprehensive loss before income taxes                  | (7,693 )                   | (3,944 )          | (18,272 )                 | (5,200 )          |
| Income tax benefit  | (1,006 )                   | (767 )            | (3,442 )                  | (576 )            |
| Other comprehensive loss, net of taxes                        | (6,687 )                   | (3,177 )          | (14,830 )                 | (4,624 )          |
| Total comprehensive income                                    | \$ 5,742                   | \$ 7,033          | \$30,920                  | \$27,327          |

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

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## CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

G&amp;K Services, Inc. and Subsidiaries

(Unaudited)

| (In thousands, except per share data)                            | Shares | Class A<br>Common<br>Stock | Additional<br>Paid-In<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) | Stockholders'<br>Equity |
|--|--------|----------------------------|----------------------------------|----------------------|--|-------------------------|
| Balance June 28, 2014  | 19,912 | \$9,956                    | \$ 62,864                        | \$297,237            | \$ 3,987   | \$ 374,044              |
| Total comprehensive income (loss)                                | —      | —                          | —                                | 45,750               | (14,830 )  | 30,920                  |
| Stock options exercised, net of shares<br>surrendered            | 206    | 103                        | 4,004                            | —                    | —  | 4,107                   |
| Issuance of restricted stock, net                                | 54     | 27                         | (27 )                            | —                    | —  | —                       |
| Share-based compensation   | —      | —                          | 5,320                            | —                    | —  | 5,320                   |
| Shares withheld for taxes under our equity<br>compensation plans | (29 )  | (14 )                      | (1,586 )                         | —                    | —  | (1,600 )                |
| Repurchase of common stock                                       | (175 ) | (87 )                      | —                                | (11,071 )            | —  | (11,158 )               |
| Excess tax benefit from share-based<br>compensation              | —      | —                          | 3,676                            | —                    | —  | 3,676                   |
| Cash dividends (\$0.93 per share)                                | —      | —                          | —                                | (18,697 )            | —  | (18,697 )               |
| Balance March 28, 2015   | 19,968 | \$9,985                    | \$ 74,251                        | \$313,219            | \$ (10,843 )   | \$ 386,612              |

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

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## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

G&amp;K Services, Inc. and Subsidiaries

(Unaudited)

|  | For the Nine Months Ended |                   |
|--|---------------------------|-------------------|
|  | March 28,<br>2015         | March 29,<br>2014 |
| (In thousands)   |                           |                   |
| Operating Activities:  |                           |                   |
| Net income   | \$45,750                  | \$31,951          |
| Adjustments to reconcile net income to net cash provided by operating activities - |                           |                   |
| Depreciation and amortization  | 23,873                    | 23,152            |
| Loss on sale of businesses   | —                         | 12,837            |
| Pension withdrawal and associated expenses   | 6,500                     | 9,854             |
| Deferred income taxes  | 3,624                     | 16,457            |
| Share-based compensation   | 5,320                     | 4,575             |
| Changes in operating items, exclusive of acquisitions and divestitures -           |                           |                   |
| Accounts receivable  | 268                       | (8,565)           |
| Inventory and merchandise in service   | (9,518)                   | (7,478)           |
| Accounts payable   | 6,224                     | (4,154)           |
| Other  | (1,175)                   | (36,087)          |
| Net cash provided by operating activities  | 80,866                    | 42,542            |
| Investing Activities:  |                           |                   |
| Capital expenditures   | (40,022)                  | (23,172)          |
| Divestiture of businesses  | —                         | 6,641             |
| Net cash used for investing activities   | (40,022)                  | (16,531)          |
| Financing Activities:  |                           |                   |
| Repayments of long-term debt   | (675)                     | (18)              |
| Repayments of revolving credit facilities, net                                     | (36,962)                  | —                 |
| Cash dividends paid  | (18,542)                  | (16,057)          |
| Net issuance of common stock, under stock option plans                             | 4,107                     | 8,582             |
| Repurchase of common stock   | (11,158)                  | (8,619)           |
| Shares withheld for taxes under our equity compensation plans                      | (1,600)                   | (1,329)           |
| Excess tax benefit from share-based compensation                                   | 3,676                     | 3,801             |
| Net cash used for financing activities   | (61,154)                  | (13,640)          |
| Effect of Exchange Rates on Cash   | (3,480)                   | (1,426)           |
| (Decrease) Increase in Cash and Cash Equivalents                                   | (23,790)                  | 10,945            |
| Cash and Cash Equivalents:   |                           |                   |
| Beginning of period  | 37,118                    | 38,590            |
| End of period  | \$13,328                  | \$49,535          |
| Supplemental Cash Flow Information:  |                           |                   |
| Cash paid for -  |                           |                   |
| Interest   | \$4,123                   | \$3,405           |
| Income taxes   | \$13,187                  | \$25,465          |
| Supplemental Non-cash Investing Information:                                       |                           |                   |
| Capital expenditures included in accounts payable                                  | \$2,862                   | \$—               |

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





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G&K SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share data)

(Unaudited)

1. Basis of Presentation for Interim Financial Statements

The Condensed Consolidated Financial Statements of G&K Services, Inc. (the "Company," "we," "our," "us" or "G&K") as set forth in this quarterly report have been prepared pursuant to the rules and regulations of the U. S. Securities and Exchange Commission for interim reporting. As permitted under those rules, certain footnotes and other financial information that are normally required by accounting principles generally accepted in the United States can be condensed or omitted. Our accounting policies are described in the Notes to the Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended June 28, 2014 ("fiscal 2014"). Management is responsible for the unaudited Condensed Consolidated Financial Statements included in this document. The Condensed Consolidated Financial Statements included in this document are unaudited but, in the opinion of management, include all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of our financial position as of March 28, 2015, and the results of our operations for the three and nine months ended March 28, 2015 and March 29, 2014 and our cash flows for the nine months ended March 28, 2015 and March 29, 2014.

The results of operations for the three and nine month periods ended March 28, 2015 and March 29, 2014 are not necessarily indicative of the results to be expected for the full year.

This Quarterly Report on Form 10-Q should be read in conjunction with our Consolidated Financial Statements and notes included in our fiscal 2014 Annual Report on Form 10-K.

2. Contingent Liabilities

Environmental Matters

From time-to-time, we are involved in environmental-related proceedings by certain governmental agencies, which relate primarily to allegedly operating certain facilities in noncompliance with required permits. In addition to these proceedings, in the normal course of our business, we are subject to, among other things, periodic inspections by regulatory agencies, and we are involved in the remediation of various properties. As of March 28, 2015 and June 28, 2014, we had reserves of approximately \$1,100 and \$900, respectively, related to these matters. There was \$174 and \$70 of expense for these matters for the three months ended March 28, 2015 and March 29, 2014, respectively, and, \$529 and \$353 for the nine months ended March 28, 2015 and March 29, 2014, respectively.

Legal Matters

The United States Office of Federal Contract Compliance Programs, or OFCCP, is, as part of routine audits, conducting a review of certain of our employment practices. The OFCCP has issued Notices of Violations to four of our facilities. Audits of eight other facilities, where the OFCCP may claim there are similar alleged violations, are ongoing. We have been engaged in discussions with the OFCCP and believe that our practices are lawful and without bias. We are negotiating, on a global basis, to settle with the OFCCP all previously issued Notices of Violations and to resolve all open audits. While we cannot predict the ultimate outcome of these matters with certainty and it is possible that we may incur additional losses in excess of established reserves, we believe the possibility of a material adverse effect on our results of operations or financial position is remote.

See Note 13, "Employee Benefit Plans," of the Notes to the Condensed Consolidated Financial Statements for information regarding disputed amounts related to our withdrawal from the Central States Southeast and Southwest Areas Pension Fund and other multi-employer pension plans.

3. New Accounting Pronouncements

In July 2013, the FASB issued updated guidance to address the presentation of an unrecognized tax benefit when a net operating loss carry-forward, a similar tax loss, or a tax credit carry-forward exists. Specifically, the new guidance requires entities to present an unrecognized tax benefit netted against certain deferred tax assets when specific requirements are met. Our adoption of this guidance in the first quarter of fiscal year 2015 did not have a material impact on our results of operations, financial position or cash flows.

In May 2014, the FASB issued updated guidance to clarify revenue recognition principles. This guidance is intended to improve disclosure requirements and enhance the comparability of revenue recognition practices. Improved disclosures under the amended guidance relate to the nature, amount, timing and uncertainty of revenue that is recognized from

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contracts with customers. This guidance will be effective for us beginning in the first quarter of fiscal 2018. We are currently evaluating the impact this new guidance will have on our Consolidated Financial Statements.

In April 2015, the FASB issued updated guidance which changes the presentation of debt issuance costs in financial statements to present such costs in the balance sheet as a direct deduction from the related debt liability rather than as an asset. Amortization of the costs is reported as interest expense. This guidance will be effective for us beginning in the first quarter of fiscal 2017. We anticipate the implementation of this guidance will not have a material impact on the presentation of our financial position and no impact on our results of operations or cash flows.

#### 4. Fair Value Measurements

Generally accepted accounting principles (GAAP) defines fair value, establishes a framework for measuring fair value and establishes disclosure requirements about fair value measurements. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. We considered non-performance risk when determining fair value of our derivative financial instruments. The fair value hierarchy prescribed under GAAP contains the following three levels:

Level 1 — unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 — other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets in non-active markets;
- inputs other than quoted prices that are observable for the asset or liability; and
- inputs that are derived principally from or corroborated by other observable market data.

Level 3 — unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

We do not have any Level 3 assets or liabilities and we did not transfer any items between fair value levels during the first three quarters of fiscal years 2014 or 2015.

The following tables summarize the assets and liabilities measured at fair value on a recurring basis as of March 28, 2015 and June 28, 2014:

|   | As of March 28, 2015 |           |           |
|---|----------------------|-----------|-----------|
|   | Level 1              | Level 2   | Total     |
| Other assets:                                   |                      |           |           |
| Money market mutual funds                       | \$ 3,916             | \$ —      | \$ 3,916  |
| Equity and fixed income mutual funds            | 30,106               | —         | 30,106    |
| Cash surrender value of life insurance policies | —                    | 14,678    | 14,678    |
| Total assets                                    | \$ 34,022            | \$ 14,678 | \$ 48,700 |
| Accrued expenses:                               |                      |           |           |
| Derivative financial instruments                | \$ —                 | \$ 374    | \$ 374    |
| Total liabilities                               | \$ —                 | \$ 374    | \$ 374    |

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As of June 28, 2014  
Fair Value Measurements Using Inputs Considered as  
Level 1                      Level 2                      Total

|   |           |           |           |
|---|-----------|-----------|-----------|
| Other assets:                                   |           |           |           |
| Money market mutual funds                       | \$ 3,309  | \$ —      | \$ 3,309  |
| Equity and fixed income mutual funds            | 29,358    | —         | 29,358    |
| Cash surrender value of life insurance policies | —         | 14,287    | 14,287    |
| Total assets                                    | \$ 32,667 | \$ 14,287 | \$ 46,954 |
| Accrued expenses:                               |           |           |           |
| Derivative financial instruments                | \$ —      | \$ 930    | \$ 930    |
| Total liabilities                               | \$ —      | \$ 930    | \$ 930    |

The cash surrender value of life insurance policies are primarily investments established to fund the obligations of the Company's non-qualified, non-contributory supplemental executive retirement plan (SERP). The money market, equity and fixed income mutual funds are investments established to fund the obligations of the Company's non-qualified deferred compensation plan.

The following tables summarize the fair values of assets and liabilities that are recorded at historical cost as of March 28, 2015 and June 28, 2014:

As of March 28, 2015  
Fair Value Measurements Using Inputs Considered as  
Level 1                      Level 2                      Total

|   |           |            |            |
|---|-----------|------------|------------|
| Cash and cash equivalents                 | \$ 13,328 | \$ —       | \$ 13,328  |
| Total assets                              | \$ 13,328 | \$ —       | \$ 13,328  |
| Current maturities of long-term debt      | \$ —      | \$ 337     | \$ 337     |
| Long-term debt, net of current maturities | \$ —      | \$ 230,673 | \$ 230,673 |
| Total liabilities                         | \$ —      | \$ 231,010 | \$ 231,010 |

As of June 28, 2014  
Fair Value Measurements Using Inputs Considered as  
Level 1                      Level 2                      Total

|   |           |            |            |
|---|-----------|------------|------------|
| Cash and cash equivalents                 | \$ 37,118 | \$ —       | \$ 37,118  |
| Total assets                              | \$ 37,118 | \$ —       | \$ 37,118  |
| Current maturities of long-term debt      | \$ —      | \$ 792     | \$ 792     |
| Long-term debt, net of current maturities | —         | 263,191    | 263,191    |
| Total liabilities                         | \$ —      | \$ 263,983 | \$ 263,983 |

#### 5. Derivative Financial Instruments

In the ordinary course of business, we are exposed to market risks. We utilize derivative financial instruments to manage interest rate risk and manage the total debt that is subject to variable and fixed interest rates. These interest rate swap contracts modify our exposure to interest rate risk by converting variable rate debt to a fixed rate or by locking in the benchmark interest rate on forecasted issuances of fixed rate debt.

For derivative financial instruments that are designated and qualify as cash flow hedges, the effective portion of the change in fair value on the derivative financial instrument is reported as a component of "Accumulated other comprehensive income" and reclassified into the "Interest expense" line item in the Condensed Consolidated Statements of Operations in the same period as the expenses from the cash flows of the interest expense is recognized. Cash payments or receipts are included in "Net cash provided by operating activities" in the Condensed Consolidated Statements of Cash Flows in the same period as the cash is settled. We perform an assessment at the inception of the hedge and on a quarterly basis thereafter to determine whether our derivatives are highly effective in offsetting changes in the value of the hedged items. Any change in the fair value resulting from hedge ineffectiveness is immediately recognized as income or expense.

We do not have any derivative financial instruments that have been designated as either a fair value hedge, a hedge of a net investment in a foreign operation, or that are held for trading or speculative purposes. Cash flows associated with

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derivative financial instruments are classified in the same category as the cash flows hedged in the Condensed Consolidated Statements of Cash Flows.

Approximately 58% of our outstanding variable rate debt had its interest payments modified using interest rate swap contracts at March 28, 2015.

As of March 28, 2015 and June 28, 2014, we had \$374 and \$930, respectively, of liabilities on interest rate swap contracts that are classified as "Accrued expenses and other current liabilities" in the Condensed Consolidated Balance Sheets. Of the \$1,290 net gain deferred in accumulated other comprehensive income as of March 28, 2015, a \$91 loss is expected to be reclassified to interest expense in the next 12 months.

As of March 28, 2015 and June 28, 2014, all derivative financial instruments were designated as hedging instruments. As of March 28, 2015, we had interest rate swap contracts to pay fixed rates of interest and to receive variable rates of interest based on the three-month London Interbank Offered Rate ("LIBOR"), all of which mature in the next 12 months. The average rate on the \$75,000 of interest rate swap contracts was 1.25% as of March 28, 2015. These interest rate swap contracts are highly effective cash flow hedges and accordingly, gains or losses on any ineffectiveness were not material to any period.

See Note 18, "Subsequent Events," of the Notes to the Condensed Consolidated Financial Statements for an interest rate swap transaction executed subsequent to March 28, 2015.

6. Income Taxes

Our effective tax rate decreased to 36.1% in the nine months ended March 28, 2015 from 37.6% in the nine months ended March 29, 2014. The decrease in the effective tax rate was driven primarily by the release of uncertain tax position accruals in the current year as a result of the expiration of certain tax statutes and the resolution of an uncertain tax position related to fiscal years 2005 to 2007.

7. Earnings Per Share

Accounting Standards Codification (ASC) 260-10-45, Participating Securities and the Two-Class Method (ASC 260-10-45), addresses whether awards granted in unvested share-based payment transactions that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and therefore are included in computing earnings per share under the two-class method. Participating securities are securities that may participate in dividends with common stock and the two-class method is an earnings allocation formula that treats a participating security as having rights to earnings that would otherwise have been available to common shareholders. Under the two-class method, earnings for the period are allocated between common shareholders and other shareholders, based on their respective rights to receive dividends. Certain restricted stock awards granted under our Equity Plans are considered participating securities as these awards receive non-forfeitable dividends at the same rate as common stock.

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The computations of our basic and diluted earnings per share are set forth below:

|   | Three Months Ended |                   | Nine Months Ended |                   |
|---|--------------------|-------------------|-------------------|-------------------|
|   | March 28,<br>2015  | March 29,<br>2014 | March 28,<br>2015 | March 29,<br>2014 |
| Net income from continuing operations   | \$12,429           | \$10,391          | \$45,750          | \$40,344          |
| Less: Income allocable to participating securities  | (235               | ) (142            | ) (771            | ) (560            |
| Net income from continuing operations available to common stockholders                              | \$12,194           | \$10,249          | \$44,979          | \$39,784          |
| Net loss from discontinued operations   | —                  | (181              | ) —               | (8,393            |
| Net income available to common stockholders   | \$12,194           | \$10,068          | \$44,979          | \$31,391          |
| Basic earnings per share (shares in thousands):   |                    |                   |                   |                   |
| Weighted average shares outstanding, basic  | 19,679             | 19,657            | 19,653            | 19,545            |
| Basic earnings (loss) per common share:   |                    |                   |                   |                   |
| From continuing operations  | \$0.62             | \$0.52            | \$2.29            | \$2.04            |
| From discontinued operations  | \$—                | \$(0.01           | ) \$—             | \$(0.43           |
| Basic earnings per share  | \$0.62             | \$0.51            | \$2.29            | \$1.61            |
| Diluted earnings per share (shares in thousands):   |                    |                   |                   |                   |
| Weighted average shares outstanding, basic  | 19,679             | 19,657            | 19,653            | 19,545            |
| Weighted average effect of non-vested restricted stock grants and assumed exercise of stock options | 395                | 339               | 384               | 379               |
| Weighted average shares outstanding, diluted  | 20,074             | 19,996            | 20,037            | 19,924            |
| Diluted earnings (loss) per common share:   |                    |                   |                   |                   |
| From continuing operations  | \$0.61             | \$0.51            | \$2.24            | \$2.00            |
| From discontinued operations  | \$—                | \$(0.01           | ) \$—             | \$(0.42           |
| Diluted earnings per share  | \$0.61             | \$0.50            | \$2.24            | \$1.58            |

We excluded potential common shares related to certain of our outstanding equity compensation grants of 4,000 and 109,000 for the three months ended March 28, 2015 and March 29, 2014, respectively, and 80,000 and 128,000 for the nine months ended March 28, 2015 and March 29, 2014, respectively, from the computation of diluted earnings per share. Inclusion of these shares would have been anti-dilutive.

#### 8. Inventory and Merchandise In Service

The components of inventory as of March 28, 2015 and June 28, 2014 are as follows:

|                 | March 28,<br>2015 | June 28,<br>2014 |
|-----------------|-------------------|------------------|
| Raw materials   | \$9,677           | \$7,952          |
| Work in process | 1,868             | 1,279            |
| Finished goods  | 28,557            | 29,192           |
| Total inventory | \$40,102          | \$38,423         |

We review the estimated useful lives of our merchandise in service assets on a periodic basis or when trends in our business indicate that the useful lives for certain products might have changed. During the fourth quarter of fiscal year 2013, we completed an analysis of certain merchandise in service assets which resulted in the estimated useful lives for these assets being extended to better reflect the estimated periods in which the assets will remain in service. The effect of the change in estimate increased income from operations by \$1,270 and \$5,346, net income by \$806 and \$3,366 and basic and diluted earnings per common share by \$0.04 and \$0.17 for the three and nine months ended March 29, 2014, respectively. The effect of the change in estimate is not material for the three and nine months ended March 28, 2015.

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## 9. Goodwill

Goodwill by segment is as follows:

|  | United States | Canada   | Total      |
|--|---------------|----------|------------|
| Balance as of June 28, 2014            | \$270,045     | \$63,169 | \$333,214  |
| Foreign currency translation and other | —             | (8,925)  | ) (8,925 ) |
| Balance as of March 28, 2015           | \$270,045     | \$54,244 | \$324,289  |

## 10. Long-Term Debt

Long-term debt as of March 28, 2015 and June 28, 2014 consists of the following:

|   | March 28, 2015 | June 28, 2014 |
|---|----------------|---------------|
| Borrowings under \$250 million Revolver           | \$25,900       | \$65,925      |
| Borrowings under \$75 million Variable Rate Notes | 75,000         | 75,000        |
| Borrowings under \$50 million A/R Line            | 28,100         | 25,075        |
| Borrowings under \$100 million Fixed Rate Notes   | 100,000        | 100,000       |
| Capital leases and other                          | 337            | 1,022         |
|   | 229,337        | 267,022       |
| Less current maturities                           | (337)          | ) (792 )      |
| Total long-term debt                              | \$229,000      | \$266,230     |

We have a \$250,000 unsecured revolving credit facility with a syndicate of banks, which expires on March 7, 2017.

Borrowings in U.S. dollars under this credit facility generally bear interest at the adjusted London Interbank Offered Rate ("LIBOR") for specified interest periods plus a margin, which can range from 1.00% to 2.00%, depending on our consolidated leverage ratio.

As of March 28, 2015, there was \$25,900 outstanding under this facility and \$636 in letters of credit outstanding under this facility primarily related to our property and casualty insurance programs. No amounts have been drawn upon these letters of credit. As of March 28, 2015, there is a fee of 0.20% of the unused daily balance of this facility. Availability of credit under this facility requires that we maintain compliance with certain covenants.

The covenants under this agreement are the most restrictive when compared to our other credit facilities. The following table illustrates compliance with regard to the material covenants required by the terms of this facility as of March 28, 2015:

|   | Required | Actual |
|---|----------|--------|
| Maximum Leverage Ratio (Debt/EBITDA)                      | 3.50     | 1.70   |
| Minimum Interest Coverage Ratio (EBITDA/Interest Expense) | 3.00     | 20.99  |

Our maximum leverage ratio and minimum interest coverage ratio covenants are calculated by adding back certain non-cash charges, as defined in our debt agreement.

Borrowings outstanding as of March 28, 2015 under this facility bear interest at a weighted average effective rate of 1.56%.

Amounts outstanding under this facility were refinanced on April 15, 2015. See Note 18, "Subsequent Events," of the Notes to the Condensed Consolidated Financial Statements.

We have \$75,000 of variable rate unsecured private placement notes bearing interest at 0.60% over LIBOR and are scheduled to mature on June 30, 2015. The notes do not require principal payments until maturity. Interest payments are reset and paid on a quarterly basis. As of March 28, 2015, the outstanding balance of the notes was \$75,000 at an effective interest rate of 0.86%. The notes require that we maintain a minimum net worth of \$358,999 as of March 28, 2015. We currently plan to repay these notes on their maturity date using borrowings from our new revolving credit facility, so we continue to classify the \$75,000 as long-term debt in the Condensed Consolidated Balance Sheets.

We maintain a \$50,000 accounts receivable securitization facility, which expires on September 27, 2016. Under the terms of the facility, we pay interest at a rate per annum equal to LIBOR plus a margin of 0.75%. The facility is subject to customary fees, including a rate per annum equal to 0.80%, for the issuance of letters of credit and 0.26% for any unused portion of the facility. As is customary with transactions of this nature, our eligible accounts receivable are sold to a consolidated subsidiary. As of March 28, 2015, there was \$28,100 outstanding under this securitization facility and there





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were \$21,900 of letters of credit outstanding, primarily related to our property and casualty insurance programs. Borrowings outstanding as of March 28, 2015 under this facility bear interest at an average effective interest rate of 0.92%.

We have \$100,000 of fixed rate unsecured senior notes with \$50,000 of the notes bearing interest at a fixed interest rate of 3.73% per annum maturing April 15, 2023 and \$50,000 of the notes bearing interest at a fixed interest rate of 3.88% per annum maturing April 15, 2025. Interest on the notes is payable semiannually. As of March 28, 2015, the outstanding balance of the notes was \$100,000 at an effective interest rate of 3.81%.

See Note 5, "Derivative Financial Instruments," of the Notes to the Condensed Consolidated Financial Statements for details of our interest rate swap and hedging activities related to our outstanding debt.

#### 11. Other Assets and Other Noncurrent Liabilities

Other assets as of March 28, 2015 and June 28, 2014 included the following:

|   | March 28, 2015 | June 28, 2014 |
|---|----------------|---------------|
| Executive deferred compensation plan assets     | \$34,022       | \$32,667      |
| Cash surrender value of life insurance policies | 14,678         | 14,287        |
| Customer contracts, net                         | 4,923          | 6,448         |
| Other assets                                    | 10,991         | 10,603        |
| Less portion classified as current assets       | (1,588         | ) (2,177      |
| Total other assets                              | \$63,026       | \$61,828      |

Customer contracts are as follows:

|                          | March 28, 2015 | June 28, 2014 |
|--------------------------|----------------|---------------|
| Customer contracts       | \$20,219       | \$23,838      |
| Accumulated amortization | (15,296        | ) (17,390     |
| Net                      | \$4,923        | \$6,448       |

The customer contracts associated with business combinations include the combined value of the written service agreements and the related customer relationship. Customer contracts are amortized over a weighted average life of approximately 11 years.

Amortization expense was \$1,560 and \$2,083 for the nine months ended March 28, 2015 and March 29, 2014, respectively. Estimated amortization expense for each of the next five fiscal years based on the intangible assets as of March 28, 2015 is as follows:

|                |       |
|----------------|-------|
| 2015 remaining | \$364 |
| 2016           | 1,393 |
| 2017           | 1,198 |
| 2018           | 416   |
| 2019           | 183   |
| 2020           | 171   |

Other noncurrent liabilities as of March 28, 2015 and June 28, 2014 included the following:

|  | March 28, 2015 | June 28, 2014 |
|--|----------------|---------------|
| Multi-employer pension withdrawal liability      | \$30,265       | \$28,516      |
| Pension plan liability                           | 14,679         | 15,422        |
| Executive deferred compensation plan liability   | 32,534         | 30,584        |
| Supplemental executive retirement plan liability | 16,731         | 16,814        |
| Accrued income taxes                             | 8,700          | 12,043        |
| Workers' compensation liability                  | 14,376         | 14,837        |
| Other liabilities                                | 4,036          | 3,477         |
| Total other noncurrent liabilities               | \$121,321      | \$121,693     |

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## 12. Share-Based Compensation

We grant share-based awards, primarily consisting of restricted stock and options to purchase our common stock. Stock options are granted to employees and directors for a fixed number of shares with an exercise price equal to the fair value of the shares at the date of grant. Share-based compensation is recognized in the Condensed Consolidated Statements of Operations on a straight-line basis over the requisite service period. The amortization of share-based compensation reflects estimated forfeitures adjusted for actual forfeiture experience. As share-based compensation expense is recognized, a deferred tax asset is recorded that represents an estimate of the future tax deduction from the exercise of stock options or release of restrictions on the restricted stock. At the time share-based awards are exercised, canceled, expire or restrictions lapse, we recognize adjustments to income tax expense or additional paid-in capital. Total compensation expense related to share-based awards was \$1,894 and \$1,370 for the three months ended March 28, 2015 and March 29, 2014, respectively, and \$5,208 and \$4,575 for the nine months ended March 28, 2015 and March 29, 2014, respectively. The number of options exercised and restricted stock vested since June 28, 2014, was 330,000 shares.

On August 23, 2012, our Chief Executive Officer was granted a performance based restricted stock award (the "Performance Award"). The Performance Award has both a financial performance component and a service component. The Performance Award has a target level of 100,000 restricted shares, a maximum award of 150,000 restricted shares and a minimum award of 50,000 restricted shares, subject to attainment of financial performance goals and service conditions.

## 13. Employee Benefit Plans

## Defined Benefit Pension Plan

On December 31, 2006, we froze our defined benefit pension plan and related SERP plans for all participants. The components of net periodic pension cost for these plans for the three months ended March 28, 2015 and March 29, 2014 are as follows:

|                           | Pension Plan       |                   | SERP               |                   |
|---------------------------|--------------------|-------------------|--------------------|-------------------|
|                           | Three Months Ended |                   | Three Months Ended |                   |
|                           | March 28,<br>2015  | March 29,<br>2014 | March 28,<br>2015  | March 29,<br>2014 |
| Interest cost             | \$1,012            | \$992             | \$185              | \$189             |
| Expected return on assets | (1,226             | ) (1,159          | ) —                | —                 |
| Amortization of net loss  | 504                | 409               | 98                 | 36                |
| Net periodic pension cost | \$290              | \$242             | \$283              | \$225             |

The components of net periodic pension cost for these plans for the nine months ended March 28, 2015 and March 29, 2014 are as follows:

|                           | Pension Plan      |                   | SERP              |                   |
|---------------------------|-------------------|-------------------|-------------------|-------------------|
|                           | Nine Months Ended |                   | Nine Months Ended |                   |
|                           | March 28,<br>2015 | March 29,<br>2014 | March 28,<br>2015 | March 29,<br>2014 |
| Interest cost             | \$3,036           | \$2,976           | \$555             | \$567             |
| Expected return on assets | (3,678            | ) (3,478          | ) —               | —                 |
| Amortization of net loss  | 1,512             | 1,227             | 294               | 108               |
| Net periodic pension cost | \$870             | \$725             | \$849             | \$675             |

During the first nine-months of fiscal year 2015, we contributed approximately \$145 to the pension plan.

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## Multi-Employer Pension Plans

Historically, we participated in five collectively bargained, union sponsored multi-employer pension plans ("MEPPs"). Consistent with the accounting for defined contribution plans, we previously recorded the required cash contributions to the MEPPs as an expense in the period incurred and recognized a liability for any contributions due and unpaid. In addition, we are responsible for our proportional share of any unfunded vested benefits related to the MEPPs. An employer's accounting for MEPPs (ASC 715-80) provides that a withdrawal liability should be recorded if circumstances that give rise to an obligation become probable and estimable.

We no longer participate in any MEPPs in the United States.

As previously disclosed in our Form 10-Q for the quarterly period ended December 27, 2014, we have received formal demand notices from four of the MEPPs to which we previously contributed and do not expect to receive a demand from the fifth as it is believed to be fully funded. Internally and with outside experts, we evaluated each of the demand notices to determine the appropriateness thereof. We have determined that the demanded amounts are appropriate for two of the MEPPs. With respect to these MEPPs, the withdrawal liabilities are within previously established reserves. However, in the case of the other two MEPPs, we either do not agree with the payment demands or are unable to ascertain the validity and accuracy of the assumptions used. Specifically, in the case of Central States Southeast and Southwest Areas Pension Fund ("Central States Fund"), we believe that, in calculating our withdrawal amount, the Central States Fund has not extended appropriate credit for our partial withdrawal payments as required by applicable law and regulations.

During the third quarter of fiscal year 2015, we entered into settlement discussions and/or requested additional information from the two MEPPs with whose demands we disagree. While we believe our positions are strong, we did so for various reasons, including the costs associated with arbitration and litigation proceedings and future interest expense. In accordance with accounting guidance for contingencies (ASC 450), in the quarter ended March 28, 2015, we increased our reserves by \$6,500 to reflect the impact of these offers and other information received. While we cannot offer any assurance that we will be successful in our negotiations, we do not expect the final resolution of these matters to have a material adverse effect on our results of operations in the period of resolution. However, the ultimate resolution may result in the payment of the entire withdrawal liability or liabilities in the period of resolution, which would be material to our cash flow from operations for that period.

Total pretax charges related to the exit from these MEPPs were \$6,500 for the three and nine month periods ended March 28, 2015, respectively, and \$8,167 and \$9,854 for the three and nine month periods ended March 29, 2014, respectively. Total remaining reserves for all MEPPs as of March 28, 2015 are \$34,546.

During the nine months ended March 28, 2015 and March 29, 2014, we made total payments related to our withdrawal liabilities of \$2,922 and \$1,693 respectively.

## 14. Segment Information

We have two operating segments, United States (includes our Dominican Republic operations) and Canada, which have been identified as components of our organization that are reviewed by our Chief Executive Officer to determine resource allocation and evaluate performance. Each operating segment derives revenues from the branded uniform and facility services programs. No single customer's transactions accounted for more than 2.0% of our total revenues.

We evaluate performance based on income from operations. Financial information by segment for the three and nine month periods ended March 28, 2015 and March 29, 2014 is as follows:

| For the Three Months Ended            | United States | Canada   | Elimination | Total     |
|---------------------------------------|---------------|----------|-------------|-----------|
| March 28, 2015                        |               |          |             |           |
| Revenues                              | \$200,005     | \$33,509 | \$—         | \$233,514 |
| Income from continuing operations     | 17,880        | 3,721    | —           | 21,601    |
| Total assets                          | 858,611       | 128,893  | (88,272 )   | 899,232   |
| Depreciation and amortization expense | 7,181         | 855      | —           | 8,036     |
| March 29, 2014                        |               |          |             |           |
| Revenues                              | \$188,058     | \$36,988 | \$—         | \$225,046 |
| Income from continuing operations     | 12,987        | 5,087    | —           | 18,074    |

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|                                       |         |         |          |           |
|---------------------------------------|---------|---------|----------|-----------|
| Total assets                          | 864,349 | 161,761 | (103,569 | ) 922,541 |
| Depreciation and amortization expense | 6,730   | 995     | —        | 7,725     |

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| For the Nine Months Ended             | United States | Canada    | Elimination | Total     |
|---------------------------------------|---------------|-----------|-------------|-----------|
| March 28, 2015                        |               |           |             |           |
| Revenues                              | \$594,803     | \$106,262 | \$—         | \$701,065 |
| Income from continuing operations     | 64,660        | 12,415    | —           | 77,075    |
| Total assets                          | 858,611       | 128,893   | (88,272 )   | 899,232   |
| Depreciation and amortization expense | 21,089        | 2,784     | —           | 23,873    |
| March 29, 2014                        |               |           |             |           |
| Revenues                              | \$559,821     | \$111,367 | \$—         | \$671,188 |
| Income from continuing operations     | 56,716        | 12,623    | —           | 69,339    |
| Total assets                          | 864,349       | 161,761   | (103,569 )  | 922,541   |
| Depreciation and amortization expense | 20,015        | 3,137     | —           | 23,152    |

## 15. Share Repurchase

As of March 28, 2015, we have a \$175,000 share repurchase program which was originally authorized by our Board of Directors in May 2007 for \$100,000 and increased to \$175,000 in May 2008. Under this repurchase program, we repurchased 56,597 shares in open market transactions totaling \$4,064 for the three months ended March 28, 2015 and 52,800 shares totaling \$3,213 for the three months ended March 29, 2014. We repurchased 174,698 shares totaling \$11,158 for the nine months ended March 28, 2015 and 146,819 shares totaling \$8,619 for the nine months ended March 29, 2014. As of March 28, 2015, we had \$35,006 remaining under this authorization.

## 16. Other Comprehensive Income

Changes in accumulated other comprehensive income, net of tax, for the three and nine months ended March 28, 2015 and March 29, 2014 were as follows:

|  | Three Months Ended March 28, 2015       |                             |                                  |             |
|--|---|-----------------------------|----------------------------------|-------------|
|  | Foreign currency translation adjustment | Pension benefit liabilities | Derivative financial instruments | Total       |
| Accumulated other comprehensive income (loss) at December 27, 2014 | \$13,621                                | \$(18,988 )                 | \$1,211                          | \$(4,156 )  |
| Other comprehensive loss before reclassifications                  | (7,146 )                                | —                           | (3 )                             | (7,149 )    |
| Reclassifications from net accumulated other comprehensive income  | —                                       | 379                         | 83                               | 462         |
| Net current period other comprehensive income (loss)               | (7,146 )                                | 379                         | 80                               | (6,687 )    |
| Accumulated other comprehensive income (loss) at March 28, 2015    | \$6,475                                 | \$(18,609 )                 | \$1,291                          | \$(10,843 ) |
|  | Nine Months Ended March 28, 2015        |                             |                                  |             |
|  | Foreign currency translation adjustment | Pension benefit liabilities | Derivative financial instruments | Total       |
| Accumulated other comprehensive income (loss) at June 28, 2014     | \$22,682                                | \$(19,748 )                 | \$1,053                          | \$3,987     |
| Other comprehensive loss before reclassifications                  | (16,207 )                               | —                           | (16 )                            | (16,223 )   |
| Reclassifications from net accumulated other comprehensive income  | —                                       | 1,139                       | 254                              | 1,393       |
| Net current period other comprehensive income (loss)               | (16,207 )                               | 1,139                       | 238                              | (14,830 )   |
| Accumulated other comprehensive income (loss) at March 28, 2015    | \$6,475                                 | \$(18,609 )                 | \$1,291                          | \$(10,843 ) |

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|  | Three Months Ended March 29, 2014                |                                   |  |          |
|--|--|-----------------------------------|--|----------|
|  | Foreign<br>currency<br>translation<br>adjustment | Pension<br>benefit<br>liabilities | Derivative<br>financial<br>instruments | Total    |
| Accumulated other comprehensive income (loss) at December 28, 2013 | \$22,072   | \$(15,084)                        | \$ 954                                 | \$7,942  |
| Other comprehensive loss before reclassifications                  | (3,497 )   | —                                 | (50 )                                  | (3,547 ) |
| Reclassifications from net accumulated other comprehensive income  | —  | 283                               | 87                                     | 370      |
| Net current period other comprehensive income (loss)               | (3,497 )   | 283                               | 37                                     | (3,177 ) |
| Accumulated other comprehensive income (loss) at March 29, 2014    | \$18,575   | \$(14,801)                        | \$ 991                                 | \$4,765  |
|  | Nine Months Ended March 29, 2014                 |                                   |  |          |
|  | Foreign<br>currency<br>translation<br>adjustment | Pension<br>benefit<br>liabilities | Derivative<br>financial<br>instruments | Total    |
| Accumulated other comprehensive income (loss) at June 29, 2013     | \$24,093   | \$(15,650)                        | \$ 946                                 | \$9,389  |
| Other comprehensive loss before reclassifications                  | (5,518 )   | —                                 | (204 )                                 | (5,722 ) |
| Reclassifications from net accumulated other comprehensive income  | —  | 849                               | 249                                    | 1,098    |
| Net current period other comprehensive income (loss)               | (5,518 )   | 849                               | 45                                     | (4,624 ) |
| Accumulated other comprehensive income (loss) at March 29, 2014    | \$18,575   | \$(14,801)                        | \$ 991                                 | \$4,765  |

Amounts reclassified from accumulated other comprehensive income for the three and nine months ended March 28, 2015 and March 29, 2014 were as follows:

|   | Three Months Ended |                   | Nine Months Ended |                   |     |
|---|--------------------|-------------------|-------------------|-------------------|-----|
|   | March 28,<br>2015  | March 29,<br>2014 | March 28,<br>2015 | March 29,<br>2014 |     |
| Losses on derivative financial instruments: |                    |                   |                   |                   |     |
| Interest rate swap contracts                | \$ 132             | \$ 134            | \$ 405            | \$ 397            | (a) |
| Tax benefit                                 | (49 )              | (47 )             | (151 )            | (148 )            | )   |
| Total, net of tax                           | 83                 | 87                | 254               | 249               |     |
| Pension benefit liabilities:                |                    |                   |                   |                   |     |
| Amortization of net loss                    | 608                | 453               | 1,825             | 1,359             | (b) |
| Tax benefit                                 | (229 )             | (170 )            | (686 )            | (510 )            | )   |
| Total, net of tax                           | 379                | 283               | 1,139             | 849               |     |
| Total amounts reclassified, net of tax      | \$462              | \$370             | \$1,393           | \$1,098           |     |

(a) Included in interest expense.

(b) Included in the computation of net periodic pension cost, which is included in cost of rental and direct sale and selling and administrative. This amount includes a pension plan which is not included in the net periodic pension cost in Note 13 because it is individually immaterial. See Note 13 for details regarding the pension plans.

#### 17. Discontinued Operations

In fiscal year 2014, we sold our Direct Sale Program business ("Program Business") and Ireland business ("Ireland Business"), which met the requirements to be presented as discontinued operations and accordingly, the results of these operations have been reclassified to discontinued operations for all periods presented in the Condensed Consolidated Statements of Operations. Both of these businesses were previously included in our United States operating segment.

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Total aggregate gross proceeds from the sales were \$6,641. Summarized financial information for discontinued operations is shown below:

|   | Three<br>Months<br>Ended<br>March 29,<br>2014 | Nine Months<br>Ended<br>March 29,<br>2014 |
|---|---|---|
| Rental and direct sale revenue from discontinued operations | \$208   | \$17,844                                  |
| Loss before income taxes                                    | (418  | ) (279 )                                  |
| Loss, net of tax  | (227  | ) (141 )                                  |
| Income (Loss) on sale and other adjustments, net of tax     | 46  | (8,252 )                                  |
| Net loss from discontinued operations                       | \$(181  | ) \$(8,393 )                              |
|   |   | Nine Months<br>Ended<br>March 29,<br>2014 |
| Loss in excess of carrying value of Program Business        |   | \$(11,559 )                               |
| Transaction and related costs                               |   | (675 )                                    |
| Loss on sale of Program Business                            |   | (12,234 )                                 |
| Loss on sale of Ireland Business                            |   | (603 )                                    |
| Pretax loss on sale of businesses                           |   | (12,837 )                                 |
| Income tax benefit  |   | 4,585                                     |
| Loss on sale and other adjustments, net of tax              |   | \$(8,252 )                                |



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18. Subsequent Events

On April 15, 2015, we refinanced our existing \$250,000 unsecured revolving credit facility, which was scheduled to expire on March 7, 2017, with a new five-year \$350,000 revolving credit facility maturing on April 15, 2020. Domestic U.S. Dollar borrowings under the new facility bears interest between 1.00% to 1.75% over LIBOR, depending on our leverage ratio and can be expanded by \$200,000, to a total of \$550,000. As of April 15, 2015, there was \$30,000 outstanding under this facility at a weighted average effective rate of 1.44%. The unused portion of the revolver may be used for general corporate purposes, acquisitions, share repurchases, dividends, working capital needs and to provide up to \$45,000 in letters of credit. We intend to use this facility to repay our \$75,000 of variable rate unsecured private placement notes which mature on June 30, 2015.

The material covenants required under the new credit facility are the same as those set forth in our existing credit facility as of March 28, 2015, which are described in Note 10, "Long-Term Debt," of the Notes to the Condensed Consolidated Financial Statements.

In addition, on April 1, 2015, we entered into a long-term interest rate swap for \$75,000 which will limit our exposure to interest rate risk where we will pay fixed rates of interest and receive variable rates of interest based on the one-month LIBOR. We will have an effective interest rate of 2.35%. The 15-year swap contract has a forward start date of July 1, 2016 and is a highly effective cash flow hedge.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(Unaudited)

Overview

G&K Services, Inc., founded in 1902 and headquartered in Minnetonka, Minnesota, is a service-focused market leader of branded uniform and facility services programs. We deliver value to our customers by enhancing their image and brand, and by promoting workplace safety, security and cleanliness. We accomplish this by providing high quality branded work apparel programs, and a variety of facility products and services, including floor mats, towels, mops and restroom hygiene products.

Beginning in fiscal year 2010, we made broad-based improvements to our business, by pursuing a strategy which included four key elements: focusing on customer satisfaction; improving day-to-day execution; increasing our focus on cost management; and addressing underperforming locations and assets. Executing this strategy has led to significant improvements in our financial results, including positive organic revenue growth, expanded operating margins and strong cash flows.

We continue to drive this same strategy in fiscal year 2015. Our approach has four parts:

1. Keep our customer promise
2. Improve how we target customers
3. Drive operational excellence
4. Strengthen our high performing team

To measure the progress of our strategy, in fiscal year 2014 we established long-term financial goals called the "12+ Plan," which includes achieving 12% operating margin, 12% ROIC, plus an added focus on revenue growth, within a two to four year time frame. In the second quarter of fiscal year 2015, we achieved the first of these two targets by achieving a 12.1% operating income margin. We are also focused on maximizing free cash flow, which we define as net cash provided by operating activities less investments in property, plant and equipment.

Our industry continues to consolidate as many family-owned, local operators and regional companies have been acquired by larger providers. We have participated in this consolidation with an acquisition strategy focused on expanding our geographic presence and/or expanding our local market share in order to further leverage our existing production facilities. We remain active in evaluating quality acquisitions that would strengthen our business.

Our operating results are affected by the volatility in commodities, especially cotton, polyester, crude oil and foreign currency exchange rates, which may contribute to significant changes in merchandise and energy costs.

We periodically adjust our operations to serve our customers in the most efficient and cost effective manner. As part of these adjustments, we may realign our workforce, close production or branch facilities or divest operations. We are continuously assessing our business and making adjustments as necessary.

In the second quarter of fiscal year 2014, we divested our Ireland Business and in the third quarter of fiscal year 2014, we sold our Program Business. These divestitures have been reflected as Discontinued Operations in our Condensed Consolidated Statements of Operations. See Note 17, "Discontinued Operations," of the Notes to the Condensed Consolidated Financial Statements for additional information.

Critical Accounting Policies

Our significant accounting policies are described in Note 1, "Summary of Significant Accounting Policies" of the Notes to the Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended June 28, 2014. The accounting policies used in preparing our interim fiscal year 2015 Condensed Consolidated Financial Statements are the same as those described in our Annual Report.

The discussion of the financial condition and results of operations are based upon the Condensed Consolidated Financial Statements, which have been prepared in conformity with United States generally accepted accounting principles (GAAP). As such, management is required to make certain estimates, judgments and assumptions that are believed to be reasonable based on the information available. These estimates and assumptions affect the reported amount of assets and liabilities, revenues and expenses, and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results may differ from these estimates under different assumptions or conditions.



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Critical accounting policies are defined as the most important and pervasive accounting policies, areas most sensitive to material changes from external factors and those that are reflective of significant judgments and estimates. Our critical accounting policies are those related to:

Revenue recognition

Employee benefit plans

Income taxes

Share based payments

Derivative financial instruments

Goodwill and intangible assets

Inventory and merchandise in service

Inventory and Merchandise In Service

We review the estimated useful lives of our merchandise in service assets on a periodic basis or when trends in our business indicate that the useful lives for certain products might have changed. During the fourth quarter of fiscal year 2013, we completed an analysis of certain merchandise in service assets which resulted in the estimated useful lives for these assets being extended to better reflect the estimated periods in which the assets will remain in service. The effect of the change in estimate increased income from operations by \$1.3 million and \$5.3 million, net income by \$0.8 million and \$3.4 million and basic and diluted earnings per common share by \$0.04 and \$0.17 for the three and nine months ended March 29, 2014. The effect of the change in estimate is not material for the three and nine months ended March 28, 2015.

#### Results of Operations

The percentage relationships to revenues of certain income and expense items for the three and nine month periods ended March 28, 2015 and March 29, 2014, and the percentage changes in these income and expense items between periods are presented in the following table:

|   | Three Months Ended |                   | Nine Months Ended |                   | Percentage Change                      |                                       |   |
|---|--------------------|-------------------|-------------------|-------------------|--|---------------------------------------|---|
|   | March 28,<br>2015  | March 29,<br>2014 | March 28,<br>2015 | March 29,<br>2014 | Three Months<br>FY 2015<br>vs. FY 2014 | Nine Months<br>FY 2015<br>vs. FY 2014 |   |
| Rental and direct sale revenue                        | 100.0              | % 100.0           | % 100.0           | % 100.0           | % 3.8                                  | % 4.5                                 | % |
| Cost of rental and direct sale revenue                | 66.2               | 66.8              | 66.0              | 66.0              | 2.9                                    | 4.5                                   |   |
| Gross margin  | 33.8               | 33.2              | 34.0              | 34.0              | 5.6                                    | 4.4                                   |   |
| Pension withdrawal and associated expenses            | 2.8                | 3.6               | 0.9               | 1.5               | (20.4                                  | ) (34.0                               | ) |
| Selling and administrative                            | 21.8               | 21.6              | 22.0              | 22.2              | 4.8                                    | 3.8                                   |   |
| Income from continuing operations                     | 9.3                | 8.0               | 11.0              | 10.3              | 19.5                                   | 11.2                                  |   |
| Interest expense                                      | 0.7                | 0.7               | 0.8               | 0.7               | 11.9                                   | 16.1                                  |   |
| Income from continuing operations before income taxes | 8.5                | 7.3               | 10.2              | 9.6               | 20.2                                   | 10.8                                  |   |
| Provision for income taxes                            | 3.2                | 2.7               | 3.7               | 3.6               | 21.3                                   | 6.5                                   |   |
| Net income from continuing operations                 | 5.3                | 4.6               | 6.5               | 6.0               | 19.6                                   | 13.4                                  |   |
| Net loss from discontinued operations                 | —                  | (0.1              | ) —               | (1.3              | )                                      |                                       |   |
| Net income  | 5.3                | % 4.5             | % 6.5             | % 4.8             | % 21.7                                 | % 43.2                                | % |

Three months ended March 28, 2015 compared to three months ended March 29, 2014

Rental and Direct Sale Revenue. Total revenue in the third quarter of fiscal 2015 increased \$8.5 million or 3.8% to \$233.5 million from \$225.0 million in the third quarter of fiscal 2014. Our organic growth rate was 5.4% compared to 4.9% in the same period of the prior fiscal year. The 5.4% organic growth rate in the current quarter was driven by record new account sales over the past 12 months, improved merchandise recovery billings and pricing. The positive

organic growth was offset by the negative impact of foreign currency translation rates. Our organic growth rate is calculated using rental and direct sale revenue, adjusted to exclude the impact of foreign currency exchange rate changes, divestitures and acquisitions. We believe that the organic revenue reflects the growth of our existing business and is, therefore, useful in analyzing our financial condition and results of operations.

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**Cost of Rental and Direct Sale Revenue.** Cost of rental and direct sale revenue, which includes merchandise, production, delivery and cost of direct sale expenses, increased 2.9% to \$154.6 million in the third quarter of fiscal 2015 from \$150.3 million in the same period of fiscal 2014. Excluding the \$1.3 million benefit from the change in merchandise lives recorded in the prior year, gross margin improved 110 basis points in the current year. This improvement was primarily due to significantly lower energy costs, continued productivity improvements in our laundry operations, lower payroll taxes and the favorable impact of fixed costs absorbed over a higher revenue base. These favorable items were partially offset by higher merchandise expense resulting from higher new account sales, a greater mix of higher priced specialty garments and higher workers compensation expense.

**Pension Withdrawal and Associated Expenses.** As discussed in Note 13, "Employee Benefit Plans," of the Notes to the Condensed Consolidated Financial Statements, we recorded a charge of \$6.5 million in the third quarter of fiscal 2015 and a charge of \$8.2 million in the third quarter of fiscal 2014 related to our withdrawal from all MEPPs.

**Selling and Administrative.** Selling and administrative expenses increased 4.8% to \$50.8 million in the third quarter of fiscal 2015 from \$48.5 million in the same period of fiscal 2014. As a percentage of total revenues, selling and administrative expenses increased to 21.8% in the third quarter of fiscal 2015 from 21.6% in the third quarter of fiscal 2014. The increase as a percentage of revenue was primarily due to higher equity compensation, workers compensation and bad debt expense.

**Income from Operations.** The following is a summary of each operating segment's income from operations (in thousands):

|               | Three Months Ended |                   |          |
|---------------|--------------------|-------------------|----------|
|               | March 28,<br>2015  | March 29,<br>2014 | Change   |
| United States | \$17,880           | \$12,987          | \$4,893  |
| Canada        | 3,721              | 5,087             | (1,366 ) |
| Total         | \$21,601           | \$18,074          | \$3,527  |

**United States.** Income from operations increased \$4.9 million to \$17.9 million in the third quarter of fiscal 2015 from \$13.0 million in the same period of fiscal 2014. The current year and prior year operating income included additional expense of \$6.5 million and \$8.2 million, respectively, associated with our MEPP withdrawal liability and a \$1.1 million benefit from the change in merchandise lives previously reported. Excluding these items, income from operations increased \$4.3 million. The increase was primarily driven by additional income from increased revenue, lower energy costs and improved productivity in our laundry operations. These favorable items were partially offset by higher merchandise expense and workers compensation.

**Canada.** Income from operations decreased \$1.4 million in the third quarter of fiscal 2015 compared to the same period of fiscal 2014. The prior year operating income included a \$0.2 million benefit from the change in merchandise lives previously reported. Excluding this item, income from operations decreased \$1.2 million. The decrease was primarily driven by the decline in the Canadian foreign exchange rate, higher selling costs and higher delivery costs. The unfavorable items were partially offset by lower energy costs, lower vehicle maintenance costs and improved productivity in our laundry operations.

**Interest Expense.** Interest expense was \$1.7 million in the third quarter of fiscal 2015, an increase from the \$1.6 million reported in the same period of fiscal 2014. The increased interest expense was due to higher average debt balances resulting from the payment of the special dividend in the fourth quarter of fiscal 2014, partially offset by lower average interest rates.

**Provision for Income Taxes.** Our effective tax rate increased to 37.4% in the third quarter of fiscal 2015 from 37.1% in the same period of fiscal 2014. The increase in the effective tax rate was driven primarily by state tax credits generated in the prior fiscal year.

**Discontinued Operations.** In the second quarter of fiscal 2014, we divested our Ireland Business and in the third quarter of fiscal year 2014, we sold our Program Business. These businesses have been reflected as discontinued operations in our Condensed Consolidated Statements of Operations. The pretax loss recognized in the third quarter of fiscal year 2014 relates to two days of operations for the Program Business and adjustments to the final sales price. See Note 17, "Discontinued Operations," of the Notes to the Condensed Consolidated Financial Statements for

additional information.

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Nine months ended March 28, 2015 compared to nine months ended March 29, 2014

**Rental and Direct Sale Revenue.** Total revenue in the first nine months of fiscal 2015 increased \$29.9 million or 4.5% to \$701.1 million from \$671.2 million in the first nine months of fiscal 2014. Our organic growth rate was 5.7% compared to 4.1% in the same period of the prior fiscal year. The 5.7% organic growth rate in the current year was driven by strong new account sales, higher merchandise recovery billings, pricing and an increase in direct sales revenue. The positive organic growth was offset by the negative impact of foreign currency translation rates. Our organic growth rate is calculated using rental and direct sale revenue, adjusted to exclude the impact of foreign currency exchange rate changes, divestitures and acquisitions. We believe that the organic revenue reflects the growth of our existing business and is, therefore, useful in analyzing our financial condition and results of operations.

**Cost of Rental and Direct Sale Revenue.** Cost of rental and direct sale revenue, which includes merchandise, production, delivery and cost of direct sale expenses, increased 4.5% to \$463.0 million in the first nine months of fiscal 2015 from \$443.1 million in the same period of fiscal 2014. Excluding the \$5.3 million benefit from the change in merchandise lives recorded in the prior year, gross margin improved 80 basis points in the current year. This improvement was primarily due to continued productivity improvements in our laundry and delivery operations, the favorable impact of fixed costs absorbed over a higher revenue base and lower energy costs. These favorable items were partially offset by higher merchandise and workers compensation expense.

**Pension Withdrawal and Associated Expenses.** As discussed in Note 13, "Employee Benefit Plans," of the Notes to the Condensed Consolidated Financial Statements, we recorded a charge of \$6.5 million in the first nine months of fiscal 2015 and a charge of \$9.9 million in the first nine months of fiscal 2014 related to our withdrawal from all MEPPs.

**Selling and Administrative.** Selling and administrative expenses increased 3.8% to \$154.5 million in the first nine months of fiscal 2015 from \$148.9 million in the same period of fiscal 2014. As a percentage of total revenues, selling and administrative expenses decreased to 22.0% in the first nine months of fiscal 2015 from 22.2% in the first nine months of fiscal 2014. The decrease as a percentage of revenue was primarily due to effective cost control as we leveraged our fixed costs over a higher revenue base, offset by higher sales commissions.

**Income from Operations.** The following is a summary of each operating segment's income from operations (in thousands):

|               | Nine Months Ended |                   | Change  |
|---------------|-------------------|-------------------|---------|
|               | March 28,<br>2015 | March 29,<br>2014 |         |
| United States | \$64,660          | \$56,716          | \$7,944 |
| Canada        | 12,415            | 12,623            | (208 )  |
| Total         | \$77,075          | \$69,339          | \$7,736 |

**United States.** Income from operations increased \$7.9 million to \$64.7 million in the first nine months of fiscal 2015 from \$56.7 million in the same period of fiscal 2014. The current year and prior year operating income included additional expense of \$6.5 million and \$9.9 million, respectively, associated with our MEPP withdrawal liability and a \$4.6 million benefit from the change in merchandise lives previously reported. Excluding these items, income from operations increased \$9.1 million. The increase was primarily driven by additional income from increased revenue, lower energy costs and improved productivity in our laundry operations. These favorable items were partially offset by higher merchandise expense.

**Canada.** Income from operations decreased \$0.2 million in the first nine months of fiscal 2015 compared to the same period of fiscal 2014. The prior year operating income included a \$0.7 million benefit from the change in merchandise lives previously reported. Excluding this item, income from operations increased \$0.5 million. The increase was primarily driven by additional income from increased revenue, improved productivity in our laundry operations, lower vehicle maintenance costs, lower energy costs and lower environmental related expenses. These favorable items were partially offset by a decrease in the Canadian foreign exchange rate and higher selling expenses due to higher staffing levels and higher commissions.

**Interest Expense.** Interest expense was \$5.5 million in the first nine months of fiscal 2015, an increase from the \$4.7 million reported in the same period of fiscal 2014. The increased interest expense was due to higher average debt balances resulting from the payment of the special dividend in the fourth quarter of fiscal 2014, partially offset by



lower average interest rates.

**Provision for Income Taxes.** Our effective tax rate decreased to 36.1% in the first nine months of fiscal 2015 from 37.6% in the same period of fiscal 2014. The decrease in the effective tax rate was driven primarily by the release of uncertain tax position accruals in the current year as a result of the expiration of certain tax statutes and the resolution of an uncertain tax position related to fiscal years 2005 to 2007.

**Discontinued Operations.** In the second quarter of fiscal 2014, we divested our Ireland Business and in the third quarter of fiscal year 2014, we sold our Program Business. These businesses have been reflected as discontinued operations in our

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Condensed Consolidated Statements of Operations. The pretax loss recognized includes the loss on sale totaling \$12.8 million and a loss from the discontinued operations totaling \$0.3 million. See Note 17, "Discontinued Operations," of the Notes to the Condensed Consolidated Financial Statements for additional information.

### Liquidity, Capital Resources and Financial Condition

Our primary sources of cash are net cash flows from operations, borrowings under our debt arrangements and proceeds from the net issuance of common stock under stock option plans. Primary uses of cash are working capital needs, capital expenditures, acquisitions, dividends, share repurchases and general corporate purposes.

Working capital at March 28, 2015 was \$153.2 million, a \$29.6 million decrease from \$182.8 million at June 28, 2014. The decrease in working capital is primarily due to the repatriation of cash from our Canadian operations, which was used to pay down our existing revolving credit facility. This decrease was offset by an increase in merchandise in service to support our revenue growth. As of March 28, 2015, approximately \$8.3 million of cash was held in our Canadian subsidiaries, none of which was considered to be permanently reinvested and therefore could be repatriated without significant additional income tax consequences.

Operating Activities. Net cash provided by operating activities increased \$38.4 million to \$80.9 million in the first nine months of fiscal 2015 from \$42.5 million in the same period of fiscal 2014. The increase was primarily due to higher net income, better working capital management related to both accounts receivable and accounts payable in the current fiscal year, and lower federal income tax payments.

Investing Activities. Net cash used for investing activities was \$40.0 million in the first nine months of fiscal 2015 compared to \$16.5 million in the same period of fiscal 2014. The increase was primarily due to increased capital expenditures related to certain information technology projects and expanding our plant capacity and the divestiture of our Program and Ireland businesses in the prior fiscal year.

Financing Activities. Cash used for financing activities was \$61.2 million in the first nine months of fiscal 2015 compared to \$13.6 million in the same period of fiscal 2014. The change was primarily due to repayments on our revolving credit facility resulting from the repatriation of Canadian cash, an increase in our quarterly dividend from \$0.27 to \$0.31, an increase in the repurchase of our common stock and a decrease in the proceeds from exercise of employee stock options.

See Note 10, "Long-Term Debt," and Note 18, "Subsequent Events," of the Notes to the Condensed Consolidated Financial Statements for details of our long-term debt and information on the refinancing of our revolving credit facility and interest rate swap transactions executed subsequent to the third quarter of fiscal 2015.

See Note 5, "Derivative Financial Instruments," of the Notes to the Condensed Consolidated Financial Statements for details of our interest rate swap and hedging activities related to our outstanding debt.

Cash Obligations. Under various agreements, we are obligated to make future cash payments in fixed amounts. These include payments under the revolving credit facility, capital lease obligations and rent payments required under operating leases with initial or remaining terms in excess of one year.

At March 28, 2015, we had approximately \$223.5 million of available capacity under our revolving and accounts receivable credit facilities, of which our revolving credit facility contributes all of the liquidity. We anticipate that our cash flows from operations and our available capacity under our credit facilities will be sufficient to satisfy our cash commitments and capital requirements for fiscal 2015. We may utilize borrowings under the revolving credit facility to supplement our cash requirements from time to time. We estimate that capital expenditures in fiscal 2015 will be approximately \$52.5 million.

### Off Balance Sheet Arrangements

At March 28, 2015, we had approximately \$22.5 million of stand-by letters of credit that were issued and outstanding, primarily in connection with our property and casualty insurance programs. No amounts have been drawn upon these letters of credit.

### Pension Obligations

Pension expense is recognized on an accrual basis over the employees' approximate service periods. Pension expense is generally independent of funding decisions or requirements. We recognized expense for our defined benefit pension plan of \$0.3 million and \$0.2 million in the third quarter of fiscal 2015 and fiscal 2014, respectively. At June 28, 2014, the fair value of our pension plan assets totaled \$76.0 million.

On December 31, 2006, we froze our defined benefit pension plan and related SERP plans for all participants.

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### Multi-Employer Pension Plans

Historically, we participated in five collectively bargained, union sponsored multi-employer pension plans ("MEPPs"). Consistent with the accounting for defined contribution plans, we previously recorded the required cash contributions to the MEPPs as an expense in the period incurred and recognized a liability for any contributions due and unpaid. In addition, we are responsible for our proportional share of any unfunded vested benefits related to the MEPPs. An employer's accounting for MEPPs (ASC 715-80) provides that a withdrawal liability should be recorded if circumstances that give rise to an obligation become probable and estimable.

We no longer participate in any MEPPs in the United States.

As previously disclosed in our Form 10-Q for the quarterly period ended December 27, 2014, we have received formal demand notices from four of the MEPPs to which we previously contributed and do not expect to receive a demand from the fifth as it is believed to be fully funded. Internally and with outside experts, we evaluated each of the demand notices to determine the appropriateness thereof. We have determined that the demanded amounts are appropriate for two of the MEPPs. With respect to these MEPPs, the withdrawal liabilities are within previously established reserves. However, in the case of the other two MEPPs, we either do not agree with the payment demands or are unable to ascertain the validity and accuracy of the assumptions used. Specifically, in the case of Central States Southeast and Southwest Areas Pension Fund ("Central States Fund"), we believe that, in calculating our withdrawal amount, the Central States Fund has not extended appropriate credit for our partial withdrawal payments as required by applicable law and regulations.

During the third quarter of fiscal year 2015, we entered into settlement discussions and/or requested additional information from the two MEPPs with whose demands we disagree. While we believe our positions are strong, we did so for various reasons, including the costs associated with arbitration and litigation proceedings and future interest expense. In accordance with accounting guidance for contingencies (ASC 450), in the quarter ended March 28, 2015, we increased our reserves by \$6.5 million to reflect the impact of these offers and other information received. While we cannot offer any assurance that we will be successful in our negotiations, we do not expect the final resolution of these matters to have a material adverse effect on our results of operations in the period of resolution. However, the ultimate resolution may result in the payment of the entire withdrawal liability or liabilities in the period of resolution, which would be material to our cash flow from operations for that period.

Total pretax charges related to the exit from all MEPPs were \$6.5 million for the three and nine month periods ended March 28, 2015, respectively, and \$8.2 million and \$9.9 million for the three and nine month periods ended March 29, 2014, respectively. Total remaining reserves for all MEPPs as of March 28, 2015 are \$34.5 million, which include both current and long-term portions of these reserves.

During the nine months ended March 28, 2015 and March 29, 2014, we made total payments related to our withdrawal liabilities of \$2.9 million and \$1.7 million, respectively.

### Litigation

We are involved in a variety of legal actions relating to personal injury, employment, environmental and other legal matters that arise in the normal course of business. In addition, we are party to certain additional legal matters described in "Part II Item 1. Legal Proceedings" of this report.

### Cautionary Statements Regarding Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a safe harbor from civil litigation for forward-looking statements. Forward-looking statements may be identified by words such as "estimates," "anticipates," "projects," "plans," "expects," "intends," "believes," "seeks," "could," "should," "may" and "will" or the negative versions thereof and similar expressions and by the context in which they are used. Such statements are based upon our current expectations and speak only as of the date made. These statements are subject to various risks, uncertainties and other factors that could cause actual results to differ from those set forth in or implied by this Form 10-Q. Factors that might cause such a difference include, but are not limited to, the possibility of greater than anticipated operating costs, lower sales volumes, the performance and costs of integration of acquisitions or assumption of unknown liabilities in connection with acquisitions, fluctuations in costs of materials and labor, costs and possible effects of union organizing or other union activities, strikes, loss of key management, uncertainties regarding any existing or newly-discovered expenses and liabilities related to environmental compliance and remediation, failure to achieve and

maintain effective internal controls for financial reporting required by the Sarbanes-Oxley Act of 2002, the initiation or outcome of arbitrations, litigation or governmental investigations, higher than assumed sourcing or distribution costs of products, the disruption of operations from catastrophic events, disruptions in capital markets, the liquidity of counterparties in financial transactions, changes in federal and state tax laws, economic uncertainties and the reactions of competitors in terms of price and service. We undertake no obligation to update any forward-looking statements to reflect events or circumstances arising after the date on which they are made, except as required by law. Additional information

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concerning potential factors that could affect future financial results is included in our Annual Report on Form 10-K for the fiscal year ended June 28, 2014.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

**Interest Rate Risk**

We are subject to market risk exposure related to changes in interest rates. We use financial instruments such as interest rate swap agreements to manage interest rate risk on our variable rate debt. Under these arrangements, we agree to exchange, at specified intervals, the difference between fixed and floating interest amounts, calculated by reference to an agreed upon notional principal amount. Interest rate swap agreements are entered into for periods consistent with related underlying exposures and do not constitute positions independent of those exposures. The estimated exposure considers the mitigating effects of interest rate swap agreements outstanding at March 28, 2015 on the change in the cost of variable rate debt. The current fair market value of all outstanding contracts at March 28, 2015 was an unrealized loss of \$0.4 million.

A sensitivity analysis was performed to measure our interest rate risk over a one-year period to changes in market interest rates for forecasted variable rate debt that was not modified by interest rate swaps. As of March 28, 2015, this debt amount was \$65.1 million. The two scenarios include measuring the sensitivity to interest expense with an immediate 50 basis point change in market interest rates and the impact of a 50 basis point change distributed evenly throughout the year. Based on the forecasted average variable rate debt level, the forecasted annual expense for our variable rate debt is \$1.0 million. The scenario with an immediate 50 basis point change would increase or decrease forecasted interest by \$0.3 million or 40.7%. The scenario that distributes the 50 basis point change would increase or decrease interest expense by \$0.2 million or 25.7%.

**Energy Cost Risk**

We are subject to market risk exposure related to changes in energy costs. To manage this risk, from time to time we have utilized derivative financial instruments to mitigate the impact of motor fuel cost volatility on our future financial results. As of March 28, 2015, we have no outstanding derivative financial instruments related to motor fuels.

We performed an analysis to measure the sensitivity of our energy costs to changes in the prices of motor fuels. The analysis used motor fuel prices at March 28, 2015 and forecasted purchases over the next 12 months. For each one percentage point increase or decrease in motor fuel prices under these assumptions, our motor fuel costs would change by approximately \$0.2 million.

Production costs at our plants are also subject to fluctuations in natural gas costs. To reduce our exposure to changes in natural gas prices, we utilize natural gas supply contracts in the normal course of business. These contracts meet the definition of "normal purchase" and, therefore, are not considered derivative instruments for accounting purposes.

**Foreign Currency Exchange Risk**

Our only material foreign subsidiaries are located in Canada. The assets and liabilities of these subsidiaries are denominated in the Canadian dollar and, as such, are translated into U.S. dollars at the exchange rate in effect at the balance sheet date. Results of operations are translated using the average exchange rates throughout the period. The effect of exchange rate fluctuations on translation of assets and liabilities are recorded as a component of stockholders' equity and are included in the "Accumulated other comprehensive income" line item of the Condensed Consolidated Balance Sheets. Gains and losses from foreign currency transactions are included in results of operations.

**ITEM 4. CONTROLS AND PROCEDURES**

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) or Rule 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this Form 10-Q. Based on their evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective.

There have been no changes in our internal controls over financial reporting that occurred during the period covered by this Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



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## PART II

## OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

We are involved in a variety of legal actions relating to personal injury, employment, environmental and other legal matters arising in the normal course of business, including, without limitation, those described below.

The United States Office of Federal Contract Compliance Programs, or OFCCP, is, as part of routine audits, conducting a review of certain of our employment practices. The OFCCP has issued Notices of Violations to four of our facilities. Audits of 8 other facilities, where the OFCCP may claim there are similar alleged violations, are ongoing. We have been engaged in discussions with the OFCCP and believe that our practices are lawful and without bias. We are negotiating, on a global basis, to settle with the OFCCP all previously issued Notices of Violations and to resolve all open audits. While we cannot predict the ultimate outcome of these matters with certainty and it is possible that we may incur additional losses in excess of established reserves, we believe the possibility of a material adverse effect on our results of operations or financial position is remote.

See Note 13, "Employee Benefit Plans," of the Notes to the Condensed Consolidated Financial Statements for information on our arbitration related to our withdrawal from the Central States Plan.

## ITEM 1A. RISK FACTORS

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended June 28, 2014, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently believe are immaterial could have a material adverse effect on our business, financial condition and/or operating results.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The table below sets forth information regarding repurchases we made of our common stock during the periods indicated.

| Period                               | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plan | Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plan |
|--------------------------------------|----------------------------------|------------------------------|---|---|
| December 28, 2014 - January 31, 2015 | —                                | \$—                          | —   | \$39,070,821  |
| February 1, 2015 - February 28, 2015 | 35,400                           | \$72.26                      | 35,400  | \$36,512,969  |
| March 1, 2015 - March 28, 2015       | 21,197                           | \$71.09                      | 21,197  | \$35,006,136  |
| Total                                | 56,597                           | \$71.82                      | 56,597  | \$35,006,136  |

As of March 28, 2015, we have a \$175.0 million share repurchase program which was originally authorized by our Board of Directors in May 2007 for \$100.0 million and increased to \$175.0 million in May 2008. Under this repurchase program, we repurchased 56,597 shares in open market transactions totaling \$4.1 million for the three months ended March 28, 2015 and 52,800 shares totaling \$3.2 million for the three months ended March 29, 2014. We repurchased 174,698 shares totaling \$11.2 million for the nine months ended March 28, 2015 and 146,819 shares totaling \$8.6 million for the nine months ended March 29, 2014. As of March 28, 2015, we had \$35.0 million remaining under this authorization.

## ITEM 6. EXHIBITS

## a. Exhibits

10.1 Credit Agreement dated April 15, 2015 (incorporated by reference to Exhibit 10.1 of Current Report on Form 8-K filed on April 20, 2015).



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- 31.1 Certification of Chief Executive Officer pursuant to Securities Exchange Act 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 Securities Exchange Act 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.
- 101 Financial statements from the quarterly report on Form 10-Q of G&K Services, Inc. for the quarter ended March 28, 2015, formatted in Extensible Business Reporting Language (XBRL): (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Operations, (iii) the Condensed Consolidated Statements of Comprehensive Income, (iv) the Condensed Consolidated Statements of Stockholders' Equity, (v) the Condensed Consolidated Statements of Cash Flows, and (vi) Notes to Condensed Consolidated Financial Statements.

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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.

G&K SERVICES, INC.  
(Registrant)

Date: April 30, 2015

By: /s/ Tracy C. Jokinen  
Tracy C. Jokinen  
Chief Financial Officer  
(Principal Financial Officer)

Date: April 30, 2015

By: /s/ Thomas J. Dietz  
Thomas J. Dietz  
Vice President and Controller  
(Principal Accounting Officer)