

LANDEC CORP \CA\
Form 10-Q
April 02, 2015

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 Fiscal Quarter Ended March 1, 2015, or

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

For the transition period from _____ to _____.

Commission file number: **0-27446**

LANDEC CORPORATION

(Exact name of registrant as specified in its charter)

Delaware **94-3025618**
(State or other jurisdiction of (IRS Employer
incorporation or organization) Identification Number)

3603 Haven Avenue

Menlo Park, California 94025

(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code:

(650) 306-1650

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 at least the past 90 days.

Yes X No ___

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

Yes X 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 definition of "large accelerated filer" and "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer ___ Accelerated Filer X
Non Accelerated Filer ___ 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 X

As of March 26, 2015, there were 26,947,394 shares of Common Stock outstanding.

LANDEC CORPORATION

FORM 10-Q For the Fiscal Quarter Ended March 1, 2015

INDEX

| | Page |
|---|------|
| Facing sheet | 1 |
| Index | 2 |
| | |
| Part I. Financial Information | |
| Item 1. Financial Statements | |
| a) Consolidated Balance Sheets as of March 1, 2015 and May 25, 2014 | 3 |
| b) Consolidated Statements of Comprehensive Income for the Three Months and Nine Months Ended March 1, 2015 and February 23, 2014 | 4 |
| c) Consolidated Statements of Cash Flows for the Nine Months Ended March 1, 2015 and February 23, 2014 | 5 |
| d) Notes to Consolidated Financial Statements | 6 |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations | 20 |
| Item 3. Quantitative and Qualitative Disclosures About Market Risk | 30 |
| Item 4. Controls and Procedures | 30 |
| Part II. Other Information | 31 |
| Item 1. Legal Proceedings | 31 |
| Item 1A. Risk Factors | 31 |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds | 31 |

| | |
|---|----|
| Item 3. Defaults Upon Senior Securities | 31 |
| Item 4. Mine Safety Disclosures | 31 |
| Item 5. Other Information | 31 |
| Item 6. Exhibits | 31 |
| Signatures | 32 |

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements****LANDEC CORPORATION****CONSOLIDATED BALANCE SHEETS****(In thousands except shares and per share amounts)**

| | March 1, 2015 (unaudited) | May 25, 2014 (1) |
|--|------------------------------|---------------------|
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 15,695 | \$ 14,243 |
| Accounts receivable, less allowance for doubtful accounts of \$418 and \$516 at March 1, 2015 and May 25, 2014, respectively | 45,275 | 44,421 |
| Accounts receivable, related party | 35 | 304 |
| Income taxes receivable | 1,211 | 2,000 |
| Inventories, net | 24,662 | 24,735 |
| Deferred taxes | 1,987 | 2,056 |
| Prepaid expenses and other current assets | 3,626 | 3,170 |
| Total Current Assets | 92,491 | 90,929 |
| Investment in non-public company, non-fair value | — | 793 |
| Investment in non-public company, fair value | 61,100 | 39,600 |
| Property and equipment, net | 78,960 | 74,140 |
| Goodwill, net | 49,620 | 49,620 |
| Trademarks/tradenames, net | 48,428 | 48,428 |
| Customer relationships, net | 8,056 | 8,720 |
| Other assets | 1,648 | 1,393 |
| Total Assets | \$ 340,303 | \$ 313,623 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current Liabilities: | | |
| Accounts payable | \$ 28,166 | \$ 31,981 |
| Accounts payable, related party | 146 | 134 |
| Accrued compensation | 4,744 | 4,096 |
| Other accrued liabilities | 4,791 | 4,871 |
| Deferred revenue | 1,102 | 1,254 |
| Lines of credit | 9,300 | — |
| Current portion of long-term debt | 7,591 | 6,055 |
| Total Current Liabilities | 55,840 | 48,391 |
| Long-term debt, less current portion | 32,901 | 28,317 |

| | | |
|--|------------|------------|
| Deferred taxes | 34,377 | 30,133 |
| Other non-current liabilities | 1,686 | 2,021 |
| Total Liabilities | 124,804 | 108,862 |
| Stockholders' Equity: | | |
| Common stock, \$0.001 par value; 50,000,000 shares authorized; 26,898,178 and 26,815,253 shares issued and outstanding at March 1, 2015 and May 25, 2014, respectively | 27 | 27 |
| Additional paid-in capital | 132,948 | 131,488 |
| Retained earnings | 80,902 | 71,554 |
| Total Stockholders' Equity | 213,877 | 203,069 |
| Non-controlling interest | 1,622 | 1,692 |
| Total Equity | 215,499 | 204,761 |
| Total Liabilities and Stockholders' Equity | \$ 340,303 | \$ 313,623 |

(1) Derived from audited financial statements.

See accompanying notes.

LANDEC CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(In thousands, except per share amounts)

| | Three Months Ended | | Nine Months Ended | |
|---|--------------------|----------------------|-------------------|----------------------|
| | March 1, 2015 | February 23, 2014 | March 1, 2015 | February 23, 2014 |
| Product sales | \$138,530 | \$126,379 | \$404,809 | \$355,884 |
| Cost of product sales | 121,645 | 106,224 | 358,071 | 309,463 |
| Gross profit | 16,885 | 20,155 | 46,738 | 46,421 |
| Operating costs and expenses: | | | | |
| Research and development | 1,755 | 1,723 | 5,375 | 5,568 |
| Selling, general and administrative | 10,298 | 8,700 | 29,106 | 25,969 |
| Total operating costs and expenses | 12,053 | 10,423 | 34,481 | 31,537 |
| Operating income | 4,832 | 9,732 | 12,257 | 14,884 |
| Dividend income | 413 | 281 | 1,015 | 844 |
| Interest income | 85 | 78 | 269 | 183 |
| Interest expense | (510) | (390) | (1,365) | (1,257) |
| Other income | 1,307 | 400 | 2,707 | 8,100 |
| Net income before taxes | 6,127 | 10,101 | 14,883 | 22,754 |
| Income tax expense | (2,324) | (3,679) | (5,409) | (8,028) |
| Consolidated net income | 3,803 | 6,422 | 9,474 | 14,726 |
| Non-controlling interest | (31) | (22) | (126) | (123) |
| Net income and comprehensive income applicable to common stockholders | \$3,772 | \$6,400 | \$9,348 | \$14,603 |
| Basic net income per share | \$0.14 | \$0.24 | \$0.35 | \$0.55 |
| Diluted net income per share | \$0.14 | \$0.24 | \$0.34 | \$0.54 |
| Shares used in per share computation | | | | |
| Basic | 26,886 | 26,697 | 26,863 | 26,574 |
| Diluted | 27,363 | 27,124 | 27,314 | 27,093 |

See accompanying notes.

-4-

LANDEC CORPORATION**Consolidated Statements of Cash Flows****(Unaudited)****(In thousands)**

| | Nine Months Ended | |
|---|-------------------|-------------------|
| | March 1, 2015 | February 23, 2014 |
| Cash flows from operating activities: | | |
| Consolidated net income | \$ 9,474 | \$ 14,726 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 5,177 | 5,364 |
| Stock-based compensation expense | 1,139 | 992 |
| Tax benefit from stock-based compensation expense | (277) | (1,909) |
| Impairment of non-public company, non-fair value investment | 793 | — |
| Net (gain) loss on disposal of property and equipment | (53) | 330 |
| Deferred taxes | 4,313 | 5,286 |
| Change in investment in non-public company, fair value | (3,500) | (8,100) |
| Changes in current assets and current liabilities: | | |
| Accounts receivable, net | (854) | (4,969) |
| | 269 | 482 |

| | | |
|--|-----------|-----------|
| Accounts receivable, related party | | |
| Income taxes receivable | 1,000 | 2,798 |
| Inventories, net | 73 | (1,555) |
| Issuance of notes and advances receivable | (4,742) | — |
| Collection of notes and advances receivable | 4,727 | — |
| Prepaid expenses and other current assets | (441) | (203) |
| Accounts payable | (3,815) | (1,845) |
| Accounts payable, related party | 12 | (677) |
| Accrued compensation | 648 | 147 |
| Other accrued liabilities | (415) | 2,541 |
| Deferred revenue | (152) | 426 |
| Net cash provided by operating activities | 13,376 | 13,834 |
| Cash flows from investing activities: | | |
| Purchases of property and equipment | (10,202) | (10,192) |
| Investment in non-public company, fair value | (18,000) | — |
| Purchase of marketable securities | — | (1,417) |
| Proceeds from maturities of marketable securities | — | 2,962 |
| Proceeds from sale of fixed assets | 922 | — |
| Net cash used in investing activities | (27,280) | (8,647) |
| Cash flows from financing activities: | | |
| Proceeds from sale of common stock | 122 | 2,147 |
| Taxes paid by Company for stock swaps and RSUs | (12) | (1,252) |
| Tax benefit from stock-based compensation expense | 277 | 1,909 |

| | | |
|---|-----------|-----------|
| Proceeds from long-term debt | 11,194 | — |
| Payments on long-term debt | (5,074) | (4,525) |
| Proceeds from lines of credit | 30,417 | 3,500 |
| Payments on lines of credit | (21,117) | (7,500) |
| Change in other assets | (255) | 29 |
| Payments to minority interest holders | (196) | (226) |
| Net cash provided by (used in) financing activities | 15,356 | (5,918) |
| Net decrease in cash and cash equivalents | 1,452 | (731) |
| Cash and cash equivalents at beginning of period | 14,243 | 13,718 |
| Cash and cash equivalents at end of period | \$ 15,695 | \$ 12,987 |

See accompanying notes.

LANDEC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Organization, Basis of Presentation and Summary of Significant Accounting Policies

Organization

Landec Corporation and its subsidiaries (“Landec” or the “Company”) design, develop, manufacture and sell differentiated products for food and biomaterials markets and license technology applications to partners. The Company has two proprietary polymer technology platforms: 1) Intelimer® polymers, and 2) hyaluronan (“HA”) biopolymers. The Company sells specialty packaged branded Eat Smart® and GreenLine® and private label fresh-cut vegetables and whole produce to retailers, club stores and foodservice operators, primarily in the United States, Canada and Asia through its Apio, Inc. (“Apio”) subsidiary and sells HA-based biomaterials through its Lifecore Biomedical, Inc. (“Lifecore”) subsidiary. The Company’s HA biopolymers are proprietary in that they are specially formulated for specific customers to meet strict regulatory requirements. The Company’s polymer technologies, along with its customer relationships and tradenames, are the foundation, and a key differentiating advantage upon which Landec has built its business.

Basis of Presentation

The accompanying unaudited consolidated financial statements of Landec have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal recurring accruals) have been made which are necessary to present fairly the financial position at March 1, 2015 and the results of operations and cash flows for all periods presented. Although Landec believes that the disclosures in these financial statements are adequate to make the information presented not misleading, certain information normally included in financial statements and related footnotes prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted in accordance with the rules and regulations of the Securities and Exchange Commission. The accompanying financial data should be reviewed in conjunction with the audited financial statements and accompanying notes included in Landec’s Annual Report on Form 10-K for the fiscal year ended May 25, 2014.

The results of operations for the nine months ended March 1, 2015 are not necessarily indicative of the results that may be expected for an entire fiscal year because there is some seasonality in Apio’s food business, particularly, Apio’s

Food Export business and the order patterns of Lifecore's customers which may lead to significant fluctuations in Landec's quarterly results of operations. In addition, the first quarter of fiscal year 2015 was a 14-week quarter which occurs once every six years compared to the standard 13-week quarter.

Basis of Consolidation

The consolidated financial statements are presented on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States and include the accounts of Landec Corporation and its subsidiaries, Apio and Lifecore. All material inter-company transactions and balances have been eliminated.

Arrangements that are not controlled through voting or similar rights are reviewed under the guidance for variable interest entities ("VIEs"). A company is required to consolidate the assets, liabilities and operations of a VIE if it is determined to be the primary beneficiary of the VIE.

An entity is a VIE and subject to consolidation, if by design: a) the total equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support provided by any parties, including equity holders or b) as a group the holders of the equity investment at risk lack any one of the following three characteristics: (i) the power, through voting rights or similar rights to direct the activities of an entity that most significantly impact the entity's economic performance, (ii) the obligation to absorb the expected losses of the entity, or (iii) the right to receive the expected residual returns of the entity. The Company reviewed the consolidation guidance and concluded that its partnership interest in Apio Cooling and its equity investments in non-public companies are not VIEs.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make certain estimates and judgments that affect the amounts reported in the financial statements and accompanying notes. The accounting estimates that require management's most significant and subjective judgments include revenue recognition; sales returns and allowances; self insurance liabilities; recognition and measurement of current and deferred income tax assets and liabilities; the assessment of recoverability of long-lived assets; the valuation of intangible assets and inventory; the valuation of investments; and the valuation and recognition of stock-based compensation.

These estimates involve the consideration of complex factors and require management to make judgments. The analysis of historical and future trends can require extended periods of time to resolve and is subject to change from period to period. Actual results may differ from management's estimates.

Cash and Cash Equivalents

The Company records all highly liquid securities with three months or less from date of purchase to maturity as cash equivalents. Cash equivalents consisted of money market funds of \$1.5 million at both March 1, 2015 and May 25, 2014. The market value of cash equivalents approximates their historical cost given their short-term nature.

Financial Instruments

The Company's financial instruments are primarily composed of marketable securities, commercial-term trade payables, grower advances, notes receivable and debt instruments. For short-term instruments, the historical carrying amount approximates the fair value of the instrument. The fair value of long-term debt and lines of credit approximates their carrying value. Fair values for long-term financial instruments not readily marketable are estimated based upon discounted future cash flows at prevailing market interest rates. Based on these assumptions, management believes the fair values of the Company's financial instruments are not materially different from their recorded amounts as of March 1, 2015 and May 25, 2014.

Investments in Non-Public Companies

The Company's investment in Aesthetic Sciences Corporation ("Aesthetic Sciences"), which had been reported as an investment in non-public company, non-fair value, in the accompanying Consolidated Balance Sheets, was carried at cost and adjusted for prior impairment losses. Based on recently received financial information from the acquirer of Aesthetic Sciences' Smartfill™ Injector System (see Note 2), the Company determined during the three months ended March 1, 2015 that its investment was other than temporarily impaired and therefore, wrote off its remaining investment of \$793,000 as of March 1, 2015.

On February 15, 2011, Apio purchased 150,000 senior preferred shares for \$15 million and 201 common shares for \$201 that were issued by Windset Holdings 2010 Ltd., a Canadian corporation ("Windset"). On July 15, 2014, Apio increased its investment in Windset by purchasing an additional 68 shares of common stock and 51,211 shares of junior preferred stock of Windset for \$11.0 million. On October 29, 2014, Apio purchased an additional 70,000 senior preferred shares of Windset for \$7.0 million. These investments are reported as an investment in non-public company, fair value, in the accompanying Consolidated Balance Sheets as of March 1, 2015 and May 25, 2014. The Company has elected to account for its investment in Windset under the fair value option (see Note 2).

Intangible Assets

The Company's intangible assets are comprised of customer relationships with a finite estimated useful life of twelve to thirteen years and trademarks, tradenames and goodwill with indefinite lives.

Finite-lived intangible assets are reviewed for possible impairment whenever events or changes in circumstances occur that indicate that the carrying amount of an asset (or asset group) may not be recoverable. Indefinite lived intangible assets are reviewed for impairment at least annually. For non-goodwill indefinite-lived intangible assets, the Company performs a qualitative analysis in accordance with ASC 350-30-35. For goodwill, the Company has historically performed a quantitative analysis in accordance with ASC 350-20-35.

Partial Self-Insurance on Employee Health Plan

The Company provides health insurance benefits to eligible employees under a self-insured plan whereby the Company pays actual medical claims subject to certain stop loss limits. The Company records self-insurance liabilities based on actual claims filed and an estimate of those claims incurred but not reported. Any projection of losses concerning the Company's liability is subject to a high degree of variability. Among the causes of this variability are unpredictable external factors such as inflation rates, changes in severity, benefit level changes, medical costs, and claims settlement patterns. This self-insurance liability is included in accrued liabilities and represents management's best estimate of the amounts that have not been paid as of March 1, 2015 and May 25, 2014. It is reasonably possible that the expense the Company ultimately incurs could differ and adjustments to future reserves may be necessary.

Long-Term Incentive Plan

On July 25, 2013, the Landec Long-Term Incentive Plan ("LTIP") was established which allows certain executives to earn a performance-based bonus that is based upon a cumulative operating income target for fiscal years 2014, 2015, and 2016. The LTIP was designed to align the interests of management with the long-term financial success of the Company. If the three-year cumulative operating income target had been met, approximately \$2.0 million in bonuses would have been paid. Through fiscal year 2014, the Company was recording the estimated plan bonus on a straight-line basis over the 36-month LTIP period. As of August 31, 2014, the Company determined it was unlikely the three-year cumulative operating income target would be attained and therefore all LTIP bonus accruals were reversed at that date. The reversal resulted in a \$677,000 reduction in selling, general, and administrative expenses during the nine months ended March 1, 2015 in the accompanying Consolidated Statements of Comprehensive Income. The long-term incentive bonuses accrued under this plan of zero and \$677,000 are included in other non-current liabilities in the accompanying Consolidated Balance Sheets as of March 1, 2015 and May 25, 2014, respectively.

Fair Value Measurements

The Company uses fair value measurement accounting for financial assets and liabilities and for financial instruments and certain other items measured at fair value. The Company has elected the fair value option for its investment in a non-public company (see Note 2). The Company has not elected the fair value option for any of its other eligible financial assets or liabilities.

The accounting guidance established a three-tier hierarchy for fair value measurements, which prioritizes the inputs used in measuring fair value as follows:

Level 1
– observable inputs such as quoted prices for identical instruments in active markets.

Level 2 inputs other than quoted prices in active markets that are observable either directly or indirectly through
– corroboration with observable market data.

Level 3 unobservable inputs in which there is little or no market data, which would require the Company to develop
– its own assumptions.

As of March 1, 2015, the Company held certain assets and liabilities that are required to be measured at fair value on a recurring basis, including an interest rate swap and a minority interest investment in Windset.

The fair value of the Company's interest rate swap is determined based on model inputs that can be observed in a liquid market, including yield curves, and is categorized as a Level 2 measurement.

The Company has elected the fair value option of accounting for its investment in Windset. The calculation of fair value utilizes significant unobservable inputs, including projected cash flows, growth rates and discount rates. As a result, the Company's investment in Windset is considered to be a Level 3 measurement investment. The change in the fair value of the Company's investment in Windset for the nine months ended March 1, 2015 was due to the Company's 26.9% minority interest in the change in the fair market value of Windset during the period. In determining the fair value of the investment in Windset, the Company utilizes the following significant unobservable inputs in the discounted cash flow models:

| | At March 1, 2015 | | | At May 25, 2014 | | |
|----------------------|------------------|----|-----|-----------------|----|-----|
| Revenue growth rates | 4% | | | 4% | | |
| Expense growth rates | 4% | | | 4% | | |
| Income tax rates | 15% | | | 15% | | |
| Discount rates | 15% | to | 21% | 16% | to | 22% |

The revenue growth, expense growth and income tax rate assumptions, consider the Company's best estimate of the trends in those items over the discount period. The discount rate assumption takes into account the risk-free rate of return, the market equity risk premium and the company's specific risk premium and then applies an additional discount for lack of liquidity of the underlying securities. The discounted cash flow valuation model used by the Company has the following sensitivity to changes in inputs and assumptions (in thousands):

Impact on value of Windset investment as of
March 1, 2015

| | |
|--------------------------------------|-----------|
| 10% increase in revenue growth rates | \$2,100 |
| 10% increase in expense growth rates | \$(1,800) |
| 10% increase in income tax rates | \$(100) |
| 10% increase in discount rates | \$(1,700) |

Imprecision in estimating unobservable market inputs can affect the amount of gain or loss recorded for a particular position. The use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The following table summarizes the fair value of the Company's assets and liabilities that are measured at fair value on a recurring basis, as of March 1, 2015 and May 25, 2014 (in thousands):

| | Fair Value at March 1, 2015 | | | Fair Value at May 25, 2014 | | |
|---------|-----------------------------|---------|---------|----------------------------|---------|---------|
| | Level 1 | Level 2 | Level 3 | Level 1 | Level 2 | Level 3 |
| Assets: | - | - | 61,100 | - | - | 39,600 |

Investment in private
company

| | | | | | | |
|-------|------|------|-----------|------|------|-----------|
| Total | \$ - | \$ - | \$ 61,100 | \$ - | \$ - | \$ 39,600 |
|-------|------|------|-----------|------|------|-----------|

Liabilities:

| | | | | | | |
|--------------------|------|------|------|------|-------|------|
| Interest rate swap | - | 2 | - | - | 44 | - |
| Total | \$ - | \$ 2 | \$ - | \$ - | \$ 44 | \$ - |

Revenue Recognition

Revenue from product sales is recognized when there is persuasive evidence that an arrangement exists, title has transferred, the price is fixed and determinable, and collectability is reasonably assured. Allowances are established for estimated uncollectible amounts, product returns, and discounts based on specific identification and historical losses.

Apio's Food Products Technology revenues generally consist of revenues generated from the sale of specialty packaged fresh-cut and whole value-added processed vegetable products that are generally washed and packaged in the Company's proprietary packaging and sold under Apio's Eat Smart and GreenLine brands and various private labels. Revenue is generally recognized upon shipment of these products to customers. The Company takes title to all produce it trades and/or packages, and therefore, records revenues and cost of sales at gross amounts in the Consolidated Statements of Comprehensive Income.

In addition, Food Products Technology value-added revenues include the revenues generated from Apio Cooling, LP, a vegetable cooling operation in which Apio is the general partner with a 60% ownership position and from the sale of BreatheWay packaging to license partners. Revenue is recognized on the vegetable cooling operations as cooling and storage services are provided to the Company's customers. Sales of BreatheWay packaging are recognized when shipped to the customer.

Apio's Food Export revenues consist of revenues generated from the purchase and sale of primarily whole commodity fruit and vegetable products to Asia by Cal-Ex. As most Cal-Ex customers are in countries outside of the U.S., title transfers and revenue is generally recognized upon arrival of the shipment in the foreign port. Apio records revenue equal to the sale price to third parties because it takes title to the product while in transit.

The HA-based Biomaterials business principally generates revenue through the sale of products containing HA. Lifecore primarily sells products to customers in three medical areas: (1) Ophthalmic, which represented approximately 60% of Lifecore's revenues in fiscal year 2014, (2) Orthopedic, which represented approximately 20% of Lifecore's revenues in fiscal year 2014 and (3) Veterinary/Other. The vast majority of revenues from the Company's HA-based Biomaterials business are recognized upon shipment.

Lifecore's business development revenues, a portion of which are included in all three medical areas, are related to contract research and development (R&D) services and multi-element arrangement services with customers where the Company provides products and/or services in a bundled arrangement.

Contract R&D revenue is recorded as earned, based on the performance requirements of the contract. Non-refundable contract fees for which no further performance obligations exist, and there is no continuing involvement by the Company, are recognized on the earlier of when the payment is received or collection is assured.

For sales arrangements that contain multiple elements, the Company splits the arrangement into separate units of accounting if the individually delivered elements have value to the customer on a standalone basis. The Company also evaluates whether multiple transactions with the same customer or related party should be considered part of a multiple element arrangement, whereby the Company assesses, among other factors, whether the contracts or agreements are negotiated or executed within a short time frame of each other or if there are indicators that the contracts are negotiated in contemplation of each other. The Company then allocates revenue to each element based on a selling price hierarchy. The relative selling price for a deliverable is based on its vendor-specific objective evidence (VSOE), if available, third-party evidence (TPE), if VSOE is not available, or estimated selling price, if neither VSOE nor TPE is available. The Company then recognizes revenue on each deliverable in accordance with its policies for product and service revenue recognition. The Company is not typically able to determine VSOE or TPE, and therefore, uses the estimated selling price to allocate revenue between the elements of an arrangement.

The Company limits the amount of revenue recognition for delivered elements to the amount that is not contingent on the future delivery of products or services or future performance obligations or subject to customer-specific cancellation rights. The Company evaluates each deliverable in an arrangement to determine whether it represents a separate unit of accounting. A deliverable constitutes a separate unit of accounting when it has stand-alone value, and for an arrangement that includes a general right of return relative to the delivered products or services, delivery or performance of the undelivered product or service is considered probable and is substantially controlled by the Company. The Company considers a deliverable to have stand-alone value if the product or service is sold separately by the Company or another vendor or could be resold by the customer. Further, the revenue arrangements generally do not include a general right of return relative to delivered products. Where the aforementioned criteria for a separate unit of accounting are not met, the deliverable is combined with the undelivered element(s) and treated as a single unit of accounting for the purposes of allocation of the arrangement consideration and revenue recognition. The Company allocates the total arrangement consideration to each separable element of an arrangement based upon the relative selling price of each element. Allocation of the consideration is determined at arrangement inception on the basis of each unit's relative selling price. In instances where the Company has not established fair value for any undelivered

element, revenue for all elements is deferred until delivery of the final element is completed and all recognition criteria are met.

Licensing revenue is recognized in accordance with prevailing accounting guidance. Initial license fees are deferred and amortized to revenue over the period of the agreement when a contract exists, the fee is fixed and determinable, and collectability is reasonably assured. Noncancellable, nonrefundable license fees are recognized over the period of the agreement, including those governing research and development activities and any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement.

From time to time, the Company offers customers sales incentives, which include volume rebates and discounts. These amounts are estimated on a quarterly basis and recorded as a reduction of revenue.

A summary of revenues by type of revenue arrangement as described above is as follows (in thousands):

| | Three months ended | Three months ended | Nine months ended | Nine months ended |
|---|-----------------------------------|-----------------------------------|----------------------------------|----------------------------------|
| | March 1, 2015 | February 23, 2014 | March 1, 2015 | February 23, 2014 |
| Recorded upon shipment | \$ 128,502 | \$ 112,902 | \$ 344,506 | \$ 295,314 |
| Recorded upon acceptance in foreign port | 8,086 | 10,677 | 56,779 | 55,006 |
| Revenue from license fees, R&D contracts and royalties/profit sharing | 153 | 447 | 788 | 648 |
| Revenue from multiple element arrangements | 1,789 | 2,353 | 2,736 | 4,916 |
| Total | \$ 138,530 | \$ 126,379 | \$ 404,809 | \$ 355,884 |

New Accounting Pronouncements

Revenue Recognition

In May 2014, the FASB issued Accounting Standard Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (Topic 606) (“ASU 2014-09”), which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The standard requires entities to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new guidance also includes a cohesive set of disclosure requirements intended to provide users of financial statements with comprehensive information about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a company’s contracts with customers. ASU 2014-09 will be effective beginning the first quarter of the Company's fiscal year 2018 and early application is not permitted. The standard allows for either “full retrospective” adoption, meaning the standard is applied to all of the periods presented, or “modified retrospective” adoption, meaning the standard is applied only to the most current period presented in the financial statements. Management is currently evaluating the effect ASU 2014-09 will have on the Company's Consolidated Financial Statements and disclosures.

2. Investments in non-public companies

In December 2005, Landec entered into a licensing agreement with Aesthetic Sciences for the exclusive rights to use Landec's Intelimer® materials technology for the development of dermal fillers worldwide under the agreement. The

Company received shares of preferred stock in exchange for the license. Aesthetic Sciences sold the rights to its Smartfil Injector System on July 16, 2010. The royalty period from the sale of the Smartfil Injector System began November 1, 2014 and as a result the Company obtained for the first time during the third quarter of fiscal year 2015 financial information for the products for which a royalty is due Aesthetic Sciences. Based on the review of this historical financial information and discussions with the acquirer, the Company concluded that its investment in Aesthetic Sciences was other than temporarily impaired, and therefore wrote off its remaining \$793,000 investment in Aesthetic Sciences as of March 1, 2015 and is included in other income in the Consolidated Statements of Comprehensive Income.

On February 15, 2011, Apio entered into a share purchase agreement (the "Windset Purchase Agreement") with Windset. Pursuant to the Windset Purchase Agreement, Apio purchased from Windset 150,000 Senior A preferred shares for \$15 million and 201 common shares for \$201. On July 15, 2014, Apio increased its investment in Windset by purchasing from the Newell Capital Corporation an additional 68 shares of common stock and 51,211 shares of junior preferred stock of Windset for \$11.0 million. After this purchase, the Company's common shares represent a 26.9% ownership interest in Windset. The non-voting Senior A preferred shares yield a cash dividend of 7.5% annually. The dividend is payable within 90 days of each anniversary of the execution of the Windset Purchase Agreement. The non-voting junior preferred stock does not yield a dividend unless declared by the Board of Directors of Windset and no such dividend has been declared.

The Windset Purchase Agreement includes a put and call option, which can be exercised on the sixth anniversary of the Windset Purchase Agreement whereby Apio can exercise the put to sell its common, Senior A preferred shares and junior preferred shares to Windset, or Windset can exercise the call to purchase those shares from Apio, in either case, at a price equal to 26.9% of the appreciation in the fair market value of Windset's common shares from the date of the Company's investment through the put and call date, plus the liquidation value of the preferred shares of \$20.1 million (\$15 million for the Senior A preferred shares and \$5.1 million for the junior preferred shares). Under the terms of the arrangement with Windset, the Company is entitled to designate one of five members on the Board of Directors of Windset.

On October 29, 2014, Apio further increased its investment in Windset by purchasing 70,000 shares of Senior B preferred shares. The Senior B Preferred Stock pays an annual dividend of 7.5% on the amount outstanding at each anniversary date of the Windset Purchase Agreement. The Senior B shares purchased by Apio have a put feature whereby Apio can sell back to Windset \$1.5 million of shares on the first anniversary, an additional \$2.75 million of shares on the second anniversary and the remaining \$2.75 million on the third anniversary. After the third anniversary, Apio may at any time put any or all of the shares not previously sold back to Windset. At any time on or after February 15, 2017, Windset has the right to call any or all of the outstanding common shares and at such time must also call the same proportion of Senior A preferred shares, Senior B preferred shares and junior preferred shares owned by Apio. Windset's partial call provision is restricted such that a partial call cannot result in Apio holding less than 10% of Windset's common shares outstanding.

The investment in Windset does not qualify for equity method accounting as the investment does not meet the criteria of in-substance common stock due to returns through the annual dividend on the non-voting senior preferred shares that are not available to the common stock holders. As the put and call options require the Purchased Shares to be put or called in equal proportions, the Company has deemed that the investment, in substance, should be treated as a single security for purposes of accounting.

During the three months ended March 1, 2015 and February 23, 2014, the Company recorded \$413,000 and \$281,000, respectively, in dividend income. During the nine months ended, March 1, 2015 and February 23, 2014, the Company recorded \$1.0 million and \$844,000, respectively, in dividend income. The change in the fair market value of the Company's investment in Windset for the three months ended March 1, 2015 and February 23, 2014 was \$2.1 million and \$400,000, respectively, and is included in other income in the Consolidated Statements of Comprehensive Income. The change in the fair market value of the Company's investment in Windset for the nine months ended March 1, 2015 and February 23, 2014 was \$3.5 million and \$8.1 million, respectively, and is included in other income in the Consolidated Statements of Comprehensive Income.

The Company also entered into an exclusive license agreement with Windset, which was executed in June 2010, prior to contemplation of Apio's investment in Windset. The license agreement allows Windset the use of Landec's proprietary breathable packaging to extend the shelf life of greenhouse grown cucumbers, peppers and tomatoes ("Exclusive Products"). In accordance with the agreement, Apio received and recorded a one-time upfront research and development fee of \$100,000 and will receive license fees equal to 3% of net revenue of the Exclusive Products utilizing the proprietary breathable packaging technology, with or without the BreatheWay® trademark. The ongoing license fees are subject to annual minimums of \$150,000 for each of the three types of exclusive product as each is added to the agreement. As of March 1, 2015, two products have been added to the agreement.

3. Stock-Based Compensation

The Company records compensation expense for stock-based awards issued to employees and directors in exchange for services provided based on the estimated fair value of the awards on their grant dates and is recognized over the

required service periods (generally the vesting period). For nonstatutory options, the cash flows resulting from the tax benefit due to tax deductions in excess of the compensation expense recognized for those options (excess tax benefit) are classified as financing activities within the statement of cash flows. The Company's stock-based awards include stock option grants and restricted stock unit awards ("RSUs").

The following table summarizes the stock-based compensation for options and RSUs (in thousands):

| | Three Months Ended March 1, 2015 | Three Months Ended February 23, 2014 | Nine Months Ended March 1, 2015 | Nine Months Ended February 23, 2014 |
|--------------------------------|---|---|--|--|
| Options | \$ 139,000 | \$ 131,000 | \$ 394,000 | \$ 416,000 |
| RSUs | 252,000 | 222,000 | 745,000 | 576,000 |
| Total stock-based compensation | \$ 391,000 | \$ 353,000 | \$ 1,139,000 | \$ 992,000 |

The following table summarizes the stock-based compensation by income statement line item:

| | Three Months Ended March 1, 2015 | Three Months Ended February 23, 2014 | Nine Months Ended March 1, 2015 | Nine Months Ended February 23, 2014 |
|-----------------------------------|---|---|--|--|
| Research and development | \$ 8,000 | \$ 14,000 | \$ 28,000 | \$ 28,000 |
| Sales, general and administrative | 383,000 | 339,000 | 1,111,000 | 964,000 |
| Total stock-based compensation | \$ 391,000 | \$ 353,000 | \$ 1,139,000 | \$ 992,000 |

The estimated fair value for stock options, which determines the Company's calculation of compensation expense, is based on the Black-Scholes option pricing model. RSUs are valued at the closing market price of the Company's common stock on the date of grant. The Company uses the straight line single option method to calculate and recognize the fair value of stock-based compensation arrangements. In addition, the Company uses historical data to estimate pre-vesting forfeitures and records stock-based compensation expense only for those awards that are expected to vest and revises those estimates in subsequent periods if the actual forfeitures differ from the prior estimates.

As of March 1, 2015, there was \$2.2 million of total unrecognized compensation expense related to unvested equity compensation awards granted under the Landec incentive stock plans. Total expense is expected to be recognized over the weighted-average period of 1.8 years for stock options and 1.7 years for RSUs.

4. Diluted Net Income Per Share

The following table calculates diluted net income per share (in thousands, except per share amounts):

| | Three Months Ended March 1, 2015 | Three Months Ended February 23, 2014 | Nine Months Ended March 1, 2015 | Nine Months Ended February 23, 2014 |
|--|--|--|---|---|
| Numerator: | | | | |
| Net income applicable to Common Stockholders | \$3,772 | \$6,400 | \$9,348 | \$14,603 |
| Denominator: | | | | |
| Weighted average shares for basic net income per share | 26,886 | 26,697 | 26,863 | 26,574 |
| Effect of dilutive securities: | | | | |
| Stock options and restricted stock units | 477 | 427 | 451 | 519 |
| Weighted average shares for diluted net income per share | 27,363 | 27,124 | 27,314 | 27,093 |
| Diluted net income per share | \$0.14 | \$0.24 | \$0.34 | \$0.54 |

For the three months ended March 1, 2015 and February 23, 2014, the computation of the diluted net income per share excludes the impact of options to purchase 390,657 shares and 342,500 shares of Common Stock, respectively, as such impacts would be antidilutive for these periods.

For the nine months ended March 1, 2015 and February 23, 2014, the computation of the diluted net income per share excludes the impact of options to purchase 349,076 shares and 332,037 shares of Common Stock, respectively, as such impacts would be antidilutive for these periods.

5. Income Taxes

The provision for income taxes for the three and nine months ended March 1, 2015 was \$2.3 million and \$5.4 million, respectively. The effective tax rate for the nine months ended March 1, 2015 was 36%, compared to 35% for the first nine months of fiscal year 2014. The effective tax rate for the nine months ended March 1, 2015 was higher than the statutory federal income tax rate of 35% primarily due to several factors, including state taxes, valuation allowance on the impairment of the investment in Aesthetic Sciences Corporation, and non-deductible stock-based compensation expense; partially offset by the domestic manufacturing deduction and state and federal research and development credits.

As of both March 1, 2015 and May 25, 2014, the Company had unrecognized tax benefits of approximately \$1.0 million. Included in the balance of unrecognized tax benefits as of March 1, 2015 and May 25, 2014 is approximately \$800,000 and \$807,000, respectively, of tax benefits that, if recognized, would result in an adjustment to the Company's effective tax rate. The Company does not expect its unrecognized tax benefits to change significantly within the next twelve months.

The Company has elected to classify interest and penalties related to uncertain tax positions as a component of its provision for income taxes. The Company has accrued an insignificant amount of interest and penalties relating to the income tax on the unrecognized tax benefits as of March 1, 2015 and May 25, 2014.

Due to tax attribute carryforwards, the Company is subject to examination for tax years 1997 forward for U.S. tax purposes. The Company is also subject to examination in various state jurisdictions for tax years 1998 forward, none of which were individually material.

6. Inventories

Inventories are stated at the lower of cost (first-in, first-out method) or market and consisted of the following (in thousands):

| | March 1, 2015 | May 25, 2014 |
|------------------|------------------|-----------------|
| Finished goods | \$10,173 | \$11,111 |
| Raw materials | 11,090 | 10,376 |
| Work in progress | 3,399 | 3,248 |
| Total | \$24,662 | \$24,735 |

7. Debt

Long-term debt consists of the following (in thousands):

| | March 1, 2015 | May 25, 2014 |
|---|------------------|-----------------|
| Real estate loan agreement with General Electric Capital Corporation (“GE Capital”); due in monthly principal and interest payments of \$133,060 through May 1, 2022 with interest based on a fixed rate of 4.02% per annum | \$15,417 | \$16,137 |
| Capital equipment loan with GE Capital; due in monthly principal and interest payments of \$175,356 through May 1, 2019 with interest based on a fixed rate of 4.39% per annum | 8,145 | 9,430 |
| Capital equipment loan with GE Capital; due in monthly principal and interest payments of \$95,120 through September 1, 2019 with interest based on a fixed rate of 3.68% per annum | 6,702 | — |
| Capital equipment loan with GE Capital; due in monthly principal and interest payments of \$55,828 through December 1, 2019 with interest based on a fixed rate of 3.74% per annum | 4,038 | — |
| Term note with BMO Harris Bank N.A. (“BMO Harris”); due in monthly payments of \$250,000 through May 23, 2016 with interest payable monthly at LIBOR plus 2% per annum | 3,750 | 6,000 |
| Industrial revenue bonds (“IRBs”) issued by Lifecore; due in annual payments through 2020 with interest at a variable rate set weekly by the bond remarketing agent (0.22% and 0.28% at March 1, 2015 and May 25, 2014, respectively) | 2,440 | 2,805 |
| Total | 40,492 | 34,372 |
| Less current portion | (7,591) | (6,055) |
| Long-term portion | \$32,901 | \$28,317 |

On July 17, 2014, Apio entered into an amendment with GE Capital, which amended the revolving line of credit dated April 23, 2012 among the parties. Under the amendment, the revolving line of credit increased from \$25 million to \$40 million, the interest rate was reduced from LIBOR plus 2.0% to LIBOR plus 1.75%, the term was extended to July 17, 2019 and the parties made certain other insignificant changes. The availability under the revolving line of credit is based on the combination of the eligible accounts receivable and eligible inventory (availability was \$18.8 million at March 1, 2015). Apio’s revolving line of credit has an unused fee of 0.375% per annum. At March 1, 2015 and May 25, 2014, \$9.3 million and zero were outstanding under Apio’s revolving line of credit.

Also on July 17, 2014, Apio entered into a new equipment loan whereby Apio can borrow up to \$25 million based on eligible equipment purchases between August 1, 2012 and August 31, 2015. Each borrowing under this new equipment loan has a five year term with a seven year amortization period. On August 28, 2014, Apio borrowed \$7.1 million under the new equipment loan at a fixed rate of 3.68%. On November 24, 2014, Apio borrowed an additional \$4.1 million under the new equipment loan at a fixed rate of 3.74%.

The GE Capital real estate, equipment and line of credit agreements (collectively the “GE Debt Agreements”) are secured by liens on all of the property of Apio and its subsidiaries. The GE Debt Agreements contain customary

events of default under which obligations could be accelerated or increased. The GE Debt Agreements are guaranteed by Landec and Landec has pledged its equity interest in Apio as collateral under the line of credit agreement. The GE Debt Agreements contain customary covenants, such as limitations on the ability to (1) incur indebtedness or grant liens or negative pledges on Apio's assets; (2) make loans or other investments; (3) pay dividends, sell stock or repurchase stock or other securities; (4) sell assets; (5) engage in mergers; (6) enter into sale and leaseback transactions; and (7) make changes in Apio's corporate structure. In addition, Apio must maintain a minimum fixed charge coverage ratio of not less than 1.10 to 1.0 if the availability under its line of credit falls below \$12.0 million. Apio was in compliance with all financial covenants as of March 1, 2015 and May 25, 2014.

During the nine months ended March 1, 2015, Apio capitalized \$318,000 of loan origination fees from the revolving line of credit amendment and from the new equipment loan with GE Capital. These fees are being amortized over a five year period. Unamortized loan origination fees associated with all of the GE Capital debt agreements were \$1.1 million and \$1.0 million at March 1, 2015 and May 25, 2014, respectively, and are included in other assets in the Consolidated Balance Sheets.

Amortization of loan origination fees for Apio recorded to interest expense for the three months ended March 1, 2015 and February 23, 2014 were \$54,000 and \$47,000, respectively. Amortization of loan origination fees for Apio recorded to interest expense for the nine months ended March 1, 2015 and February 23, 2014 were \$151,000 and \$140,000, respectively.

On May 23, 2012, Lifecore entered into two financing agreements with BMO Harris and/or its affiliates, collectively (the "Lifecore Loan Agreements"):

1) A Credit and Security Agreement (the "Credit Agreement") which includes (a) a one-year, \$10.0 million asset-based working capital revolving line of credit, with an interest rate of LIBOR plus 1.85%, with availability based on the combination of Lifecore's eligible accounts receivable and inventory balances (availability was \$7.3 million at March 1, 2015) and with no unused fee (at March 1, 2015 and May 25, 2014, no amounts were outstanding under the line of credit) and (b) a \$12.0 million term loan which matures in May 2016 due in monthly payments of \$250,000 with interest payable monthly based on a variable interest rate of LIBOR plus 2% (the "Term Loan").

2) A Reimbursement Agreement pursuant to which BMO Harris caused its affiliate Bank of Montreal to issue an irrevocable letter of credit in the amount of \$3.5 million (the "Letter of Credit") which is securing the IRB described below.

The obligations of Lifecore under the Lifecore Loan Agreements are secured by liens on all of the property of Lifecore. The Lifecore Loan Agreements contain customary covenants, such as limitations on the ability to (1) incur indebtedness or grant liens or negative pledges on Lifecore's assets; (2) make loans or other investments; (3) pay dividends or repurchase stock or other securities; (4) sell assets; (5) engage in mergers; (6) enter into sale and leaseback transactions; (7) adopt certain benefit plans; and (8) make changes in Lifecore's corporate structure. In addition, under the Credit Agreement, Lifecore must maintain (a) a minimum fixed charge coverage ratio of 1.10 to 1.0 and a minimum quick ratio of 1.25 to 1.00, both of which must be satisfied as of the end of each fiscal quarter and (b) a minimum tangible net worth of \$29,000,000, measured as of the end of each fiscal year. Lifecore was in compliance with all financial covenants as of March 1, 2015 and May 25, 2014.

Unamortized loan origination fees for the Lifecore Loan Agreements were \$61,000 and \$98,000 at March 1, 2015 and May 25, 2014, respectively, and are included in other assets in the Consolidated Balance Sheets. Amortization of loan origination fees recorded to interest expense for both the three months ended March 1, 2015 and February 23, 2014

was \$13,000. Amortization of loan origination fees recorded to interest expense for both the nine months ended March 1, 2015 and February 23, 2014 was \$38,000.

The market value of the Company's debt approximates its recorded value as the interest rate on each debt instrument approximates current market rates.

The Term Loan was used to repay Lifecore's former credit facility with Wells Fargo Bank, N.A. ("Wells Fargo"). The Letter of Credit (which replaces a letter of credit previously provided by Wells Fargo) provides liquidity and credit support for the IRBs.

On August 19, 2004, Lifecore issued variable rate industrial revenue bonds ("IRBs") which were assumed by Landec in the acquisition of Lifecore. The IRBs are collateralized by a bank letter of credit which is secured by a first mortgage on the Company's facility in Chaska, Minnesota. In addition, the Company pays an annual remarketing fee equal to 0.125% and an annual letter of credit fee of 0.75% on the outstanding principal balance. The maturities on the IRBs are held in a sinking fund account, recorded in other assets in the accompanying Consolidated Balance Sheets, and are paid out each year on September 1st.

8. Derivative Financial Instruments

In May 2010, the Company entered into a five-year interest rate swap agreement under its prior credit agreement with Wells Fargo, which expires on April 30, 2015. The interest rate swap was originally designated as a cash flow hedge of future interest payments of LIBOR and had a notional amount of \$20 million. As a result of the interest rate swap transaction, the Company fixed for a five-year period the interest rate at 4.24% subject to market based interest rate risk on \$20 million of borrowings under the credit agreement with Wells Fargo. The Company's obligations under the interest rate swap transaction as to the scheduled payments were guaranteed and secured on the same basis as its obligations under the credit agreement with Wells Fargo at the time the agreement was consummated. Upon entering into the new Term Loan with BMO Harris, the Company used the proceeds from that loan to pay off the Wells Fargo credit facility. The swap with Wells Fargo was not terminated upon the extinguishment of the debt with Wells Fargo. The fair value of the swap arrangement as of March 1, 2015 and May 25, 2014 was \$2,000 and \$44,000, respectively, and is included in other accrued liabilities in the accompanying Consolidated Balance Sheets.

9. Related Party

The Company sells products to and earns license fees from Windset. During the three months ended March 1, 2015 and February 23, 2014, the Company recognized revenues of \$35,000 and \$50,000, respectively. During the nine months ended March 1, 2015 and February 23, 2014, the Company recognized revenues of \$230,000 and \$81,000, respectively. These amounts have been included in product sales in the accompanying Consolidated Statements of Comprehensive Income, from the sale of products to and license fees from Windset. The related receivable balances of \$35,000 and \$304,000 are included in accounts receivable, related party, in the accompanying Consolidated Balance Sheets as of March 1, 2015 and May 25, 2014, respectively.

Additionally, unrelated to the revenue transactions above, the Company purchases produce from Windset for sale to third parties. During the three months ended March 1, 2015 and February 23, 2014, the Company recognized cost of product sales of \$617,000 and \$405,000, respectively. During the nine months ended March 1, 2015 and February 23, 2014, the Company recognized cost of product sales of \$1.3 million and \$1.2 million, respectively. These amounts have been included in cost of product sales in the accompanying Consolidated Statements of Comprehensive Income, from the sale of products purchased from Windset. The related accounts payable of \$146,000 and \$134,000 are included in accounts payable, related party in the accompanying Consolidated Balance Sheets as of March 1, 2015 and May 25, 2014, respectively.

All related party transactions are monitored quarterly by the Company and approved by the Audit Committee of the Board of Directors.

10. Stockholders' Equity

During the three months ended March 1, 2015, the Company granted options to purchase 90,000 shares of common stock and awarded 30,000 restricted stock units. During the nine months ended March 1, 2015, the Company granted options to purchase 120,000 shares of common stock and awarded 73,752 restricted stock units.

As of March 1, 2015 the Company has reserved 3.0 million shares of Common Stock for future issuance under its current and former equity plans.

On July 14, 2010, the Company announced that the Board of Directors of the Company had approved the establishment of a stock repurchase plan authorizing the repurchase of up to \$10 million of the Company's Common Stock. The Company may repurchase its common stock from time to time in open market purchases or in privately negotiated transactions. The timing and actual number of shares repurchased is at the discretion of management of the Company and will depend on a variety of factors, including stock price, corporate and regulatory requirements, market conditions, the relative attractiveness of other capital deployment opportunities and other corporate priorities. The stock repurchase program does not obligate Landec to acquire any amount of its common stock and the program may be modified, suspended or terminated at any time at the Company's discretion without prior notice. During the three and nine months ended March 1, 2015, the Company did not purchase any shares on the open market.

Consolidated Statements of Changes in Stockholders' Equity (in thousands, except share amounts):**Common Stock Shares**

| | |
|---|------------|
| Balance at May 25, 2014 | 26,815,253 |
| Stock options exercised, net of shares tendered | 53,429 |
| Vested restricted stock units, net of shares tendered | 29,496 |
| Balance at March 1, 2015 | 26,898,178 |

Common Stock

| | |
|---|------|
| Balance at May 25, 2014 | \$27 |
| Stock options exercised, net of shares tendered | — |
| Vested restricted stock units, net of shares tendered | — |
| Balance at March 1, 2015 | \$27 |

Additional Paid-in Capital

| | |
|--|-----------|
| Balance at May 25, 2014 | \$131,488 |
| Stock options exercised, net of shares tendered | 122 |
| Vested restricted stock units, net of shares tendered | — |
| Taxes paid by Company for stock swaps and restricted stock units | (12) |
| Stock-based compensation expense | 1,139 |
| Tax benefit from stock based compensation | 211 |
| Balance at March 1, 2015 | \$132,948 |

Retained Earnings

| | |
|--------------------------|----------|
| Balance at May 25, 2014 | \$71,554 |
| Net income | 9,348 |
| Balance at March 1, 2015 | \$80,902 |

Non-controlling Interest

| | |
|---|---------|
| Balance at May 25, 2014 | \$1,692 |
| Non-controlling interest in net income | 126 |
| Distributions to non-controlling interest | (196) |
| Balance at March 1, 2015 | \$1,622 |

11. Business Segment Reporting

The Company manages its business operations through three strategic business units. Based upon the information reported to the chief operating decision maker, who is the Chief Executive Officer, the Company has the following reportable segments: the Food Products Technology segment, the Food Export segment and the Hyaluronan-based Biomaterials segment.

The Food Products Technology segment markets and packs specialty packaged whole and fresh-cut fruit and vegetables, the majority of which incorporate the BreatheWay specialty packaging for retail grocery, club store and food services industries. In addition, the Food Products Technology segment sells BreatheWay packaging to partners for non-vegetable products. The Food Export segment consists of revenues generated from the purchase and sale of primarily whole commodity fruit and vegetable products to Asia and domestically. The HA-based Biomaterials segment sells products utilizing hyaluronan, a naturally occurring polysaccharide that is widely distributed in the extracellular matrix of connective tissues in both animals and humans, for medical use primarily in the Ophthalmic, Orthopedic and Veterinary markets. Corporate licenses Landec's patented Intellicoat® seed coatings to the farming industry and licenses the Company's Intelimer polymers for personal care products and other industrial products. The Corporate segment also includes general and administrative expenses, non-Food Products Technology and non HA-based Biomaterials interest income and income tax expenses. All of the assets of the Company are located within the United States of America.

The Company's international sales were as follows (in millions):

| | Three Months Ended | | Nine Months Ended | |
|-----------|-----------------------|-------------------------|----------------------|-------------------------|
| | March 1, 2015 | February 23, 2014 | March 1, 2015 | February 23, 2014 |
| Canada | \$21.6 | \$ 12.1 | \$56.8 | \$ 31.8 |
| Taiwan | \$2.2 | \$ 2.6 | \$27.8 | \$ 27.2 |
| Indonesia | \$1.6 | \$ 2.2 | \$8.1 | \$ 7.1 |
| China | \$0.4 | \$ 1.3 | \$7.7 | \$ 6.6 |
| Japan | \$1.1 | \$ 1.8 | \$6.2 | \$ 7.1 |
| Belgium | \$5.7 | \$ 11.1 | | |