

TreeHouse Foods, Inc.
Form 10-Q
November 07, 2012
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934
For the Quarterly Period Ended September 30, 2012.**

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 001-32504

TreeHouse Foods, Inc.

(Exact name of the registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

20-2311383
(I.R.S. employer identification no.)

2021 Spring Road, Suite 600

Oak Brook, IL
(Address of principal executive offices)

60523
(Zip Code)
(Registrant's telephone number, including area code) **(708) 483-1300**

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

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer (Do not check if a smaller reporting company)	<input type="checkbox"/>	Smaller reporting Company	<input type="checkbox"/>

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

Yes No

Number of shares of Common Stock, \$0.01 par value, outstanding as of October 31, 2012: 36,184,194

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Table of Contents**Part I Financial Information****Item 1. Financial Statements****TREEHOUSE FOODS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands, except per share data)

	September 30, 2012	December 31, 2011
	(Unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 83,797	\$ 3,279
Receivables, net	128,495	115,168
Inventories, net	391,306	329,374
Deferred income taxes	4,224	3,854
Prepaid expenses and other current assets	13,746	12,638
Assets held for sale	4,081	4,081
Total current assets	625,649	468,394
Property, plant and equipment, net	424,241	406,558
Goodwill	1,072,516	1,068,419
Intangible assets, net	424,046	437,860
Other assets, net	22,282	23,298
Total assets	\$ 2,568,734	\$ 2,404,529
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 200,993	\$ 169,525
Current portion of long-term debt	2,016	1,954
Total current liabilities	203,009	171,479
Long-term debt	953,474	902,929
Deferred income taxes	210,876	202,258
Other long-term liabilities	43,676	54,346
Total liabilities	1,411,035	1,331,012
Commitments and contingencies (Note 17)		
Stockholders' equity:		
Preferred stock, par value \$0.01 per share, 10,000 shares authorized, none issued		
Common stock, par value \$0.01 per share, 90,000 shares authorized, 36,169		
and 35,921 shares issued and outstanding, respectively	362	359
Additional paid-in capital	722,711	714,932
Retained earnings	443,725	380,588
Accumulated other comprehensive loss	(9,099)	(22,362)

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Total stockholders' equity		1,157,699		1,073,517
Total liabilities and stockholders' equity		\$ 2,568,734	\$	2,404,529

See Notes to Condensed Consolidated Financial Statements.

Table of Contents**TREEHOUSE FOODS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(In thousands, except per share data)

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
	(Unaudited)		(Unaudited)	
Net sales	\$ 538,112	\$ 528,050	\$ 1,589,344	\$ 1,514,183
Cost of sales	424,903	402,518	1,254,612	1,158,285
Gross profit	113,209	125,532	334,732	355,898
Operating expenses:				
Selling and distribution	32,546	34,932	100,698	106,750
General and administrative	27,929	27,376	77,237	87,221
Other operating expense, net	3,541	1,733	3,952	5,731
Amortization expense	7,848	8,839	24,735	25,207
Total operating expenses	71,864	72,880	206,622	224,909
Operating income	41,345	52,652	128,110	130,989
Other expense (income):				
Interest expense	12,760	12,610	38,410	39,931
Loss (gain) on foreign currency exchange	237	(5,620)	643	(5,065)
Other (income) expense, net	(614)	547	895	(170)
Total other expense	12,383	7,537	39,948	34,696
Income before income taxes	28,962	45,115	88,162	96,293
Income taxes	7,408	14,725	25,023	31,750
Net income	\$ 21,554	\$ 30,390	\$ 63,139	\$ 64,543
Net earnings per common share:				
Basic	\$.60	\$.84	\$ 1.75	\$ 1.81
Diluted	\$.58	\$.82	\$ 1.70	\$ 1.75
Weighted average common shares:				
Basic	36,149	35,967	36,116	35,721
Diluted	37,074	36,911	37,116	36,894

See Notes to Condensed Consolidated Financial Statements.

Table of Contents**TREEHOUSE FOODS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(In thousands)

	Three Months Ended September 30		Nine Months Ended September 30	
	2012	2011	2012	2011
	(Unaudited)		(Unaudited)	
Net income	\$ 21,554	\$ 30,390	\$ 63,139	\$ 64,543
Other comprehensive income (loss):				
Foreign currency translation adjustments	14,085	(17,829)	12,301	(10,453)
Pension and post-retirement reclassification adjustment (1)	280	169	841	507
Derivative reclassification adjustment (2)	40	40	121	120
Other comprehensive income (loss)	14,405	(17,620)	13,263	(9,826)
Comprehensive income	\$ 35,959	\$ 12,770	\$ 76,402	\$ 54,717

- (1) Net of tax of \$178 and \$106 for the three months ended September 30, 2012 and 2011, respectively, and \$530 and \$317 for the nine months ended September 30, 2012 and 2011, respectively.
- (2) Net of tax of \$25 for the three months ended September 30, 2012 and 2011, respectively, and \$76 for the nine months ended September 30, 2012 and 2011, respectively.

See Notes to Condensed Consolidated Financial Statements

Table of Contents**TREEHOUSE FOODS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

	Nine Months Ended September 30, 2012		2011	
	(Unaudited)			
Cash flows from operating activities:				
Net income	\$	63,139	\$	64,543
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation		42,088		36,473
Amortization		24,735		25,207
Gain on foreign currency exchange		(233)		(274)
Mark to market adjustment on derivative contracts		972		(1,742)
Excess tax benefits from stock-based compensation		(2,540)		(3,888)
Stock-based compensation		9,112		12,573
Loss on disposition of assets		2,572		663
Write-down of tangible assets				2,891
Deferred income taxes		8,248		5,303
Other		1,372		121
Changes in operating assets and liabilities, net of acquisitions:				
Receivables		(5,928)		(23,806)
Inventories		(51,593)		(81,540)
Prepaid expenses and other assets		1,313		2,447
Accounts payable, accrued expenses and other liabilities		11,313		11,908
Net cash provided by operating activities		104,570		50,879
Cash flows from investing activities:				
Additions to property, plant and equipment		(44,539)		(52,817)
Additions to other intangible assets		(6,812)		(7,615)
Acquisition of business, net of cash acquired		(25,000)		3,243
Proceeds from sale of fixed assets		42		233
Net cash used in investing activities		(76,309)		(56,956)
Cash flows from financing activities:				
Borrowings under revolving credit facility		276,600		225,600
Payments under revolving credit facility		(224,400)		(213,900)
Payments on capitalized lease obligations		(1,491)		(961)
Payment of deferred financing costs				(1,518)
Net payments related to stock-based award activities		(3,812)		(8,672)
Excess tax benefits from stock-based compensation		2,540		3,888
Net cash provided by financing activities		49,437		4,437
Effect of exchange rate changes on cash and cash equivalents		2,820		(1,603)
Net increase (decrease) in cash and cash equivalents		80,518		(3,243)
Cash and cash equivalents, beginning of period		3,279		6,323
Cash and cash equivalents, end of period	\$	83,797	\$	3,080

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See Notes to Condensed Consolidated Financial Statements.

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TREEHOUSE FOODS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

As of and for the nine months ended September 30, 2012

(Unaudited)

1. Basis of Presentation

The unaudited Condensed Consolidated Financial Statements included herein have been prepared by TreeHouse Foods, Inc. (the Company, we, us, or our), pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) applicable to quarterly reporting on Form 10-Q. In our opinion, these statements include all adjustments necessary for a fair presentation of the results of all interim periods reported herein. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted as permitted by such rules and regulations. The Condensed Consolidated Financial Statements and related notes should be read in conjunction with the Consolidated Financial Statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011. Results of operations for interim periods are not necessarily indicative of annual results.

The preparation of our Condensed Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires us to use our judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities at the date of the Condensed Consolidated Financial Statements, and the reported amounts of net sales and expenses during the reporting period. Actual results could differ from these estimates.

A detailed description of the Company's significant accounting policies can be found in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

2. Recent Accounting Pronouncements

In July 2012, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2012-02, *Intangibles Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment*, which is intended to simplify how an entity tests other intangible assets for impairment, by allowing companies the option of performing a qualitative assessment before calculating the fair value of the asset when testing indefinite-lived intangible assets for impairment. The ASU also revises the examples of events and circumstances that an entity should consider in interim periods. This ASU is effective for annual and interim period impairment tests performed for fiscal years beginning after September 15, 2012. This ASU does not change how intangible assets are accounted for, accordingly, the Company does not believe this ASU will have a significant impact on the Company's financial statements.

On June 16, 2011, the FASB issued ASU 2011-05, *Presentation of Comprehensive Income* which revises the manner in which entities present comprehensive income in their financial statements. This ASU removes the current presentation guidance and requires comprehensive income to be presented either in a single continuous statement of comprehensive income or two separate but consecutive statements. This guidance is effective for fiscal years and interim periods within those years, beginning after December 15, 2011. ASU 2011-05 does not change current accounting and adoption of this ASU did not have a significant impact on the Company's financial statements. The Company adopted this guidance using the two separate but consecutive statements approach.

On May 12, 2011, the FASB issued ASU 2011-04, *Fair Value Measurement: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. This ASU provides converged guidance on how (not when) to measure fair value. The ASU provides expanded disclosure requirements and other amendments, including those that eliminate unnecessary wording differences between U.S. GAAP and International Financial Reporting Standards (IFRS). This ASU is effective for interim and annual periods beginning after December 15, 2011 and adoption of this ASU did not have a significant impact on the Company's disclosures or fair value measurements as presented in Note 19.

Table of Contents**TREEHOUSE FOODS, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. Restructuring**

Soup restructuring - On August 7, 2012, following a strategic review of the soup category and its related business, the Company announced a restructuring plan that includes the closure of its Mendota, Illinois soup plant. Subsequently, the Company amended the plan to include reductions to the cost structure of the Pittsburgh, Pennsylvania facility by reorganizing and simplifying the soup business at the Pittsburgh facility. The restructuring will reduce manufacturing costs by streamlining operations and transferring production to the Company's Pittsburgh, Pennsylvania soup plant. Production at the Mendota facility was primarily related to the North American Retail Grocery segment and is expected to end in the first quarter of 2013, with full plant closure occurring in the same quarter. Total costs are expected to be approximately \$21.4 million as detailed below, of which \$6.4 million is expected to be in cash. The total expected costs increased from \$17.7 million, as previously reported, as estimates were refined. Expenses associated with the restructuring are aggregated in the Other operating expense, net line item of the Condensed Consolidated Statement of Income with the exception of accelerated depreciation, which is recorded in Cost of sales.

Seaforth, Ontario, Canada - On August 7, 2012, the Company announced the closure of its salad dressing plant in Seaforth, Ontario, Canada and the transfer of production to facilities where the Company has lower production costs. Production at the Seaforth, Ontario facility was primarily related to the North American Retail Grocery segment and is expected to end in the second quarter of 2013, with full plant closure expected in the third quarter of 2013. Total costs to close the Seaforth facility are expected to be approximately \$13.6 million as detailed below, of which \$6.5 million is expected to be in cash. The total expected costs decreased from \$17.3 million, as previously reported, as estimates were refined. Expenses incurred associated with the facility closure are aggregated in the Other operating expense, net line item of the Condensed Consolidated Statement of Income with the exception of accelerated depreciation, which is recorded in Cost of sales.

	Soup Restructuring		Seaforth Closure	
	Three and Nine Months Ended	Total Expected Costs	Three and Nine Months Ended	Total Expected Costs
	September 30, 2012	(In thousands)	September 30, 2012	(In thousands)
Accelerated depreciation	\$ 823	\$ 15,067	\$ 1,799	\$ 7,100
Severance and outplacement	75	2,625	2,136	3,930
Other closure costs	325	3,743	40	2,520
Total	\$ 1,223	\$ 21,435	\$ 3,975	\$ 13,550

As disclosed in footnote 4, the Company acquired substantially all of the assets of Naturally Fresh, Inc. Subsequent to the acquisition, during the third quarter of 2012, the Company closed the trucking operations of Naturally Fresh that were acquired in the purchase. This action resulted in approximately \$0.8 million of severance costs that are recorded in the Other operating expense, net line of the Condensed Consolidated Statements of Income.

Liabilities recorded as of September 30, 2012 associated with the restructurings include severance costs of \$2.7 million and are included in the Accounts payable and accrued expenses line of the Condensed Consolidated Balance Sheets. The table below presents a reconciliation of the severance liability as of September 30, 2012.

Severance Liability
(In thousands)

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Balance as of June 30, 2012	\$	
Expense		2,963
Payments		292
Balance as of September 30,2012	\$	2,671

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TREEHOUSE FOODS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Springfield, MO - As of December 31, 2011, the Company closed its pickle plant in Springfield, Missouri. Production ceased in August 2011 and has been transferred to other pickle facilities. Production at the Springfield facility was primarily related to the Food Away From Home segment. Closure costs for the three and nine months ended September 30, 2012 were insignificant. For the three and nine months ended September 30, 2011, total closure costs were \$1.4 million and \$4.6 million, respectively. These costs are included in Other operating expense, net line in our Condensed Consolidated Statements of Income.

4. Acquisitions

On April 13, 2012, the Company completed its acquisition of substantially all the assets of Naturally Fresh, Inc. (Naturally Fresh), a privately owned Atlanta, Georgia based manufacturer of refrigerated dressings, sauces, marinades, dips and specialty items sold within each of our segments. Naturally Fresh has annual revenues of approximately \$80 million. The purchase price was approximately \$26 million, net of cash. The acquisition was financed through borrowings under the Company's revolving credit facility. The acquisition expanded the Company's refrigerated manufacturing and packaging capabilities, broaden its distribution footprint and further develop its presence within the growing category of fresh foods. Naturally Fresh's Atlanta facility, coupled with the Company's existing West Coast and Chicago based refrigerated food plants, will allow the Company to more efficiently service customers from coast to coast.

The acquisition is being accounted for under the acquisition method of accounting and the results of operations are included in our financial statements from the date of acquisition and are in each of our segments. Included in the Company's Condensed Consolidated Statements of Income are Naturally Fresh net sales of \$21.1 million and \$39.7 million and operating income of \$0.3 million and loss of \$1.3 million for the three and nine months ended September 30, 2012, respectively. At the date of acquisition, the purchase price was allocated to the assets and liabilities acquired based upon fair market values, and is subject to adjustments. No goodwill was created with this acquisition and an insignificant bargain purchase gain was recognized and recorded in the Other operating (income) expense, net line of the Condensed Consolidated Statement of Income. Prior to recognizing the gain, the Company reassessed the fair value of the assets acquired and liabilities assumed in the acquisition. The insignificant bargain purchase gain is the result of the difference between the fair value of the assets acquired and the purchase price. Pro forma disclosures related to the transaction are not included since they are not considered material. We have made an allocation to net tangible and intangible assets acquired and liabilities assumed as follows:

Table of Contents**TREEHOUSE FOODS, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

	(In thousands)
Cash	\$ 975
Receivables	6,603
Inventory	8,574
Property plant and equipment	16,953
Customer relationships	1,300
Trade Names	800
Non-compete agreement	120
Other intangible assets	111
Other assets	1,176
Assumed liabilities	(9,641)
Fair value of net assets acquired	26,971
Gain on bargain purchase	(41)
Total purchase price	\$ 26,930

The Company allocated \$1.3 million to customer relationships that have an estimated life of twenty years, \$0.8 million to trade names that have an estimated life of ten years, \$0.1 million to a non-compete agreement with a life of five years, and \$0.1 million to other intangible assets with a weighted average life of approximately four years. The Company increased the cost of inventories by \$0.4 million, and expensed the amount as a component of cost of goods sold in the second quarter of 2012. The Company incurred approximately \$0.8 million in acquisition related costs. These costs are included in the General and administrative expense line of the Condensed Consolidated Statements of Income.

5. Inventories

	September 30, 2012	December 31, 2011
	(In thousands)	
Raw materials and supplies	\$ 138,089	\$ 115,719
Finished goods	273,372	233,408
LIFO reserve	(20,155)	(19,753)
Total	\$ 391,306	\$ 329,374

Approximately \$101.2 million and \$82.0 million of our inventory was accounted for under the Last-in, First-out (LIFO) method of accounting at September 30, 2012 and December 31, 2011, respectively.

6. Property, Plant and Equipment

	September 30, 2012	December 31, 2011
	(In thousands)	
Land	\$ 25,472	\$ 19,256

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Buildings and improvements	174,458	158,370
Machinery and equipment	460,750	417,156
Construction in progress	34,107	42,683
Total	694,787	637,465
Less accumulated depreciation	(270,546)	(230,907)
Property, plant and equipment, net	\$ 424,241	\$ 406,558

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Changes in the carrying amount of goodwill for the nine months ended September 30, 2012 are as follows:

	North American Retail Grocery	Food Away From Home	Industrial and Export	Total
	(In thousands)			
Balance at December 31, 2011	\$ 842,801	\$ 92,036	\$ 133,582	\$ 1,068,419
Currency exchange adjustment	3,583	514		4,097
Balance at September 30, 2012	\$ 846,384	\$ 92,550	\$ 133,582	\$ 1,072,516

The Company has not incurred any goodwill impairments since its inception.

The gross carrying amount and accumulated amortization of intangible assets other than goodwill as of September 30, 2012 and December 31, 2011 are as follows:

	September 30, 2012			December 31, 2011		
	Gross Carrying Amount	Accumulated Amortization (In thousands)	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization (In thousands)	Net Carrying Amount
Intangible assets with indefinite lives:						
Trademarks	\$ 33,121		\$ 33,121	\$ 32,155		\$ 32,155
Intangible assets with finite lives:						
Customer-related	448,340	(101,768)	346,572	444,540	(82,152)	362,388
Non-compete agreement	120	(12)	108	1,000	(1,000)	
Trademarks	20,810	(5,403)	15,407	20,010	(4,555)	15,455
Formulas/recipes	6,927	(4,366)	2,561	6,799	(3,302)	3,497
Computer software	41,677	(15,400)	26,277	35,721	(11,356)	24,365
Total	\$ 550,995	\$ (126,949)	\$ 424,046	\$ 540,225	\$ (102,365)	\$ 437,860

Amortization expense on intangible assets for the three months ended September 30, 2012 and 2011 was \$7.8 million and \$8.8 million, respectively, and \$24.7 million and \$25.2 million for the nine months ended September 30, 2012 and 2011, respectively. Estimated amortization expense on intangible assets for 2012 and the next four years is as follows:

	(In thousands)
2012	\$ 32,645
2013	\$ 31,330
2014	\$ 30,924
2015	\$ 29,819
2016	\$ 29,664

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	September 30, 2012	December 31, 2011
	(In thousands)	
Accounts payable	\$ 147,992	\$ 109,178
Payroll and benefits	25,068	17,079
Interest and taxes	8,465	20,659
Health insurance, workers' compensation and other insurance costs	6,400	5,584
Marketing expenses	6,182	7,148
Other accrued liabilities	6,886	9,877
Total	\$ 200,993	\$ 169,525

9. Income Taxes

Income tax expense was recorded at an effective rate of 25.6% and 28.4% for the three and nine months ended September 30, 2012, respectively, compared to 32.6% and 33.0% for the three and nine months ended September 30, 2011, respectively. The Company's effective tax rate is favorably impacted by an intercompany financing structure entered into in conjunction with the E.D. Smith Foods, Ltd. (E.D. Smith) acquisition in 2007. The decrease in the effective tax rate for the three and nine months ended September 30, 2012 as compared to 2011 is attributable to the tax impact of the repayment of certain intercompany debt, a decrease in the Canadian statutory tax rate and a decrease in state tax expense.

During the second quarter of 2012, the IRS initiated an examination of TreeHouse Foods' 2010 tax year, and the Canadian Revenue Agency (CRA) initiated an examination of the E.D. Smith 2008, 2009, and 2010 tax years. During the fourth quarter of 2011 the IRS initiated an examination of S.T. Specialty Foods, Inc.'s (S.T. Specialty Foods) pre-acquisition tax year ended October 28, 2010. The IRS and CRA ex