

BWAY CORP
Form 10-Q
May 07, 2009
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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 29, 2009

Commission	Registrant and State	I.R.S. Employer
File Number 001-33527	of Incorporation Address and Telephone Number BWAY Holding Company (Delaware) 8607 Roberts Drive, Suite 250 Atlanta, Georgia 30350-2237 (770) 645-4800	Identification Number 55-0800054
001-12415	BWAY Corporation (Delaware) 8607 Roberts Drive, Suite 250 Atlanta, Georgia 30350-2237 (770) 645-4800	36-3624491

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.

Registrant

BWAY Holding Company Yes No
BWAY Corporation 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

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for such shorter period that the registrant was required to submit and post such files).

Registrant

BWAY Holding Company Yes No

BWAY Corporation Yes No

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

Registrant	Large		Non-	Smaller Reporting Company
	Accelerated	Accelerated	Accelerated	
	Filer	Filer	Filer	
BWAY Holding Company	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
BWAY Corporation	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>

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

Registrant

BWAY Holding Company Yes No

BWAY Corporation Yes No

Shares Outstanding at

Registrant	Description of Common Stock	May 5, 2009
BWAY Holding Company	Par Value \$0.01 per share	21,907,380
BWAY Corporation	Par Value \$0.01 per share	1,000

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BWAY HOLDING COMPANY

BWAY CORPORATION

Quarterly Report on Form 10-Q

For the quarterly period ended March 29, 2009

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Table of Contents**PART I****FINANCIAL INFORMATION****Item 1. Financial Statements****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS****BWAY Holding Company and Subsidiaries**

(\$ in millions, except par value)

	March 29, 2009	September 28, 2008
Assets		
<u>Current Assets</u>		
Cash and cash equivalents	\$ 44.7	\$ 92.1
Accounts receivable, net of allowance for doubtful accounts of \$0.6 and \$1.2	98.2	113.3
Inventories, net	93.3	112.2
Other current assets	13.0	20.7
Total current assets	249.2	338.3
Property, plant and equipment, net	132.6	141.9
Goodwill	245.4	251.0
Other intangible assets, net	130.7	142.2
Other assets	7.4	9.0
Total assets	\$ 765.3	\$ 882.4
Liabilities and Stockholders' Equity		
<u>Current Liabilities</u>		
Accounts payable	\$ 62.2	\$ 149.8
Other current liabilities	47.3	52.4
Current portion of long-term debt	1.0	18.9
Total current liabilities	110.5	221.1
Long-term debt	393.2	402.4
Deferred tax liabilities	55.7	55.8
Other liabilities	29.3	29.4
Total liabilities	588.7	708.7
Commitments and contingencies (Note 11)		
<u>Stockholders' Equity</u>		
Preferred stock, \$0.01 par value, 20,000,000 shares authorized		
Common stock, \$0.01 par value, 200,000,000 shares authorized; 21,907,380 and 21,860,650 shares issued and outstanding	0.2	0.2
Additional paid-in capital	135.2	133.7
Retained earnings	46.5	40.5
Accumulated other comprehensive loss	(5.3)	(0.7)
Total stockholders' equity	176.6	173.7

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Total liabilities and stockholders' equity	\$ 765.3	\$ 882.4
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The accompanying notes are an integral part of the condensed consolidated financial statements.

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Table of Contents**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****BWAY Holding Company and Subsidiaries**

(\$ in millions, except per share amounts)

	Three Months Ended		Six Months Ended	
	March 29, 2009	March 30, 2008	March 29, 2009	March 30, 2008
Net sales	\$ 206.1	\$ 243.6	\$ 418.6	\$ 461.0
<u>Costs and expenses</u>				
Cost of products sold (excluding depreciation and amortization)	166.7	211.4	358.8	408.3
Depreciation and amortization	10.8	11.5	21.9	22.6
Selling and administrative	6.4	5.6	12.0	11.5
Restructuring	0.7	4.2	1.4	4.2
Interest, net	7.4	9.3	15.6	18.8
Other	0.2	0.1	(0.6)	0.2
Total costs and expenses	192.2	242.1	409.1	465.6
Income (loss) before income taxes	13.9	1.5	9.5	(4.6)
Provision for (benefit from) income taxes	5.2	0.4	3.5	(1.8)
Net income (loss)	\$ 8.7	\$ 1.1	\$ 6.0	\$ (2.8)
<u>Net income (loss) per share (Note 9)</u>				
Basic	\$ 0.40	\$ 0.05	\$ 0.27	\$ (0.13)
Diluted	0.38	0.05	0.26	(0.13)

The accompanying notes are an integral part of the condensed consolidated financial statements.

Table of Contents**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****BWAY Holding Company and Subsidiaries**

(\$ in millions)

	Six Months Ended	
	March 29, 2009	March 30, 2008
Cash Flows from Operating Activities		
Net income (loss)	\$ 6.0	\$ (2.8)
<u>Adjustments to reconcile net income (loss) to net cash used in operating activities</u>		
Depreciation	14.5	14.7
Amortization of other intangible assets	7.4	7.9
Amortization of deferred financing costs	1.0	1.1
Benefit from doubtful accounts	(0.5)	(0.9)
Deferred income taxes	0.1	(0.2)
Stock-based compensation expense	1.2	3.6
Changes in operating assets and liabilities:		
Accounts receivable	14.0	(8.9)
Inventories	17.6	(0.5)
Other assets	5.8	(0.4)
Accounts payable	(85.5)	(24.7)
Other liabilities	(4.9)	(2.8)
Income taxes, net	2.3	(4.3)
Net cash used in operating activities	(21.0)	(18.2)
Cash Flows from Investing Activities		
Capital expenditures	(6.7)	(20.4)
Net cash used in investing activities	(6.7)	(20.4)
Cash Flows from Financing Activities		
Repayments of long-term debt	(18.1)	(0.7)
Principal repayments under capital lease obligations	(0.1)	(0.1)
Net cash used in financing activities	(18.2)	(0.8)
Effect of exchange rate changes on cash and cash equivalents	(1.5)	(0.3)
Net decrease in cash and cash equivalents	(47.4)	(39.7)
Cash and cash equivalents, beginning of period	92.1	53.4
Cash and cash equivalents, end of period	\$ 44.7	\$ 13.7

The accompanying notes are an integral part of the condensed consolidated financial statements.

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(\$ in millions, except par value)

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Long-term debt	393.2	402.4
Deferred tax liabilities	55.7	55.8
Other liabilities	29.3	29.4
Total liabilities	588.7	708.7
Commitments and contingencies (Note 11)		
<u>Stockholder's Equity</u>		
Preferred stock, \$0.01 par value, 500 shares authorized		
Common stock, \$0.01 par value, 2,500 shares authorized; 1,000 shares issued and outstanding		
Additional paid-in capital	141.9	140.4
Retained earnings	40.0	34.0
Accumulated other comprehensive loss	(5.3)	(0.7)
Total stockholder's equity	176.6	173.7
Total liabilities and stockholder's equity	\$ 765.3	\$ 882.4

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Other	0.2	0.1	(0.6)	0.2
Total costs and expenses	192.2	242.1	409.1	465.6
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Depreciation	14.5	14.7
Amortization of other intangible assets	7.4	7.9
Amortization of deferred financing costs	1.0	1.1
Benefit from doubtful accounts	(0.5)	(0.9)
Deferred income taxes	0.1	(0.2)
Stock-based compensation expense	1.2	3.6
Changes in operating assets and liabilities:		
Accounts receivable	14.0	(8.9)
Inventories	17.6	(0.5)
Other assets	5.8	(0.4)
Accounts payable	(85.5)	(24.7)
Other liabilities	(4.9)	(2.8)
Income taxes, net	2.3	(4.3)
Net cash used in operating activities	(21.0)	(18.2)
Cash Flows from Investing Activities		
Capital expenditures	(6.7)	(20.4)
Net cash used in investing activities	(6.7)	(20.4)
Cash Flows from Financing Activities		
Repayments of long-term debt	(18.1)	(0.7)
Principal repayments under capital lease obligations	(0.1)	(0.1)
Net cash used in financing activities	(18.2)	(0.8)
Effect of exchange rate changes on cash and cash equivalents	(1.5)	(0.3)
Net decrease in cash and cash equivalents	(47.4)	(39.7)
Cash and cash equivalents, beginning of period	92.1	53.4
Cash and cash equivalents, end of period	\$ 44.7	\$ 13.7

The accompanying notes are an integral part of the condensed consolidated financial statements.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

BWAY Holding Company and Subsidiaries

BWAY Corporation and Subsidiaries

1. GENERAL

Principles of Consolidation and Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of BWAY Holding Company (BHC) include the accounts of BHC and its wholly-owned subsidiary, BWAY Corporation (BWAY). The accompanying unaudited condensed consolidated financial statements of BWAY include the accounts of BWAY and its subsidiaries, each wholly-owned. In these notes, BHC and BWAY are collectively referred to as the Company, we or our.

The unaudited condensed consolidated financial statements and these notes should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended September 28, 2008 (the Annual Report). The unaudited condensed consolidated financial statements include all normal recurring adjustments necessary for a fair presentation of the financial position, results of operations and cash flows for the periods presented. Certain information and footnote disclosures, including critical and significant accounting policies, normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted.

These notes are applicable equally to BHC and BWAY with the exception of Net Income (Loss) per Share in Note 9, Stockholders Equity, which is applicable only to BHC and Note 14, Supplemental Guarantor Subsidiaries Information, which is applicable only to BWAY.

Results of operations and cash flows for interim periods presented in the unaudited condensed consolidated financial statements are not necessarily indicative of results of operations or cash flows that may be expected for the full fiscal year.

Unless otherwise indicated, references in these notes to years relate to fiscal years and references to U.S. based subsidiaries or operations include the Commonwealth of Puerto Rico.

Our fiscal year ends on the Sunday closest to September 30. Our North America Packaging Corporation (NAMPAC) and ICL Industrial Containers ULC (ICL) subsidiaries report their financial position, results of operations and cash flows on a calendar month basis with a fiscal year ending on September 30. NAMPAC and ICL are included in the unaudited condensed consolidated financial statements as of March 29, 2009 and September 28, 2008 and for the three and six months ended March 29, 2009 and March 30, 2008. There were no significant or unusual transactions between the calendar and fiscal ending dates that should have been considered in the consolidated financial statements.

Business and Segment Information

BHC is a holding company without independent operations. BWAY, the operating subsidiary of BHC, manufactures and distributes metal and rigid plastic containers primarily to manufacturers of industrial and consumer products for use as packaging. We have operations in the United States and Canada and primarily sell to customers located in these geographic markets. We report our operations in two business segments: metal packaging and plastic packaging (see Note 12, Business Segments.)

Recent Accounting Pronouncements Not Yet Adopted

In March 2008, the Financial Accounting Standards Board (the FASB) issued Statement of Financial Accounting Standards (SFAS) No.161, Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No.133 (SFAS No.161). SFAS No.161 is intended to enhance the current disclosure

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framework of FASB Statement No.133, Accounting for Derivative Instruments and Hedging Activities. SFAS No.161 is effective for us at the beginning of 2010. We are currently evaluating the potential impact of SFAS No. 161 on the financial statements.

2. SUPPLEMENTAL CASH FLOW DISCLOSURES

The following information supplements the unaudited condensed consolidated statements of cash flows for the six months ended March 29, 2009 and March 30, 2008:

(\$ in millions)

	Six Months Ended	
	March 29, 2009	March 30, 2008
<u>Cash paid during the period for:</u>		
Interest	\$ 13.6	\$ 19.4
Income taxes	1.3	2.6
<u>Non-cash investing and financing activities</u>		
Amounts owed for capital expenditures	\$ 0.7	\$ 1.9
Assets acquired through capital lease		0.4

3. INVENTORIES

The components of inventories as of March 29, 2009 and September 28, 2008 were:

(\$ in millions)

	March 29, 2009	September 28, 2008
Raw materials	\$ 24.3	\$ 32.6
Work-in-progress	39.0	39.0
Finished goods	30.0	40.6
Total inventories	\$ 93.3	\$ 112.2

4. OTHER CURRENT ASSETS AND LIABILITIES

The components of other current assets and other current liabilities as of March 29, 2009 and September 28, 2008 were:

(\$ in millions)

	March 29, 2009	September 28, 2008
<u>Other current assets</u>		
Income taxes receivable	\$ 0.4	\$ 2.8
Deferred tax assets	7.2	7.2

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Other		5.4		10.7
Total other current assets		\$ 13.0		\$ 20.7
<u>Other current liabilities</u>				
Accrued salaries and wages		\$ 12.1		\$ 13.5
Accrued interest		11.1		10.1
Accrued rebates		6.3		10.6
Other		17.8		18.2
Total other current liabilities		\$ 47.3		\$ 52.4

Table of Contents**5. GOODWILL AND OTHER INTANGIBLE ASSETS****Goodwill**

The change in goodwill for the six months ended March 29, 2009 by reportable segment was:

(\$ in millions)

	Metal Packaging	Plastic Packaging	Total
Balance, September 28, 2008	\$ 122.3	\$ 128.7	\$ 251.0
Currency translation adjustment	(1.7)	(3.9)	(5.6)
Balance, March 29, 2009	\$ 120.6	\$ 124.8	\$ 245.4

Other Intangible Assets

The components of other intangible assets as of March 29, 2009 and September 28, 2008 were:

(\$ in millions)

	March 29, 2009			September 28, 2008		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
<u>Amortizable intangible assets</u>						
Customer relationships	\$ 180.8	\$ (66.9)	\$ 113.9	\$ 185.5	\$ (61.5)	\$ 124.0
Tradenames	25.7	(9.5)	16.2	26.2	(8.6)	17.6
Total amortizable intangible assets	206.5	(76.4)	130.1	211.7	(70.1)	141.6
<u>Unamortizable intangible assets</u>						
Technology	0.6		0.6	0.6		0.6
Total other intangible assets	\$ 207.1	\$ (76.4)	\$ 130.7	\$ 212.3	\$ (70.1)	\$ 142.2

The useful lives of customer relationships range from 14 to 18 years and the useful lives of tradenames range from 10 to 15 years.

Expected Future Amortization Expense

Expected future amortization expense as of March 29, 2009 was:

(\$ in millions)

<u>Fiscal year</u>	Amortization Expense
2009 (remainder)	\$ 7.4

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2010	14.6
2011	14.0
2012	13.4
2013	12.4
Thereafter	68.3
Total expected future amortization expense	\$ 130.1

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Long-term debt outstanding as of March 29, 2009 and September 28, 2008 consisted of:

(\$ in millions)

	March 29, 2009	September 28, 2008
<u>Long-term debt</u>		
10% senior subordinated notes due October 2010	\$ 200.0	\$ 200.0
Variable rate term loan, U.S. dollar denominated, maturing July 2013	153.8	168.2
Variable rate term loan, Canadian dollar denominated, maturing July 2013	40.4	53.1
Total long-term debt	394.2	421.3
Less current portion of long-term debt	(1.0)	(18.9)
Long-term debt, net of current portion	\$ 393.2	\$ 402.4

The current portion of long-term debt as of September 28, 2008 included a mandatory repayment of \$18.4 million. Of the repayment, \$14.0 million represented a repayment on the U.S. dollar denominated term loan and \$4.4 million represented a repayment on the Canadian dollar denominated term loan (at the time of repayment, the amount was \$3.7 million due to a change in the exchange rate between the U.S. dollar and the Canadian dollar.) The repayments occurred in December 2008.

The current portion of long-term debt as of September 28, 2008 also included a \$0.5 million scheduled repayment on the U.S. dollar denominated term loan that occurred on September 30, 2008. Under the terms of the credit agreement, non-scheduled repayments generally reduce the subsequent four scheduled payments and then reduce the remaining payments thereafter on a pro rata basis. The next scheduled repayments on the term loans are not due until December 2009 because of the prepayments in December 2008.

The weighted-average interest rate on variable rate credit facility borrowings as of March 29, 2009 and September 28, 2008 was approximately 3.7% and 4.8%, respectively.

Scheduled Maturities of Long-Term Debt

Scheduled maturities of long-term debt as of March 29, 2009 were:

(\$ in millions)

<u>Fiscal year</u>	Amount Due
2009 (<i>remainder</i>)	\$
2010	2.0
2011	202.0
2012	2.0
2013	188.2
Thereafter	
Total scheduled maturities of long-term debt	\$ 394.2

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Senior Subordinated Notes

All of BWAY's U.S. subsidiaries have fully and unconditionally guaranteed \$200.0 million principal amount of 10% Senior Subordinated Notes due October 15, 2010 (the 2010 Notes). The notes were redeemable prior to maturity at 101.67% of the principal amount during the twelve-month period that began on October 15, 2008. In the third quarter of 2009, BWAY redeemed all of the 2010 Notes. The notes were redeemed, in part, with the proceeds of a new senior subordinated note offering due 2014. See Note 13, Subsequent Event.

As of March 29, 2009, we were in compliance with applicable financial covenants related to the senior notes.

Credit Facility

Our credit facility consists of a U.S. denominated term loan (the U.S. term loan), a \$50.0 million revolving credit facility (the U.S. revolver), a Canadian denominated term loan (the Canadian term loan) and a US\$5.0 million equivalent revolving credit facility (the Canadian revolver), (collectively, the credit facility). We initially borrowed \$190.0 million on the U.S. term loan and Cdn\$56.4 million (US\$50.0 million equivalent at the borrowing date) on the Canadian term loan. We have subsequently made repayments of these term loans that we may not re-borrow.

BWAY is the borrower of the U.S. term loan and only BWAY can borrow on the U.S. revolver. ICL is the borrower of the Canadian term loan and only ICL can borrow on the Canadian revolver. The Canadian revolver can be drawn in either U.S. dollars or Canadian dollars, at the option of the borrower.

The term loans mature on July 17, 2013 and the revolving credit facilities mature on July 17, 2012.

The term loans are subject to scheduled quarterly repayments. Scheduled repayments may be offset by voluntary prepayments or by mandatory repayments. In December 2008, we made a \$14.0 million mandatory repayment on the U.S. term loan and a \$3.7 million mandatory repayment on the Canadian term loan. These mandatory repayments offset the scheduled quarterly repayments for 2009. Scheduled quarterly repayments of approximately \$0.4 million on the U.S. term loan and approximately \$0.1 million on the Canadian term loan will resume in December 2009 and continue through March 31, 2013. The remaining unpaid balance is due on the maturity date.

Amounts repaid on the term loans may not be re-borrowed. The mandatory repayments in December 2008 represented a portion of excess cash flow, as defined in the credit agreement, from 2008.

Interest accrues on the term loans at a variable base rate plus a fixed margin. As of March 29, 2009, the effective interest rate on outstanding U.S. and Canadian term loan borrowings was approximately 3.6% and 4.0%, respectively.

Interest on outstanding revolving credit facility borrowings, if any, accrues at a variable base rate plus a variable margin. The margin is based on a consolidated total leverage ratio, as defined in the credit agreement. As of March 29, 2009, we had \$5.7 million in standby letter of credit commitments that reduced the amount available to borrow under the U.S. revolver to \$44.3 million. As of March 29, 2009, we had \$0.1 million in standby letter of credit commitments that reduced the amount available to borrow under the Canadian revolver to \$4.9 million.

BHC and each of our U.S. subsidiaries have guaranteed the U.S. term loan and U.S. revolver, each of which is secured by substantially all the U.S. assets of BWAY and the assets of BHC. In addition, we have pledged as collateral all of the issued and outstanding stock of our U.S. subsidiaries, which are wholly-owned, and, subject to certain limitations, the outstanding stock of ICL. ICL has guaranteed the Canadian term loan and Canadian revolver, each of which is secured by all of the assets of ICL.

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The credit agreement contains covenants that, among other things, limit our ability (and the ability of some or all of our subsidiaries) to: incur additional debt, pay dividends or distributions on our capital stock or to repurchase our capital stock, make certain investments, loans or advances, create liens on our assets to secure debt, engage in transactions with affiliates, merge or consolidate with another company, transfer and sell assets and make acquisitions. We are limited in the amount of capital expenditures we may expend annually, and we may be required to make mandatory repayments of the term loans based on excess cash flow.

We are required to maintain a minimum consolidated interest coverage ratio, as defined in the credit agreement, and to not exceed a maximum consolidated total leverage ratio, as defined in the credit agreement. The calculation of these ratios is based on consolidated EBITDA, which, as defined in the credit agreement, permits certain adjustments including cash restructuring charges. However, these adjustments, including cash restructuring charges, may be limited over a certain period or in the aggregate.

The required minimum consolidated interest coverage ratio is 3.05. For the twelve months ended March 29, 2009, the consolidated total leverage ratio could not exceed 3.80. These ratios are determined at the end of each quarter for the twelve month period then ended.

The covenants contained in the credit agreement, including the ratios discussed above, are subject to a number of important limitations and exceptions. As of March 29, 2009, we were in compliance with all applicable financial covenants contained in the credit agreement.

Deferred Financing Costs

We are amortizing approximately \$15.0 million in financing costs related to the senior notes and credit facility. Financing costs are amortized to interest expense over the term of the related debt utilizing a method that approximates the effective yield method. As of March 29, 2009 and September 28, 2008, approximately \$5.7 million and \$6.9 million, respectively, of the deferred costs remained to be amortized. Deferred financing costs are recorded in other assets.

In the third quarter of 2009, BWAY redeemed the 2010 Notes and wrote-off the related unamortized deferred financing costs. BWAY also issued new notes and deferred the related financing costs, which will be amortized over the term of the notes. See Note 13, Subsequent Event.

7. EMPLOYEE BENEFIT OBLIGATIONS**Employee Benefit Obligation Liabilities**

Employee benefit obligations as of March 29, 2009 and September 28, 2008 were:

(\$ in millions)

	March 29, 2009	September 28, 2008
<u>Employee benefit obligation liabilities</u>		
Defined benefit pension plan	\$ 3.4	\$ 3.5
Retiree medical and other postretirement benefits	6.8	6.7
Deferred compensation	6.0	6.0
Total employee benefit obligation liabilities	\$ 16.2	\$ 16.2

As of March 29, 2009 and September 28, 2008, approximately \$1.2 million of employee benefit obligation liabilities were recorded in other current liabilities and approximately \$15.0 million of employee benefit obligation liabilities were recorded in other liabilities.

Table of Contents**Components of Net Periodic Benefit Cost**

The components of net periodic benefit costs for the three and six months ended March 29, 2009 and March 30, 2008 were:

(\$ in millions)

	Three Months Ended		Six Months Ended	
	March 29, 2009	March 30, 2008	March 29, 2009	March 30, 2008
<u>Defined benefit pension plan</u>				
Interest cost	\$ 0.2	\$ 0.1	\$ 0.4	\$ 0.3
Expected return on plan assets	(0.2)	(0.2)	(0.3)	(0.4)
		(0.1)	0.1	(0.1)
<u>Other benefits</u>				
Interest cost	0.1	0.1	0.2	0.2
Total net period benefit cost	\$ 0.1	\$	\$ 0.3	\$ 0.1

Multiemployer Pension Liabilities

As of March 29, 2009 and September 28, 2008, we had accrued pension withdrawal liabilities of \$3.4 million related to multiemployer pension plans that covered certain union employees at our facility in Franklin Park, Illinois (Franklin Park) that we closed in 2008 (see Note 8, Restructuring.)

8. RESTRUCTURING

In connection with our on-going productivity and cost-savings initiatives, in March 2008 we announced our intent to close Franklin Park and in May 2008 we announced our intent to close our manufacturing facility in Cleveland, Ohio (Cleveland.) We began the closure of Franklin Park during the second quarter of 2008 and began the closure of Cleveland during the third quarter of 2008. As of September 28, 2008, operations had ceased at these facilities and as of March 30, 2009 the closure of these facilities was substantially complete.

In the first six months of 2009, we eliminated approximately 50 salaried positions and recorded a restructuring charge of approximately \$0.5 million related to severance and benefits. We recorded a restructuring charge of \$0.4 million in the first six months of 2009 primarily related to severance and benefits for the closure of Cleveland, costs associated with the removal of equipment from the closed facilities and holding costs associated with the closed facilities. We expect to record additional restructuring charges of approximately \$0.3 million during the remainder of 2009 related to these restructuring plans.

The restructuring plans for Franklin Park and Cleveland are discussed in further detail in Note 15, Restructuring and Reorganization Liabilities, of Notes to Consolidated Financial Statements in Item 8 of the Annual Report.

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The components of restructuring liabilities by reportable segment as of September 28, 2008 and March 29, 2009 and the change in the liabilities during the six months ended March 29, 2009 were:

(\$ in millions)

	Balance, September 28, 2008	Additions	Expenditures	Balance, March 29, 2009
<u>Plastic packaging segment</u>				
Severance and benefit costs	\$ 0.5	\$ 0.2	\$ (0.6)	\$ 0.1
Facility closure costs	1.1	0.4	(0.5)	1.0
Total plastic packaging segment restructuring liability	1.6	0.6	(1.1)	1.1
<u>Metal packaging segment</u>				
Severance and benefit costs	0.2	0.4	(0.6)	
Pension withdrawal liabilities	3.4			3.4
Facility closure costs	1.6	0.4	(0.7)	1.3
Total metal packaging segment restructuring liability	5.2	0.8	(1.3)	4.7
Total restructuring liabilities	\$ 6.8	\$ 1.4	\$ (2.4)	\$ 5.8

As of September 28, 2008 and March 29, 2009, restructuring liabilities were recorded in the other current liabilities with the exception of \$3.4 million related to the Franklin Park pension withdrawal liabilities which were recorded in other liabilities.

9. STOCKHOLDERS EQUITY**Net Income (Loss) per Share**

Net income (loss) per share for the three and six months ended March 29, 2009 and March 30, 2008 was:

(\$ in millions, except per share amounts)

	Three Months Ended		Six Months Ended	
	March 29, 2009	March 30, 2008	March 29, 2009	March 30, 2008
Net income (loss)	\$ 8.7	\$ 1.1	\$ 6.0	\$ (2.8)
<u>Basic net income (loss) per share</u>				
Weighted-average number of shares outstanding (000s)	21,907	21,679	21,886	21,670
Basic net income (loss) per share	\$ 0.40	\$ 0.05	\$ 0.27	\$ (0.13)
<u>Diluted net income (loss) per share</u>				
Weighted-average number of shares outstanding (000s)	21,907	21,679	21,886	21,670
Dilutive effect of stock options (000s)	1,088	2,471	1,021	
	22,995	24,150	22,907	21,670

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Weighted-average number of shares outstanding assuming dilution
(000s)

Diluted net income (loss) per share	\$ 0.38	\$ 0.05	\$ 0.26	\$ (0.13)
Common stock equivalents excluded from the computation of diluted earnings per share due to anti-dilutive effect (000s)	952	382	900	2,853

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Table of Contents**Comprehensive Income (Loss) Information**

The components of comprehensive income (loss) for the three and six months ended March 29, 2009 and March 30, 2008 were:

(\$ in millions)

	Three Months Ended		Six Months Ended	
	March 29, 2009	March 30, 2008	March 29, 2009	March 30, 2008
<u>Comprehensive Income (Loss)</u>				
Net income (loss)	\$ 8.7	\$ 1.1	\$ 6.0	\$ (2.8)
Foreign currency translation adjustments	(0.5)	(1.1)	(4.6)	(0.8)
Comprehensive income (loss)	\$ 8.2	\$	\$ 1.4	\$ (3.6)

The components of accumulated other comprehensive loss as of September 28, 2008 and March 29, 2009 and the change during the period were:

(\$ in millions)

	Pension and Other Postretirement Items (net of tax)	Cumulative Foreign Currency Translation Adjustments	Total Accumulated Other Comprehensive Loss
<u>Accumulated other comprehensive loss</u>			
Balance, September 28, 2008	\$ (2.5)	\$ 1.8	\$ (0.7)
Change		(4.6)	(4.6)
Balance, March 29, 2009	\$ (2.5)	\$ (2.8)	\$ (5.3)

10. SHARE-BASED COMPENSATION**Summary of Share-Based Compensation Plans**

Our share-based compensation plans are described in Note 10, Share-Based Compensation, of Notes to Consolidated Financial Statements in Item 8 of the Annual Report.

In the first six months of 2009, options to acquire 145,000 shares of BHC common stock were granted under the BWAY Holding Company 2007 Annual Incentive Plan (the Omnibus Incentive Plan). As of March 29, 2009, there were 1,825,767 options available for grant under the Omnibus Incentive Plan. All options outstanding under the Omnibus Incentive Plan will vest annually in three equal tranches beginning on the first anniversary of the grant date.

There were no grants under the Amended and Restated BCO Holding Stock Incentive Plan (the Holding Incentive Plan) during the six months ended March 29, 2009. In December 2008, the compensation committee of the board of directors terminated the Holding Incentive Plan. The termination does not affect outstanding options previously granted under the plan.

As of March 29, 2009, unvested options outstanding under the Holding Incentive Plan will become vested in three equal tranches based on an average per share closing price of BHC common stock over a consecutive 45 day period with a minimum closing price on the 45th day for each tranche. The first tranche will vest if the average per share closing price of BHC's common stock over any consecutive 45 day period during

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which the stock trades is at least \$19.26 and the closing price on the 45th such day is at least \$16.37.

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The weighted-average fair value at the grant date for options granted during the first six months of 2009 was \$2.70 per share subject to option, which we estimated utilizing a Black-Scholes valuation model with the following weighted-average assumptions: (i) no dividend yield on BHC's common stock; (ii) expected stock price volatility of 40.0%; (iii) a risk-free interest rate of 1.7%; and (iv) an expected option term of 6.0 years. The common stock of BHC has only been publicly traded for a limited period and sufficient historical data does not exist to provide a reasonable basis upon which to estimate an expected option term. As such, we use the simplified method provided for in SEC Staff Accounting Bulletin (SAB) Topic 14.D.2, Share-Based Payment Certain Assumptions Used in Valuation Methods Expected Term, which is applicable to plain vanilla options and for companies that conclude that historical exercise experience does not provide a reasonable basis upon which to estimate an expected term. All options granted during the first six months of 2009 were plain vanilla.

Stock-Based Compensation Expense

Stock-based compensation expense for the three and six months ended March 29, 2009 and March 30, 2008 was recorded in the statement of operations as follows:

(\$ in millions)

	Three Months Ended		Six Months Ended	
	March 29, 2009	March 30, 2008	March 29, 2009	March 30, 2008
<u>Stock-based compensation expense</u>				
Cost of products sold (excluding depreciation and amortization)	\$ (0.2)	\$ 0.5	\$	\$ 1.0
Selling and administrative expense	0.5	1.3	1.2	2.6
Total stock-based compensation expense	\$ 0.3	\$ 1.8	\$ 1.2	\$ 3.6

Stock-based compensation expense is included in undistributed corporate expense in the business segment disclosure in Note 12, Business Segments.

The vesting criteria for certain unvested options outstanding under the Holding Incentive Plan as of the public offering of BHC common stock in 2007 were modified to condition vesting based on the market performance of BHC common stock. The modification resulted in stock-based compensation expense to be recognized over a derived service period of approximately 38 months beginning in June 2007. We have recognized approximately \$9.6 million of the expense through March 29, 2009 and expect to recognize approximately \$0.4 million in the remainder of 2009. Stock-based compensation expense in the three and six months ended March 29, 2009 and March 30, 2008 related to this modification with the exception of less than \$0.1 million that related to grants subsequent to the public offering.

Although the entire expense related to the modification will be fully accrued in fiscal 2009, until the related options are vested (based on the performance criteria discussed above), future stock-based compensation expense may be reduced for any forfeitures of the unvested options in excess of estimated forfeiture rates (primarily because of employee terminations).

11. COMMITMENTS AND CONTINGENCIES**Environmental**

We are subject to a broad range of federal, state, provincial and local environmental, health and safety laws, including those governing discharges to air, soil and water, the handling and disposal of hazardous substances and the investigation and remediation of contamination resulting from the release of hazardous substances. We

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believe that we are currently in material compliance with all applicable environmental, health and safety laws, although future expenditures may be necessary in order to maintain such compliance, including compliance with air emission control requirements for volatile organic compounds. In addition, in the course of operations we use, store and dispose of hazardous substances.

Some of our current and former facilities are currently involved in environmental investigations, remediation or other claims resulting from the release of hazardous substances or the presence of other contaminants. Except to the extent otherwise disclosed, we believe the likelihood is remote that any material losses may have resulted from identified environmental remediation matters or environmental investigations relating to current or former facilities. While we do not believe that any identified investigation or remediation obligations will have a material adverse effect on our financial position, results of operations or cash flows, there is no assurance that such obligations will not arise in the future. Many of our facilities have a history of industrial usage for which investigation and remediation obligations could arise in the future and which could have a material adverse effect on our financial position, results of operations or cash flows.

In a letter dated March 14, 2007, the United States Environmental Protection Agency (EPA) informed us that corrective action was required at our Cincinnati facility to address documented releases of hazardous substances at the site. The documented releases referenced by the EPA occurred prior to our ownership of the site. The EPA has requested that we enter into an Administrative Order on Consent under the Resource Conservation and Recovery Act (RCRA) with respect to corrective action obligations. We are working with the EPA to address their concerns, and we have notified the former owner of the site that we believe has indemnity obligations to us with respect to these claims.

In July 2008, we received a letter from the EPA stating that certain requirements of the RCRA were violated, based on a compliance review inspection, at our Homerville facility. We settled this matter in the second quarter of 2009 for \$0.2 million, which was accrued as of March 29, 2009 and September 28, 2008.

From time to time, we receive requests for information or are identified as a potentially responsible party (PRP) pursuant to the Federal Comprehensive Environmental Response, Compensation and Liability Act or analogous state laws with respect to off-site waste disposal sites utilized by current or former facilities or our predecessors in interest. We do not believe that any of these identified matters will have a material adverse effect on our financial position, results of operations or cash flows. We cannot, however, provide assurance that such obligations will not arise in the future.

We are a member of a PRP group related to a waste disposal site in Georgia. Our status as a PRP was based on documents indicating that waste materials were transported to the site from our Homerville, Georgia facility prior to our acquisition of the facility in 1989. We joined the PRP group in order to reduce exposure, which is estimated to be approximately \$0.1 million.

We record reserves for environmental liabilities when environmental investigation and remediation obligations are probable and related costs are reasonably estimable. The amounts related to these liabilities (including those amounts noted above) are included in other current liabilities and were approximately \$0.4 million as of March 29, 2009 and as of September 28, 2008. These accruals are estimates and future expenditures may exceed these amounts.

Self Insurance

The majority of our medical and workers' compensation benefits are under high-deductible plans with certain stop loss arrangements. We determine our workers' compensation liability using actuarial data based on filed claims, and we determine our medical claims liability based on our analysis of actual claims. The amounts related to these claims are included in other current liabilities and were \$6.4 million as of March 29, 2009 and \$7.4 million as of September 28, 2008.

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Litigation

We are involved in legal proceedings from time to time in the ordinary course of business. We believe that the outcome of these proceedings will not have a material effect on our financial condition, results of operations or cash flows. We are also involved in certain proceedings relating to environmental matters as described under Environmental above. We had accrued liabilities relating to pending litigation matters, other than as discussed below, of approximately \$0.7 million and \$0.4 million as of March 29, 2009 and September 28, 2008, respectively.

As of March 29, 2009 and September 28, 2008, we had accrued approximately \$0.2 million in legal fees and expenses related to lead paint litigation, which is described under Lead Paint Litigation in Note 16, Contingencies, of Notes to Consolidated Financial Statements in Item 8 of the Annual Report.

Letters of Credit

As of March 29, 2009, a bank had issued standby letters of credit on our behalf in the aggregate amount of \$5.8 million primarily in favor of our workers' compensation insurers.

Collective Bargaining Agreements

As of March 29, 2009, approximately 29% of our hourly workforce was covered by seven separate collective bargaining agreements. One of the collective bargaining agreements, representing approximately 14% of our unionized workforce, will become amendable in 2009.

Commodity Risk

We are subject to various risks and uncertainties related to changing commodity prices for, and the availability of, the raw materials (primarily steel and plastic resin) and energy (primarily electricity and natural gas) used in our manufacturing processes.

In 2008, we purchased approximately 80% of our steel requirements from four suppliers of steel. During 2009, we expect to continue to purchase approximately 80% of our steel requirements from at least four suppliers of steel.

12. BUSINESS SEGMENTS

Our operations are organized and reviewed by management along our product lines in two reportable segments: metal packaging and plastic packaging. We operate these reportable segments as separate divisions and differentiate the segments based on the nature of the products they manufacture. The primary raw material and manufacturing process are unique for each segment. Our business segments are further described below.

Metal Packaging. The metal packaging segment includes the metal packaging products that we have historically offered. Primary products in this segment include paint cans, aerosol containers, ammunition boxes and other general line containers made from steel. Metal packaging is included in a separate division of the company with management and production facilities and processes distinct from our plastic packaging segment. The metal packaging segment includes steel pails manufactured by ICL.

Plastic Packaging. The plastic packaging segment includes the plastic packaging products manufactured and distributed by NAMPAC and ICL. Primary products in this segment include open- and tight-head pails and drums and other multi-purpose rigid industrial plastic packaging. Plastic packaging is included in a separate division of the company with management and production facilities and processes distinct from our metal packaging segment.

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We do not allocate stock-based compensation expense or certain administrative expenses, related primarily to accounting and finance, information technology, payroll and human resources and other general administrative expenses, each to the extent not allocated to the divisions, to the business segments for reporting purposes. These unallocated expenses are included in our business segment disclosures as corporate undistributed expenses.

Segment asset disclosures include inventories, property, plant and equipment, goodwill and other intangible assets. The accounting policies of our segments are the same as those described in Note 2, Summary of Significant Accounting Policies of Notes to Consolidated Financial Statements in Item 8 of the Annual Report. There were no inter-segment sales in the periods presented. Management's evaluation of segment performance is principally based on a measure of segment earnings, which we calculate as segment gross profit (excluding depreciation and amortization) less selling expenses (Segment Earnings).

The following tables set forth certain financial information attributable to our business segments for the three and six months ended March 29, 2009 and March 30, 2008:

(\$ in millions)

	Three Months Ended		Six Months Ended	
	March 29, 2009	March 30, 2008	March 29, 2009	March 30, 2008
Net sales				
Metal packaging	\$ 133.6	\$ 140.5	\$ 264.5	\$ 264.9
Plastic packaging	72.5	103.1	154.1	196.1
Consolidated net sales	\$ 206.1	\$ 243.6	\$ 418.6	\$ 461.0
Income (Loss) Before Income Taxes				
Segment earnings				
Metal packaging	\$ 22.3	\$ 19.9	\$ 33.8	\$ 30.4
Plastic packaging	14.7	10.3	21.5	18.4
Segment earnings	37.0	30.2	55.3	48.8
Expenses not distributed to segments				
Corporate undistributed expenses	4.0	3.6	7.5	7.6
Depreciation and amortization (summarized below)	10.8	11.5	21.9	22.6
Restructuring	0.7	4.2	1.4	4.2
Interest, net	7.4	9.3	15.6	18.8
Other	0.2	0.1	(0.6)	0.2
Total expenses not distributed to segments	23.1	28.7	45.8	53.4
Consolidated income (loss) before income taxes	\$ 13.9	\$ 1.5	\$ 9.5	\$ (4.6)
Depreciation and amortization				
Metal packaging	\$ 5.0	\$ 5.9	\$ 10.4	\$ 11.5
Plastic packaging	5.4	5.4	10.8	10.7
Segment depreciation and amortization	10.4	11.3	21.2	22.2
Corporate	0.4	0.2	0.7	0.4
Consolidated depreciation and amortization	\$ 10.8	\$ 11.5	\$ 21.9	\$ 22.6

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The following table sets forth total assets attributable to our business segments as of March 29, 2009 and September 28, 2008:

(\$ in millions)

	March 29, 2009	September 28, 2008
Total assets		
Metal packaging	\$ 306.8	\$ 322.6
Plastic packaging	285.8	316.6
Segment total assets	592.6	639.2
Corporate	172.7	243.2
Total assets	\$ 765.3	\$ 882.4

For the three and six months ended March 29, 2009, approximately 92% of net sales were to customers in the United States and approximately 8% were to customers in Canada. For the three and six months ended March 30, 2008, approximately 90% of net sales were to customers in the United States, approximately 9% were to customers in Canada and the remainder were to customers in other countries.

For the three and six months ended March 29, 2009, approximately 93% of metal packaging segment net sales were to customers in the United States, approximately 6% were to customers in Canada and the remainder were to customers in other countries. For the three and six months ended March 30, 2008, approximately 92% of metal packaging segment net sales were to customers in the United States and approximately 8% were to customers in Canada.

For the three and six months ended March 29, 2009, approximately 89% of plastic packaging segment net sales were to customers in the United States, approximately 10% were to customers in Canada and the remainder were to customers in other countries. For the three and six months ended March 30, 2008, approximately 88% of plastic packaging segment net sales were to customers in the United States and approximately 12% were to customers in Canada.

As of March 29, 2009 and September 28, 2008, approximately \$7.3 million and \$8.8 million, respectively, of our long-lived assets were located in Canada.

13. SUBSEQUENT EVENT**Senior Subordinated Notes****2014 Notes**

On April 6, 2009, BWAY completed a private placement offering of approximately \$228.5 million aggregate principal amount of 10% Senior Subordinated Notes due April 15, 2014 (2014 Notes) which priced at a discount to par of 87.513%. The 2014 Notes were issued pursuant to an indenture, dated as of April 6, 2009 (the Indenture), among BWAY, the Guarantors (as defined below) and The Bank of New York Mellon Trust Company, N.A., as trustee (the Trustee.)

The 2014 Notes are unsecured and subordinated to all of BWAY s existing and future senior debt, including its existing credit facilities. Each of BWAY s wholly-owned U.S. subsidiaries (the Guarantors) will guarantee the 2014 Notes with a guarantee that will be unsecured and subordinated to all existing and future senior debt of each such subsidiary. If any subsidiary of BWAY that is not a Guarantor guarantees certain indebtedness of BWAY in the future, such subsidiary will guarantee the 2014 Notes.

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BWAY may redeem the 2014 Notes, in whole or in part, at any time on or after April 15, 2011 at the redemption prices set forth in the 2014 Notes. In addition, prior to April 15, 2011, BWAY may redeem up to 35% of the 2014 Notes with the net proceeds of one or more equity offerings at a redemption price equal to 110% of the principal amount plus accrued interest. If BWAY undergoes a change of control or sells certain of its assets, it may be required to offer to purchase the 2014 Notes from holders at a purchase price equal to 101% of the principal amount plus accrued interest.

The Indenture contains covenants limiting BWAY's and the Guarantors' ability to: (i) incur additional debt or issue certain preferred stock; (ii) pay dividends or distributions on capital stock or repurchase capital stock; (iii) make certain investments; (iv) create liens on assets to secure debt; (v) engage in transactions with affiliates; (vi) merge or consolidate with another company; and (vii) transfer and sell assets, in each case subject to a number of limitations and exceptions provided in the Indenture.

Upon the occurrence of customary events of default the Trustee or the holders of 25% of the principal amount of the outstanding 2014 Notes may declare the principal of and accrued and unpaid interest on the 2014 Notes to be due and payable. Upon the occurrence of certain bankruptcy events affecting BWAY or certain of its subsidiaries the principal of and accrued and unpaid interest on the 2014 Notes will become immediately due and payable without any declaration or other act on the part of the Trustee or any holder.

The 2014 Notes were offered in the United States to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended (the "Securities Act"), and outside the United States pursuant to Regulation S under the Securities Act.

In connection with the issuance of the 2014 Notes, BWAY and the Guarantors entered into a registration rights agreement, dated as of April 6, 2009, with the initial purchasers of the 2014 Notes (the "Registration Rights Agreement"), obligating BWAY, to use its commercially reasonable efforts to file with the Securities and Exchange Commission (the "Commission") and cause to become effective a registration statement relating to an offer to exchange the 2014 Notes for new notes evidencing the same continuing indebtedness as the 2014 Notes with terms substantially identical to the 2014 Notes. BWAY will not be required to consummate the exchange offer to the extent that before April 7, 2010 (1) the 2014 Notes are freely tradeable pursuant to Rule 144 under the Securities Act and (2) the restrictive legend has been removed from the 2014 Notes. If applicable interpretations of the staff of the Commission do not permit BWAY to effect the exchange offer, BWAY will be required to use its commercially reasonable efforts to make available an effective shelf registration statement relating to resales of any 2014 Notes. In the event that BWAY defaults on these obligations, it will be required to pay additional interest on the 2014 Notes with respect to which such default exists until the default is cured.

We expect to incur financing costs associated with the 2014 Notes of approximately \$5.3 million, which includes an underwriting fee of approximately \$4.3 million. The financing costs will be capitalized and amortized to interest expense over the term of the 2014 Notes.

2010 Notes

On April 6, 2009, BWAY used the net cash proceeds from the offering of the 2014 Notes and approximately \$14.5 million of cash on hand to pre-fund the redemption of the 2010 Notes and to satisfy and discharge its obligations under the indenture governing the 2010 Notes. BWAY provided notice of redemption to holders of the 2010 Notes to redeem the notes on May 6, 2009. The \$14.5 million included a redemption premium of \$3.3 million (1.667% of the outstanding principal) and accrued interest through May 6, 2009 of \$11.2 million, which includes approximately \$1.7 million of interest accrued from the date the redemption was pre-funded to the redemption date. Under the terms of the indenture, BWAY could not redeem the notes earlier than 30 days after giving the notice of redemption.

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In the third quarter of 2009, BWAY expects to record an approximately \$4.8 million loss on extinguishment of debt, which includes the redemption premium of \$3.3 million and the write-off of approximately \$1.5 million of unamortized deferred financing costs associated with the 2010 Notes.

14. SUPPLEMENTAL GUARANTOR SUBSIDIARIES INFORMATION

The 2010 Notes are guaranteed on a full, unconditional joint and several basis by our U.S. based subsidiaries, which are wholly-owned. The following is condensed, consolidating financial information for BWAY and its subsidiaries, segregating the guarantor subsidiaries and non-guarantor subsidiaries, as of March 29, 2009 and September 28, 2008, and for the three and six months ended March 29, 2009 and March 30, 2008. We have not presented separate financial statements for the guarantor subsidiaries or the non-guarantor subsidiaries because we believe the statements would not provide materially useful information to investors.

Table of Contents**BWAY Corporation and Subsidiaries****Supplemental Unaudited Condensed Consolidating Balance Sheet Information****March 29, 2009**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Assets					
Current Assets					
Cash and cash equivalents	\$ 39.5	\$ 2.4	\$ 2.8	\$	\$ 44.7
Accounts receivable, net	57.1	34.3	6.8		98.2
Inventories, net	71.9	16.5	4.9		93.3
Other current assets	39.6	2.9	0.5	(30.0)	13.0
Total current assets	208.1	56.1	15.0	(30.0)	249.2
Property, plant and equipment, net	75.1	50.2	7.3		132.6
Goodwill	120.2	97.7	27.5		245.4
Other intangible assets, net	36.4	74.8	19.5		130.7
Other assets	6.4	0.3	0.7		7.4
Intercompany		93.9		(93.9)	
Investment in subsidiaries	282.2	22.7		(304.9)	
Total assets	\$ 728.4	\$ 395.7	\$ 70.0	\$ (428.8)	\$ 765.3
Liabilities and Stockholders Equity					
Current Liabilities					
Accounts payable	\$ 30.3	\$ 28.3	\$ 3.6	\$	\$ 62.2
Other current liabilities	38.6	37.0	1.7	(30.0)	47.3
Current portion of long-term debt	0.8		0.2		1.0
Total current liabilities	69.7	65.3	5.5	(30.0)	110.5
Long-term debt	353.0		40.2		393.2
Deferred tax liabilities	15.1	39.7	0.9		55.7
Intercompany	89.6	3.8	0.5	(93.9)	
Other liabilities	24.4	4.7	0.2		29.3
Total liabilities	551.8	113.5	47.3	(123.9)	588.7
Stockholders Equity					
Preferred stock					
Common stock					
Additional paid-in capital	141.9	233.7	19.6	(253.3)	141.9
Retained earnings	40.0	52.9	5.8	(58.7)	40.0
Accumulated other comprehensive loss	(5.3)	(4.4)	(2.7)	7.1	(5.3)
Total stockholders equity	176.6	282.2	22.7	(304.9)	176.6
Total liabilities and stockholders equity	\$ 728.4	\$ 395.7	\$ 70.0	\$ (428.8)	\$ 765.3

Table of Contents**BWAY Corporation and Subsidiaries****Supplemental Unaudited Condensed Consolidating Balance Sheet Information****September 28, 2008**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Assets					
Current Assets					
Cash and cash equivalents	\$ 78.3	\$ 5.3	\$ 8.5	\$	\$ 92.1
Accounts receivable, net	54.6	48.5	10.2		113.3
Inventories, net	74.0	30.4	7.8		112.2
Other current assets	43.0	(23.3)	1.0		20.7
Total current assets	249.9	60.9	27.5		338.3
Property, plant and equipment, net	79.2	53.8	8.9		141.9
Goodwill	120.3	97.7	33.0		251.0
Other intangible assets, net	39.3	78.2	24.7		142.2
Other assets	7.8	0.3	0.9		9.0
Intercompany					
Investment in subsidiaries	278.9	26.2		(305.1)	
Total assets	\$ 775.4	\$ 317.1	\$ 95.0	\$ (305.1)	\$ 882.4
Liabilities and Stockholders' Equity					
Current Liabilities					
Accounts payable	\$ 70.8	\$ 67.3	\$ 11.7	\$	\$ 149.8
Other current liabilities	43.1	7.6	1.7		52.4
Current portion of long-term debt	14.5		4.4		18.9
Total current liabilities	128.4	74.9	17.8		221.1
Long-term debt	353.7		48.7		402.4
Deferred tax liabilities	15.1	39.6	1.1		55.8
Intercompany	80.1	(81.2)	1.1		
Other liabilities	24.4	4.9	0.1		29.4
Total liabilities	601.7	38.2	68.8		708.7
Stockholders' Equity					
Preferred stock					
Common stock					
Additional paid-in capital	140.4	233.7	19.6	(253.3)	140.4
Retained earnings	34.0	45.1	4.8	(49.9)	34.0
Accumulated other comprehensive (loss) income	(0.7)	0.1	1.8	(1.9)	(0.7)
Total stockholders' equity	173.7	278.9	26.2	(305.1)	173.7
Total liabilities and stockholders' equity	\$ 775.4	\$ 317.1	\$ 95.0	\$ (305.1)	\$ 882.4

Table of Contents**BWAY Corporation and Subsidiaries****Supplemental Unaudited Condensed Consolidating Statement of Operations Information****For the three months ended March 29, 2009**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Net sales	\$ 129.6	\$ 65.0	\$ 11.5	\$	\$ 206.1
Costs and expenses					
Cost of products sold (excluding depreciation and amortization)	106.5	51.0	9.3	(0.1)	166.7
Depreciation and amortization	5.2	4.8	0.8		10.8
Selling and administrative	5.3	0.9	0.2		6.4
Restructuring	0.4	0.2	0.1		0.7
Interest, net	6.9		0.5		7.4
Other	0.4	(0.3)		0.1	0.2
Total costs and expenses	124.7	56.6	10.9		192.2
Income before income taxes	4.9	8.4	0.6		13.9
Provision for income taxes	1.8	3.2	0.2		5.2
Equity in income of subsidiaries	5.6	0.4		(6.0)	
Net income	\$ 8.7	\$ 5.6	\$ 0.4	\$ (6.0)	\$ 8.7

BWAY Corporation and Subsidiaries**Supplemental Unaudited Condensed Consolidating Statement of Operations Information****For the three months ended March 30, 2008**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Net sales	\$ 134.8	\$ 90.7	\$ 18.1	\$	\$ 243.6
Costs and expenses					
Cost of products sold (excluding depreciation and amortization)	115.5	79.9	16.1	(0.1)	211.4
Depreciation and amortization	5.6	5.0	0.9		11.5
Selling and administrative	4.7	0.7	0.2		5.6
Restructuring	3.8		0.4		4.2
Interest, net	8.4		0.9		9.3
Other	0.1	(0.1)		0.1	0.1
Total costs and expenses	138.1	85.5	18.5		242.1
(Loss) income before income taxes	(3.3)	5.2	(0.4)		1.5
(Benefit from) provision for income taxes	(1.0)	1.7	(0.3)		0.4
Equity in income (loss) of subsidiaries	3.4	(0.1)		(3.3)	

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Net income (loss)	\$	1.1	\$	3.4	\$	(0.1)	\$	(3.3)	\$	1.1
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Table of Contents**BWAY Corporation and Subsidiaries****Supplemental Unaudited Condensed Consolidating Statement of Operations Information****For the six months ended March 29, 2009**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Net sales	\$ 256.2	\$ 137.3	\$ 25.1	\$	\$ 418.6
Costs and expenses					
Cost of products sold (excluding depreciation and amortization)	222.7	115.1	21.2	(0.2)	358.8
Depreciation and amortization	10.4	9.8	1.7		21.9
Selling and administrative	10.0	1.6	0.4		12.0
Restructuring	0.8	0.5	0.1		1.4
Interest, net	14.5		1.1		15.6
Other	0.6	(0.4)	(1.0)	0.2	(0.6)
Total costs and expenses	259.0	126.6	23.5		409.1
(Loss) income before income taxes	(2.8)	10.7	1.6		9.5
(Benefit from) provision for income taxes	(1.0)	3.9	0.6		3.5
Equity in income of subsidiaries	7.8	1.0		(8.8)	
Net income	\$ 6.0	\$ 7.8	\$ 1.0	\$ (8.8)	\$ 6.0

BWAY Corporation and Subsidiaries**Supplemental Unaudited Condensed Consolidating Statement of Operations Information****For the six months ended March 30, 2008**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Net sales	\$ 252.4	\$ 171.7	\$ 36.9	\$	\$ 461.0
Costs and expenses					
Cost of products sold (excluding depreciation and amortization)	223.8	152.1	32.7	(0.3)	408.3
Depreciation and amortization	11.0	9.8	1.8		22.6
Selling and administrative	9.5	1.5	0.5		11.5
Restructuring	3.8		0.4		4.2
Interest, net	16.9		1.9		18.8
Other	0.2	(0.3)		0.3	0.2
Total costs and expenses	265.2	163.1	37.3		465.6
(Loss) income before income taxes	(12.8)	8.6	(0.4)		(4.6)
(Benefit from) provision for income taxes	(4.4)	2.9	(0.3)		(1.8)
Equity in income (loss) of subsidiaries	5.6	(0.1)		(5.5)	

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Net (loss) income	\$	(2.8)	\$	5.6	\$	(0.1)	\$	(5.5)	\$	(2.8)
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Table of Contents**BWAY Corporation and Subsidiaries****Supplemental Unaudited Condensed Consolidating Statement of Cash Flows Information****For the six months ended March 29, 2009**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Net cash used in operating activities	\$ (11.3)	\$ (9.1)	\$ (0.6)	\$	\$ (21.0)
<u>Cash Flows from Investing Activities</u>					
Capital expenditures	(3.5)	(2.8)	(0.4)		(6.7)
Change in intercompany		9.0	0.5	(9.5)	
Net cash (used in) provided by investing activities	(3.5)	6.2	0.1	(9.5)	(6.7)
<u>Cash Flows from Financing Activities</u>					
Repayments of long-term debt	(14.4)		(3.7)		(18.1)
Other	(0.1)				(0.1)
Change in intercompany	(9.5)			9.5	
Net cash (used in) provided by financing activities	(24.0)		(3.7)	9.5	(18.2)
Effect of exchange rate changes on cash and cash equivalents			(1.5)		(1.5)
Net (decrease) increase in cash and cash equivalents	(38.8)	(2.9)	(5.7)		(47.4)
Cash and cash equivalents, beginning of period	78.3	5.3	8.5		92.1
Cash and cash equivalents, end of period	\$ 39.5	\$ 2.4	\$ 2.8	\$	\$ 44.7

BWAY Corporation and Subsidiaries**Supplemental Unaudited Condensed Consolidating Statement of Cash Flows Information****For the six months ended March 30, 2008**

(\$ in millions)	BWAY Corporation	Guarantor Subsidiaries	Other Subsidiaries	Eliminations	Consolidated
Net cash (used in) provided by operating activities	\$ (29.3)	\$ 11.4	\$ (0.3)	\$	\$ (18.2)
<u>Cash Flows from Investing Activities</u>					
Capital expenditures	(10.2)	(8.8)	(1.4)		(20.4)
Net cash used in investing activities	(10.2)	(8.8)	(1.4)		(20.4)

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<u>Cash Flows from Financing Activities</u>				
Repayments of long-term debt	(0.4)		(0.3)	(0.7)
Other	(0.1)			(0.1)
Net cash (used in) provided by financing activities	(0.5)		(0.3)	(0.8)
Effect of exchange rate changes on cash and cash equivalents			(0.3)	(0.3)
Net (decrease) increase in cash and cash equivalents	(40.0)	2.6	(2.3)	(39.7)
Cash and cash equivalents, beginning of period	44.3	1.5	7.6	53.4
Cash and cash equivalents, end of period	\$ 4.3	\$ 4.1	\$ 5.3	\$ 13.7

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

In this management's discussion and analysis, references to gross margin refer to net sales less cost of products sold (excluding depreciation and amortization) and references to gross margin percentage refer to such gross margin as a percentage of net sales. In addition, a reference to a year is a reference to our fiscal year unless otherwise indicated. The 2009 fiscal year ends on September 27, 2009.

Segments

We report our results of operations in two segments: metal packaging and plastic packaging. Our products within each of these segments include:

Metal packaging: general line rigid metal containers made from steel, including paint cans and components, aerosol cans, steel pails, oblong cans and a variety of other specialty cans, including ammunition boxes, that our customers use to package paint, household and personal care products, automotive after-market products, paint thinners, driveway and deck sealants, ammunition and other end-use products.

Plastic packaging: injection-molded plastic pails and blow-molded tight-head containers, bottles and drums that our customers use to package petroleum products, agricultural chemicals, other chemical applications, paint, ink, edible oils, high-tech coatings, high-solid coatings, roofing mastic and adhesives, driveway sealants and other end-use products.

Factors Affecting Our Results of Operations

For a discussion of factors affecting our results of operations, including net sales, expenses and raw materials, see "Factors Affecting Our Results of Operations" in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operation" in the Annual Report.

Overview

Principal changes in our results of operations for the three months ended March 29, 2009 (the second quarter of 2009) as compared to the three months ended March 30, 2008 (the second quarter of 2008) (each, the second quarter) and for the six months ended March 29, 2009 (year to date 2009 or the first six months of 2009) as compared to the six months ended March 30, 2008 (year to date 2008 or the first six months of 2008) (each, year to date or the first six months) were these:

For the second quarter, net sales decreased 15.4% to \$206.1 million and gross margin increased 22.4% to \$39.4 million. For the year to date, net sales decreased 9.2% to \$418.6 million and gross margin increased 13.5% to \$59.8 million.

For the metal packaging segment in the second quarter, net sales decreased 4.9% to \$133.6 million and gross margin increased 9.8% to \$23.5 million. For the metal packaging segment year to date, net sales decreased 0.2% to \$264.5 million and gross margin increased 9.0% to \$36.3 million.

For the plastic packaging segment in the second quarter, net sales decreased 29.7% to \$72.5 million and gross margin increased 38.9% to \$15.7 million. For the plastic packaging segment year to date, net sales decreased 21.4% to \$154.1 million and gross margin increased 15.2% to \$23.5 million.

In the second quarter, consolidated net sales decreased approximately 19% due to lower volume, metal packaging segment net sales declined approximately 21% on volume and plastic packaging segment net sales declined approximately 16% on volume. For the year to date, consolidated net sales, metal packaging segment net sales and plastic packaging segment net sales each decreased approximately 17% due to lower volume.

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For the second quarter and year to date consolidated and metal packaging net sales, the impact of the decline in volume was offset by higher selling prices previously implemented in response to an increase in the cost of raw materials and by a favorable change in the mix of products sold. In addition to the impact from lower volume, plastic packaging segment net sales decreased in the second quarter and year to date due to lower selling prices resulting from the pass through of decreases in the cost of resin and to an unfavorable change in the mix of products sold.

For the second quarter, consolidated gross margin percentage increased to 19.1% from 13.2%, metal packaging segment gross margin percentage increased to 17.6% from 15.2% and plastic packaging segment gross margin percentage increased to 21.7% from 11.0%. For the year to date, consolidated gross margin percentage increased to 14.3% from 11.4%, metal packaging segment gross margin percentage increased to 13.7% from 12.6% and plastic packaging segment gross margin percentage increased to 15.2% from 10.4%. For the second quarter and year to date, we were able to offset the impact of declines in volume on the gross margin percentages through changes in selling prices relative to the pass through of changes in raw material costs and cost reduction initiatives implemented in the latter part of 2008.

Interest expense, net, decreased 20.4% to \$7.4 million for the second quarter and decreased 17.0% to \$15.6 million for the year to date, each primarily because of lower interest rates and lower average outstanding borrowings.

Results of Operations

Our operations are organized and reviewed by management along our product lines in two reportable segments: metal packaging and plastic packaging. For a discussion of our business segments, see Note 12, Business Segments, of Notes to Condensed Consolidated Financial Statements, included in Part I, Item 1 of this report.

The following tables set forth changes in our statements of operations for the periods indicated.

Three months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
Net sales	\$ 206.1	\$ 243.6	(15.4)%
Cost of products sold (excluding depreciation and amortization)	166.7	211.4	(21.1)
Gross margin	39.4	32.2	22.4
Depreciation and amortization	10.8	11.5	(6.1)
Selling and administrative expense	6.4	5.6	14.3
Restructuring expense	0.7	4.2	(83.3)
Interest expense, net	7.4	9.3	(20.4)
Other	0.2	0.1	100.0
Income before income taxes	13.9	1.5	NM
Provision for income taxes	5.2	0.4	NM
Net income	\$ 8.7	\$ 1.1	NM%

NM Not Meaningful

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Six months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
Net sales	\$ 418.6	\$ 461.0	(9.2)%
Cost of products sold (excluding depreciation and amortization)	358.8	408.3	(12.1)
Gross margin	59.8	52.7	13.5
Depreciation and amortization	21.9	22.6	(3.1)
Selling and administrative expense	12.0	11.5	4.3
Restructuring expense	1.4	4.2	(66.7)
Interest expense, net	15.6	18.8	(17.0)
Other	(0.6)	0.2	NM
Income (loss) before income taxes	9.5	(4.6)	NM
Provision for (benefit from) income taxes	3.5	(1.8)	NM
Net income (loss)	\$ 6.0	\$ (2.8)	NM%

NM Not Meaningful

Net Sales

Three months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
Net sales by segment			
Metal packaging	\$ 133.6	\$ 140.5	(4.9)%
Plastic packaging	72.5	103.1	(29.7)
Consolidated net sales	\$ 206.1	\$ 243.6	(15.4)%

Six months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
Net sales by segment			
Metal packaging	\$ 264.5	\$ 264.9	(0.2)%
Plastic packaging	154.1	196.1	(21.4)

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Consolidated net sales	\$ 418.6	\$ 461.0	(9.2)%
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The 4.9% decrease in metal packaging segment net sales in the second quarter of 2009 as compared to the second quarter of 2008 resulted from a decrease in metal packaging segment volume of approximately 21% partially offset by price increases in 2008 to pass through increases in raw material costs and a favorable mix of products sold. Metal packaging net sales decreased slightly year to date as compared to year to date 2008 as volume declines in the second quarter nearly offset the impact of favorable cost pass through in the first quarter. The decrease in metal packaging segment sales overall volume was primarily due to lower demand for paint and other

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general line containers. Demand for architectural paint and coatings, the largest end use market segment for our metal packaging containers, remained weak during the quarter due to the weak overall general economic environment. Product mix had a favorable impact on metal packaging segment net sales as volumes for larger containers, which typically have higher sales prices, were proportionately higher than volumes for smaller containers.

The 29.7% decrease in plastic packaging segment net sales in the second quarter of 2009 as compared to the second quarter of 2008 resulted from lower volume of approximately 16%, an unfavorable mix of products sold and lower selling prices resulting from the pass through of decreases in the cost of resin. The decrease in plastic packaging segment net sales year to date as compared to year to date 2008 was due to the lower volume and lower selling prices resulting from the pass through of decreases in the cost of resin. Consistent with the change in metal packaging segment net sales, the largest end use market segment for our plastic packaging containers (architectural paint and coatings), remained weak during the quarter due to the weak overall general economic environment.

Cost of Products Sold and Gross Margin

Three months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Cost of products sold by segment</u>			
Metal packaging	\$ 110.1	\$ 119.1	(7.6)%
Plastic packaging	56.8	91.8	(38.1)
Segment CPS	166.9	210.9	(20.9)
Corporate undistributed expenses	(0.2)	0.5	NM
Consolidated CPS	\$ 166.7	\$ 211.4	(21.1)%

NM Not Meaningful

Six months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Cost of products sold by segment</u>			
Metal packaging	\$ 228.2	\$ 231.6	(1.5)%
Plastic packaging	130.6	175.7	(25.7)
Segment CPS	358.8	407.3	(11.9)
Corporate undistributed expenses		1.0	(100.0)
Consolidated CPS	\$ 358.8	\$ 408.3	(12.1)%

NM Not Meaningful

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Three months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Gross margin by segment</u>			
Metal packaging	\$ 23.5	\$ 21.4	9.8%
<i>Gross margin percentage</i>	<i>17.6%</i>	<i>15.2%</i>	
Plastic packaging	15.7	11.3	38.9
<i>Gross margin percentage</i>	<i>21.7%</i>	<i>11.0%</i>	
Segment gross margin	39.2	32.7	19.9
Corporate undistributed expenses	0.2	(0.5)	NM
Consolidated gross margin	\$ 39.4	\$ 32.2	22.4%
<i>Gross margin percentage</i>	<i>19.1%</i>	<i>13.2%</i>	

NM Not Meaningful

Six months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Gross margin by segment</u>			
Metal packaging	\$ 36.3	\$ 33.3	9.0%
<i>Gross margin percentage</i>	<i>13.7%</i>	<i>12.6%</i>	
Plastic packaging	\$ 23.5	\$ 20.4	15.2
<i>Gross margin percentage</i>	<i>15.2%</i>	<i>10.4%</i>	
Segment gross margin	\$ 59.8	\$ 53.7	11.4
Corporate undistributed expenses		(1.0)	(100.0)
Consolidated gross margin	\$ 59.8	\$ 52.7	13.5%
<i>Gross margin percentage</i>	<i>14.3%</i>	<i>11.4%</i>	

NM Not Meaningful

Metal packaging segment cost of products sold, excluding depreciation and amortization, (CPS) decreased in the second quarter and first six months of 2009 compared to the second quarter and first six months of 2008 primarily due to lower volume partially offset by higher steel costs.

Metal packaging segment gross margin percentage increased to 17.6% and 13.7% in the second quarter and first six months of 2009, respectively, from 15.2% and 12.6% in the second quarter and first six months of 2008, respectively. The increases in metal packaging segment gross margin percentage were positively affected by higher selling prices resulting from the pass through of higher steel costs and a cost reduction program implemented in the latter part of 2008, partially offset by lower volume.

Plastic packaging segment CPS decreased in the second quarter and first six months of 2009 compared to the second quarter and first six months of 2008 primarily due to lower volume and lower resin costs.

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Plastic packaging segment gross margin percentage increased to 21.7% and 15.2% in the second quarter and first six months of 2009, respectively, from 11.0% and 10.4% in the second quarter and first six months of 2008, respectively. The increases in plastic packaging segment gross margin percentage were positively affected by lower selling prices relative to lower resin costs and a cost reduction program implemented in the latter part of 2008, partially offset by lower volume.

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The increase in plastic packaging segment gross margin percentage in the second quarter is partially due to unusual fluctuations in the market price of resin. The improvement in plastic packaging segment gross margin percentage for the second quarter is due to the timing of changes in selling price relative to raw material costs resulting from the market fluctuations.

Depreciation and Amortization

Three months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Depreciation and amortization by segment</u>			
Metal packaging	\$ 5.0	\$ 5.9	(15.3)%
Plastic packaging	5.4	5.4	
Segment depreciation and amortization	10.4	11.3	(8.0)
Corporate undistributed expenses	0.4	0.2	100.0
Consolidated depreciation and amortization	\$ 10.8	\$ 11.5	(6.1)%

NM Not Meaningful

Six months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Depreciation and amortization by segment</u>			
Metal packaging	\$ 10.4	\$ 11.5	(9.6)%
Plastic packaging	10.8	10.7	0.9
Segment depreciation and amortization	21.2	22.2	(4.5)
Corporate undistributed expenses	0.7	0.4	75.0
Consolidated depreciation and amortization	\$ 21.9	\$ 22.6	(3.1)%

NM Not Meaningful

The decrease in depreciation and amortization expense (D&A) in the second quarter and first six months of 2009 from the second quarter and first six months of 2008 is a result of lower amortization expense as amortization expense decreases over the life of the other intangibles partially offset by higher depreciation expense associated with higher capital expenditures in 2008. Metal packaging segment depreciation expense in the second quarter and first six months of 2008 included \$0.5 million of additional depreciation associated with the closure of Franklin Park.

Table of Contents***Selling and Administrative Expense***

Three months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Selling and administrative expense by segment</u>			
Metal packaging	\$ 1.2	\$ 1.5	(20.0)%
Plastic packaging	1.0	1.0	
Segment selling and administrative expense	2.2	2.5	(12.0)
Corporate undistributed expenses	4.2	3.1	35.5
Consolidated selling and administrative expense	\$ 6.4	\$ 5.6	14.3%

NM Not Meaningful

Six months ended March 29, 2009 (2009) and March 30, 2008 (2008)

(\$ in millions)

	2009	2008	Percentage Change
<u>Selling and administrative expense by segment</u>			
Metal packaging	\$ 2.5	\$ 2.9	(13.8)%
Plastic packaging	2.0	2.0	
Segment selling and administrative expense	4.5	4.9	(8.2)
Corporate undistributed expenses	7.5	6.6	13.6
Consolidated selling and administrative expense	\$ 12.0	\$ 11.5	4.3%

NM Not Meaningful

Corporate undistributed selling and administrative expenses in the second quarter and first six months of 2008 included a \$1.0 million reduction in the allowance for doubtful accounts based on revised estimates of collectability. Excluding this adjustment, corporate undistributed selling and administrative expenses increased \$0.2 million in the second quarter of 2009 compared to the second quarter of 2008 and were unchanged in the first six months of 2009 compared to the first six months of 2008. The increase in the second quarter was primarily due to higher performance based bonus expense partially offset by lower stock-based compensation. The decrease in stock-based compensation in 2009 is consistent with the expected decrease as stock-based compensation expense related to modifications made in 2007 declines at the end of the amortization period.

Restructuring Expense

In the second quarter and first six months of 2009, we recorded approximately \$0.1 million and \$0.5 million, respectively, related to severance and benefits associated with headcount reductions in 2009. In addition, we recorded approximately \$0.5 million and \$0.8 million in the second quarter and first six months of 2009, respectively, in expenses related to the closure of Franklin Park and Cleveland in 2008. Restructuring charges in the second quarter and first six months of 2008 included the initial \$4.3 million charge for expenses associated with closure of

Franklin Park.

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We expect to record approximately \$0.3 million in the remainder of 2009 related to these closures. See Note 8, Restructuring, of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for further information.

Interest, Other and Income Taxes

Interest Expense, Net. The decrease in interest expense, net, in the second quarter and first six months of 2009 as compared to the second quarter and first six months of 2008 is primarily due to lower interest rates and a decrease in average outstanding debt.

Other. Other income, net, in the first six months of 2009 was \$0.6 million compared to other expense, net, of \$0.2 million in the first six months of 2008. The change in other is primarily related to gains realized on foreign exchange transactions as the U.S. dollar strengthened against the Canadian dollar in the first quarter.

Provision For (Benefit From) Income Taxes. The provision for income taxes in the first six months of 2009 was \$3.5 million for an effective tax rate of approximately 37% as compared to benefit from income taxes of \$1.8 million for an effective tax rate of approximately 39% in the first six months of 2008.

Liquidity and Capital Resources

See our discussion of Liquidity and Capital Resources in Item 7, Management's Discussion and Analysis in the Annual Report for certain risk factors that could affect our liquidity and access to capital. These risks remain unchanged as of March 29, 2009 except as related to the maturity and refinancing of the senior notes due 2010. The risk factor related to the maturity and refinancing of the senior notes due 2010 was mitigated in the third quarter of 2009 when the notes were redeemed using proceeds from a new senior debt offering (see below). Other risk factors related to the 2010 notes are generally applicable to the new notes which are due in April 2014.

We expect cash on hand, cash provided by operations and borrowings available under revolving credit facilities to provide sufficient working capital to operate our business, to make expected capital expenditures and to meet foreseeable liquidity requirements, including debt service on our long-term debt, in the next 12 months. We expect to use cash provided by operations in excess of amounts needed for capital expenditures and required debt repayments to reduce our debt, to fund potential acquisitions or for other general corporate purposes.

Our long-term debt, including available revolving credit facilities and certain covenants and restrictions, is discussed in Note 6, Long-Term Debt, of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report. As of March 29, 2009, we were in compliance with our debt covenants. With certain exceptions, we are prohibited by our long-term debt arrangements from paying cash dividends, including cash dividends between BWAY and BHC.

As of March 29, 2009, BWAY had \$44.3 million and ICL had \$4.9 million available under revolving credit facilities. As of March 29, 2009, we had \$44.7 million of cash on hand.

In the first quarter of 2009, we repaid \$18.1 million on the term loans, including a mandatory Excess Cash Flow (as defined in the credit agreement) repayment of \$17.7 million in December 2008. As such, there are no scheduled quarterly repayments due in 2009. Scheduled quarterly repayments of approximately \$0.5 million will resume in December 2009 and continue through March 2013.

As of March 29, 2009, there was \$194.2 million in outstanding borrowings subject to variable interest rates at a weighted-average borrowing rate of 3.7%.

We expect capital expenditures in 2009 of approximately \$18.0 million to \$20.0 million. Approximately \$8.0 million of planned capital expenditures in 2009 are for projects begun in 2008.

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In the third quarter of 2009, BWAY redeemed its \$200.0 million in aggregate principal amount of 10% senior subordinated notes due 2010 at a redemption price of 101.667% of the outstanding principal plus accrued interest. The 2010 notes were redeemed using the proceeds from the issuance of approximately \$228.5 million of 10% senior subordinated notes due 2014 that were issued at a discount to par of 87.513% and cash on hand. For a further discussion of the 2014 notes, see Note 13, Subsequent Event of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report. The new notes will result in additional interest payments of approximately \$2.9 million annually.

Cash Flow Information

Summary of cash flows and changes in cash and cash equivalents for the six months ended March 29, 2009 (2009) and March 30, 2008 (2008):

(\$ in millions)

	2009	2008	Percentage Change
Cash used in operating activities	\$ (21.0)	\$ (18.2)	15.4 %
Cash used in investing activities	(6.7)	(20.4)	(67.2)
Cash used in financing activities	(18.2)	(0.8)	NM
Effect of exchange rate changes	(1.5)	(0.3)	NM
Net decrease in cash and cash equivalents	\$ (47.4)	\$ (39.7)	19.4%
Cash and cash equivalents, end of period	\$ 44.7	\$ 13.7	NM %

NM Not Meaningful

Operating Activities

Cash used in operating activities increased \$2.8 million to \$21.0 million in the first six months of 2009 compared to cash used in operating activities in the first six months of 2008. The increase is primarily due to an increase in primary working capital (accounts receivable and inventories less accounts payable) of \$53.9 million in the first six months of 2009 compared to \$34.1 million in the first six months of 2008. The increase in primary working capital in the first six months of 2009 compared with the first six months of 2008 is due to a decrease in accounts payable partially offset by reductions in accounts receivable and inventory. The decrease in accounts payable in the first six months of 2009 is primarily due to the timing of disbursements at the end of the quarter, to lower inventory levels and to the decrease in the value of resin included in accounts payable at the end of the quarter. The reduction in accounts receivable in the first six months of 2009 is primarily due to lower sales. The reduction in inventory in the first six months of 2009 is primarily due to lower volume, lower cost of resin in inventory and more effective management of inventory levels.

Investing Activities

Cash used in investing activities decreased \$13.6 million in the first six months of 2009 as compared to the first six months of 2008. The decrease is due to higher capital expenditures in 2008 to complete projects related to machinery and equipment for the production of new plastic containers developed in 2007 and for the production of aerosol components.

Financing Activities

Cash used in financing activities increased \$17.4 million in the first six months of 2009 as compared to the first six months of 2008. The increase is due to an \$18.1 million mandatory excess cash flow debt repayment of the

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term loans in December 2008. A mandatory, unscheduled debt repayment was not required and we did not make a voluntary debt repayment in the first six months of 2008 due to the use of cash in the second half of 2007 related to the June 2007 initial public offering of BHC common stock.

Long-term debt outstanding, including the current portion, decreased \$27.1 million or 6.4% in the first six months of 2009 to \$394.2 million as of March 29, 2009. The decrease was due to debt repayments of \$18.1 million and changes in the exchange rate used to translate Canadian dollar denominated debt to U.S. dollars for reporting purposes of \$9.0 million. Our Canadian dollar denominated debt is serviced by our Canadian operations, which are denominated in Canadian dollars and, as such, cash flows servicing the debt are not affected by the exchange rate.

Market Risk

Our cash flows and earnings are exposed to the market risk of interest rate changes resulting from variable rate borrowings under our credit facility. Credit facility borrowings bear interest at an applicable margin (based on certain ratios contained in the credit agreement) plus a market rate of interest. As of March 29, 2009, we had borrowings of \$194.2 million that were subject to interest rate risk. Each 100 basis point increase in interest rates relative to these borrowings would reduce quarterly pretax earnings by approximately \$0.5 million.

Foreign Exchange

Our reported results of operations are exposed to fluctuations of the Canadian dollar against the U.S. dollar, our reporting currency. For the first six months of 2009 and 2008, approximately 9% of net sales were denominated in Canadian dollars. Excluding purchases denominated in Canadian dollars that are funded through operations in Canada, other purchases from foreign suppliers in transactions not denominated in U.S. dollars are not significant, and we do not believe we are exposed to a significant market risk of exchange rate changes related to such purchases.

Commodity Risk

We are exposed to commodity price and quantity risks for steel and plastic resin, the principal raw materials used in our manufacturing processes. We are also exposed to fluctuations in the price of energy, primarily electricity and natural gas, and the cost of freight, which is impacted by fluctuations in the price of fuel. We purchase all of our raw materials and energy from external sources.

We manage these risks by consolidating our purchases among a select group of suppliers and, as discussed below, through certain cost change pass through mechanisms in our sales agreements. The consolidation of suppliers enables us to use leverage in negotiating pricing and supply. However, an interruption in the ability of these suppliers to provide raw materials could have a material adverse effect on our financial position, results of operations and cash flows. The availability and price of raw materials may also be subject to shortages in supply, suppliers' allocations to other purchasers, interruptions in production by suppliers, changes in exchange rates and global demand.

The price of raw materials has been subject to volatility in the past, and we do not foresee stabilization in these markets in the near future. Historically, we have been able to pass certain cost changes through to our customers. However, we may not be able to do so in the future.

In addition to steel and plastic resin, the prices of other items used in our manufacturing processes are exposed to commodity price risks, and we have experienced increases in the cost of these items above expected trends. Historically, we have not passed these price increases through to our customers.

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To the extent we are not able to leverage our purchasing power in the future as successfully as we have in the past or are not able to increase the selling price of our products to reflect increases in the costs of raw materials, or if we experience interruptions or shortages in the supply of raw materials, our operating margins could be adversely affected. In addition, our manufacturing operations are dependent on the availability of natural gas and electricity. In certain cases, these energy sources may become difficult to obtain on acceptable terms due to external factors, or may only be available at a substantially increased cost, which could increase our operating costs or interrupt our ability to produce our products.

For an additional discussion of changes in steel and plastic resin costs and their impact on selling prices, see *Factors Affecting Our Results of Operations* in the Annual Report.

Critical Accounting Policies

For a summary of our critical accounting policies, see Item 7, *Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies* of the Annual Report. Our critical accounting policies have not changed since September 28, 2008 (see *Recently Adopted Accounting Standards* in Note 1, *General*, of Notes to Consolidated Financial Statements, included in Item 8 of the Annual Report, which is incorporated herein by reference).

Off-Balance Sheet Arrangements

As of March 29, 2009, a bank had issued standby letters of credit on our behalf in the aggregate amount of \$5.9 million primarily in favor of our workers' compensation insurers.

Other than these standby letters of credit, we do not have any off-balance sheet arrangements.

Contractual Obligations

We expect to pay approximately \$3.4 million related to a multi-employer pension withdrawal liability associated with the closure of Franklin Park (see Note 8, *Restructuring*, in Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report). The exact amount of the liability and repayment terms will be determined following the end of the plan year in which the last covered employee is terminated.

For a further discussion of the pension withdrawal liability and a summary of our other significant contractual obligations, see Item 7, *Management's Discussion and Analysis of Financial Condition and Results of Operations - Contractual Obligations and Commercial Commitments*, of the Annual Report. The nature of the obligations presented in the Annual Report has not materially changed as of March 29, 2009. As discussed above under *Liquidity and Capital Resources*, in the third quarter of 2009, BWAY redeemed its senior notes due in October 2010 using the proceeds of a new senior debt offering due in April 2014. The affected amounts in the contractual obligations table will be disclosed in the Form 10-Q for the third quarter of 2009.

Environmental Matters

For a discussion of contingencies related to environmental matters, see *Environmental Matters* in Note 11, *Commitments and Contingencies*, of Notes to Condensed Consolidated Financial Statements, included in Part I, Item 1 of this report, which is incorporated herein by reference.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

We do not purchase, sell or hold derivatives or other market risk-sensitive instruments to hedge commodity price risk, interest rate risk or exchange rate risk or for trading purposes.

For a discussion of interest rate risk and its relation to our indebtedness, see Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources, which is incorporated herein by reference.

Our business is exposed to variations in prices of raw materials and energy. See Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations Commodity Risk, which is incorporated herein by reference.

Our purchases from foreign suppliers in transactions denominated in foreign currencies are not significant and we do not believe we are exposed to a significant market risk of exchange rate changes related to fluctuations in the value of these foreign currencies in related to the U.S. Dollar.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Management, including the principal executive and principal financial officers, performed an evaluation of the effectiveness of the Company's disclosure controls and procedures as of March 29, 2009. Based on this evaluation, management, including the principal executive and principal financial officers, concluded that the disclosure controls and procedures of the Company were effective as of March 29, 2009.

Changes in Internal Control over Financial Reporting

There has been no change in the Company's internal control over financial reporting during the most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II

OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in legal proceedings from time to time in the ordinary course of business. We believe that the outcome of these proceedings will not have a material effect on our financial condition, results of operations or cash flows. We are also involved in certain proceedings relating to environmental matters as described under *Environmental* in Part I, Item 2, *Management's Discussion and Analysis of Financial Condition and Results of Operations*. We had accrued liabilities relating to pending litigation matters, other than as discussed below, of approximately \$0.7 million and \$0.4 million as of March 29, 2009 and September 28, 2008, respectively.

Other than as noted below, there have been no material changes to the legal proceedings disclosed in the Annual Report.

Aerosol Can Litigation

Plaze, Inc. and Claire-Sprayway, Inc. v. Bway Corporation, In the Superior Court of the State of Delaware in and for New Castle County, Case No. 08C-12-216-JRJ

On or about December 28, 2008, Plaze, Inc. (Plaze) and Claire-Sprayway, Inc. (Claire) filed the above-captioned lawsuit against BWAY. The lawsuit arises from BWAY's supply of aerosol cans to Plaze and Claire and attempts to state two causes of action against BWAY: (1) bad faith breach of contract and (2) fraudulent inducement. Plaze alleges losses and seeks to recover all available damages in an amount no less than three times Plaze's non-punitive damages, attorneys' fees and costs and any other damages the court deems appropriate.

BWAY filed a partial motion to dismiss the Plaze complaint on February 13, 2009. Pursuant to an agreement between the parties, plaintiffs will be filing an amended complaint. Discovery recently has begun.

We intend to defend the lawsuit vigorously. Given the preliminary nature of this lawsuit, we cannot at this time assess whether an adverse judgment ultimately may be returned against BWAY and what the impact of any such judgment might be.

Lead Pigment and Lead Paint Litigation

Personal Injury Cases

Wisconsin Personal Injury Lawsuits

In early January 2009, Defendant Millennium Holdings, LLC (Millennium) filed its *Suggestion of Bankruptcy* in these cases, which reflects that Millennium filed for Chapter 11 Bankruptcy protection on January 6, 2009. It appears that while these cases will be stayed as to Millennium, they will proceed as to the other Defendants. Plaintiffs' counsel recently indicated that it intends to move the courts to substitute Millennium's insurers for Millennium in these actions.

Public Nuisance Cases

State Of Ohio

This action was dismissed by Plaintiff, without prejudice, on February 6, 2009.

As of March 29, 2009 and September 28, 2008, we had accrued approximately \$0.2 million in legal fees and expenses related to the lead paint litigation.

Table of Contents**Item 4. Submission of Matters to a Vote of Security Holders**

BWAY Holding held its annual meeting of stockholders on February 27, 2009 at which time the stockholders voted on the ratification of the selection of Deloitte & Touche LLP as the Company's independent registered public accounting firm for the fiscal year ending September 29, 2009 as follows:

For:	18,981,088	99.7%
Against:	7,208	%
Abstain:	65,586	0.3%

There were 2,853,497 broker non-votes.

Item 6. Exhibits

Exhibit Number	Description of Document
10.1	Employment Agreement between BWAY Corporation and Kenneth M. Roessler made as of February 24, 2009.*
31.1	Certification of Chief Executive Officer required by Rule 13a-14(a) (17 C.F.R. 240.13a-14(a)).
31.2	Certification of Chief Financial Officer required by Rule 13a-14(a) (17 C.F.R. 240.13a-14(a)).
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Indicates a management contract or compensatory plan or arrangement.

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FORWARD-LOOKING STATEMENTS

This document contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. You should not place reliance on these statements. Forward-looking statements include information concerning our liquidity and our possible or assumed future results of operations, including descriptions of our business strategies. These statements often include words such as believe, expect, anticipate, intend, plan, estimate, seek, will, may or similar expressions. These statements are based on assumptions that we have made in light of our experience in the industry as well as our perceptions of historical trends, current conditions, expected future developments and other factors we believe are appropriate in these circumstances. As you read and consider this document, you should understand that these statements are not guarantees of performance or results. They involve risks, uncertainties and assumptions. Many factors could affect our actual financial results and could cause actual results to differ materially from those expressed in the forward-looking statements. Some important factors include competitive risk from other container manufacturers or self-manufacture by customers, termination of our customer contracts, loss or reduction of business from key customers, dependence on key personnel, changes in steel, resin, other raw material and energy costs or availability, product liability or product recall costs, lead pigment and lead paint litigation, increased consolidation in our end markets, consolidation of key suppliers, deceleration of growth in our end markets, increased use of alternative packaging, labor unrest, environmental, health and safety costs, management's inability to evaluate and selectively pursue acquisitions, fluctuation of our quarterly operating results, an increase in interest rates, inability to repay or refinance the senior subordinated notes, restrictions in our debt agreements, fluctuations of the Canadian dollar, and the other factors discussed in our filings with the Securities and Exchange Commission. In light of these risks, uncertainties and assumptions, the forward-looking statements contained in this document might not prove to be accurate and you should not place undue reliance upon them. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the foregoing cautionary statements. All such statements speak only as of the date made, and we undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

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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.

BWAY Holding Company

(Registrant)

Date: May 7, 2009

By: /s/ Kenneth M. Roessler
Kenneth M. Roessler
President and Chief Executive Officer

(Principal Executive Officer)

Date: May 7, 2009

By: /s/ Michael B. Clauer
Michael B. Clauer
Executive Vice President and Chief Financial Officer

(Principal Financial Officer)

BWAY Corporation

(Registrant)

Date: May 7, 2009

By: /s/ Kenneth M. Roessler
Kenneth M. Roessler
President and Chief Executive Officer

(Principal Executive Officer)

Date: May 7, 2009

By: /s/ Michael B. Clauer
Michael B. Clauer
Executive Vice President and Chief Financial Officer

(Principal Financial Officer)

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Net cash provided by operating operations

274,681 559,438

Cash flows from investing activities:

Purchases of property and equipment

(35,511) (33,870)

Purchases of patents and trademarks

(43,622) (12,775)

Net cash used in investing activities

(79,133) (46,645)

Cash flows from financing activities:

Payments under capital lease

- (5,068)
Net cash used in financing activities
- (5,068)
Net increase in cash and cash equivalents
195,548 507,725
Cash, beginning of year
811,403 303,678
Cash, end of year
\$1,006,951 \$811,403
Supplemental disclosures of cash flow information:

Non-cash investing and financing activities:

Conversion of Series C Convertible Preferred Stock and related dividends into common stock
\$1,671 \$16,712
Cash paid for:

Interest
\$- \$2,235
Income Taxes
\$18,502 \$76,420

The accompanying notes are an integral part of these consolidated financial statements.

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2008

1. ORGANIZATION AND BUSINESS

Andrea Electronics Corporation, incorporated in the State of New York in 1934, (together with its subsidiaries, “Andrea” or the “Company”) has been engaged in the electronic communications industry since its inception. Since the early 1990s, Andrea has been primarily focused on developing and manufacturing state-of-the-art microphone technologies and products for enhancing speech-based applications software and communications, primarily in the computer and business enterprise markets that require high quality, clear voice signals. Andrea’s technologies eliminate unwanted background noise to enable the optimum performance of various speech-based and audio applications. Andrea DSP Microphone and Audio Software Products and Andrea Anti-Noise Products have been designed for applications that are controlled by or depend on speech across a broad range of hardware and software platforms. These products incorporate Digital Signal Processing, Noise Cancellation, Active Noise Cancellation and Active Noise Reduction microphone technologies, and are designed to cancel background noise in a wide range of noisy environments, such as homes, offices, factories and automobiles. Andrea also manufactures a line of accessories for these products for the consumer and commercial markets in the United States as well as in Europe and Asia.

Management’s Liquidity Plans

As of December 31, 2008, Andrea had working capital of \$2,196,689, an accumulated deficit of \$72,620,296 and cash of \$1,006,951. Andrea’s loss from operations was \$330,828 for the year ended December 31, 2008. Andrea plans to continue to improve its cash flows during 2009 by aggressively pursuing additional licensing opportunities related to Andrea DSP Audio Software and increasing its Andrea Anti-Noise Headset Products sales through sales of refreshed product line, which they introduced in September 2008, as well as the increased efforts the Company is dedicating to its sales and marketing efforts. However, there can be no assurance that Andrea will be able to successfully execute the aforementioned plans.

As of March 25, 2009, Andrea has approximately \$1,600,000 of cash. Management projects that Andrea has sufficient liquidity available to operate through at least December 2009. While Andrea explores opportunities to increase revenues in new business areas, the Company also continues to examine additional opportunities for cost reduction and further diversification of its business. Since the third quarter of 2006, Andrea has generated cash flows from operations. Although these steps are encouraging, if Andrea fails to develop additional revenues from sales of its products and licensing of its technology or to generate adequate funding from operations, or if Andrea fails to obtain additional financing through a capital transaction or other type of financing, Andrea will be required to continue to significantly reduce its operating expenses and/or operations or Andrea may have to relinquish its products, technologies or markets which could have a materially adverse effect on revenue and operations. Andrea has no commitment for additional financing and may experience difficulty in obtaining additional financing on favorable terms, if at all.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The financial statements include the accounts of Andrea and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Loss (earnings) Per Share

Basic (loss) earnings per share is computed by dividing the net (loss) income by the weighted average number of common shares outstanding during the period. Diluted (loss) earnings adjusts basic (loss) earnings per share for the effects of convertible securities, stock options and other potentially dilutive financial instruments, only in the periods in which such effect is dilutive. Securities that could potentially dilute basic earnings per share (“EPS”) in the future that were not included in the computation of the diluted EPS because to do so would have been anti-dilutive for the periods presented, consist of the following:

	December 31, 2008	December 31, 2007
Total potentially dilutive common shares as of:		
Options to purchase common stock (Note 13)	14,661,820	9,686,820
Series C Convertible Preferred Stock and related accrued dividends (Note 7)	4,103,984	4,149,736
Series D Convertible Preferred Stock and related warrants (Note 8)	9,358,348	9,929,776
Total potentially dilutive common shares	28,124,152	23,766,332

Cash

Cash includes cash and highly liquid investments with original maturities of three months or less. At times during the years ended December 31, 2008 and 2007, the Company has cash deposits in excess of the maximum amounts insured by the Federal Deposit Insurance Corporation insurance limits. At December 31, 2008, the Company’s cash is held at three financial institutions.

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2008

Concentration of Credit Risk

The following customers accounted for 10% or more of Andrea's consolidated net revenues during at least one of the periods presented below:

	December 31,	
	2008	2007
Customer A	14%	11%
Customer B	*	18%
Customer C	22%	*

* Amounts are less than 10%

As of December 31, 2008, Customer C and Customer A accounted for approximately 61% and 13% of accounts receivable and as of December 31, 2007, Customer C and Customer A accounted for approximately 15% and 5% of accounts receivable.

The following suppliers accounted for 10% or more of Andrea's purchases during the periods presented below:

	December 31,	
	2008	2007
Supplier A	57%	34%
Supplier B	28%	55%

At December 31, 2008 and December 31, 2007, Supplier A accounted for approximately \$137,000 or 50% and 105,000 or 22 %, respectively of accounts payable. At December 31, 2007, Supplier B accounted for approximately \$191,000 or 40% of accounts payable.

Allowance for Doubtful Accounts

The Company performs on-going credit evaluations of its customers and adjusts credit limits based upon payment history and the customer's current credit worthiness, as determined by the review of their current credit information. Collections and payments from customers are continuously monitored. The Company maintains an allowance for doubtful accounts, which is based upon historical experience as well as specific customer collection issues that have been identified. While such bad debt expenses have historically been within expectations and allowances established, the Company cannot guarantee that it will continue to experience the same credit loss rates that it has in the past. If the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Inventories

Inventories are stated at the lower of cost (on a first-in, first-out) or market basis. The cost of inventory is based on the respective cost of materials. Andrea reviews its inventory reserve for obsolescence on a quarterly basis and establishes reserves on inventories based on the specific identification method as well as a general reserve. Andrea

records charges in inventory reserves as part of cost of revenues.

Property and Equipment

Property and equipment is stated at cost less accumulated depreciation and amortization. Depreciation is provided on a straight-line basis over the estimated useful lives of the assets ranging from 3 to 7 years. Leasehold improvements are amortized on a straight-line basis over the shorter of the lives of the respective leases or the expected useful lives of those improvements.

Expenditures for maintenance and repairs that do not materially prolong the normal useful life of an asset are charged to operations as incurred. Improvements that substantially extend the useful lives of the assets are capitalized. Upon sale or other disposition of assets, the cost and related accumulated depreciation and amortization are removed from the accounts and the resulting gain or loss, if any, is reflected in the statement of operations.

Other Intangible Assets

Andrea amortizes its core technology and patents and trademarks on a straight-line basis over their estimated useful lives that range from 15 to 17 years.

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2008

Long-Lived Assets

Andrea accounts for its long-lived assets in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets,” for purposes of determining and measuring impairment of its long-lived assets (primarily intangible assets) other than goodwill. Andrea’s policy is to review the value assigned to its long lived assets to determine if they have been permanently impaired by adverse conditions which may affect Andrea whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If Andrea identifies a permanent impairment such that the carrying amount of Andrea’s long lived assets is not recoverable using the sum of an undiscounted cash flow projection (gross margin dollars from product sales), the impaired asset is adjusted to its estimated fair value, based on an estimate of future discounted cash flows which becomes the new cost basis for the impaired asset. Considerable management judgment is necessary to estimate undiscounted future operating cash flows and fair values and, accordingly, actual results could vary significantly from such estimates. No impairment charges were recognized during the years ended December 31, 2008 and 2007.

Revenue Recognition

Non software-related revenue, which is generally comprised of microphones and microphone connectivity product revenues, is recognized when title and risk of loss pass to the customer, which is generally upon shipment. With respect to licensing revenues, Andrea recognizes revenue in accordance with Statement of Position (“SOP”) 97-2, “Software Revenue Recognition,” as amended, and Staff Accounting Bulletin Topic 13 “Revenue Recognition in Financial Statement.” License revenue is recognized based on the terms and conditions of individual contracts. In addition, fee based services, which are short-term in nature, are generally performed on a time-and-material basis under separate service arrangements and the corresponding revenue is generally recognized as the services are performed.

Income Taxes

The provision for income taxes is a result of certain licensing revenues that are subject to withholding of income tax as mandated by the foreign jurisdiction in which the revenues are earned. For all other income taxes, Andrea accounts for income taxes in accordance with SFAS No. 109, “Accounting for Income Taxes.” SFAS No. 109 requires an asset and liability approach for financial accounting and reporting for income taxes. The provision for income taxes is based upon income or loss after adjustment for those permanent items that are not considered in the determination of taxable income. Deferred income taxes represent the tax effects of differences between the financial reporting and tax bases of the Company’s assets and liabilities at the enacted tax rates in effect for the years in which the differences are expected to reverse. The Company evaluates the recoverability of deferred tax assets and establishes a valuation allowance when it is more likely than not that some portion or all of the deferred tax assets will not be realized. If it becomes more likely than not that a tax asset will be used, the related valuation allowance on such assets would be reversed. Management makes judgments as to the interpretation of the tax laws that might be challenged upon an audit and cause changes to previous estimates of tax liability. In management’s opinion, adequate provisions for income taxes have been made for all years. If actual taxable income by tax jurisdiction varies from estimates, additional allowances or reversals of reserves may be necessary. Income tax expense consists of the tax payable for the period and the change during the period in deferred tax assets and liabilities.

Effective January 1, 2007, the Company adopted the provisions of Financial Accounting Standards Board (“FASB”) issued Interpretation No. 48 “Accounting for Uncertainty in Income Taxes”—an Interpretation of FASB Statement No. 109 (“FIN 48”). FIN 48 establishes for all entities a minimum threshold for financial statement recognition of the

benefit of tax positions, and requires certain expanded disclosures. The adoption of FIN. 48 did not have a material effect on the Company's condensed consolidated financial position or results of operations or cash flows (Note 11).

Stock-Based Compensation

At December 31, 2008, Andrea had three stock-based employee compensation plans, which are described more fully in Note 13. Effective, January 1, 2006, the Company adopted the provisions of SFAS No. 123R, "Share-Based Payment." SFAS No. 123R establishes accounting for stock-based awards exchanged for employee services. Under the provisions of SFAS No. 123R, share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense over the employee's requisite service period (generally the vesting period of the equity grant). The fair value of the Company's common stock options are estimated using the Black Scholes option-pricing model with the following assumptions: expected volatility, dividend rate, risk free interest rate and the expected life. The Company expenses stock-based compensation by using the straight-line method. The Company elected to adopt the modified prospective transition method as provided by SFAS No. 123R. In accordance with the requirements of the modified prospective transition method, consolidated financial statements for prior year periods have not been restated to reflect the fair value method of expensing share-based compensation. Additionally, effective with the adoption of SFAS No. 123R excess tax benefits realized from the exercise of stock-based awards are classified in cash flows from financing activities. The future realization of the reserved deferred tax assets related to these tax benefits associated with the exercise of stock option will result in a credit to additional paid in capital if the related tax deduction reduces taxes payable.

Research and Development

Andrea expenses all research and development costs as incurred.

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2008

Shipping and Handling Costs

Andrea incurs shipping and handling costs in its operations. These costs are included in "Cost of revenues" in the consolidated statements of operations. \$90,608 and \$79,243 were billed to customers and are included in net revenues for the years ended December 31, 2008 and 2007, respectively.

Advertising Expenses

In accordance with SOP 93-7, "Reporting on Advertising Costs," all media costs of newspaper and magazine advertisements as well as trade show costs are expensed as incurred. Total advertising and marketing expenses for the years ended December 31, 2008 and 2007 were \$30,249 and \$20,677, respectively and are included in general, administrative and selling expenses.

Fair Value of Financial Instruments

SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS 157 applies to all assets and liabilities that are measured and reported on a fair value basis.

SFAS 157 establishes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value as follows:

Level 1 – Observable inputs such as quoted prices in active markets

Level 2 – Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly

Level 3 – Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions

SFAS 157 was effective for fiscal years beginning after November 15, 2007. FASB Staff Position ("FSP") FAS 157-2, "Effective Date of FASB Statement No. 157", delays the effective date of SFAS 157 for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed in the financial statements on a nonrecurring basis until fiscal years beginning after November 15, 2008. The Company does not have any assets or liabilities measured at fair value on a recurring basis at December 31, 2008; accordingly, the partial adoption of SFAS 157 did not have any impact on the Company's financial statements. The Company will apply the provisions of SFAS 157 to nonfinancial assets and liabilities beginning January 1, 2009 as required by FSP FAS 157-2. Andrea calculates the fair value of financial instruments and includes this additional information in the notes to financial statements when the fair value is different than the book value of those financial instruments. When the book value approximates fair value, no additional disclosure is made. Andrea uses quoted market prices whenever available to calculate these fair values. When quoted market prices are not available, Andrea uses standard pricing models for various types of financial instruments which take into account the present value of estimated future cash flows. As of December 31, 2008 and 2007, the carrying value of all financial instruments approximated fair value.

Recently Issued Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141R, "Business Combinations" ("SFAS 141R"), which replaces SFAS No. 141, "Business Combinations." SFAS 141R establishes principles and requirements for determining how an

enterprise recognizes and measures the fair value of certain assets and liabilities acquired in a business combination, including noncontrolling interests, contingent consideration, and certain acquired contingencies. SFAS 141R also requires acquisition-related transaction expenses and restructuring costs be expensed as incurred rather than capitalized as a component of the business combination. SFAS 141R will be applicable to the Company for fiscal 2009. SFAS 141R would have an impact on accounting for any businesses acquired after the effective date of this pronouncement.

In February 2007, the FASB issued SFAS No. 159 “The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment of FASB Statement No. 115” (“SFAS No. 159”), which permits entities to choose to measure many financial instruments and certain other items at fair value. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Adoption is required for fiscal years beginning after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 159. The adoption of this pronouncement did not have any material effects on the Company’s consolidated financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements – An Amendment of ARB No. 51” (“SFAS 160”). SFAS 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary (previously referred to as minority interests). SFAS 160 also requires that a retained noncontrolling interest upon the deconsolidation of a subsidiary be initially measured at its fair value. Upon adoption of SFAS 160, the Company would be required to report any noncontrolling interests as a separate component of stockholders’ equity. The Company would also be required to present any net income allocable to noncontrolling interests and net income attributable to the stockholders of the Company separately in its consolidated statements of operations. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. SFAS 160 requires retroactive adoption of the presentation and disclosure requirements for existing minority interests. All other requirements of SFAS 160 shall be applied prospectively. SFAS 160 would have an impact on the presentation and disclosure of the noncontrolling interests of any non wholly-owned businesses acquired in the future.

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

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In March 2008, the FASB issued SFAS 161, "Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133", which amends and expands the disclosure requirements of SFAS 133 to require qualitative disclosure about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. This statement will be effective for the Company beginning on January 1, 2009. The adoption of this statement will change the disclosures related to derivative instruments that might be held by the Company.

In June 2008, the FASB ratified EITF No. 07-5, "Determining Whether an Instrument (or an Embedded Feature) is Indexed to an Entity's Own Stock" ("EITF 07-5"). EITF 07-5 provides that an entity should use a two-step approach to evaluate whether an equity-linked financial instrument (or embedded feature) is indexed to its own stock, including evaluating the instrument's contingent exercise and settlement provisions. EITF 07-5 is effective for financial statements issued for fiscal years beginning after December 15, 2008. Early application is not permitted. The Company is assessing the potential impact of this EITF 07-5 on the financial condition and results of operations.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

Management bases its estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. The most significant estimates, among other things, are used in accounting for allowances for bad debts, inventory valuation and obsolescence, product warranty, depreciation, deferred income taxes, expected realizable values for assets (primarily intangible assets), contingencies, revenue recognition as well as the recording and presentation of the Company's convertible preferred stock. Estimates and assumptions are periodically reviewed and the effects of any material revisions are reflected in the consolidated financial statements in the period that they are determined to be necessary. Actual results could differ from those estimates and assumptions.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

3. INTANGIBLE ASSETS

Intangible assets, net, consists of the following:

	December 31,	
	2008	2007
Core Technology	\$ 8,567,448	\$ 8,567,448
Trademarks and Patents	572,893	529,271
	9,140,341	9,096,719
Less: accumulated amortization	(6,596,560)	(6,119,046)

\$	2,543,781	\$	2,977,673
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The changes in the carrying amount of intangible assets during the years ended December 31, 2008 and 2007 were as follows:

	Core Technology	Trademarks and Patents	Totals
Balance as of January 1, 2007	3,089,948	347,484	3,437,432
Additions during the period	-	12,775	12,775
Amortization	(441,421)	(31,113)	(472,534)
Balance as of December 31, 2007	\$ 2,648,527	\$ 329,146	\$ 2,977,673
Additions during the period	-	43,622	43,622
Amortization	(441,421)	(36,093)	(477,514)
Balance as of December 31, 2008	\$ 2,207,106	\$ 336,675	\$ 2,543,781

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

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Andrea accounts for its long-lived assets in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" for purposes of determining and measuring impairment of its long-lived assets (primarily intangible assets) other than goodwill. Andrea's policy is to periodically review the value assigned to its long-lived assets to determine if they have been permanently impaired by adverse conditions which may affect Andrea. If Andrea identifies a permanent impairment such that the carrying amount of Andrea's long lived assets are not recoverable using the sum of an undiscounted cash flow projection (gross margin dollars from product revenues), a new cost basis for the impaired asset will be established. If required, an impairment charge is recorded based on an estimate of future discounted cash flows. This new cost basis will be net of any recorded impairment.

In 2007 because the revenues from the Andrea DSP Microphone and Audio Software Products business segment were lower than expected and this business segment was still operating at a loss, management compared the sum of Andrea's undiscounted cash flow projections (gross margin dollars from product sales) of the Andrea DSP Microphone and Audio Software core technology to the carrying value of that technology. The results of this test indicated that there was not an impairment. This process utilized probability weighted undiscounted cash flow projections which include a significant amount of management's judgment and estimates as to future revenue. If these probability weighted projections do not come to fruition, the Company could be required to record an impairment charge in the near term and such impairment could be material.

Amortization expense was \$477,514 and \$472,534 for the years ended December 31, 2008 and 2007, respectively. Amortization of core technology is expected to be approximately \$441,421 per year for the next six years. Trademarks and patents are amortized on a straight-line basis over 17 years. Assuming no changes in the Company's intangible assets, estimated amortization expense for each of the five succeeding fiscal years ending December 31 is expected to be approximately \$474,905 per year.

4. INVENTORIES, net

Inventories, net, consist of the following:

	December 31,	
	2008	2007
Raw materials	\$ 31,550	\$ 62,834
Work in Process	36,291	-
Finished goods	1,502,193	1,218,971
	1,570,034	1,281,805
Less: reserve for obsolescence	(701,821)	(566,941)
	\$ 868,213	\$ 714,864

5. PROPERTY AND EQUIPMENT, net

Property and equipment, net, consists of the following:

	December 31,	
	2008	2007
Machinery and equipment	\$ 528,500	\$ 492,989
Less: accumulated depreciation	(467,596)	(435,238)
	\$ 60,904	\$ 57,751

Depreciation of property and equipment was \$32,358 and \$15,362 for the years ended December 31, 2008 and 2007, respectively.

6. OTHER CURRENT LIABILITIES

Other current liabilities consist of the following:

	December 31,	
	2008	2007
Accrued payroll and related expenses	\$ 71,073	\$ 55,634
Accrued professional and other service fees	72,425	65,451
Deferred Revenue	40,000	-
Accrued other	1,754	183
	\$ 185,252	\$ 121,268

7. SERIES C CONVERTIBLE PREFERRED STOCK

On October 10, 2000, Andrea issued and sold in a private placement \$7,500,000 of Series C Redeemable Convertible Preferred Stock (the "Series C Preferred Stock"). Each of these shares of Series C Preferred Stock had a stated value of \$10,000 plus a \$1,671.23 increase in the stated value, which sum is convertible into Common Stock at a conversion price of \$0.2551. On February 17, 2004, Andrea announced that it had entered into an Exchange and Termination Agreement and an Acknowledgment and Waiver Agreement, which eliminated the dividend of 5% per annum on the stated value. The additional amount of \$1,671.23 represents the 5% per annum from October 10, 2000 through February 17, 2004.

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On April 11, 2007, 10 shares of Series C Preferred Stock, together with related accrued dividends of \$16,712, were converted into 457,516 shares of Common Stock at a conversion price of \$0.2551.

On November 10, 2008, 1 share of Series C Preferred Stock, together with \$1,672 of previously accrued dividends, were converted into 45,752 shares of Common Stock at the conversion price of \$0.2551.

As of December 31, 2008, there were 89.701477 shares of Series C Preferred Stock outstanding, which were convertible into 4,103,984 shares of Common Stock and remaining accrued dividends of \$149,912.

8. SERIES D CONVERTIBLE PREFERRED STOCK

On February 17, 2004, Andrea entered into a Securities Purchase Agreement (including a Registration Rights Agreement) with certain holders of the Series C Preferred Stock and other investors (collectively, the "Buyers") pursuant to which the Buyers agreed to invest a total of \$2,500,000. In connection with this agreement, on February 23, 2004, the Buyers purchased, for a purchase price of \$1,250,000, an aggregate of 1,250,000 shares of a new class of preferred stock, the Series D Preferred Stock, convertible into 5,000,000 shares of Common Stock (an effective conversion price of \$0.25 per share) and Common Stock warrants exercisable for an aggregate of 2,500,000 shares of Common Stock. The warrants are exercisable at any time after August 17, 2004 and before February 23, 2009 at an exercise price of \$0.38 per share. On February 23, 2009, these warrants expired without being exercised.

In addition, on June 4, 2004, the Buyers purchased for an additional \$1,250,000, an additional 1,250,000 shares of Series D Preferred Stock convertible into 5,000,000 shares of Common Stock (an effective conversion price of \$0.25 per share) and Common Stock warrants exercisable for an aggregate of 2,500,000 shares of Common Stock. The warrants are exercisable at any time after December 4, 2004 and before June 4, 2009 at an exercise price of \$0.17 per share.

Knightsbridge Capital served as a financial advisor to Andrea in connection with the aforementioned transactions and the initial issuance of the Series D Preferred Stock and related warrants. In connection with these transactions, Andrea agreed to pay Knightsbridge Capital \$300,000 in cash and to issue warrants exercisable for an aggregate of 377,094 shares of Common Stock. The warrants were exercisable at any time after August 17, 2004 and before February 23, 2009 at an exercise price of \$0.38 per share. On February 23, 2009, these warrants expired without being exercised.

The Company is required to maintain an effective registration statement from the time of issuance until the earlier of (i) the date as of which the investors may sell all of the registrable securities covered by the registration statement without restriction under SEC rules or (ii) the date on which the investors shall have sold all the registrable securities covered by the registration statement. In the event that the holder of the Series D Preferred Stock and related warrants is unable to convert these securities into Andrea Common stock the Company shall pay to each such holder of such registrable securities a Registration Delay Payment. This payment is to be paid in cash and is equal to the product of (i) the stated value of such Preferred Shares multiplied by (ii) the product of (1) .0005 multiplied by (2) the number of days that sales cannot be made pursuant to the Registration Statement (excluding any days during that may be considered grace periods as defined by the Registration Rights Agreement).

Prior to 2007, there were 281,250 exercises of Series D Preferred Stock Warrants. There were no Series D Preferred Stock Warrant exercises during the year ended December 31, 2008 and 2007.

On March 16, 2007, 25,000 shares of Series D Preferred Stock were converted into 100,000 shares of Common Stock at a conversion price of \$0.25. On April 11, 2007, 25,000 shares of Series D Preferred Stock were converted into 100,000 shares of Common Stock at a conversion price of \$0.25. On December 5, 2008, 142,857 shares of Series D Preferred Stock were converted into 571,428 shares of Common Stock at a conversion price of \$0.25.

As of December 31, 2008, there are 1,050,001 shares of Series D Preferred Stock and 5,158,344 related warrants outstanding, which are convertible and exercisable into 9,358,348 shares of Common Stock. On February 23, 2009, 2,877,094 warrants expired. As of March 25, 2009, there are 1,050,001 shares of Series D Preferred Stock and 2,281,250 related warrants outstanding which are convertible and exercisable into 6,481,254 shares of Common Stock.

9. LICENSING AGREEMENTS

The Company has entered into various licensing, production and distribution agreements with manufacturers of PC and related components. These agreements provide for revenues based on the terms of each individual agreement. The Company's three largest licensing customers accounted for \$410,049, \$46,641 and \$1,037,041 of revenues in 2008 and for \$244,558, \$233,033 and \$159,525 of revenues in 2007.

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

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10. RETIREMENT PLAN

Andrea has a defined contribution profit sharing plan that is qualified under Section 401(k) of the Internal Revenue Code and is available to substantially all of its employees. Andrea did not make any contributions to this plan for the years ended December 31, 2008 and 2007.

11. INCOME TAXES

The Company has adopted the provisions of FIN 48, on January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement 109, "Accounting for Income Taxes," and prescribes a recognition threshold and measurement process for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim period, disclosure and transition. There were no unrecognized tax benefits as of January 1, 2007.

Upon the adoption of FIN 48, the Company was required to evaluate all of its tax positions including any limitations from the result of a change in control under Section 382. During 2007, the Company performed a preliminary evaluation as to whether a change in control had taken place. Management has determined that a change in control may have taken place. As a result of its preliminary evaluation management has determined that \$30 million of its \$50 million of total NOL may be subject to limitation and accordingly reduced its net deferred tax asset and related evaluation allowance by \$11.7 million.

The Company has identified its federal tax return and its state tax return in New York as "major" tax jurisdictions, as defined in FIN 48. Based on the Company's evaluation, it has been concluded that there are no significant uncertain tax positions requiring recognition in the Company's financial statements. The Company's evaluation was performed for tax years ended 2004 through 2008. The Company believes that its income tax positions and deductions will be sustained on audit and does not anticipate any adjustments that will result in a material change to its financial position. In addition, the Company did not record a cumulative effect adjustment related to the adoption of FIN 48.

The Company's policy for recording interest and penalties associated with audits is to record such items as a component of income tax expense. There were no amounts accrued for penalties or interest as of or during the year ended December 31, 2008. The Company does not expect its unrecognized tax benefit position to change during the next twelve months. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position.

The components of earnings before income taxes are as follows:

	For the Years Ended December 31,	
	2008	2007
Domestic	\$ (369,886)	\$ (630,420)
Foreign	48,050	269,705
(Loss) income before income taxes	\$ (321,836)	\$ (360,715)

The provision for income tax consists of the following:

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	For the Years Ended December 31,	
	2008	2007
Current:		
Federal	\$ -	\$ -
Foreign	4,902	29,409
State and Local:	-	-
Deferred		
Federal	(82,000)	(10,255,000)
Foreign	-	-
State and Local:	(12,000)	(1,508,000)
Adjustment to valuation allowance related to net deferred tax assets	94,000	11,763,000
	\$ 4,902	\$ 29,409

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

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A reconciliation between the effective rate for income taxes and the amount computed by applying the statutory Federal income tax rate to loss from continuing operations before provision (benefit) for income taxes is as follows:

	For the Years Ended December 31,	
	2008	2007
Tax provision at statutory rate	(34)%	(34)%
State and local taxes	(5)%	(4)%
Core technology amortization	46%	42%
Stock Option Expense Related to Incentive Stock Options	22%	18%
Foreign income and withholding taxes	2%	8%
Change in valuation allowance for net deferred tax assets	(29)%	(22)%
	2%	8%

The effective tax rate for the years ended December 31, 2008 and December 31, 2007 is a result of certain licensing revenues that are subject to withholding of income tax as mandated by the respective foreign jurisdiction in which the revenues are earned.

The components of temporary differences that give rise to significant portions of the deferred tax asset, net, are as follows:

	For the Years Ended December 31,	
	2008	2007
Deferred tax assets:		
Accrued expenses	\$ 35,000	\$ 50,000
Allowance for doubtful accounts	3,000	8,000
Reserve for obsolescence	274,000	221,000
Expense associated with non-qualified stock options	43,000	-
Deferred Revenue	16,000	-
Foreign tax credit	97,000	93,000
NOL carryforward	7,647,000	7,837,000
	8,115,000	8,209,000
Less: valuation allowance	(8,115,000)	(8,209,000)
Deferred tax asset, net	\$ -	\$ -

The change in the valuation allowance for deferred tax assets are summarized as follows:

	For the Years Ended December 31,	
	2008	2007
Beginning Balance	\$ 8,209,000	\$ 19,972,000
Change in Allowance	(94,000)	(11,763,000)
Ending Balance	\$ 8,115,000	\$ 8,209,000

SFAS No. 109 requires that a valuation allowance be established when it is "more likely than not" that all or a portion of deferred tax assets will not be realized. A review of all available positive and negative evidence needs to be

considered, including a company's performance, the market environment in which the company operates, the length of carryback and carryforward periods, and expectations of future profits, etc.

SFAS No. 109 further states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years. Therefore, cumulative losses weigh heavily in the overall assessment. Andrea will provide a full valuation allowance on future tax benefits until it can sustain a level of profitability that demonstrates its ability to utilize the assets, or other significant positive evidence arises that suggests Andrea's ability to utilize such assets.

As of December 31, 2008, Andrea had net operating loss and credit carryforwards of approximately \$19.6 million (net amount after potential Section 382 limitations) expiring in varying amounts beginning in 2009 through 2027. Andrea has foreign tax credits of approximately \$97,000 expiring in varying amounts beginning 2016 through 2018. The Company has elected the "with and without approach" regarding ordering of windfall tax benefits to determine whether the windfall tax benefit did reduce taxes payable in the current year. Under this approach the windfall tax benefit would be recognized in additional paid-in-capital only if an incremental tax benefit is realized after considering all other benefits presently available.

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

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12. COMMITMENTS AND CONTINGENCIES

Leases

Andrea leases its corporate headquarters located in Bohemia, New York. The lease from an unrelated party, which currently expires in February 2014, is for approximately 11,000 square feet and houses Andrea's warehousing, sales and executive offices. Rent expense under this operating lease was approximately \$83,717 and \$81,279 for the year ended December 31, 2008 and 2007, respectively.

As of December 31, 2008, the minimum annual future lease payments, under this lease and all other noncancellable operating leases, are as follows:

2009	\$ 98,103
2010	93,377
2011	95,818
2012	98,556
2012	96,814
Thereafter	133,283
Total	\$ 615,951

Employment Agreements

In November 2008, the Company entered into an employment agreement with the Chairman of the Board, Douglas J Andrea. The effective date of the employment agreement is August 1, 2008 and expires July 31, 2010 and is subject to renewal as approved by the Compensation Committee of the Board of Directors. Pursuant to his employment agreement, Mr. Andrea will receive an annual base salary of \$312,500 through July 31, 2009 and for the period of August 1, 2009 through July 31, 2010 Mr. Andrea will receive an annual base salary of \$325,000. The employment agreement provides for quarterly bonuses equal to 25% of the Company's pre-bonus net after tax quarterly earnings in excess of \$25,000 for a total quarterly bonus amount not to exceed \$12,500; and annual bonuses equal to 10% of the Company's annual pre-bonus net after tax earnings in excess of \$300,000. All bonuses shall be payable as soon as the Company's cash flow permits. All bonus determinations or any additional bonus in excess of the above will be made in the sole discretion of the Compensation Committee. On August 8, 2008, the Board granted Mr. Andrea 2,000,000 stock options and 1,000,000 stock options with an aggregate fair value of \$120,000 (fair value was estimated using the Black-Scholes option-pricing model). The 2,000,000 grant vests in three equal annual installments over a three year period commencing August 1, 2009. The 1,000,000 grant vests in three equal annual installments over a three year period commencing August 1, 2010. All stock options granted have an exercise price of \$0.04 per share, which was the fair market value of the Company's common stock at the date of grant, and a term of 10 years. Pursuant to the employment agreement and subject to the approval of the Board, the Compensation Committee will recommend a second grant of 1,000,000 stock options as soon as practical after August 1, 2009, with an exercise price equal to the per share fair market value of the Company's common stock on the date of grant. Mr. Andrea is also entitled to a change in control payment equal to two times his salary with continuation of health and medical benefits for two years in the event of a change in control, as defined in the agreement. At December 31, 2008, the future minimum cash commitments under this agreement aggregate \$507,292.

In November 1999, as amended August 2008, the Company entered into a change in control agreement with the Chief Financial Officer, Corisa L. Guiffre. This agreement provides for a change in control payment equal to three times her

average annual compensation for the five preceding taxable years, with continuation of health and medical benefits for three years in the event of a change in control of the Company, as defined in the agreement, and subsequent termination of employment other than for cause.

Legal Proceedings

Andrea is involved in routine litigation incidental to the normal course of business. While it is not feasible to predict or determine the final outcome of the claims, Andrea believes the resolution of these matters will not have a material adverse effect on Andrea's financial position, results of operations or liquidity.

13. STOCK PLANS AND STOCK-BASED COMPENSATION

In 1991, the Board of Directors of Andrea (the "Board") adopted the 1991 Performance Equity Plan ("1991 Plan"), which was approved by the shareholders. The 1991 Plan, as amended, authorizes the granting of awards, the exercise of which would allow up to an aggregate of 4,000,000 shares of Andrea's Common Stock to be acquired by the holders of those awards. Stock options granted to employees and directors under the 1991 Plan were granted for terms of up to 10 years at an exercise price equal to the market value at the date of grant. No further awards will be granted under the 1991 Plan.

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In 1998, the Board adopted the 1998 Stock Option Plan (“1998 Plan”), which was subsequently approved by the shareholders. The 1998 Plan, as amended, authorizes the granting of awards, the exercise of which would allow up to an aggregate of 6,375,000 shares of Andrea’s Common Stock to be acquired by the holders of those awards. The awards can take the form of stock options, stock appreciation rights, restricted stock, deferred stock, stock reload options or other stock-based awards. Awards may be granted to key employees, officers, directors and consultants. No further awards will be granted under the 1998 Plan.

In October 2006, the Board adopted the Andrea Electronics Corporation 2006 Equity Compensation Plan (“2006 Plan”), which was subsequently approved by the shareholders. The 2006 Plan authorizes the granting of awards, the exercise of which would allow up to an aggregate of 10,000,000 shares of Andrea’s Common Stock to be acquired by the holders of those awards. The awards can take the form of stock options, stock appreciation rights, restricted stock or other stock-based awards. Awards may be granted to key employees, officers, directors and consultants. At December 31, 2008, there were 101,345 shares available for further issuance under the 2006 Plan.

The stock option awards granted under these plans have been granted with an exercise price equal to the market price of the Company’s stock at the date of grant; with vesting periods of up to four years and 10-year contractual terms.

The fair values of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model that uses the weighted-average assumptions noted in the following table. Expected volatilities are based on implied volatilities from historical volatility of the Company’s stock. The expected term of options granted represents the period of time that options granted are expected to be outstanding. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

The fair values of the stock options granted were estimated on the date of grant using the Black-Scholes option-pricing model that uses the following weighted-average assumptions for the year ended December 31, 2008 and 2007:

	December 31, 2008	December 31, 2007
Expected life in years (based on simplified method)	6	6
Risk-free interest rates	3.38%	4.17%
Volatility (based on historical volatility)	146.6%	100.6%
Dividend yield	0%	0%

Option activity during 2008 is summarized as follows:

	Options Outstanding				Options Exercisable			
	Options Outstanding	Weighted Average Exercise Price	Weighted Average Fair Value	Weighted Average Remaining Contractual Life	Options Exercisable	Weighted Average Exercise Price	Weighted Average Fair Value	Weighted Average Remaining Contractual Life
At January 1, 2008	9,686,820	\$ 0.76	\$ 0.59	7.79 years	5,355,590	\$ 1.29	\$ 1.00	6.57 years

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Granted	5,185,000	\$	0.04	\$	0.04					
Cancelled	(210,000)	\$	13.89	\$	11.33					
At December										
31, 2008	14,661,820	\$	0.32	\$	0.24	7.89 years	6,973,385	\$	0.60	\$ 0.45 6.45 years

During the year ended December 31, 2008, 1,827,795 options vested with a weighted average exercise price of \$0.12 and a weighted average fair value of \$0.10 per option. Based on the December 31, 2008, fair market value of the Company's common stock of \$0.04, there is no aggregate intrinsic value for the 14,661,820 options outstanding and 6,973,385 shares exercisable.

During the year ended December 31, 2007, 1,113,090 options vested with a weighted average exercise price of \$0.12 and a weighted average fair value of \$0.10 per option. Based on the December 31, 2007, fair market value of the Company's common stock of \$0.06, the aggregate intrinsic value of the 9,686,820 options outstanding and 5,355,590 shares exercisable is \$26,500.

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Total compensation expense recognized related to stock option awards was \$230,994 and \$185,099 for the year ended December 31, 2008 and 2007, respectively. In the accompanying consolidated statement of operations for the year ending December 31, 2008, \$180,919 of expense is included in general, administrative and selling expenses, \$48,654 is included in research and development expenses and \$1,421 is included in cost of revenues. In the accompanying consolidated statement of operations for the year ending December 31, 2007, \$145,607 of expense is included in general, administrative and selling expenses, \$38,002 is included in research and development expenses and \$1,490 is included in cost of revenues.

As of December 31, 2008, there was \$236,614 of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the 1998 and 2006 Plans. This unrecognized compensation cost is expected to be recognized over the next 3 years (\$166,637 in 2009, \$57,056 in 2010 and \$12,921 in 2011).

Pursuant to Andrea's compensation policy for outside directors, Andrea granted 400,000 shares of Common Stock with a fair market value of \$0.05 per share in 2007 and 500,000 shares of Common Stock with a fair market value of \$0.04 per share in 2008. These stock grants were fully vested on the date of grant. Compensation expense related to these awards was \$22,501 and \$22,500 for the years ended December 31, 2008 and 2007, respectively.

14. SEGMENT INFORMATION

Andrea follows the provisions of SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." Reportable operating segments are determined based on Andrea's management approach. The management approach, as defined by SFAS No. 131, is based on the way that the chief operating decision-maker organizes the segments within an enterprise for making operating decisions and assessing performance. While Andrea's results of operations are primarily reviewed on a consolidated basis, the chief operating decision-maker also manages the enterprise in two segments: (i) Andrea DSP Microphone and Audio Software Products and (ii) Andrea Anti-Noise Products. Andrea DSP Microphone and Audio Software Products primarily include products based on the use of some, or all, of the following technologies: Andrea Digital Super Directional Array microphone technology (DSDA), Andrea Direction Finding and Tracking Array microphone technology (DFTA), Andrea PureAudio noise filtering technology, and Andrea EchoStop, an advanced acoustic echo cancellation technology. Our Andrea Anti-Noise Products include noise cancellation and active noise cancellation computer headset products and related computer peripheral products. The following represents selected consolidated financial information for Andrea's segments for the years ended December 31, 2008 and 2007:

2008 Segment Data	Andrea DSP Microphone and Audio Software Products	Andrea Anti- Noise Products	Total 2008
Net revenues from external customers	\$ 749,010	\$ 2,430,936	\$ 3,179,946
License revenues	1,531,148	-	1,531,148
Income (loss) from operations	54,793	(385,621)	(330,828)
Depreciation and Amortization	470,728	39,144	509,872
Purchases of property and equipments	8,616	26,895	35,511
Purchases of patents and trademarks	8,862	34,760	43,622
Assets	3,583,439	1,838,402	5,421,841

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Total long lived assets	2,393,721	223,828	2,617,549
	Andrea DSP Microphone and Audio Software Products	Andrea Anti- Noise Products	Total 2007
2007 Segment Data			
Net revenues from external customers	\$ 1,732,126	\$ 2,618,864	\$ 4,350,990
License revenues	695,223	-	695,223
Loss from operations	329,097	40,240	369,337
Depreciation and Amortization	468,706	19,190	487,896
Capital expenditures	-	33,870	33,870
Purchases of patents and trademarks	3,700	9,075	12,775
Assets	4,021,688	1,611,318	5,633,006
Total long lived assets	2,858,713	189,575	3,048,288

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ANDREA ELECTRONICS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2008

Management of Andrea assesses assets and non-operating income statement data on a consolidated basis only. International revenues are based on the country in which the end-user is located. For the years ended December 31, 2008 and 2007, and as of each respective year-end, net revenues and accounts receivable by geographic area are as follows:

Geographic Data	2008	2007
Net Revenues:		
United States	\$ 4,218,958	\$ 3,609,523
Foreign(1)	492,136	1,436,690
	\$ 4,711,094	\$ 5,046,213
Accounts receivable:		
United States	\$ 804,433	\$ 736,122
Foreign	-	258,324
	\$ 804,433	\$ 994,446

(1) Net revenue to the People's Republic of China and Singapore represented 19% and 4%, respectively of total net revenues for year ended December 31, 2007.

\$45,655 of our property and equipment, net represents product tools and molds. These tools and molds are located in Asia at the manufacturing facility, which produces the respective product. All of our remaining property and equipment, net is located at our facility in Bohemia, New York.

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SIGNATURES

Pursuant to the requirements of the Section 13 or 15(d) 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.

ANDREA ELECTRONICS CORPORATION

By: /s/ DOUGLAS J. ANDREA
Name: Douglas J. Andrea
Title: Chairman of the Board,
President,
Chief Executive Officer and Corporate
Secretary

Date: March 30, 2009

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons in the capacities and on the dates indicated.

/s/ DOUGLAS J. ANDREA Douglas J. Andrea	Chairman of the Board, President, Chief Executive Officer and Corporate Secretary	March 30, 2009
/s/ CORISA L. GUIFFRE Corisa L. Guiffre	Vice President, Chief Financial Officer and Assistant Corporate Secretary	March 30, 2009
/s/ GARY A. JONES Gary A. Jones	Director	March 30, 2009
/s/ LOUIS LIBIN Louis Libin	Director	March 30, 2009
/s/ JOSEPH J. MIGLIOZZI Joseph J. Miglioizzi	Director	March 30, 2009
/s/ JONATHAN D. SPAET Jonathan D. Spaet	Director	March 30, 2009