

SPARTAN STORES INC  
Form 10-Q  
February 04, 2010

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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 January 2, 2010.

**OR**

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number: 000-31127

**SPARTAN STORES, INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Michigan**

(State or Other Jurisdiction  
of Incorporation or Organization)

**38-0593940**

(I.R.S. Employer  
Identification No.)

**850 76<sup>th</sup> Street, S.W.**

**P.O. Box 8700**

**Grand Rapids, Michigan**

(Address of Principal Executive Offices)

**49518**

(Zip Code)

**(616) 878-2000**

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒

No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☐

No ☐

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

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|                         |                       |                           |                                  |
|-------------------------|-----------------------|---------------------------|----------------------------------|
| Large accelerated filer | <input type="radio"/> | Accelerated filer         | <input checked="" type="radio"/> |
| Non-accelerated filer   | <input type="radio"/> | Smaller Reporting Company | <input type="radio"/>            |

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

Yes ☐

No ☒

As of February 1, 2010 the registrant had 22,453,134 outstanding shares of common stock, no par value.

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## FORWARD-LOOKING STATEMENTS

The matters discussed in this Quarterly Report on Form 10-Q, in our press releases and in our website-accessible conference calls and investor presentations include "forward-looking statements" about the plans, strategies, objectives, goals or expectations of Spartan Stores, Inc. (together with its subsidiaries, "Spartan Stores"). These forward-looking statements are identifiable by words or phrases indicating that Spartan Stores or management "expects," "anticipates," "plans," "believes," "estimates," "intends," is "optimistic" or "confident" that a particular occurrence or event "began," "will," "may," "could," "should" or "will likely" result or occur or "continue" in the future, that the "outlook" or "trend" is toward a particular result or occurrence, that a development is an "opportunity," a "priority" or "strategy" or similarly stated expectations. Accounting estimates, such as those described under the heading "Critical Accounting Policies" in Part I, Item 2 of this Form 10-Q, are inherently forward-looking. Our asset impairment and exit cost provisions are estimates and actual costs may be more or less than these estimates and differences may be material. You should not place undue reliance on these forward-looking statements, which speak only as of the date of the Quarterly Report, release, presentation, or statement.

In addition to other risks and uncertainties described in connection with the forward-looking statements contained in this Quarterly Report on Form 10-Q, Spartan Stores' Annual Report on Form 10-K for the year ended March 28, 2009 (in particular, you should refer to the discussion of "Risk Factors" in Item 1A of our Annual Report on Form 10-K) and other periodic reports filed with the Securities and Exchange Commission, there are many important factors that could cause actual results to differ materially. Our ability to maintain and strengthen our retail-store performance; assimilate acquired stores; successfully transition our Plymouth distribution operations to our Grand Rapids distribution center; maintain or grow sales; respond successfully to competitors; maintain or increase gross margin; anticipate and successfully respond to openings of competitors; maintain and improve customer and supplier relationships; realize expected benefits of new relationships; realize growth opportunities; expand our customer base; reduce operating costs; generate cash; continue to meet the terms of our debt covenants; continue to pay dividends; and implement the other programs, plans, priorities, strategies, objectives, goals or expectations described in this Quarterly Report, our other reports or presentations, our press releases and our public comments is not certain and will be affected by changes in economic conditions generally or in the markets and geographic areas that we serve, adverse effects of the changing food and distribution industries and other factors including, but not limited to, those discussed below.

Anticipated future sales are subject to competitive pressures from many sources. Our Distribution and Retail businesses compete with many distributors, supercenters, warehouse discount stores, supermarkets and other retail stores selling food and related products, pharmacies and product manufacturers. Future sales will be dependent on the number of retail stores that we own and operate, our ability to retain and add to the retail stores to whom we distribute, competitive pressures in the retail industry generally and our geographic markets specifically, our ability to implement effective new marketing and merchandising programs and unseasonable weather conditions. Competitive pressures in these and other business segments may result in unexpected reductions in sales volumes, product prices or service fees.

Our operating and administrative expenses, and as a result, our net earnings and cash flows, may be adversely affected by changes in costs associated with, among other factors: difficulties in the operation of our business segments; future business acquisitions; adverse effects on business relationships with independent retail grocery store customers; difficulties in the retention or hiring of employees; labor stoppages or disputes; business and asset divestitures; increased transportation or fuel costs; current or future lawsuits and administrative proceedings; and losses of, or financial difficulties of, customers or suppliers. Our future costs for pension and postretirement benefit costs may be adversely affected by changes in actuarial assumptions and methods, investment return and the composition of the group of employees and retirees covered, changes in our business that result in a withdrawal

liability under multi-employer plans, and the actions and contributions of other employers who participate in multi-employer plans to which we contribute. Our future income tax expense, and as a result, our net earnings and cash flows, could be adversely affected by changes in tax laws and related interpretations. Our accounting estimates could change and the actual effects of changes in accounting principles could deviate from our estimates due to changes in facts, assumptions, or acceptable methods, and actual results may vary materially from our estimates. Our operating and administrative expenses, net earnings and cash flow could also be adversely affected by changes in our sales mix. Our ongoing cost

reduction initiatives and changes in our marketing and merchandising programs may not be as successful as anticipated. Acts of terrorism, war, natural disaster, fire, accident, severe weather, general economic conditions and unemployment, particularly in Michigan, government assistance programs, or other circumstances beyond our control could have adverse effects on the availability of and our ability to operate our warehouses and other facilities, consumer buying behavior, fuel costs, shipping and transportation, product imports, product cost inflation or deflation and its impact on LIFO expense and other factors affecting our company and the grocery industry generally. A combination of the aforementioned factors coupled with a prolonged general economic recession could result in goodwill and other long-lived asset impairment charges.

Our future interest expense and income also may differ from current expectations, depending upon, among other factors: the amount of additional borrowings; changes in our borrowing agreements; changes in the interest rate environment; changes in accounting pronouncements; and changes in the amount of fees received or paid. The availability of our secured loan agreement depends on compliance with the terms of the loan agreement and financial stability of the banking community.

Our dividend policy does not commit the Board of Directors to declare future dividends. Each future dividend will be considered and declared by the Board of Directors in its discretion. The ability of the Board of Directors to continue to declare dividends will depend on a number of factors, including our future financial condition and profitability and compliance with the terms of our credit facilities.

This section is intended to provide meaningful cautionary statements. This should not be construed as a complete list of all economic, competitive, governmental, technological and other factors that could adversely affect our expected consolidated financial position, results of operations or liquidity. Additional risks and uncertainties not currently known to Spartan Stores or that Spartan Stores currently believes are immaterial also may impair its business, operations, liquidity, financial condition and prospects. We undertake no obligation to update or revise our forward-looking statements to reflect developments that occur or information obtained after the date of this Quarterly Report.

**PART I**  
**FINANCIAL INFORMATION**

**ITEM 1. Financial Statements**

**SPARTAN STORES, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands)

(Unaudited)

| <u>Assets</u>                                                      | January 2,<br>2010 | March 28,<br>2009 |
|--------------------------------------------------------------------|--------------------|-------------------|
|                                                                    |                    |                   |
| <b>Current assets</b>                                              |                    |                   |
| Cash and cash equivalents                                          | \$ 7,180           | \$ 6,519          |
| Accounts receivable, net                                           | 52,020             | 51,470            |
| Inventories, net                                                   | 135,718            | 113,790           |
| Prepaid expenses and other current assets                          | 9,531              | 9,579             |
| Deferred taxes on income                                           | 4,174              | 5,201             |
|                                                                    |                    |                   |
| <b>Total current assets</b>                                        | 208,623            | 186,559           |
| <b>Other assets</b>                                                |                    |                   |
| Goodwill                                                           | 251,491            | 249,303           |
| Other, net                                                         | 55,809             | 52,643            |
|                                                                    |                    |                   |
| <b>Total other assets</b>                                          | 307,300            | 301,946           |
| <b>Property and equipment, net</b>                                 | 249,915            | 234,806           |
|                                                                    |                    |                   |
| <b>Total assets</b>                                                | \$ 765,838         | \$ 723,311        |
|                                                                    |                    |                   |
| <b><u>Liabilities and Shareholders' Equity</u></b>                 |                    |                   |
| <b>Current liabilities</b>                                         |                    |                   |
| Accounts payable                                                   | \$ 112,457         | \$ 97,248         |
| Accrued payroll and benefits                                       | 30,394             | 35,456            |
| Other accrued expenses                                             | 20,805             | 19,195            |
| Current portion of exit costs                                      | 10,234             | 9,759             |
| Current maturities of long-term debt and capital lease obligations | 3,883              | 3,932             |
|                                                                    |                    |                   |
| <b>Total current liabilities</b>                                   | 177,773            | 165,590           |
| <b>Long-term liabilities</b>                                       |                    |                   |
| Deferred income taxes                                              | 46,277             | 35,338            |
| Postretirement benefits                                            | 23,029             | 25,401            |
| Other long-term liabilities                                        | 18,521             | 20,876            |
| Exit costs                                                         | 30,408             | 34,786            |

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|                                                                                                    |                   |                   |
|----------------------------------------------------------------------------------------------------|-------------------|-------------------|
| Long-term debt and capital lease obligations                                                       | 199,921           | 194,115           |
| <b>Total long-term liabilities</b>                                                                 | <b>318,156</b>    | <b>310,516</b>    |
| <b>Commitments and contingencies (Note 6)</b>                                                      |                   |                   |
| <b>Shareholders' equity</b>                                                                        |                   |                   |
| Common stock, voting, no par value; 50,000 shares authorized; 22,453 and 22,213 shares outstanding | 157,360           | 153,778           |
| Preferred stock, no par value, 10,000 shares authorized; no shares outstanding                     | -                 | -                 |
| Accumulated other comprehensive loss                                                               | (13,984)          | (14,151)          |
| Retained earnings                                                                                  | 126,533           | 107,578           |
| <b>Total shareholders' equity</b>                                                                  | <b>269,909</b>    | <b>247,205</b>    |
| <b>Total liabilities and shareholders' equity</b>                                                  | <b>\$ 765,838</b> | <b>\$ 723,311</b> |

*See accompanying notes to condensed consolidated financial statements.*



**SPARTAN STORES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF EARNINGS**

(In thousands, except per share data)

(Unaudited)

|                                                                   | 16 Weeks Ended     |                    | 40 Weeks Ended     |                    |
|-------------------------------------------------------------------|--------------------|--------------------|--------------------|--------------------|
|                                                                   | January 2,<br>2010 | January 3,<br>2009 | January 2,<br>2010 | January 3,<br>2009 |
| <b>Net sales</b>                                                  | \$ 786,930         | \$ 781,949         | \$ 1,993,179       | \$ 1,995,484       |
| <b>Cost of sales</b>                                              | 621,439            | 624,509            | 1,560,661          | 1,594,996          |
| <b>Gross margin</b>                                               | 165,491            | 157,440            | 432,518            | 400,488            |
| <b>Operating expenses</b>                                         | 151,813            | 139,552            | 382,710            | 345,043            |
| <b>Operating earnings</b>                                         | 13,678             | 17,888             | 49,808             | 55,445             |
| <b>Other income and expenses</b>                                  |                    |                    |                    |                    |
| Interest expense                                                  | 5,188              | 4,190              | 12,578             | 10,461             |
| Other, net                                                        | (43)               | (142)              | (96)               | (351)              |
| <b>Total other income and expenses</b>                            | 5,145              | 4,048              | 12,482             | 10,110             |
| <b>Earnings before income taxes and discontinued operations</b>   | 8,533              | 13,840             | 37,326             | 45,335             |
| Income taxes                                                      | 3,272              | 5,754              | 14,724             | 18,502             |
| <b>Earnings from continuing operations</b>                        | 5,261              | 8,086              | 22,602             | 26,833             |
| <b>(Loss) earnings from discontinued operations, net of taxes</b> | (232)              | 229                | (280)              | 1,608              |
| <b>Net earnings</b>                                               | \$ 5,029           | \$ 8,315           | \$ 22,322          | \$ 28,441          |
| <b>Basic earnings per share:</b>                                  |                    |                    |                    |                    |
| Earnings from continuing operations                               | \$ 0.23            | \$ 0.37            | \$ 1.01            | \$ 1.22            |
| (Loss) earnings from discontinued operations                      | (0.01)             | 0.01               | (0.01)             | 0.07               |
| <b>Net earnings</b>                                               | \$ 0.22            | \$ 0.38            | \$ 1.00            | \$ 1.29            |
| <b>Diluted earnings per share:</b>                                |                    |                    |                    |                    |
| Earnings from continuing operations                               | \$ 0.23            | \$ 0.36            | \$ 1.01            | \$ 1.21            |
|                                                                   | (0.01)             | 0.01               | (0.02)*            | 0.07               |

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|                                              |         |         |         |         |
|----------------------------------------------|---------|---------|---------|---------|
| (Loss) earnings from discontinued operations |         |         |         |         |
| Net earnings                                 | \$ 0.22 | \$ 0.37 | \$ 0.99 | \$ 1.28 |

**Weighted average shares outstanding:**

|         |        |        |        |        |
|---------|--------|--------|--------|--------|
| Basic   | 22,436 | 22,130 | 22,393 | 22,075 |
| Diluted | 22,515 | 22,305 | 22,468 | 22,253 |

*\*Includes rounding*

*See accompanying notes to condensed consolidated financial statements.*

**SPARTAN STORES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY**

(In thousands)

(Unaudited)

|                                                                                 | Shares<br>Outstanding | Common<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Loss | Retained<br>Earnings | Total      |
|---------------------------------------------------------------------------------|-----------------------|-----------------|-----------------------------------------------|----------------------|------------|
| <b>Balance - March 29, 2009</b>                                                 | 22,213                | \$ 153,778      | \$ (14,151)                                   | \$ 107,578           | \$ 247,205 |
| <b>Comprehensive income, net of tax:</b>                                        |                       |                 |                                               |                      |            |
| Net earnings                                                                    | -                     | -               | -                                             | 22,322               | 22,322     |
| Change in fair value of interest rate<br>swap, net of taxes of \$107            |                       |                 | 167                                           |                      | 167        |
| <b>Total comprehensive income</b>                                               |                       |                 |                                               |                      | 22,489     |
| Dividends - \$.15 per share                                                     | -                     | -               | -                                             | (3,367)              | (3,367)    |
| Stock-based employee compensation                                               | -                     | 3,802           | -                                             | -                    | 3,802      |
| Issuances of common stock and related<br>tax benefits on stock option exercises | 27                    | 220             | -                                             | -                    | 220        |
| Issuances of restricted stock and<br>related income tax benefits                | 293                   | 489             | -                                             | -                    | 489        |
| Cancellations of restricted stock                                               | (80)                  | (929)           | -                                             | -                    | (929)      |
| <b>Balance - January 2, 2010</b>                                                | 22,453                | \$ 157,360      | \$ (13,984)                                   | \$ 126,533           | \$ 269,909 |

*See accompanying notes to condensed consolidated financial statements.*

**SPARTAN STORES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

(Unaudited)

|                                                                                     | <b>40 Weeks Ended</b>      |                            |
|-------------------------------------------------------------------------------------|----------------------------|----------------------------|
|                                                                                     | <b>January 2,<br/>2010</b> | <b>January 3,<br/>2009</b> |
| <b>Cash flows from operating activities</b>                                         |                            |                            |
| Net earnings                                                                        | \$ 22,322                  | \$ 28,441                  |
| Loss (earnings) from discontinued operations                                        | 280                        | (1,608)                    |
| Earnings from continuing operations                                                 | 22,602                     | 26,833                     |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |                            |                            |
| Provision for asset impairments and exit costs                                      | 1,316                      | -                          |
| Non-cash convertible debt interest                                                  | 2,686                      | 2,478                      |
| Depreciation and amortization                                                       | 26,908                     | 21,088                     |
| Postretirement benefits expense                                                     | 2,601                      | 1,023                      |
| Deferred taxes on income                                                            | 10,995                     | 17,754                     |
| Stock-based compensation expense                                                    | 3,797                      | 4,047                      |
| Excess tax benefit on stock compensation                                            | (328)                      | (1,924)                    |
| Other                                                                               | 126                        | 13                         |
| Change in operating assets and liabilities:                                         |                            |                            |
| Accounts receivable                                                                 | 16                         | 8,123                      |
| Inventories                                                                         | (21,907)                   | (14,469)                   |
| Prepaid expenses and other assets                                                   | 978                        | (1,312)                    |
| Accounts payable                                                                    | 16,601                     | 3,388                      |
| Accrued payroll and benefits                                                        | (5,181)                    | (2,968)                    |
| Postretirement benefits payments                                                    | (5,249)                    | (3,387)                    |
| Other accrued expenses and other liabilities                                        | (1,631)                    | (13,863)                   |
| <b>Net cash provided by operating activities</b>                                    | <b>54,330</b>              | <b>46,824</b>              |
| <b>Cash flows from investing activities</b>                                         |                            |                            |
| Purchases of property and equipment                                                 | (37,623)                   | (42,557)                   |
| Net proceeds from the sale of assets                                                | 108                        | 815                        |
| Acquisitions, net of cash acquired                                                  | (4,821)                    | (101,773)                  |
| Other                                                                               | (1,372)                    | 3                          |
| <b>Net cash used in investing activities</b>                                        | <b>(43,708)</b>            | <b>(143,512)</b>           |
| <b>Cash flows from financing activities</b>                                         |                            |                            |
| Net (payments on) proceeds from revolving credit facility                           | (1,504)                    | 85,485                     |
| Repayment of long-term borrowings                                                   | (3,067)                    | (10,326)                   |
| Excess tax benefit on stock compensation                                            | 328                        | 1,924                      |
| Proceeds from exercise of stock options                                             | 190                        | 844                        |
| Dividends paid                                                                      | (3,367)                    | (3,317)                    |

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|                                                               |          |          |
|---------------------------------------------------------------|----------|----------|
| <b>Net cash (used in) provided by financing activities</b>    | (7,420)  | 74,610   |
| <b>Cash flows from discontinued operations</b>                |          |          |
| Net cash used in operating activities                         | (2,559)  | (1,933)  |
| Net cash provided by investing activities                     | 18       | 13,794   |
| <b>Net cash (used in) provided by discontinued operations</b> | (2,541)  | 11,861   |
| <b>Net increase (decrease) in cash and cash equivalents</b>   | 661      | (10,217) |
| <b>Cash and cash equivalents at beginning of period</b>       | 6,519    | 19,867   |
| <b>Cash and cash equivalents at end of period</b>             | \$ 7,180 | \$ 9,650 |

*See accompanying notes to condensed consolidated financial statements.*

**SPARTAN STORES, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**Note 1**

**Basis of Presentation and Significant Accounting Policies**

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of Spartan Stores, Inc. and its subsidiaries ("Spartan Stores"). All significant intercompany accounts and transactions have been eliminated.

In the opinion of management, the accompanying condensed consolidated financial statements, taken as a whole, contain all adjustments, which are of a normal recurring nature, necessary to present fairly the financial position of Spartan Stores as of January 2, 2010 and the results of its operations and cash flows for the interim periods presented. Interim results are not necessarily indicative of results for a full year.

**Note 2**

**Changes in Accounting Principles**

*ASC Subtopic 470-20*

Effective March 29, 2009, Spartan Stores adopted the provisions of Accounting Standards Codification (ASC) Subtopic 470-20 ("ASC 470-20", originally issued as Financial Accounting Standards Board (FASB) Staff Position No. APB 14-1, "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)"), which changed the accounting treatment for convertible debt instruments that allow for either mandatory or optional cash settlements. Spartan Stores is required to recognize non-cash interest expense on its \$110 million convertible senior notes based on the market rate for similar debt instruments without the conversion feature. Convertible debt instruments are separated into their debt and equity components. The value assigned to the debt component is the estimated fair value, as of the issuance date, of a similar debt instrument without the conversion feature, and the difference between the proceeds from the issuance and the amount reflected as a debt liability is assigned to equity. As a result, the debt is effectively recorded at a discount reflecting its below market coupon interest rate. The debt is subsequently accreted to its par value over its expected life, with the rate of interest that reflects the market rate at issuance being reflected in the consolidated statements of earnings. Additionally, transaction costs incurred with third parties shall be allocated to and accounted for as debt issuance costs and equity issuance costs in proportion to the allocation of proceeds between the liability and equity component, respectively. Retrospective application to all periods presented is required.

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The following table sets forth the retrospective accounting impacts of the adoption of ASC 470-20 on the Consolidated Statement of Earnings for the quarter and year-to-date period ended January 3, 2009 and the Consolidated Balance Sheet as of March 28, 2009.

(In thousands, except per share amounts)

| <b>16 Weeks Ended January 3, 2009</b>      |                     |            |             |
|--------------------------------------------|---------------------|------------|-------------|
|                                            | As Reported         | Adjustment | As Adjusted |
| <b>Consolidated Statement of Earnings:</b> |                     |            |             |
| Interest expense                           | \$ 3,216            | \$ 974     | \$ 4,190    |
| Income taxes                               | 6,132               | (378)      | 5,754       |
| Earnings from continuing operations        | 8,682               | (596)      | 8,086       |
| Net earnings                               | 8,911               | (596)      | 8,315       |
| Basic earnings per share:                  |                     |            |             |
| Earnings from continuing operations        | 0.39 <sup>(1)</sup> | (0.02)     | 0.37        |
| Net earnings                               | 0.40 <sup>(1)</sup> | (0.02)     | 0.38        |
| Diluted earnings per share:                |                     |            |             |
| Earnings from continuing operations        | 0.39 <sup>(1)</sup> | (0.03)     | 0.36        |
| Net earnings                               | 0.40 <sup>(1)</sup> | (0.03)     | 0.37        |
| <b>40 Weeks Ended January 3, 2009</b>      |                     |            |             |
|                                            | As Reported         | Adjustment | As Adjusted |
| Interest expense                           | \$ 8,076            | \$ 2,385   | \$ 10,461   |
| Income taxes                               | 19,426              | (924)      | 18,502      |
| Earnings from continuing operations        | 28,294              | (1,461)    | 26,833      |
| Net earnings                               | 29,902              | (1,461)    | 28,441      |
| Basic earnings per share:                  |                     |            |             |
| Earnings from continuing operations        | 1.28 <sup>(1)</sup> | (0.06)     | 1.22        |
| Net earnings                               | 1.35 <sup>(1)</sup> | (0.06)     | 1.29        |
| Diluted earnings per share:                |                     |            |             |
| Earnings from continuing operations        | 1.27 <sup>(1)</sup> | (0.06)     | 1.21        |
| Net earnings                               | 1.34 <sup>(1)</sup> | (0.06)     | 1.28        |

<sup>(1)</sup> Amounts are after giving effect to the adoption of ASC 260 (see below)

(In thousands)

| <b>March 28, 2009</b>             |             |            |             |
|-----------------------------------|-------------|------------|-------------|
|                                   | As Reported | Adjustment | As Adjusted |
| <b>Consolidated Balance Sheet</b> |             |            |             |
| Other, net                        | \$ 53,264   | \$ (621)   | \$ 52,643   |
| Deferred income taxes             | 27,224      | 8,114      | 35,338      |

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|                            |         |          |         |
|----------------------------|---------|----------|---------|
| Long-term debt             | 215,686 | (21,571) | 194,115 |
| Common stock               | 137,358 | 16,420   | 153,778 |
| Retained earnings          | 111,162 | (3,584)  | 107,578 |
| Total shareholders' equity | 234,369 | 12,836   | 247,205 |

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The amount of interest expense recognized and the effective interest rate for Spartan Stores' convertible senior notes were as follows:

| (In thousands)                                       | 16 Weeks Ended     |                    | 40 Weeks Ended     |                    |
|------------------------------------------------------|--------------------|--------------------|--------------------|--------------------|
|                                                      | January 2,<br>2010 | January 3,<br>2009 | January 2,<br>2010 | January 3,<br>2009 |
| Contractual coupon interest                          | \$ 1,142           | \$ 1,142           | \$ 2,865           | \$ 2,865           |
| Amortization of discount on convertible senior notes | 1,094              | 1,011              | 2,686              | 2,478              |
| Interest expense                                     | \$ 2,236           | \$ 2,153           | \$ 5,551           | \$ 5,343           |
| Effective interest rate                              | 8.125%             | 8.125%             | 8.125%             | 8.125%             |

The debt and equity components recognized for Spartan Stores' convertible senior notes were as follows:

| (In thousands)                               | January 2,<br>2010    | March 28,<br>2009 |
|----------------------------------------------|-----------------------|-------------------|
| Principal amount of convertible senior notes | \$ 110,000            | \$ 110,000        |
| Unamortized discount                         | 18,885 <sup>(1)</sup> | 21,571            |
| Net carrying amount                          | 91,115                | 88,429            |
| Common stock                                 | 16,420                | 16,420            |

<sup>(1)</sup> Will be recognized over a remaining period of 4.4 years.

### ASC Topic 260

Effective March 29, 2009, Spartan Stores adopted the updated provisions of ASC Topic 260 (originally issued as FSP No. EITF 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities"). The updated provisions of ASC 260 clarify that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents are participating securities and must be included in the computation of basic earnings per share pursuant to the two-class method. The updated provisions of ASC 260 must be applied on a retrospective basis. Historically, Spartan Stores' unvested restricted shares have been included in the calculation of diluted earnings per share under the treasury stock method. These shares are now included in the computation of basic earnings per share. For the quarter ended January 3, 2009, basic and diluted earnings per share from continuing operations and net earnings were reduced by \$0.01. For the year-to-date period ended January 3, 2009, basic earnings per share from continuing operations and net earnings were reduced by \$0.04 and diluted earnings per share from continuing operations and net earnings were reduced by \$0.03.

The following table sets forth the computation of basic and diluted earnings per share for continuing operations and net earnings:

(In thousands, except per share amounts)

|                                                              | 16 Weeks Ended     |                 |            |             |
|--------------------------------------------------------------|--------------------|-----------------|------------|-------------|
|                                                              | January 2,<br>2010 | January 3, 2009 |            |             |
|                                                              |                    | As Reported     | Adjustment | As Adjusted |
| Numerator:                                                   |                    |                 |            |             |
| Earnings from continuing operations <sup>(1)</sup>           | \$ 5,261           | \$ 8,682        | \$ (596)   | \$ 8,086    |
| Denominator:                                                 |                    |                 |            |             |
| Weighted average shares outstanding - basic                  | 22,436             | 21,547          | 583        | 22,130      |
| Effect of dilutive options and restricted shares outstanding | 79                 | 314             | (139)      | 175         |
| Weighted average shares outstanding - diluted                | 22,515             | 21,861          | 444        | 22,305      |
| Basic earnings per share:                                    |                    |                 |            |             |
| Earnings from continuing operations                          | \$ 0.23            | \$ 0.40         | \$ (0.03)  | \$ 0.37     |
| Net earnings                                                 | 0.22               | 0.41            | (0.03)     | 0.38        |
| Diluted earnings per share:                                  |                    |                 |            |             |
| Earnings from continuing operations                          | \$ 0.23            | \$ 0.40         | \$ (0.04)  | \$ 0.36     |
| Net earnings                                                 | 0.22               | 0.41            | (0.04)     | 0.37        |

<sup>(1)</sup> Retrospective application of ASC 470-20 resulted in the recognition of additional non-cash interest expense for the quarter ended January 3, 2009. See above.

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(In thousands, except per share amounts)

|                                                              | 40 Weeks Ended     |                 |            |             |
|--------------------------------------------------------------|--------------------|-----------------|------------|-------------|
|                                                              | January 2,<br>2010 | January 3, 2009 |            |             |
|                                                              |                    | As Reported     | Adjustment | As Adjusted |
| Numerator:                                                   |                    |                 |            |             |
| Earnings from continuing operations <sup>(1)</sup>           | \$ 22,602          | \$ 28,294       | \$ (1,461) | \$ 26,833   |
| Denominator:                                                 |                    |                 |            |             |
| Weighted average shares outstanding - basic                  | 22,393             | 21,486          | 589        | 22,075      |
| Effect of dilutive options and restricted shares outstanding | 75                 | 311             | (133)      | 178         |
| Weighted average shares outstanding - diluted                | 22,468             | 21,797          | 456        | 22,253      |
| Basic earnings per share:                                    |                    |                 |            |             |
| Earnings from continuing operations                          | \$ 1.01            | \$ 1.32         | \$ (0.10)  | \$ 1.22     |
| Net earnings                                                 | 1.00               | 1.39            | (0.10)     | 1.29        |
| Diluted earnings per share:                                  |                    |                 |            |             |
| Earnings from continuing operations                          | \$ 1.01            | \$ 1.30         | \$ (0.09)  | \$ 1.21     |
| Net earnings                                                 | 0.99               | 1.37            | (0.09)     | 1.28        |

<sup>(1)</sup> Retrospective application of ASC 470-20 resulted in the recognition of additional non-cash interest expense for the quarter and year-to-date period ended January 3, 2009. See above.

Weighted average shares issuable upon the exercise of stock options that were not included in the earnings per share calculations because they were antidilutive were 537,985 and 250,270 for the quarters ended January 2, 2010 and January 3, 2009, respectively, and 532,091 and 321,480 for the year-to-date periods ended January 2, 2010 and January 3, 2009.

The senior subordinated convertible notes due 2027 will be convertible at the option of the holder, only upon the occurrence of certain events, at an initial conversion rate of 28.0310 shares of Spartan Stores common stock per \$1,000 principal amount at maturity of the notes (equal to an initial conversion price of approximately \$35.67 per share). Upon conversion, Spartan Stores will pay the holder the conversion value in cash up to the accreted principal amount of the note and the excess conversion value, if any, in shares of Spartan Stores common stock - unless Spartan Stores elects to satisfy its obligation under such conversion by delivering only shares of common stock. Therefore, the notes are not currently dilutive to earnings per share as they are only dilutive above the accreted value.

Restricted stock units granted in fiscal 2010 are only issuable if certain performance criteria are met, making these shares contingently issuable under ASC Topic 260. Therefore, the restricted stock units are included in diluted earnings per share at the expected payout percentage based on performance criteria results as of the end of the respective reporting period. Accordingly, the impact of 83,083 restricted stock units for the quarter and year-to-date period ended January 2, 2010 were excluded from the computation of diluted shares.



**Note 3****Asset Impairment and Exit Costs**

The following table provides the activity of exit costs for our Retail segment for the 40 weeks ended January 2, 2010. Exit costs recorded in the Consolidated Balance Sheets are included in "Current portion of exit costs" in Current liabilities and "Exit costs" in Long-term liabilities based on when the obligations are expected to be paid.

(In thousands)

|                                      |    |         |
|--------------------------------------|----|---------|
| Balance at March 29, 2009            | \$ | 44,545  |
| Exit costs related to store closings |    | 1,111   |
| Changes in estimates                 |    | (100)   |
| Payments, net of interest accretion  |    | (4,914) |
|                                      |    | <hr/>   |
| Balance at January 2, 2010           | \$ | 40,642  |
|                                      |    | <hr/>   |

Asset impairments of \$0.2 million and exit costs of \$1.1 million were recognized related to the closing of two stores for store lease obligations and severance. The store lease obligations include the present value of future minimum lease payments, calculated using a risk-free interest rate, and related ancillary costs from the date of closure to the end of the remaining lease term, net of estimated sublease income.

**Note 4****Fair Value Measurements**

Financial instruments include cash and cash equivalents, accounts and notes receivable, accounts payable and long-term debt. The carrying amounts of cash and cash equivalents, accounts and notes receivable, and accounts payable approximate fair value because of the short-term nature of these financial instruments. At January 2, 2010 and March 28, 2009 the estimated fair value and the book value of our debt instruments were as follows:

(In thousands)

|                                                                    | <b>January 2,<br/>2010</b> | <b>March 28,<br/>2009</b> |
|--------------------------------------------------------------------|----------------------------|---------------------------|
|                                                                    | <hr/>                      | <hr/>                     |
| Book value of debt instruments:                                    |                            |                           |
| Current maturities of long-term debt and capital lease obligations | \$ 3,883                   | \$ 3,932                  |
| Long-term debt and capital lease obligations                       | 199,921                    | 194,115                   |
| Equity component of convertible debt                               | 18,885                     | 21,571                    |
|                                                                    | <hr/>                      | <hr/>                     |
| Total book value of debt instruments                               | 222,689                    | 219,618                   |
| Fair value of debt instruments                                     | 197,969                    | 184,110                   |
|                                                                    | <hr/>                      | <hr/>                     |
| Excess of book value over fair value                               | \$ 24,720                  | \$ 35,508                 |
|                                                                    | <hr/>                      | <hr/>                     |

The estimated fair value of debt is based on market quotes for instruments with similar terms and remaining maturities.

In September 2006, the FASB issued ASC Topic 820 ("ASC 820", originally issued as SFAS No. 157, "Fair Value Measurements"). ASC 820 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosures about fair value measurements. This statement does not

require any new fair value measurements, but applies under other accounting pronouncements that require or permit fair value measurements. Effective March 30, 2008, Spartan Stores adopted the provisions of ASC 820 related to financial assets and liabilities recognized or disclosed on a recurring basis. Additionally, on March 29, 2009, Spartan Stores began applying the principles of ASC 820 to non-financial assets and liabilities. Adoption of ASC 820 had no impact on the consolidated financial statements.

ASC 820 prioritizes the inputs to valuation techniques used to measure fair value into the following hierarchy:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.  
 Level 3: Unobservable inputs for the asset or liability, reflecting the reporting entity's own assumptions about the assumptions that market participants would use in pricing.

At January 2, 2010 and March 28, 2009, the fair value of the interest rate swap liability was approximately \$0.2 million and \$0.5 million, respectively, and is included in other long-term liabilities in the accompanying consolidated balance sheets. The fair value measurements are classified within Level 2 of the hierarchy as significant observable market inputs are readily available as the basis of the fair value measurements.

## Note 5

### Derivative Instruments

Spartan Stores has limited involvement with derivative financial instruments and uses them only to manage well-defined interest rate risk exposure when appropriate, based on market conditions. Spartan Stores' objective in managing exposure to changes in interest rates is to reduce fluctuations in earnings and cash flows, and consequently, from time to time Spartan Stores uses interest rate swap agreements to manage this risk. Spartan Stores does not use financial instruments or derivatives for any trading or other speculative purposes.

On January 2, 2009, Spartan Stores entered into an interest rate swap agreement. The interest rate swap has been designated as a cash flow hedge of interest payments on \$45.0 million of borrowings under Spartan Stores' senior secured revolving credit facility by effectively converting a portion of the variable rate debt to a fixed rate basis. Under the terms of the agreement, Spartan Stores has agreed to pay the counterparty a fixed interest rate of 3.33 percent and the counterparty has agreed to pay Spartan Stores a floating interest rate based upon the 1-month LIBOR plus 1.25 percent (1.48 percent at January 2, 2010) on a notional amount of \$45 million. The interest rate swap agreement expires concurrently with the senior secured revolving credit facility on December 24, 2012.

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period during which the hedged transaction affects earnings. Gains and losses on the derivative representing hedge ineffectiveness are recognized in current earnings.

The following table provides a summary of the fair value and balance sheet classification of the derivative financial instrument designated as an interest rate cash flow hedge:

| Balance Sheet Classification | January 2,<br>2010 | March 28,<br>2009 |
|------------------------------|--------------------|-------------------|
| Other long-term liabilities  | \$ 188             | \$ 462            |

The following table provides a summary of the financial statement effect of the derivative financial instrument designated as an interest rate cash flow hedge for the quarter and year-to-date period ended January 2, 2010:

|                                                                | <u>Location in Consolidated Financial<br/>Statements</u> | <u>16 Weeks Ended<br/>January 2,<br/>2010</u> | <u>40 Weeks Ended<br/>January 2,<br/>2010</u> |
|----------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------|-----------------------------------------------|
| Gain, net of taxes, recognized in other comprehensive income   | Other comprehensive income                               | \$ 105                                        | \$ 167                                        |
| Pre-tax loss reclassified from accumulated other comprehensive | Interest expense                                         | (237)                                         | (606)                                         |

loss

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**Note 6****Commitments and Contingencies**

Various lawsuits and claims, arising in the ordinary course of business, are pending or have been asserted against Spartan Stores. While the ultimate effect of such actions cannot be predicted with certainty, management believes that their outcome will not result in a material adverse effect on the consolidated financial position, operating results or liquidity of Spartan Stores.

**Note 7****Associate Retirement Plans**

The following table provides the components of net periodic pension and postretirement benefit costs for the third quarter and year-to-date periods ended January 2, 2010 and January 3, 2009:

(In thousands)

| <b>16 Weeks Ended</b>              | Pension Benefits |                 | SERP Benefits   |                 | Postretirement Benefits |                 |
|------------------------------------|------------------|-----------------|-----------------|-----------------|-------------------------|-----------------|
|                                    | Jan. 2,<br>2010  | Jan. 3,<br>2009 | Jan. 2,<br>2010 | Jan. 3,<br>2009 | Jan. 2,<br>2010         | Jan. 3,<br>2009 |
| Service cost                       | \$ 908           | \$ 665          | \$ 25           | \$ 13           | \$ 41                   | \$ 42           |
| Interest cost                      | 1,109            | 797             | 18              | 11              | 135                     | 93              |
| Expected return on plan assets     | (1,252)          | (1,082)         | -               | -               | -                       | -               |
| Amortization of prior service cost | (196)            | (173)           | -               | -               | (16)                    | (13)            |
| Recognized actuarial net loss      | 202              | 87              | 13              | 9               | 6                       | -               |
| Net periodic benefit cost          | <u>\$ 771</u>    | <u>\$ 294</u>   | <u>\$ 56</u>    | <u>\$ 33</u>    | <u>\$ 166</u>           | <u>\$ 122</u>   |

(In thousands)

| <b>40 Weeks Ended</b>              | Pension Benefits |                 | SERP Benefits   |                 | Postretirement Benefits |                 |
|------------------------------------|------------------|-----------------|-----------------|-----------------|-------------------------|-----------------|
|                                    | Jan. 2,<br>2010  | Jan. 3,<br>2009 | Jan. 2,<br>2010 | Jan. 3,<br>2009 | Jan. 2,<br>2010         | Jan. 3,<br>2009 |
| Service cost                       | \$ 2,269         | \$ 1,995        | \$ 63           | \$ 39           | \$ 102                  | \$ 126          |
| Interest cost                      | 2,773            | 2,392           | 44              | 33              | 338                     | 278             |
| Expected return on plan assets     | (3,130)          | (3,247)         | -               | -               | -                       | -               |
| Amortization of prior service cost | (490)            | (518)           | -               | (1)             | (41)                    | (40)            |
| Recognized actuarial net loss      | 506              | 260             | 33              | 27              | 16                      | -               |
| Net periodic benefit cost          | <u>\$ 1,928</u>  | <u>\$ 882</u>   | <u>\$ 140</u>   | <u>\$ 98</u>    | <u>\$ 415</u>           | <u>\$ 364</u>   |

No payments are required to be made in fiscal 2010 to meet the minimum funding requirements; however, Spartan Stores made a voluntary contribution of \$5.2 million in the third quarter to move the plan closer to a fully funded status and reduce future pension expense.

**Note 8**

**Taxes on Income**

As of January 2, 2010, there have been no material changes to the amount of unrecognized tax benefits. Spartan Stores does not anticipate that total unrecognized tax benefits will significantly change prior to January 1, 2011.

The effective income tax rate is higher than the statutory Federal income tax rate primarily due to state income taxes.

**Note 9**

**Stock-Based Compensation**

Spartan Stores has two shareholder-approved stock incentive plans that provide for the granting of incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units, stock awards, and other stock-based awards to directors, officers and other key associates.

Spartan Stores accounts for stock-based compensation awards in accordance with the provisions of ASC Topic 718 ("ASC 718", originally issued as SFAS No. 123(R), "Share-Based Payment - Revised") which requires that share-based payment transactions be accounted for using a fair value method and the related compensation cost recognized in the consolidated financial statements over the period that an employee is required to provide services in exchange for the award. Spartan Stores recognized stock-based compensation expense (net of tax) of \$0.9 million (\$0.04 per diluted share) and \$0.8 million (\$0.04 per diluted share) in the third quarter of fiscal 2010 and 2009, respectively, as a component of Selling, general and administrative expenses in the Consolidated Statements of Earnings. Stock-based compensation expense (net of tax) was \$2.3 million (\$0.10 per diluted share) and \$2.4 million (\$0.11 per diluted share) for the year-to-date period ended January 2, 2010 and January 3, 2009, respectively.

Historically, awards have been granted in the form of stock options and restricted stock. In fiscal 2010, Spartan Stores also granted restricted stock units ("RSU's") to certain executive employees of the Company. The RSU's have a service condition and a performance condition that must be met in order for the awards to vest. Depending on whether the Company achieves specified threshold, target, or maximum levels of earnings per share as defined in the award documents, an employee could receive a number of shares of Spartan Stores common stock ranging from zero to 200 percent of the number of RSU's granted. Any shares received upon conversion are subject to a cliff vesting period ending on the third anniversary of the grant date as designated in the award documents. Compensation expense is recognized over the service vesting period if and when the Company concludes it is probable that the performance vesting condition will be satisfied. If the performance condition is not satisfied, then no compensation cost is recorded and any compensation cost previously recognized will be reversed.

The following table summarizes activity in the share-based compensation plans for the year-to-date period ended January 2, 2010:

|                                                                     | Shares<br>Under<br>Options | Weighted<br>Average<br>Exercise Price | Restricted<br>Stock<br>Awards | Weighted<br>Average<br>Grant-Date<br>Fair Value |
|---------------------------------------------------------------------|----------------------------|---------------------------------------|-------------------------------|-------------------------------------------------|
| <b>Outstanding at March 29, 2009</b>                                | 706,367                    | \$ 17.99                              | 590,693                       | \$ 19.12                                        |
| Granted                                                             | 179,382                    | 13.87                                 | 333,746                       | 13.88                                           |
| Exercised/Vested                                                    | (26,744)                   | 7.11                                  | (202,429)                     | 15.67                                           |
| Cancelled/Forfeited                                                 | (25,437)                   | 20.70                                 | (19,047)                      | 18.91                                           |
| <b>Outstanding at January 2, 2010</b>                               | <b>833,568</b>             | <b>\$ 17.37</b>                       | <b>702,963</b>                | <b>\$ 17.59</b>                                 |
| <b>Vested and expected to vest in the future at January 2, 2010</b> | <b>813,668</b>             | <b>\$ 17.33</b>                       |                               |                                                 |
| <b>Exercisable at January 2, 2010</b>                               | <b>367,541</b>             | <b>\$ 15.11</b>                       |                               |                                                 |

The weighted average grant-date fair value of stock options granted during the third quarter ended January 3, 2009 was \$9.35. No stock options were granted during the third quarter ended January 2, 2010. The weighted average grant-date fair value of stock options granted during the year-to-date period ended January 2, 2010 and January 3, 2009 was \$5.26 and \$8.92, respectively. The fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The following weighted average assumptions were used to estimate the

fair value of stock options at the date of grant using the Black-Scholes option-pricing model:

|                         | 40 Weeks Ended     |                    |
|-------------------------|--------------------|--------------------|
|                         | January 2,<br>2010 | January 3,<br>2009 |
| Dividend yield          | 1.43%              | 0.86% - 0.88%      |
| Expected volatility     | 41.50% - 42.30%    | 37.55% - 38.56%    |
| Risk-free interest rate | 2.28% - 2.92%      | 3.16% - 3.28%      |
| Expected life of option | 6.25 years         | 6.25 years         |

Due to certain events that are considered unusual and/or infrequent in nature, and that resulted in significant business changes during the limited historical exercise period, management does not believe that Spartan Stores' historical exercise data will provide a reasonable basis upon which to estimate the expected term of stock options. Therefore, the expected term of stock options granted is determined using the "simplified" method as described in SEC Staff Accounting Bulletins that uses the following formula: ((vesting term + original contract term)/2).

As of January 2, 2010, total unrecognized compensation cost related to nonvested share-based awards granted under our stock incentive plans was \$1.8 million for stock options and \$9.9 million for restricted stock/units. The remaining compensation costs not yet recognized are expected to be recognized over a weighted average period of 2.4 years for stock options and 3.1 years for restricted stock/units.

## Note 10

### Discontinued Operations

In the first and second quarters of fiscal 2009, Spartan Stores completed the closure and disposition of the prescription files of the 14 remaining *The Pharm* stores, allowing Spartan Stores to concentrate efforts and resources on business opportunities with the best long-term growth potential and focus more on core distribution and conventional supermarket operations. Total net cash proceeds of \$13.8 million were received during the prior year-to-date period. Asset impairment charges and exit costs of \$6.4 million were also recognized in the prior year-to-date period. The results of operations of these stores have been classified as discontinued operations in the consolidated financial statements for all periods presented.

Results of the discontinued operations are excluded from the accompanying notes to the consolidated financial statements for all periods presented, unless otherwise noted.

The following table details the results of discontinued operations reported on the Consolidated Statements of Earnings:

(In thousands)

|                                                                                  | 16 Weeks Ended     |                    |
|----------------------------------------------------------------------------------|--------------------|--------------------|
|                                                                                  | January 2,<br>2010 | January 3,<br>2009 |
| (Loss) earnings from discontinued operations (net of taxes of (\$158) and \$148) | \$ (232)           | \$ 157             |
| Gain on disposal of discontinued operations (net of taxes of \$67)               | -                  | 72                 |
| Total (loss) earnings from discontinued operations                               | \$ (232)           | \$ 229             |

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(In thousands)

|                                                                           | 40 Weeks Ended     |                    |
|---------------------------------------------------------------------------|--------------------|--------------------|
|                                                                           | January 2,<br>2010 | January 3,<br>2009 |
| Loss from discontinued operations (net of taxes of (\$195) and (\$4,665)) | \$ (280)           | \$ (6,138)         |
| Gain on disposal of discontinued operations (net of taxes of \$5,887)     | -                  | 7,746              |
| Total (loss) earnings from discontinued operations                        | \$ (280)           | \$ 1,608           |

**Note 11****Supplemental Cash Flow Information**

Non-cash financing activities include the issuance of restricted stock/units to employees and directors of \$4.6 million and \$5.0 million for the year-to-date periods ended January 2, 2010 and January 3, 2009, respectively. Non-cash investing activities include capital expenditures included in other accrued expenses of \$2.0 million and \$2.8 million for the year-to-date periods ended January 2, 2010 and January 3, 2009, respectively, and capital lease obligations of \$7.6 million and \$0.3 million for the year-to-date periods ended January 2, 2010 and January 3, 2009.

**Note 12****Operating Segment Information**

The following tables set forth information about Spartan Stores by operating segment:

(In thousands)

|                                       | Distribution       | Retail            | Total        |
|---------------------------------------|--------------------|-------------------|--------------|
| <b>16 Weeks Ended January 2, 2010</b> |                    |                   |              |
| Net sales                             | \$ 343,554         | \$ 443,376        | \$ 786,930   |
| Inter-segment sales                   | 215,264            |                   | 215,264      |
| Depreciation and amortization         | 2,506              | 8,022             | 10,528       |
| Operating earnings                    | 11,745             | 1,933             | 13,678       |
| Capital expenditures                  | 2,447              | 12,469            | 14,916       |
| <b>16 Weeks Ended January 3, 2009</b> |                    |                   |              |
| Net sales                             | \$ 397,947         | \$ 384,002        | \$ 781,949   |
| Inter-segment sales                   | 196,313            |                   | 196,313      |
| Depreciation and amortization         | 2,528              | 5,852             | 8,380        |
| Operating earnings                    | 11,065             | 6,823             | 17,888       |
| Capital expenditures                  | 4,814              | 12,866            | 17,680       |
| <b>40 Weeks Ended January 2, 2010</b> |                    |                   |              |
| Net sales                             | \$ 846,948         | \$ 1,146,231      | \$ 1,993,179 |
| Inter-segment sales                   | 542,310            |                   | 542,310      |
| Depreciation and amortization         | 6,710              | 19,968            | 26,678       |
| Operating earnings                    | 30,122             | 19,686            | 49,808       |
| Capital expenditures                  | 6,558              | 31,065            | 37,623       |
| <b>40 Weeks Ended January 3, 2009</b> |                    |                   |              |
| Net sales                             | \$ 999,393         | \$ 996,091        | \$ 1,995,484 |
| Inter-segment sales                   | 476,523            |                   | 476,523      |
| Depreciation and amortization         | 6,150              | 14,315            | 20,465       |
| Operating earnings                    | 28,550             | 26,895            | 55,445       |
| Capital expenditures                  | 9,861              | 32,696            | 42,557       |
|                                       | January 2,<br>2010 | March 28,<br>2009 |              |

**Total assets**

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|                         |    |                   |    |                   |
|-------------------------|----|-------------------|----|-------------------|
| Distribution            | \$ | 241,228           | \$ | 233,450           |
| Retail                  |    | 518,926           |    | 484,029           |
| Discontinued operations |    | 5,684             |    | 5,832             |
|                         |    | <u>          </u> |    | <u>          </u> |
| Total                   | \$ | 765,838           | \$ | 723,311           |
|                         |    | <u>          </u> |    | <u>          </u> |

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The following table presents sales by type of similar product and services:

|                                | 16 Weeks Ended  |         |      |                 |         | 40 Weeks Ended  |    |           |                 |    |           |      |
|--------------------------------|-----------------|---------|------|-----------------|---------|-----------------|----|-----------|-----------------|----|-----------|------|
| (Dollars in thousands)         | January 2, 2010 |         |      | January 3, 2009 |         | January 2, 2010 |    |           | January 3, 2009 |    |           |      |
| Non-perishables <sup>(1)</sup> | \$              | 429,211 | 54%  | \$              | 421,543 | 54%             | \$ | 1,072,783 | 54%             | \$ | 1,052,793 | 53%  |
| Perishables <sup>(2)</sup>     |                 | 266,443 | 34   |                 | 277,445 | 36              |    | 700,732   | 35              |    | 706,010   | 35   |
| Pharmacy                       |                 | 60,510  | 8    |                 | 57,501  | 7               |    | 148,679   | 7               |    | 153,592   | 8    |
| Fuel                           |                 | 30,766  | 4    |                 | 25,460  | 3               |    | 70,985    | 4               |    | 83,089    | 4    |
| Consolidated net sales         | \$              | 786,930 | 100% | \$              | 781,949 | 100%            | \$ | 1,993,179 | 100%            | \$ | 1,995,484 | 100% |

<sup>(1)</sup> Consists primarily of general merchandise, grocery, beverages, snacks and frozen foods.

<sup>(2)</sup> Consists primarily of produce, dairy, meat, bakery, deli, floral and seafood.

### Note 13

#### Subsequent Events

At the beginning of the fourth quarter of fiscal 2010, Spartan Stores began implementing the conclusions of a comprehensive, multi-year supply chain optimization study. Spartan Stores reached an agreement with the Teamsters Local 337 to transition its Plymouth, Michigan dry grocery distribution operation to its Grand Rapids, Michigan facility. The transition is expected to be substantially complete by the end of the fourth quarter of fiscal 2010. Also, in the fourth quarter of fiscal 2010, we implemented an administrative cost reduction initiative by eliminating certain positions. As a result of the closing and optimization of the warehouse facility, in addition to administrative cost reduction and real estate initiatives, we expect to incur a fiscal 2010 fourth quarter net after tax charge of approximately \$2.5 million for severance and other related one-time costs. We also expect to incur a fiscal 2011 first quarter after tax benefit of approximately \$0.2 million to \$0.6 million for a favorable LIFO inventory benefit due to inventory reductions, net of lease termination and additional distribution center closing costs that are anticipated to occur during the quarter. Excluding the previously mentioned charges, annualized after tax cost savings from these initiatives are expected to range from approximately \$2.0 million to \$3.0 million.

Events or transactions occurring after the balance sheet date have been evaluated through February 4, 2010, the date the financial statements were issued. The financial statements do not reflect events or transactions after this date.

**ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
**Executive Overview**

Spartan Stores is a leading regional grocery distributor and grocery retailer, operating principally in Michigan and Indiana.

We operate two reportable business segments: Distribution and Retail. Our Distribution segment provides a full line of grocery, general merchandise, health and beauty care, frozen and perishable items to approximately 350 independently owned grocery stores and our 96 corporate owned stores. Our Retail segment operates 96 retail supermarkets in Michigan under the banners *Glen's Markets*, *Family Fare Supermarkets*, *D&W Fresh Markets*, *Felpausch Food Centers* and *VG's Food and Pharmacy* and 24 fuel centers/convenience stores, included at our supermarket locations, under the banners *Glen's Quick Stop*, *Family Fare Quick Stop*, *D&W Fresh Markets Quick Stop*, *Felpausch Quick Stop* and *VG's Quick Stop*. Our retail supermarkets have a "neighborhood market" focus to distinguish them from supercenters and limited assortment stores.

Our sales and operating performance vary with seasonality. Our first and fourth quarters are typically our lowest sales quarters and therefore operating results are generally lower during these two quarters. Additionally, these two quarters can be affected by the timing of the Easter holiday, which results in a strong sales week. Many northern Michigan stores are dependent on tourism, which is affected by the economic environment and seasonal weather patterns, including, but not limited to, the amount and timing of snowfall during the winter months and the range of temperature during the summer months. All quarters are 12 weeks, except for our third quarter, which is 16 weeks and includes the Thanksgiving and Christmas holidays.

At the beginning of the fourth quarter of fiscal 2010, we began implementing the conclusions of a comprehensive, multi-year supply chain optimization study. This is another important step in our ongoing strategy of maintaining a low cost grocery distribution operation. We reached an agreement with the Teamsters Local 337 to transition our Plymouth, Michigan dry grocery distribution operation to our Grand Rapids, Michigan facility. We expect the transition to be substantially complete by the end of the fourth quarter of fiscal 2010. During the past several years, we have prudently invested capital to upgrade our distribution system technology, expand our produce ripening operations, upgrade our entire fleet of trucks, and completed a major warehouse re-racking project at our Grand Rapids grocery distribution center that significantly increased warehouse capacity and improved space utilization. In addition to improved customer service through a centralized Grand Rapids facility, this decision along with our other cost reduction initiatives will also ensure better alignment between the current level of business activity and our cost structure. In conjunction with the warehouse optimization, we implemented another administrative cost reduction initiative by eliminating certain positions. As a result of the closing and optimization of the warehouse facility, in addition to administrative and real estate initiatives, we expect to incur a fiscal 2010 fourth quarter net after tax charge of approximately \$2.5 million for severance and other related one-time costs. We also expect to incur a fiscal 2011 first quarter after tax benefit of approximately \$0.2 million to \$0.6 million for a favorable LIFO inventory benefit due to inventory reductions, net of lease termination and additional distribution center closing costs that are anticipated to occur during the quarter. Excluding the previously mentioned charges, annualized after tax cost savings from these initiatives are expected to range from approximately \$2.0 million to \$3.0 million.

We continued the integration of the *VG's* retail store acquisition. We are using the additional insight gained during the integration process to further refine our product offerings and services in all of our markets to address the current challenging economic environment.

We launched three retail programs in fiscal 2010 that are intended to enhance the value delivered to consumers. As part of our emphasis on consumer health and wellness, we began a major nutrition guide program in our *D&W* and *Family Fare* retail stores early in the third quarter. Although consumers are looking for good value, our research

indicates that they also want to eat healthy foods. Our program introduces new shelf tags that clearly and simply identify the health and nutrition benefits on approximately 16,000 products. The labels are color coded by FDA category, and we believe are easy to understand, simple to follow and help consumers to quickly identify the

health and nutrition attributes of the food they buy. We also launched our Michigan's Best initiative which clearly identifies and promotes 2,400 products grown, made or processed in Michigan. Consumers in our market have a strong desire to support their state. In addition, we implemented our new rewards-based customer loyalty program at our *Glen's* stores late in the first quarter. We believe that the new customer loyalty program is providing a better and more sophisticated understanding of our customers' purchasing behavior, which we will use to improve the effectiveness of our promotions, marketing and merchandising programs. We also expect the program will help solidify our long-term customer loyalty, improve our sales growth opportunities and further strengthen our market position.

We continued the execution of our capital investment program by completing one store relocation, completing five major store remodels and opening five new fuel centers.

We expect the economic climate in markets where we operate to weaken slightly, but begin to moderate in fiscal 2011. We also expect the impact of the competitive environment to begin to improve as we fully cycle the new store openings in our markets. We also anticipate that the rate of product price deflation will begin to temper during fiscal 2011. We will continue to make tactical adjustments to our marketing, merchandising and pricing strategies to make them more effective in this economic environment. We will also remain focused on completing the integration of our *VG's* acquisition and continuing with our targeted capital investment program. We believe these steps will position our company to benefit when the economy recovers.

## Results of Operations

The following table sets forth items from our Consolidated Statements of Earnings as a percentage of net sales and the year-to-year percentage change in dollar amounts:

(Unaudited)

|                                                               | Percentage of Net Sales |                 |                 |                 | Percentage Change |                 |
|---------------------------------------------------------------|-------------------------|-----------------|-----------------|-----------------|-------------------|-----------------|
|                                                               | 16 Weeks Ended          |                 | 40 Weeks Ended  |                 | 16 Weeks Ended    | 40 Weeks Ended  |
|                                                               | Jan. 2,<br>2010         | Jan. 3,<br>2009 | Jan. 2,<br>2010 | Jan. 3,<br>2009 | Jan. 2,<br>2010   | Jan. 2,<br>2010 |
| Net sales                                                     | 100.0                   | 100.0           | 100.0           | 100.0           | 0.6               | (0.1)           |
| Gross margin                                                  | 21.0                    | 20.1            | 21.7            | 20.1            | 5.1               | 8.0             |
| Operating expenses                                            | 19.3                    | 17.8            | 19.2            | 17.3            | 8.8               | 10.9            |
| Operating earnings                                            | 1.7                     | 2.3             | 2.5             | 2.8             | (23.5)            | (10.2)          |
| Other income and expenses                                     | 0.7                     | 0.5             | 0.6             | 0.6             | 27.1              | 23.5            |
| Earnings before income taxes<br>and discontinued operations   | 1.0                     | 1.8             | 1.9             | 2.2             | (38.3)            | (17.7)          |
| Income taxes                                                  | 0.4                     | 0.7             | 0.8             | 0.9             | (43.1)            | (20.4)          |
| Earnings from continuing<br>operations                        | 0.6                     | 1.1             | 1.1             | 1.3             | (34.9)            | (15.8)          |
| (Loss) earnings from discontinued<br>operations, net of taxes | 0.0                     | 0.0             | 0.0             | 0.1             | *                 | *               |
| Net earnings                                                  | 0.6                     | 1.1             | 1.1             | 1.4             | (39.5)            | (21.5)          |

\* Percentage change is not meaningful

**Net Sales** - Net sales for the quarter ended January 2, 2010 ("third quarter") increased \$5.0 million, or 0.6 percent, from \$781.9 million in the quarter ended January 3, 2009 ("prior year third quarter") to \$786.9 million. Net sales for the year-to-date period ended January 2, 2010 ("current year-to-date") decreased \$2.3 million, or 0.1 percent, from \$1,995.5 million in the prior year-to-date period ended January 3, 2009 ("prior year-to-date") to \$1,993.2 million.

Net sales for the third quarter in our Retail segment increased \$59.4 million, or 15.5 percent, from \$384.0 million in the prior year third quarter to \$443.4 million. Net sales for the year-to-date period increased \$150.1 million, or 15.1 percent, from \$996.1 million in the prior year-to-date period to \$1,146.2 million. The third quarter increase was primarily due to incremental sales from the recently acquired VG's retail stores of \$77.2 million and an increase in fuel center sales of \$6.4 million due to an increase in the retail pump prices and in the number of fuel centers operated, partially offset by a 6.0% decrease in supermarket comparable sales and \$6.4 million of lost sales relating to three closed stores and one sold store. The year-to-date increase was primarily due to incremental sales from the recently acquired VG's retail stores of \$210.2 million, partially offset by a decrease in supermarket comparable sales of \$37.6 million, lost sales of \$13.3 million relating to four closed stores, one temporarily closed store undergoing a major remodel and one sold store. A decrease in fuel center sales of \$9.7 million due to a decrease in the retail pump prices, partially offset by an increase in the number of fuel centers, also impacted year-to-date sales.

The majority of the comparable store sales decrease was a result of cautious consumer spending due to Michigan's current economic state, retail price deflation and competitive activity. We define a retail store as comparable when it is in operation for 14 accounting periods (a period equals four weeks), and we include remodeled, expanded and relocated stores in comparable stores.

Net sales for the third quarter in our Distribution segment decreased \$54.4 million, or 13.7 percent, from \$397.9 million in the prior year third quarter to \$343.6 million. Net sales for the current year-to-date period decreased \$152.5 million, or 15.3 percent, from \$999.4 million in the prior year-to-date period to \$846.9 million. The third quarter decrease was due to the elimination of sales to VG's stores of \$44.2 million (due to our acquisition of the stores) and a net decrease of \$10.2 million in sales driven by product price deflation and the current economic environment, partially offset by the addition of new distribution business. The year-to-date decrease was due to the elimination of sales to VG's stores of \$110.8 million (due to our acquisitions of the stores), a net decrease of \$41.7 million in sales to existing customers and lower sales in our pharmacy distribution program, partially offset by the addition of new distribution business.

We expect that the retail industry will continue to be pressured by the current environment. As a result, we expect retail comparable sales, excluding fuel, to approximate negative eight percent for the fourth quarter of fiscal 2010 due primarily to the continued difficult economic and competitive environment, the inclusion of our recently acquired stores into comparable store sales and the cycling of the prior year's highly successful grand opening of a relocated store. We expect comparable store sales to begin improving in early fiscal 2011. We also expect distribution sales, excluding the effect of the VG's acquisition, to decline at a rate slightly above the third quarter decline.

**Gross Margin** - Gross margin represents sales less cost of sales, which include purchase costs and promotional allowances. Vendor allowances that relate to our buying and merchandising activities consist primarily of promotional allowances, which are generally allowances on purchased quantities and, to a lesser extent, slotting allowances, which are billed to vendors for our merchandising costs, such as setting up warehouse infrastructure. Vendor allowances associated with product cost are recognized as a reduction in cost of sales when the product is sold. Lump sum payments received for multi-year contracts are amortized over the life of the contracts based on contractual terms.

Gross margin for the third quarter increased \$8.1 million, or 5.1 percent, from \$157.4 million in the prior year third quarter to \$165.5 million. As a percent of net sales, gross margin for the third quarter increased to 21.0 percent from 20.1 percent. Gross margin for the year-to-date period increased \$32.0 million, or 8.0 percent, from \$400.5 million in the prior year-to-date period to \$432.5 million. As a percent of net sales, gross margin for the year-to-date period increased to 21.7 percent from 20.1 percent. The improved gross margin rate was due principally to an increase in the mix of higher margin retail sales as a percentage of consolidated sales compared with the prior year resulting from the acquisition of VG's.

***Operating Expenses*** - Operating expenses consist primarily of salaries and wages, employee benefits, warehousing costs, store occupancy costs, utilities, equipment rental, depreciation, asset impairment and exit costs and other administrative costs.

Operating expenses for the third quarter increased \$12.3 million, or 8.8 percent, from \$139.6 million in the prior year third quarter to \$151.8 million. As a percent of net sales, operating expenses were 19.3 percent for the third quarter compared to 17.8 percent in the prior year third quarter. Operating expenses for the year-to-date period increased \$37.7 million, or 10.9 percent, from \$345.0 million in the prior year-to-date period to \$382.7 million. As a percent of net sales, operating expenses were 19.2 percent in the current year-to-date period compared to 17.3 percent in the prior year-to-date period.

The net increase in third quarter operating expenses was primarily due to the following:

- Added operating costs associated with the acquired VG's retail stores of \$19.4 million.
- Asset impairment and exit costs of \$0.7 million related to two store closures.
- Added operating costs of \$0.7 million associated with new fuel centers.
- Decreased compensation and benefits of \$3.5 million due to reductions in store labor, incentive compensation and other cost containment initiatives.
- Reduced operating costs related to the closure three stores and sale of one store of \$1.7 million.
- Decreased supplies of \$0.8 million.
- Decreases in various other expenses due to a general focus on containing costs.

The net increase in year-to-date operating expenses was primarily due to the following:

- Added operating costs associated with the acquired VG's retail stores of \$51.8 million.
- Asset impairment and exit costs of \$1.3 million related to three store closures.
- Costs related to the introduction of a new customer loyalty program of \$0.6 million.
- Decreased compensation and benefits of \$5.9 million due to reductions in store labor, incentive compensation and other cost containment initiatives.
- Reduced operating costs related to four closed stores, one temporarily closed store undergoing a major remodel and one sold store of \$3.2 million.
- Decreases in transportation fuel of \$2.3 million.
- Decreased supplies of \$1.5 million.
- Decreases in various other expenses due to a general focus on containing costs.

**Interest Expense** - Interest expense increased \$1.0 million, or 23.8%, from \$4.2 million in the prior year third quarter to \$5.2 million. Interest expense increased \$2.1 million, or 20.2%, from \$10.5 million in the prior year-to-date period to \$12.6 million. The increase in interest expense was due to primarily to an increase in average outstanding borrowings resulting from the VG's acquisition.

On January 2, 2009, we entered into an interest rate swap agreement. The interest rate swap is considered to be a cash flow hedge of interest payments on \$45.0 million of borrowings under our senior secured revolving credit facility by effectively converting a portion of the variable rate debt to a fixed rate basis. Under the terms of the agreement, we have agreed to pay the counterparty a fixed interest rate of 3.33% and the counterparty has agreed to pay Spartan Stores a floating interest rate based upon the 1-month LIBOR plus 1.25 percent (1.48 percent at January 2, 2010) on a notional amount of \$45 million. The interest rate swap agreement expires concurrently with its senior secured revolving credit facility on December 24, 2012.

Effective March 29, 2009 we adopted the provisions of Accounting Standards Codification (ASC) Subtopic 470-20 ("ASC 470-20", originally issued as Financial Accounting Standards Board (FASB) Staff Position No. APB 14-1, "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)"). In short, this requires that we recognize non-cash interest expense on our \$110.0 million convertible senior notes. ASC 470-20 must be applied on a retrospective basis; therefore, upon adoption we retroactively recorded additional non-cash interest expense of approximately \$1.0 million and \$2.4 million, pre-tax, in the prior year third quarter and year-to-date period.



***Income Taxes*** - The effective tax rate is 38.3% and 39.4% for the third quarter and current year-to-date period, respectively. The difference from the statutory rate is primarily due to State of Michigan income taxes.

## Discontinued Operations

Certain of our retail and grocery distribution operations have been recorded as discontinued operations. Results of the discontinued operations are excluded from the accompanying notes to the condensed consolidated financial statements for all periods presented, unless otherwise noted.

In the first and second quarters of fiscal 2009, we completed the closure and disposition of the prescription files of *The Pharm* stores, allowing us to concentrate efforts and resources on business opportunities with the best long-term growth potential and focus more on core distribution and conventional supermarket operations. Cash proceeds of \$13.8 million were received. Asset impairment charges and exit costs of \$6.4 million were recognized.

## Liquidity and Capital Resources

The following table summarizes our consolidated statements of cash flows for the year-to-date and prior year-to-date periods:

(In thousands)

|                                                        | January 2,<br>2010 | January 3,<br>2009 |
|--------------------------------------------------------|--------------------|--------------------|
| Net cash provided by operating activities              | \$ 54,330          | \$ 46,824          |
| Net cash used in investing activities                  | (43,708)           | (143,512)          |
| Net cash (used in) provided by financing activities    | (7,420)            | 74,610             |
| Net cash (used in) provided by discontinued operations | (2,541)            | 11,861             |
| Net increase (decrease) in cash and cash equivalents   | 661                | (10,217)           |
| Cash and cash equivalents at beginning of year         | 6,519              | 19,867             |
| Cash and cash equivalents at end of period             | \$ 7,180           | \$ 9,650           |

Net cash provided by operating activities increased from the prior year-to-date period primarily due to improved inventory leverage and working capital management.

Net cash used in investing activities decreased during the current fiscal year primarily due to the acquisition of VG's in the prior year. Capital expenditures, which do not include acquisitions, also decreased \$4.9 million to \$37.6 million, of which our Retail and Distribution segments utilized 82.6% and 17.4%, respectively. Expenditures were used for new stores, land, store remodels and refurbishments, new fuel centers and new equipment and software. Under the terms of our senior secured revolving credit facility, should our available borrowings fall below certain levels, our capital expenditures would be restricted each fiscal year. Our current available borrowings are over \$95 million above these limits as of January 2, 2010 and we do not expect to fall below these levels. Including VG's, we expect capital and real estate development expenditures to range from \$48.0 million to \$52.0 million for fiscal 2010. Our planned capital expenditures for the remainder of fiscal 2010, include substantial completion of one new store, minor store remodels, new equipment and software and the beginning of construction of one replacement store.

Net cash (used in) provided by financing activities includes cash paid and received related to our long-term borrowings, dividends paid, tax benefits of stock compensation and proceeds from the issuance of common stock. The decrease in cash from financing activities was primarily due to payments on amounts borrowed on our senior secured revolving credit facility that were used to finance the VG's acquisition in the prior year-to-date period. Cash dividends

of \$3.4 million and \$3.3 million were paid in the current year-to-date and prior year-to-date periods, respectively. Although we expect to continue to pay a quarterly cash dividend, adoption of a dividend policy does not commit the board of directors to declare future dividends. Each future dividend will be considered and declared by the board of directors in its discretion. Whether the board of directors continues to declare dividends depends on a number of factors, including our future financial condition and profitability and compliance with the terms of our credit facilities. Our current maturities of long-term debt and capital lease obligations at January 2, 2010 are \$3.9 million. Our ability to borrow additional funds is governed by the terms of our credit facilities.

Net cash (used in) provided by discontinued operations includes the net cash flows of our discontinued operations and consists primarily of the proceeds from the sale of assets and the payment of store exit cost reserves, insurance run-off claims and other liabilities. Included in the prior year cash flows from discontinued operations are proceeds on the disposal of assets of \$13.8 million. We expect cash used in our discontinued operations will be approximately \$3.0 million to \$4.0 million in fiscal 2010.

Our principal sources of liquidity are cash flows generated from operations and our senior secured revolving credit facility. Interest on our convertible senior notes is payable on May 15 and November 15 of each year. The revolving credit facility matures December 2012, and is secured by substantially all of our assets. As of January 2, 2010, our senior secured revolving credit facility had outstanding borrowings of \$63.4 million, available borrowings of \$115.2 million and maximum availability of \$125.2 million, which exceeds the minimum excess availability levels, as defined in the credit agreement. We believe that cash generated from operating activities and available borrowings under the credit facility will be sufficient to meet anticipated requirements for working capital, capital expenditures, dividend payments, and debt service obligations for the foreseeable future. However, there can be no assurance that Spartan Stores' business will continue to generate cash flow at or above current levels or that we will maintain our ability to borrow under our credit facility.

Our current ratio increased to 1.17:1.00 at January 2, 2010 from 1.13:1.00 at March 28, 2009 and our investment in working capital was \$30.9 million at January 2, 2010 versus \$21.0 million at March 28, 2009. Our debt to total capital ratio at January 2, 2010 was 0.43:1.00 versus 0.44:1.00 at March 28, 2009. The change in these ratios was primarily due to the timing of inventory purchases for the post holiday season.

For information on contractual obligations, see our Annual Report on Form 10-K for the fiscal year ended March 28, 2009. At January 2, 2010, there have been no material changes to our significant contractual obligations outside the ordinary course of business.

#### *Indebtedness and Liabilities of Subsidiaries*

On May 30, 2007, the Company sold \$110 million aggregate principal amount of 3.375% Convertible Senior Notes due 2027 (the "Notes"). The Notes are general unsecured obligations and rank equally in right of payment with all of the Company's other existing and future obligations that are unsecured and unsubordinated. Because the Notes are unsecured, they are structurally subordinated to our subsidiaries' existing and future indebtedness and other liabilities and any preferred equity issued by our subsidiaries. We rely in part on distributions and advances from our subsidiaries in order to meet our payment obligations under the notes and our other obligations. The Notes are not guaranteed by our subsidiaries. Many of our subsidiaries serve as guarantors with respect to our existing credit facility. Creditors of each of our subsidiaries, including trade creditors, and preferred equity holders, generally have priority with respect to the assets and earnings of the subsidiary over the claims of our creditors, including holders of the Notes. The Notes, therefore, are effectively subordinated to the claims of creditors, including trade creditors, judgment creditors and equity holders of our subsidiaries. In addition, our rights and the rights of our creditors, including the holders of the notes, to participate in the assets of a subsidiary during its liquidation or reorganization are effectively subordinated to all existing and future liabilities and preferred equity of that subsidiary. The Notes are effectively subordinated to our existing and future secured indebtedness to the extent of the assets securing such indebtedness and to existing and future indebtedness and other liabilities of our subsidiaries (including subsidiary guarantees of our senior credit facility).



The following table shows the indebtedness and other liabilities of our subsidiaries as of January 2, 2010:

| <b>Spartan Stores Subsidiaries Only</b><br><b>(In thousands)</b>   |    | <b>January 2,</b><br><b>2010</b> |
|--------------------------------------------------------------------|----|----------------------------------|
|                                                                    |    | <hr/>                            |
| <b>Current Liabilities</b>                                         |    |                                  |
| Accounts payable                                                   | \$ | 112,334                          |
| Accrued payroll and benefits                                       |    | 29,646                           |
| Other accrued expenses                                             |    | 19,610                           |
| Current portion of exit costs                                      |    | 10,234                           |
| Current maturities of long-term debt and capital lease obligations |    | 3,883                            |
|                                                                    |    | <hr/>                            |
| <b>Total current liabilities</b>                                   |    | 175,707                          |
| <b>Long-term Liabilities</b>                                       |    |                                  |
| Postretirement benefits                                            |    | 22,191                           |
| Other long-term liabilities                                        |    | 18,126                           |
| Exit costs                                                         |    | 30,408                           |
| Long-term debt and capital lease obligations                       |    | 45,370                           |
|                                                                    |    | <hr/>                            |
| <b>Total long-term liabilities</b>                                 |    | 116,095                          |
|                                                                    |    | <hr/>                            |
| <b>Total Subsidiary Liabilities</b>                                |    | 291,802                          |
| <b>Operating Leases</b>                                            |    | 151,115                          |
|                                                                    |    | <hr/>                            |
| <b>Total Subsidiary Liabilities and Operating Leases</b>           | \$ | 442,917                          |
|                                                                    |    | <hr/>                            |

#### *Ratio of Earnings to Fixed Charges*

Our ratio of earnings to fixed charges was 1.96:1.00 and 2.85:1.00 for the third quarter and prior year third quarter, respectively, and 2.71:1.00 and 3.43:1.00 for the year-to-date and prior year-to-date periods, respectively. For purposes of calculating the ratio of earnings to fixed charges, earnings consist of pretax earnings from continuing operations plus fixed charges (excluding capitalized interest). Fixed charges consist of interest costs, whether expensed or capitalized, the interest component of rental expense and amortization of debt issue costs, whether expensed or capitalized.

#### **Off-Balance Sheet Arrangements**

We had letters of credit of \$4.1 million outstanding and unused at January 2, 2010. The letters of credit are maintained primarily to support payment or deposit obligations. We pay a commission of approximately 2% on the face amount of the letters of credit.

#### **Recently Adopted Accounting Standards**

In September 2006, the FASB issued ASC Topic 820 ("ASC 820", originally issued as SFAS No. 157, "Fair Value Measurements"). ASC 820 defines fair value, establishes a framework for measuring fair value under generally

accepted accounting principles, and expands disclosures about fair value measurements. This statement does not require any new fair value measurements, but applies under other accounting pronouncements that require or permit fair value measurements. Effective March 30, 2008, we adopted the provisions of ASC 820 related to financial assets and liabilities recognized or disclosed on a recurring basis. Additionally, on March 29, 2009, we began applying the principles of ASC 820 to non-financial assets and liabilities. Adoption of ASC 820 had no impact on the consolidated financial statements.

In May 2008, the FASB issued ASC Topic 470-20 (originally issued as FASB Staff Position No. APB 14-1, "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)") that changes the accounting treatment for convertible debt instruments that allow for either mandatory or optional cash settlements. ASC 470-20 requires us to recognize non-cash interest expense on our \$110 million convertible senior notes based on the market rate for similar debt instruments without the conversion feature as of the date of debt issuance. ASC 470-20 was adopted on March 29, 2009 and was applied on a retrospective basis. As required, upon adoption on March 29, 2009, we retroactively recorded additional non-cash interest expense of approximately \$1.0 million and \$2.4 million for the prior year third quarter and year-to-date period, respectively. We also retroactively recorded an increase in shareholders' equity of \$16.4 million, net of deferred taxes, and a decrease in long-term debt of \$27.6 million.

In June 2008, the FASB updated ASC Topic 260 (originally issued as FSP No. EITF 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities"). The updated provisions of ASC 260 clarify that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents are participating securities and must be included in the computation of earnings per share pursuant to the two-class method. The updated provisions of ASC 260 were adopted on March 29, 2009 and applied on a retrospective basis as required.

### **Critical Accounting Policies**

This discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts. On an ongoing basis, we evaluate our estimates, including those related to bad debts, inventories, intangible assets, assets held for sale, long-lived assets, income taxes, self-insurance reserves, exit costs, retirement benefits, stock-based compensation and contingencies and litigation. We base our estimates on historical experience and on various other assumptions and factors that we believe to be reasonable under the circumstances. Based on our ongoing review, we make adjustments we consider appropriate under the facts and circumstances. We have discussed the development, selection and disclosure of these estimates with the Audit Committee. The accompanying condensed consolidated financial statements are prepared using the same critical accounting policies discussed in our Annual Report on Form 10-K for the fiscal year ended March 28, 2009.

#### **ITEM 3. Quantitative and Qualitative Disclosure About Market Risk**

There have been no material changes in market risk of Spartan Stores from the information provided under Part II, Item 7A, "Quantitative and Qualitative Disclosure About Market Risk", of the Company's Annual Report on Form 10-K for the fiscal year ended March 28, 2009.

#### **ITEM 4. Controls and Procedures**

An evaluation of the effectiveness of the design and operation of Spartan Stores' disclosure controls and procedures (as currently defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) was performed as of January 2, 2010 (the "Evaluation Date"). This evaluation was performed under the supervision and with the participation of Spartan Stores' management, including its Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"). As of the Evaluation Date, Spartan Stores' management, including the CEO and CFO, concluded that Spartan Stores' disclosure controls and procedures were effective as of the Evaluation Date to ensure that material information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities and Exchange Act of 1934 is accumulated and communicated to management, including our principal executive and principal financial officers as appropriate to allow for timely decisions regarding required disclosure. During the last fiscal



quarter there was no change in Spartan Stores' internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, Spartan Stores' internal control over financial reporting.

## PART II

### OTHER INFORMATION

#### ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides information regarding the Company's purchases of its own common stock during the third quarter. The Company has no public stock repurchase plans or programs. All transactions reported are with associates under stock compensation plans. These include: (1) shares of Spartan Stores, Inc. stock delivered in satisfaction of the exercise price and/or tax withholding obligations by holders of employee stock options who exercised options, and (2) shares submitted for cancellation to satisfy tax withholding obligations that occur upon the vesting of the restricted shares. The value of the shares delivered or withheld is determined by the applicable stock compensation plan.

#### Spartan Stores, Inc. Purchases of Equity Securities

| Period                                        | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price Paid<br>per Share |
|-----------------------------------------------|-------------------------------------------|------------------------------------|
| September 13 - October 10, 2009               |                                           |                                    |
| Employee Transactions                         | 1,078                                     | \$ 14.06                           |
| October 11 - November 7, 2009                 |                                           |                                    |
| Employee Transactions                         | 15                                        | \$ 14.00                           |
| November 8 - December 5, 2009                 |                                           |                                    |
| Employee Transactions                         | -                                         | \$ -                               |
| December 6 - January 2, 2010                  |                                           |                                    |
| Employee Transactions                         | -                                         | \$ -                               |
| Total for Third Quarter ended January 2, 2010 | 1,093                                     | \$ 14.05                           |

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### ITEM 6. Exhibits

The following documents are filed as exhibits to this Quarterly Report on Form 10-Q:

| <u>Exhibit Number</u> | <u>Document</u>                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
|-----------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 2.1                   | Asset purchase agreement dated March 31, 2008 between Rite Aid of Ohio, Inc. and Seaway Food Town, Inc., with amendments. Previously filed as an exhibit to Spartan Stores' Annual Report on Form 10-K, filed for the fiscal year ended March 29, 2008. Here incorporated by reference. Exhibits and schedules to this agreement are listed and identified in the agreement. Omitted exhibits and schedules will be furnished supplementally to the Commission upon request.            |
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| 32.1                  | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                                                                                                                                                                                                                                                                                                                                                                                                                |

**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.

SPARTAN STORES, INC.  
(Registrant)

Date: February 4, 2010

By

/s/ David M. Staples

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David M. Staples  
Executive Vice President and Chief Financial  
Officer  
(Principal Financial Officer and duly authorized  
signatory for Registrant)

**EXHIBIT INDEX**

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