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 quarter ended March 25, 2022

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

Commission File Number 1-7635

TWIN DISC, INCORPORATED

(Exact name of registrant as specified in its charter)

Wisconsin	**39-0667110**
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)

1328 Racine Street, Racine, Wisconsin 53403
(Address of principal executive offices)

(262) 638-4000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock (No Par Value)	TWIN	The NASDAQ Stock Market LLC

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 every Interactive Data File required to be submitted 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 such files).

Yes ☑ No ☐

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

Large Accelerated Filer ☐	Accelerated Filer ☑
Non-accelerated filer ☐	Smaller reporting company ☑
Emerging growth company ☐	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

Yes ☐ No ☑

At April 29, 2022, the registrant had 13,651,611 shares of its common stock outstanding.

Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

TWIN DISC, INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AMOUNTS)
(UNAUDITED)

	March 25, 2022	June 30, 2021
ASSETS		
Current assets:		
Cash	$ 12,825	$ 12,340
Trade accounts receivable, net	38,977	39,491
Inventories	131,080	114,967
Assets held for sale	3,082	9,539
Prepaid expenses	6,984	5,704
Other	8,447	9,926
Total current assets	201,395	191,967
Property, plant and equipment, net	42,753	45,463
Right-of-use assets operating leases	13,692	14,736
Intangible assets, net	13,944	17,480
Deferred income taxes	2,258	2,511
Other assets	3,682	3,256
Total assets	$ 277,724	$ 275,413
LIABILITIES AND EQUITY		
Current liabilities:		
Current maturities of long-term debt	$ 2,000	$ 2,000
Accounts payable	34,195	31,011
Accrued liabilities	48,779	45,549
Total current liabilities	84,974	78,560
Long-term debt	32,069	30,085
Lease obligations	11,543	12,887
Accrued retirement benefits	10,065	11,176
Deferred income taxes	3,959	5,045
Other long-term liabilities	5,659	7,000
Total liabilities	148,269	144,753
Commitments and contingencies (Note D)		
Equity:		
Twin Disc shareholders' equity:		
Preferred shares authorized: 200,000; issued: none; no par value	-	-
Common shares authorized: 30,000,000; issued: 14,632,802; no par value	42,048	40,972
Retained earnings	127,251	126,936
Accumulated other comprehensive loss	(25,724)	(22,615)
	143,575	145,293
Less treasury stock, at cost (965,987 and 984,139 shares, respectively)	14,805	15,083
Total Twin Disc shareholders' equity	128,770	130,210
Noncontrolling interest	685	450
Total equity	129,455	130,660
Total liabilities and equity	$ 277,724	$ 275,413

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

TWIN DISC, INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE (LOSS) INCOME
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

	For the Quarter Ended		For the Three Quarters Ended	
	March 25, 2022	March 26, 2021	March 25, 2022	March 26, 2021
Net sales	$ 59,289	$ 57,640	$ 166,939	$ 152,377
Cost of goods sold	41,598	43,678	122,319	119,835
Gross profit	17,691	13,962	44,620	32,542
Marketing, engineering and administrative expenses	14,396	13,196	42,753	39,000
Restructuring expenses	303	251	1,542	777
Other operating income	(63)	-	(2,957)	-
Income (loss) from operations	3,055	515	3,282	(7,235)
Interest expense	490	606	1,594	1,769
Other (income) expense, net	(498)	(557)	(608)	2,314
	(8)	49	986	4,083
Income (loss) before income taxes and noncontrolling interest	3,063	466	2,296	(11,318)
Income tax expense (benefit)	753	300	1,757	(3,267)
Net income (loss)	2,310	166	539	(8,051)
Less: Net earnings attributable to noncontrolling interest, net of tax	(79)	(72)	(223)	(147)
Net income (loss) attributable to Twin Disc	$ 2,231	$ 94	$ 316	$ (8,198)
Income (loss) per share data:				
Basic income (loss) per share attributable to Twin Disc common shareholders	$ 0.17	$ 0.01	$ 0.02	$ (0.62)
Diluted income (loss) per share attributable to Twin Disc common shareholders	$ 0.17	$ 0.01	$ 0.02	$ (0.62)
Weighted average shares outstanding data:				
Basic shares outstanding	13,397	13,269	13,339	13,240
Diluted shares outstanding	13,457	13,295	13,373	13,240
Comprehensive income (loss)				
Net income (loss)	$ 2,310	$ 166	$ 539	$ (8,051)
Benefit plan adjustments, net of income taxes of $4, $177, $4 and $529, respectively	505	583	1,512	1,691
Foreign currency translation adjustment	(2,721)	(3,008)	(6,359)	5,503
Unrealized gain on cash flow hedge, net of income taxes of $0, $60, $0 and $115, respectively	810	193	1,748	372
Comprehensive income (loss)	904	(2,066)	(2,560)	(485)
Less: Comprehensive income (loss) attributable to noncontrolling interest	38	(34)	235	(133)
Comprehensive income (loss) attributable to Twin Disc	$ 942	$ (2,100)	$ (2,325)	$ (618)

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

TWIN DISC, INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	For the Three Quarters Ended	
	March 25, 2022	March 26, 2021
Cash flows from operating activities:		
Net income (loss)	$ 539	$ (8,051)
Adjustments to reconcile net income (loss) to net cash (used) provided by operating activities:		
Depreciation and amortization	7,317	8,366
Gain on sale of assets	(2,939)	-
Restructuring expenses	(487)	215
Provision for deferred income taxes	(1,383)	(6,052)
Stock compensation expense and other non-cash changes, net	2,642	1,934
Net change in operating assets and liabilities	(12,912)	8,603
Net cash (used) provided by operating activities	(7,223)	5,015
Cash flows from investing activities:		
Acquisitions of property, plant and equipment	(2,371)	(3,851)
Proceeds from sale of fixed assets	9,152	76
Proceeds on note receivable	500	700
Other, net	465	(18)
Net cash provided (used) by investing activities	7,746	(3,093)
Cash flows from financing activities:		
Borrowings under revolving loan arrangement	78,142	56,463
Repayments of revolver loans	(73,192)	(58,497)
Repayments of other long term debt	(2,789)	(411)
Payments of withholding taxes on stock compensation	(487)	(224)
Net cash provided (used) by financing activities	1,674	(2,669)
Effect of exchange rate changes on cash	(1,712)	1,653
Net change in cash	485	906
Cash:		
Beginning of period	12,340	10,688
End of period	$ 12,825	$ 11,594

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

A. Basis of Presentation

The unaudited condensed consolidated financial statements have been prepared by Twin Disc, Incorporated (the "Company") pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") and, in the opinion of the Company, include adjustments, consisting primarily of normal recurring items, necessary for a fair statement of results for each period. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such SEC rules and regulations. The Company believes that the disclosures made are adequate to make the information presented not misleading. It is suggested that these financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report filed on Form 10-K for June 30, 2021. The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States.

Reclassification

Certain prior year amounts primarily in cost of goods sold and marketing, engineering, and administrative expenses have been reclassified for consistency with current year presentation.

Recently Adopted Accounting Standards

In December 2019, the FASB issued guidance (ASU 2019-12) intended to simplify the accounting for income taxes. The Company adopted this guidance effective July 1, 2021. The adoption of this guidance did not have a material impact on the Company's disclosures.

New Accounting Releases

In June 2016, the FASB issued updated guidance (ASU 2016-13) and also issued subsequent amendments to the initial guidance under ASU 2018-19, ASU 2019-04, ASU 2019-05 and ASU 2019-10 (collectively ASC 326). ASC 326 requires the measurement and recognition of expected credit losses for financial assets held at amortized cost. This replaces the existing incurred loss model with an expected loss model and requires the use of forward-looking information to calculate credit loss estimates. The amendments in this guidance are effective for filers, excluding smaller reporting companies, for fiscal years beginning after December 15, 2019, and for smaller reporting companies for fiscal years beginning after December 15, 2022 (the Company's fiscal 2024), with early adoption permitted for certain amendments. ASC 326 must be adopted by applying a cumulative effect adjustment to retained earnings. The Company is currently evaluating the potential impact of this guidance on the Company's disclosures.

In March 2020 and January 2021, the FASB issued guidance (ASU 2020-04 and ASU 2021-01, respectively), intended to provide optional expedients and exceptions for applying generally accepted accounting principles to contracts, hedging relationships, and other transactions affected by the discontinuation of the London Interbank Offered Rate ("LIBOR") or by another reference rate expected to be discontinued. The amendments in this guidance are effective beginning on March 12, 2020, and the Company may elect to apply the amendments prospectively through December 31, 2022. The Company is working with its lender and currently evaluating the potential impact of this guidance on the Company's financial statements and disclosures.

Special Note Regarding Smaller Reporting Company Status

Under SEC Release 33-10513; 34-83550, Amendments to Smaller Reporting Company Definition, the Company qualifies as a smaller reporting company and accordingly, it has scaled some of its disclosures of financial and non-financial information in this quarterly report. The Company will continue to determine whether to provide additional scaled disclosures of financial or non-financial information in future quarterly reports, annual reports and/or proxy statements if it remains a smaller reporting company under SEC rules.

B. Inventories

The major classes of inventories were as follows:

	March 25, 2022	June 30, 2021
Inventories:		
Finished parts	$ 68,166	$ 59,761
Work in process	19,580	17,908
Raw materials	43,334	37,298
	$ 131,080	$ 114,967

C. Warranty

The Company engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its suppliers. However, its warranty obligation is affected by product failure rates, the number of units affected by the failure and the expense involved in satisfactorily addressing the situation. The warranty reserve is established based on our best estimate of the amounts necessary to settle future and existing claims on products sold as of the balance sheet date. When evaluating the adequacy of the reserve for warranty costs, management takes into consideration the term of the warranty coverage, historical claim rates and costs of repair, knowledge of the type and volume of new products and economic trends. While we believe the warranty reserve is adequate and that the judgment applied is appropriate, such amounts estimated to be due and payable in the future could differ materially from what actually transpires. The following is a listing of the activity in the warranty reserve for the quarters ended March 25, 2022 and March 26, 2021:

	For the Quarter Ended		For the Three Quarters Ended	
	March 25, 2022	March 26, 2021	March 25, 2022	March 26, 2021
Reserve balance, beginning of period	$ 3,483	$ 4,474	$ 4,369	$ 4,460
Current period expense and adjustments	339	805	658	2,550
Payments or credits to customers	(518)	(995)	(1,688)	(2,814)
Translation	(27)	(28)	(62)	60
Reserve balance, end of period	$ 3,277	$ 4,256	$ 3,277	$ 4,256

The current portion of the warranty accrual ($2,757 and $3,314 as of March 25, 2022 and March 26, 2021, respectively) is reflected in accrued liabilities, while the long-term portion ($520 and $942 as of March 25, 2022 and March 26, 2021, respectively) is included in other long-term liabilities on the consolidated balance sheets.

D. Contingencies

The Company is involved in litigation of which the ultimate outcome and liability to the Company, if any, is not presently determinable. Management believes that final disposition of such litigation will not have a material impact on the Company’s results of operations, financial position or cash flows.

E. Business Segments

The Company and its subsidiaries are engaged in the manufacture and sale of marine and heavy-duty off-highway power transmission equipment. Principal products include marine transmissions, azimuth drives, surface drives, propellers and boat management systems, as well as power-shift transmissions, hydraulic torque converters, power take-offs, industrial clutches and controls systems. The Company sells to both domestic and foreign customers in a variety of market areas, principally pleasure craft, commercial and military marine markets, as well as in the energy and natural resources, government and industrial markets. The Company's worldwide sales to both domestic and foreign customers are transacted through a direct sales force and a distributor network.

The Company has two reportable segments: manufacturing and distribution. These segment structures reflect the way management makes operating decisions and manages the growth and profitability of the business. It also corresponds with management’s approach of allocating resources and assessing the performance of its segments. The accounting practices of the segments are the same as those described in the summary of significant accounting policies. Transfers between segments are at established inter-company selling prices. Management evaluates the performance of its segments based on their net income.

Information about the Company's segments is summarized as follows:

	For the Quarter Ended		For the Three Quarters Ended	
	March 25, 2022	March 26, 2021	March 25, 2022	March 26, 2021
Net sales				
Manufacturing segment sales	$ 56,403	$ 52,138	$ 147,296	$ 132,338
Distribution segment sales	23,660	26,221	72,485	71,950
Inter/Intra segment elimination – manufacturing	(16,672)	(15,074)	(40,815)	(37,892)
Inter/Intra segment elimination – distribution	(4,102)	(5,645)	(12,027)	(14,019)
	$ 59,289	$ 57,640	$ 166,939	$ 152,377
Net (loss) income attributable to Twin Disc				
Manufacturing segment net (loss) income	$ 6,000	$ 2,422	$ 9,230	$ (3,352)
Distribution segment net income	1,415	697	3,396	2,352
Corporate and eliminations	(5,184)	(3,025)	(12,310)	(7,198)
	$ 2,231	$ 94	$ 316	$ (8,198)

Assets	March 25, 2022	June 30, 2021
Manufacturing segment assets	$ 356,154	$ 364,379
Distribution segment assets	54,629	46,956
Corporate assets and elimination of intercompany assets	(133,059)	(135,922)
	$ 277,724	$ 275,413

Disaggregated revenue:

The following table presents details deemed most relevant to the users of the financial statements for the quarters and three quarters ended March 25, 2022 and March 26, 2021.

Net sales by product group for the quarter ended March 25, 2022 is summarized as follows:

	Manufacturing	Distribution	Elimination of Intercompany Sales	Total
Industrial	$ 7,947	$ 1,449	$ (935)	$ 8,461
Land-based transmissions	17,448	7,173	(8,535)	16,086
Marine and propulsion systems	30,820	13,108	(10,766)	33,162
Other	188	1,930	(538)	1,580
Total	$ 56,403	$ 23,660	$ (20,774)	$ 59,289

Net sales by product group for the quarter ended March 26, 2021 is summarized as follows:

	Manufacturing	Distribution	Elimination of Intercompany Sales	Total
Industrial	$ 5,652	$ 1,491	$ (1,307)	$ 5,836
Land-based transmissions	13,793	6,892	(5,419)	15,266
Marine and propulsion systems	32,671	15,016	(13,951)	33,736
Other	22	2,822	(42)	2,802
Total	$ 52,138	$ 26,221	$ (20,719)	$ 57,640

Net sales by product group for the three quarters ended March 25, 2022 is summarized as follows:

	Manufacturing	Distribution	Elimination of Intercompany Sales	Total
Industrial	$ 20,939	$ 4,377	$ (3,016)	$ 22,300
Land-based transmissions	41,158	18,775	(18,287)	41,646
Marine and propulsion systems	84,968	41,330	(30,983)	95,315
Other	231	8,003	(556)	7,678
Total	$ 147,296	$ 72,485	$ (52,842)	$ 166,939

Net sales by product group for the three quarters ended March 26, 2021 is summarized as follows:

	Manufacturing	Distribution	Elimination of Intercompany Sales	Total
Industrial	$ 15,744	$ 4,168	$ (3,369)	$ 16,543
Land-based transmissions	34,388	19,267	(14,388)	39,267
Marine and propulsion systems	82,152	41,996	(34,095)	90,053
Other	54	6,519	(59)	6,514
Total	$ 132,338	$ 71,950	$ (51,911)	$ 152,377

F. Stock-Based Compensation

Performance Stock Awards ("PSA")

During the three quarters of fiscal 2022 and 2021, the Company granted a target number of 103.6 and 265.3 PSAs, respectively, to various employees of the Company, including executive officers. The fiscal 2022 PSAs will vest if the Company achieves performance-based target objectives relating to average return on invested capital, cumulative sales revenue, and adjusted annual earnings per share ("EPS") (as defined in the PSA Grant Agreement), in the cumulative three fiscal year period ending June 30, 2024. These PSAs are subject to adjustment if the Company's return on invested capital, net sales, and EPS for the period falls below or exceeds the specified target objective, and the maximum number of performance shares that can be awarded if the target objective is exceeded is 155.4. Based upon actual results to date, the Company is currently accruing compensation expense for these PSAs.

The fiscal 2021 PSAs will vest if the Company achieves performance-based target objectives relating to average return on invested capital, cumulative sales revenue, and cumulative free cashflow (as defined in the PSA Grant Agreement), in the cumulative three fiscal year period ending June 30, 2023. These PSAs are subject to adjustment if the Company's return on invested capital, sales revenue, or free cashflow for the period falls below or exceeds the specified target objective, and the maximum number of performance shares that can be awarded if the target objective is exceeded is 334.6. Based upon actual results to date, the Company is currently accruing compensation expense for these PSAs.

There were 440.9 and 433.1 unvested PSAs outstanding at March 25, 2022 and March 26, 2021, respectively. The fair value of the PSAs (on the date of grant) is expensed over the performance period for the shares that are expected to ultimately vest. Compensation expense of $237 and $132 was recognized for the quarters ended March 25, 2022 and March 26, 2021, respectively, related to PSAs. Compensation expense of $672 and $360 was recognized for the three quarters ended March 25, 2022 and March 26, 2021, respectively, related to PSAs. The weighted average grant date fair value of the unvested awards at March 25, 2022 was $9.18. At March 25, 2022, the Company had $2,895 of unrecognized compensation expense related to the unvested shares that would vest if the specified target objective was achieved for the fiscal 2022, 2021 and 2020 awards. The total fair value of PSAs vested as of March 25, 2022 and March 26, 2021 was $0.

Restricted Stock Awards ("RS")

The Company has unvested RS awards outstanding that will vest if certain service conditions are fulfilled. The fair value of the RS grants is recorded as compensation expense over the vesting period, which is generally 1 to 3 years. During the three quarters of fiscal 2022 and 2021, the Company granted 51.7 and 250.3 service based restricted shares, respectively, to employees and non-employee directors. There were 268.5 and 377.5 unvested shares outstanding at March 25, 2022 and March 26, 2021, respectively. A total of 29.8 and 6.8 shares of RS were forfeited during the three quarters ended March 25, 2022 and March 26, 2021, respectively. Compensation expense of $294 and $302 associated with RS was recognized for the quarters ended March 25, 2022 and March 26, 2021, respectively. Compensation expense of $913 and $991 associated with RS was recognized for the three quarters ended March 25, 2022 and March 26, 2021, respectively. The total fair value of RS grants vested as of March 25, 2022 and March 26, 2021 was $1,695 and $533, respectively. As of March 25, 2022, the Company had $840 of unrecognized compensation expense related to RS which will be recognized over the next three years.

Restricted Stock Unit Awards ("RSU")

Under the 2018 and 2021 Long Term Incentive Plans, the Company has been authorized to issue RSUs. The RSUs entitle the employee to shares of common stock of the Company if the employee remains employed by the Company through a specified date, generally three years from the date of grant. The fair value of the RSUs (on the date of grant) is recorded as compensation expense over the vesting period. During the three quarters of fiscal 2022 and 2021, the Company granted 67.4 and 0.0 of employment based RSUs, respectively. There were 67.4 and 34.8 unvested RSUs outstanding at March 25, 2022 and March 26, 2021, respectively. Compensation expense of $89 and $90 was recognized for the quarters ended March 25, 2022 and March 26, 2021, respectively. Compensation expense of $255 and $253 associated with RSU's was recognized for the three quarters ended March 25, 2022 and March 26, 2021, respectively. The total fair value of restricted stock units vested as of March 25, 2022 and March 26, 2021 was $475 and $25, respectively. The weighted average grant date fair value of the unvested awards at March 25, 2022 was $14.19. As of March 25, 2022, the Company had $727 of unrecognized compensation expense related to restricted stock which will be recognized over the next two years.

G. Pension and Other Postretirement Benefit Plans

The Company has non-contributory, qualified defined benefit plans covering substantially all domestic employees hired prior to October 1, 2003 and certain foreign employees. Additionally, the Company provides healthcare and life insurance benefits for certain domestic retirees. The components of the net periodic benefit cost for the defined benefit pension plans and the other postretirement benefit plan are as follows:

	For the Quarter Ended		For the Three Quarters Ended	
	March 25, 2022	March 26, 2021	March 25, 2022	March 26, 2021
Pension Benefits:				
Service cost	$ 137	$ 144	$ 406	$ 432
Prior service cost	10	16	30	48
Interest cost	709	715	2,055	2,072
Expected return on plan assets	(1,258)	(1,133)	(3,773)	(3,400)
Amortization of transition obligation	9	9	28	28
Amortization of prior service cost	(4)	(4)	(12)	(12)
Amortization of actuarial net loss	562	811	1,687	2,434
Net periodic benefit cost	$ 165	$ 558	$ 421	$ 1,602
Postretirement Benefits:				
Service cost	$ 4	$ 4	$ 11	$ 12
Interest cost	35	39	105	116
Amortization of prior service cost	(69)	(69)	(206)	(206)
Net periodic benefit gain	$ (30)	$ (26)	$ (90)	$ (78)

The service cost component is included in cost of goods sold and marketing, engineering and administrative expenses. All other components of net periodic benefit cost are included in other expense (income), net.

The Company expects to contribute approximately $733 to its pension plans in fiscal 2022. For the three quarters ended March 25, 2022, the amount of $701 in contributions to the pension plans were made.

The Company has reclassified $505 (net of $4 in taxes) of benefit plan adjustments from accumulated other comprehensive loss during the quarter ended March 25, 2022, and $583 (net of $177 in taxes) during the quarter ended March 26, 2021. These reclassifications are included in the computation of net periodic benefit cost. The Company has reclassified $1,513 (net of $4 in taxes) of benefit plan adjustments from accumulated other comprehensive loss during the three quarters ended March 25, 2022, and $1,691 (net of $529 in taxes) during the three quarters ended March 26, 2021. These reclassifications are included in the computation of net periodic benefit cost.

H. Income Taxes

Accounting policies for interim reporting require the Company to adjust its effective tax rate each quarter to be consistent with the estimated Annual Effective Tax Rate (AETR). Under this effective tax rate methodology, the Company applies an estimated annual income tax rate to its year-to-date ordinary earnings to derive its income tax provision each quarter. To calculate its AETR, an entity must estimate its ordinary income or loss and the related tax expense or benefit for its full fiscal year. In situations in which an entity is in a loss position and recognizes a full valuation allowance, the guidance in ASC 740-270-25-9 applies. Due to continued historical domestic losses and uncertain future domestic earnings, the Company recognizes a full US valuation allowance. Permanent differences continue to fluctuate and are significant compared to projected ordinary income. Therefore per ASC guidance, the fully valued domestic entity was removed from the annualized effective rate calculation. Because of the full US valuation allowance, the US entity may only recognize tax expense / benefit recorded for ASU 740-10 adjustments.

For the three quarters ended March 25, 2022 and March 26, 2021 the Company's effective income tax rate was 76.5% and 28.9% respectively. For the quarter ended March 26, 2021 the company did not recognize a full U.S. valuation allowance so the tax expense realized was based on the estimated AETR. Due to the different methodologies utilized to calculate the interim tax provisions, it is not reasonable to numerically reconcile the change in estimated tax rate.

On January 30, 2020, the World Health Organization ("WHO") announced a global health emergency because of a new strain of a novel coronavirus originating in Wuhan, China (the "COVID-19 outbreak") and the risks to the international community as the virus spreads globally. In March 2020, the World Health Organization classified the COVID-19 outbreak a pandemic, based on the rapid increase in exposure globally. The spread of the COVID-19 outbreak has caused significant volatility and uncertainty in U.S. and international markets. On March 27, 2020 the Coronavirus Aid, Relief and Economic Security ("CARES") Act was signed into law. The CARES Act includes many measures to assist companies, including temporary changes to income and non-income-based tax laws, some of which were enacted under the Tax Cuts and Jobs Act ("TCJA") in 2017. In addition, governments around the world continue to initiate various forms of assistance. The Consolidated Appropriations Act of 2021 was signed into law on December 27, 2020. Changes in the tax treatment of certain items have been reflected during this quarter. These changes did not have a material impact to the Company's effective tax rate. On March 11, 2021, President Biden signed into law The American Rescue Plan Act of 2021 ("ARPA"), which among other things, further changed executive compensation rules. Under the ARPA, which is effective for tax years beginning after December 31, 2026, the definition of covered employee has been expanded to include employees who are among the five highest compensated employees for the year, not limited to only officers. This is in addition to the existing pool of officers who are defined as "covered employees" under the current IRC 162(m) rules. Management will continue to monitor these new rules and apply them as required. Currently, the anticipated impact is minimal. The full impact of the COVID-19 outbreak continues to evolve as of the date of this report. As such it is uncertain as to the full magnitude that the COVID-19 outbreak will have on the Company's financial condition, liquidity, and future results of operations.

The Company maintains valuation allowances when it is more likely than not that all or a portion of a deferred tax asset will not be realized. Changes in valuation allowances from period to period are included in the tax provision in the period of change. In determining whether a valuation allowance is required, the Company takes into account such factors as prior earnings history, expected future earnings, carry-back and carry-forward periods, and tax strategies that could potentially enhance the likelihood of realization of a deferred tax asset. In addition, all other available positive and negative evidence is taken into consideration, including all new impacts of tax reform. The Company has evaluated the realizability of the net deferred tax assets related to its foreign operations and based on this evaluation management has concluded that no valuation allowances are required. However, due to continued historical domestic losses and uncertain future domestic earnings, the company continues to recognize a full domestic valuation allowance.

The Company has approximately $752 of unrecognized tax benefits, including related interest and penalties, as of March 25, 2022, which, if recognized, would favorably impact the effective tax rate. There were no significant changes in the total unrecognized tax benefits due to the settlement of audits, the expiration of statutes of limitations or for other items during the quarter ended March 25, 2022. It appears possible that the amount of unrecognized tax benefits could change in the next twelve months due to on-going activity.

Annually, the Company files income tax returns in various taxing jurisdictions inside and outside the United States. In general, the tax years that remain subject to examination in foreign jurisdictions are 2014 through 2021. The tax years open to examination in the Netherlands are for years subsequent to 2018. The tax years open to examination in the U.S. are for years subsequent to fiscal 2017. It is reasonably possible that other audit cycles will be completed during fiscal 2022.

I. Intangible Assets

As of March 25, 2022, the following acquired intangible assets have definite useful lives and are subject to amortization:

	Net Book Value Rollforward			Net Book Value By Asset Type			
	Gross Carrying Amount	Accumulated Amortization / Impairment	Net Book Value	Customer Relationships	Technology Know-how	Trade Name	Other
Balance at June 30, 2021	$ 41,142	$ (23,662)	$ 17,480	$ 10,321	$ 4,883	$ 1,282	$ 994
Addition	9	-	$ 9	-	-	-	9
Amortization	-	(2,415)	$ (2,415)	(1,225)	(888)	(133)	(169)
Translation adjustment	(1,130)	-	$ (1,130)	(707)	(321)	(89)	(13)
Balance at March 25, 2022	$ 40,021	$ (26,077)	$ 13,944	$ 8,389	$ 3,674	$ 1,060	$ 821

Other intangibles consist mainly of computer software. Amortization is recorded on the basis of straight-line or accelerated, as appropriate, over the estimated useful lives of the assets.

The weighted average remaining useful life of the intangible assets included in the table above is approximately 7 years.

Intangible amortization expense was $785 and $838 for the quarters ended March 25, 2022, and March 26, 2021, respectively. Intangible amortization expense was $2,415 and $2,516 for the three quarters ended March 25, 2022, and March 26, 2021, respectively. Estimated intangible amortization expense for the remainder of fiscal 2022 and each of the next five fiscal years and thereafter is as follows:

Fiscal Year	
2022	791
2023	2,924
2024	2,779
2025	2,661
2026	1,343
Thereafter	3,446

J. Long-term Debt

Long-term debt at March 25, 2022 and June 30, 2021 consisted of the following:

	March 25, 2022	June 30, 2021
Credit Agreement Debt		
Revolving loans (expire June 2023)	$ 19,472	$ 15,415
Term loan (due March 2026)	14,500	16,500
Other	97	170
Subtotal	34,069	32,085
Less: current maturities	(2,000)	(2,000)
Total long-term debt	$ 32,069	$ 30,085

Credit Agreement Debt: The Company's credit agreement debt represents borrowings made under the credit agreement, as amended, which it entered into with BMO Harris Bank N.A, ("BMO") on June 29, 2018 ("Credit Agreement"). Under the agreement, the Company, among other obligations, is subject to a minimum earnings before interest, taxes, depreciation, and amortization ("EBITDA") financial covenant.

On January 27, 2021, the Company and BMO entered into a forbearance agreement and amendment to the Credit Agreement (the "Forbearance Agreement"). Under this agreement, BMO agreed to forbear from exercising its rights and remedies against the Company with respect to its noncompliance with the minimum EBITDA covenant, for the period beginning with the date of the amendment through September 30, 2021.

On September 30, 2021, the Company and BMO entered into an amended and restated forbearance agreement and amendment to the Credit Agreement (the "Amended and Restated Forbearance Agreement"). The Amended and Restated Forbearance Agreement extends the forbearance period through February 28, 2022, or if earlier, through the date on which a default under the Amended and Restated Forbearance Agreement or Credit Agreement occurs. During the extended forbearance period, BMO will continue to forbear from exercising its rights and remedies against the Company under the Credit Agreement with respect to the Company's noncompliance with its minimum EBITDA covenants. The Amended and Restated Forbearance Agreement also makes certain adjustments to the Credit Agreement. When the forbearance period ends, the Company is subject to a maximum total funded debt to EBITDA ratio of 3.00 to 1.00.

On February 28, 2022, the Company entered into a second amended and restated forbearance agreement and amendment No. 8 to Credit Agreement (the "Second Amended and Restated Forbearance Agreement") that amends the Credit Agreement dated as of June 29, 2018, as amended between the Company and BMO. The Second Amended and Restated Forbearance Agreement extends the Forbearance Period through June 30, 2022, or if earlier, through the date on which a default under the Amended and Restated Forbearance Agreement or Credit Agreement occurs. During the extended Forbearance Period, BMO will continue to forbear from exercising its rights and remedies against the Company under the Credit Agreement with respect to the Company's noncompliance with its minimum EBITDA covenants. The Company also executed a Third Amended and Restated Revolving Note with BMO, reflecting the maximum Revolving Credit Commitment of $40,000,000.

For the quarter ended March 25, 2022, as a result of the Second Amended and Restated Forbearance Agreement, the Company was not required to meet the minimum EBITDA financial covenant. The Company expects to be in compliance with the terms of the Credit Agreement following the forbearance period, and therefore continues to classify its debt as long term.

The Company remains in compliance with its liquidity and other covenants, and has agreed to provide additional financial reports to BMO.

The Credit Agreement, including its amendments, is more fully described in the Company's Annual Report filed on Form 10-K for June 30, 2021, as well as in Item 2 of this quarterly report.

As of March 25, 2022, current maturities include $2,000 of term loan payments due within the coming year.

Other: Other long-term debt pertains mainly to a financing arrangement in Europe. These liabilities carry terms of three to five years and implied interest rates ranging from 7% to 25%. A total amount of $63 in principal was paid on these liabilities during the current fiscal year.

During the quarters ended March 25, 2022, the average interest rate was 3.98% on the Term Loan, and 4.25% on the Revolving Loans.

As of March 25, 2022, the Company's borrowing capacity on the revolving loans under the terms of the Credit Agreement was $35,339, and the Company had approximately $15,866 of available borrowings. In addition to the Credit Agreement, the Company has established unsecured lines of credit that are used from time to time to secure certain performance obligations by the Company.

The Company's borrowings described above approximate fair value at March 25, 2022 and June 30, 2021. If measured at fair value in the financial statements, long-term debt (including the current portion) would be classified as Level 2 in the fair value hierarchy.

The Company is party to an interest rate swap arrangement with Bank of Montreal, with an initial notional amount of $20,000 and a maturity date of March 4, 2026 to hedge the Term Loan. As of March 25, 2022, the notional amount was $14,500. This swap has been designated as a cash flow hedge under ASC 815, Derivatives and Hedging. This swap is included in the disclosures in Note O, Derivative Financial Instruments.

During the fourth quarter of fiscal 2021, the Company designated its euro denominated revolving loan as a net investment hedge to mitigate the risk of variability in its euro denominated net investments in wholly-owned foreign companies. Effective upon the designation, all changes in the fair value of the euro revolver are reported in accumulated other comprehensive loss along with the foreign currency translation adjustments on those foreign investments. This net investment hedge is included in the disclosures in Note O, Derivative Financial Instruments.

K. Shareholders' Equity

The Company, from time to time, makes open market purchases of its common stock under authorizations given to it by the Board of Directors, of which 315.0 shares as of March 25, 2022 remain authorized for purchase. The Company did not make any open market purchases of its shares during the quarters ended March 25, 2022 and March 26, 2021.

The following is a reconciliation of the Company's equity balances for the first three fiscal quarters of 2022 and 2021:

	Twin Disc, Inc. Shareholders' Equity					
	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Non-Controlling Interest	Total Equity
Balance, June 30, 2021	$ 40,972	$ 126,936	$ (22,615)	$ (15,083)	$ 450	$ 130,660
Net (loss) income		1,920			60	1,980
Translation adjustments			(2,014)		76	(1,938)
Benefit plan adjustments, net of tax			384			384
Unrealized gain on cash flow hedge, net of tax			204			204
Compensation expense	625					625
Shares (acquired) issued, net	(432)			141		(291)
Balance, September 24, 2021	41,165	128,856	(24,041)	(14,942)	586	131,624
Net (loss) income		(3,836)			86	(3,750)
Translation adjustments			(1,676)		(25)	(1,701)
Benefit plan adjustments, net of tax			623			623
Unrealized gain on cash flow hedge, net of tax			735			735
Compensation expense	595					595
Shares (acquired) issued, net	(169)			(26)		(195)
Balance, December 31, 2021	$ 41,591	$ 125,020	$ (24,359)	$ (14,968)	$ 647	$ 127,931
Net income		2,231			79	2,310
Translation adjustments			(2,680)		(41)	(2,721)
Benefit plan adjustments, net of tax			505			505
Unrealized loss on cash flow hedge, net of tax			810			810
Compensation expense	620					620
Shares issued (acquired), net	(163)			163		0
Balance, March 25, 2022	$ 42,048	$ 127,251	$ (25,724)	$ (14,805)	$ 685	$ 129,455

	Twin Disc, Inc. Shareholders' Equity					
	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Non-Controlling Interest	Total Equity
Balance, June 30, 2020	$ 42,756	$ 156,655	$ (41,226)	$ (18,796)	$ 569	$ 139,958
Net (loss) income		(3,979)			42	(3,937)
Translation adjustments			3,600		12	3,612
Benefit plan adjustments, net of tax			553			553
Unrealized gain on cash flow hedge, net of tax			75			75
Compensation expense	518					518
Shares (acquired) issued, net	(2,460)			2,236		(224)
Balance, September 25, 2020	40,814	152,676	(36,998)	(16,560)	623	140,555
Net (loss) income		(4,313)			33	(4,280)
Translation adjustments			4,887		12	4,899
Benefit plan adjustments, net of tax			555			555
Unrealized gain on cash flow hedge, net of tax			104			104
Compensation expense	562					562
Shares (acquired) issued, net	(1,458)			1,458		-
Balance, December 25, 2020	39,918	148,363	(31,452)	(15,102)	668	142,395
Net (loss) income		94			72	166
Translation adjustments			(2,970)		(38)	(3,008)
Benefit plan adjustments, net of tax			583			583
Unrealized loss on cash flow hedge, net of tax			193			193
Compensation expense	524					524
Shares issued (acquired), net	4			(4)		-
Balance, March 26, 2021	$ 40,446	$ 148,457	$ (33,646)	$ (15,106)	$ 702	$ 140,853

Reconciliations for the changes in accumulated other comprehensive income (loss), net of tax, by component for the quarters ended March 25, 2022 and March 26, 2021 are as follows:

	Translation Adjustment	Benefit Plan Adjustment	Cash Flow Hedges	Net Investment Hedges
Balance at June 30, 2021	$ 9,192	$ (31,463)	$ (678)	$ 334
Translation adjustment during the quarter	(2,014)	-	-	-
Amounts reclassified from accumulated other comprehensive income	-	384	68	136
Net current period other comprehensive (loss) income	(2,014)	384	68	136
Balance at September 24, 2021	$ 7,178	$ (31,079)	$ (610)	$ 470
Translation adjustment during the quarter	(1,676)	-	-	-
Amounts reclassified from accumulated other comprehensive income	-	623	232	503
Net current period other comprehensive (loss) income	(1,676)	623	232	503
Balance at December 31, 2021	5,502	(30,456)	(378)	973
Translation adjustment during the quarter	(2,680)	-	-	-
Amounts reclassified from accumulated other comprehensive income	-	505	556	254
Net current period other comprehensive (loss) income	(2,680)	505	556	254
Balance at March 25, 2022	$ 2,822	$ (29,951)	$ 178	$ 1,227

	Translation Adjustment	Benefit Plan Adjustment	Cash Flow Hedges
Balance at June 30, 2020	$ 3,454	$ (43,576)	$ (1,104)
Translation adjustment during the quarter	3,600	-	-
Amounts reclassified from accumulated other comprehensive income	-	553	75
Net current period other comprehensive income	3,600	553	75
Balance at September 25, 2020	7,054	(43,023)	(1,029)
Translation adjustment during the quarter	4,887	-	-
Amounts reclassified from accumulated other comprehensive income	-	555	104
Net current period other comprehensive income	4,887	555	104
Balance at December 25, 2020	$ 11,941	$ (42,468)	$ (925)
Translation adjustment during the quarter	(2,970)	-	-
Amounts reclassified from accumulated other comprehensive income	-	583	193
Net current period other comprehensive (loss) income	(2,970)	583	193
Balance at March 26, 2021	$ 8,971	$ (41,885)	$ (732)

Reconciliation for the changes in benefit plan adjustments, net of tax for the quarter ended March 25, 2022 are as follows:

	Amount Reclassified Quarter Ended March 25, 2022	Amount Reclassified Three Quarters Ended March 25, 2022
Changes in benefit plan items		
Actuarial losses	$ 573 (a)	$ 1,707 (a)
Transition asset and prior service benefit	(64) (a)	(191) (a)
Total amortization	509	1,516
Income tax (benefit) expense	4	4
Total reclassification net of tax	$ 505	$ 1,512

Reconciliation for the changes in benefit plan adjustments, net of tax for the quarter ended March 26, 2021 is as follows:

	Amount Reclassified Quarter Ended March 26, 2021	Amount Reclassified Three Quarters Ended March 26, 2021
Changes in benefit plan items		
Actuarial losses	$ 824 (a)	$ 2,410 (a)
Transition asset and prior service benefit	(64) (a)	(190) (a)
Total amortization	760	2,220
Income tax expense	177	529
Total reclassification net of tax	$ 583	$ 1,691

(a) These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note G, "Pension and Other Postretirement Benefit Plans" for further details).

L. Restructuring of Operations

Restructuring expenses

The Company has implemented various restructuring programs in response to unfavorable macroeconomic trends in certain of the Company's markets since the fourth quarter of fiscal 2015. These programs primarily involved the reduction of workforce in several of the Company's manufacturing locations, under a combination of voluntary and involuntary programs. During the fourth quarter of fiscal 2021, the Company undertook a series of steps to accelerate its focus on its core competencies, improve its fixed cost structure, and monetize some of its under-utilized assets.

With regard to its Belgian operations, on June 30, 2021, the Company announced a new phase in its restructuring plans. Under this plan, the Belgian operation's workforce will be reduced by 23 employees. This reduction in force resulted in an initial accrual of $2,200, pertaining to the Company's current estimate for the payment of severance benefits, which is expected to be completed by December 2022. The action was taken to allow the Belgian operation to focus its resources on core manufacturing processes, while allowing for savings on the outsourcing of non-core processes. The Company anticipates annual pre-tax savings upon completion of the restructuring of approximately $1,600.

In the second quarter, the Company and the union representing certain of the employees affected by the restructuring of the Belgian operations came to an agreement on a final settlement amount of $3,200. The Company incurred an additional $1,000 in restructuring charges during the second quarter of fiscal 2022.

Total restructuring charges relating to streamlining operations totaled to $303 and $251 in the quarters ending March 25, 2022 and March 26, 2021, respectively. Total restructuring charges relating to streamlining operations totaled to $1,542 and $777 in the three quarters ending March 25, 2022 and March 26, 2021, respectively. Restructuring activities since June 2015 have resulted in the elimination of 259 full-time employees in the manufacturing segment. Accumulated costs to date under these programs within the manufacturing segment through March 25, 2022 were $16,807.

The following is a roll-forward of restructuring activity:

Accrued restructuring liability, June 30, 2021	$	2,352
Additions		1,542
Payments, adjustments and write-offs during the year		(2,028)
Accrued restructuring liability, March 25, 2022	$	1,866

Assets held for sale

To improve its fixed cost structure and monetize some of its under-utilized assets, the Company commenced the active marketing of three of its real estate properties, namely, its corporate headquarters in Racine, its propeller machining plant and office in Switzerland, and a spare warehouse in Italy during the fourth quarter of fiscal 2021.

During the second quarter of fiscal 2022, the Company completed the sale of its propeller machining plant and office in Switzerland and received $9,138 in proceeds, net of fees and local taxes and recorded a gain of $2,939 in other operating income in the condensed consolidated statements of operations and comprehensive income.

During the third quarter of fiscal 2022, the Company accepted an offer for the sale of its corporate headquarters building in Racine for a purchase price of $3,250. The agreement contains a lease back period for up to 18 months with monthly lease payments of approximately $25. The sale is expected to be finalized by the first quarter of fiscal year 2023. During the third quarter fiscal 2022, the company recorded additional selling charges associated with the sale of approximately $230, reducing assets held for sale by the same amount.

Additionally, during the third quarter of fiscal 2022, the Company accepted an offer to sell its spare warehouse in Italy for a purchase price of 275 euro (approximately $305). The sale was finalized on April 20, 2022; the agreement contains a lease back period for two years with minimal lease payments. In the fourth quarter of fiscal 2022, the Company plans to record a gain on this sale of approximately $184 in other operating income in the condensed consolidated statements of operations and comprehensive income.

M. Earnings Per Share

The Company calculates basic earnings per share based upon the weighted average number of common shares outstanding during the period, while the calculation of diluted earnings per share includes the dilutive effect of potential common shares outstanding during the period. The calculation of diluted earnings per share excludes all potential common shares if their inclusion would have an anti-dilutive effect. Certain restricted stock award recipients have a non-forfeitable right to receive dividends declared by the Company, and are therefore included in computing earnings per share pursuant to the two-class method.

The components of basic and diluted earnings per share were as follows:

	For the Quarter Ended		For the Three Quarters Ended	
	March 25, 2022	March 26, 2021	March 25, 2022	March 26, 2021
Basic:				
Net income (loss)	$ 2,310	$ 166	$ 539	$ (8,051)
Less: Net earnings attributable to noncontrolling interest	(79)	(72)	(223)	(147)
Less: Undistributed earnings attributable to unvested shares	-	-	-	-
Net income (loss) available to Twin Disc shareholders	2,231	94	316	(8,198)
Weighted average shares outstanding - basic	13,397	13,269	13,339	13,240
Basic Loss Per Share:				
Net earnings (loss) per share - basic	**$ 0.17**	**$ 0.01**	**$ 0.02**	**$ (0.62)**
Diluted:				
Net income (loss)	$ 2,310	$ 166	$ 539	$ (8,051)
Less: Net earnings attributable to noncontrolling interest	(79)	(72)	(223)	(147)
Less: Undistributed earnings attributable to unvested shares	-	-	-	-
Net income (loss) available to Twin Disc shareholders	2,231	94	316	(8,198)
Weighted average shares outstanding - basic	13,397	13,269	13,339	13,240
Effect of dilutive stock awards	60	26	34	-
Weighted average shares outstanding - diluted	13,457	13,295	13,373	13,240
Diluted Income (Loss) Per Share:				
Net earnings (loss) per share - diluted	**$ 0.17**	**$ 0.01**	**$ 0.02**	**$ (0.62)**

The following potential common shares were excluded from diluted EPS for the quarter and three quarters ended March 26, 2021 as the Company reported a net loss: 433.1 related to the Company's unvested PSAs, 377.5 related to the Company's unvested RS awards, and 34.8 related to the Company's unvested RSUs.

N. Lease Liabilities

The Company leases certain office and warehouse space, as well as production and office equipment.

The Company determines if an arrangement is a lease at contract inception. The lease term begins upon lease commencement, which is when the Company takes possession of the asset, and may include options to extend or terminate the lease when it is reasonably certain that such options will be exercised. As its lease agreements typically do not provide an implicit rate, the Company primarily uses an incremental borrowing rate based upon the information available at lease commencement. In determining the incremental borrowing rate, the Company considers its current borrowing rate, the term of the lease, and the economic environments where the lease activity is concentrated.

The components of lease expense were as follows:

	For the Quarter Ended		For the Three Quarters Ended	
	March 25, 2022	March 26, 2021	March 25, 2022	March 26, 2021
Finance lease cost:				
Amortization of right-of-use assets	$ 162	$ 154	$ 492	$ 421
Interest on lease liabilities	68	73	211	201
Operating lease cost	800	717	2,190	2,097
Short-term lease cost	13	17	53	29
Variable lease cost	46	36	127	118
Total lease cost	1,089	997	3,073	2,866
Less: Sublease income	(19)	(23)	(57)	(135)
Net lease cost	$ 1,070	$ 974	$ 3,016	$ 2,731

Other information related to leases was as follows:

	For the Quarter Ended		For the Three Quarters Ended	
	March 25, 2022	March 26, 2021	March 25, 2022	March 26, 2021
Cash paid for amounts included in the measurement of lease liabilities:				
Operating cash flows from operating leases	$ 808	$ 747	$ 2,281	$ 2,275
Operating cash flows from finance leases	207	125	623	343
Financing cash flows from finance leases	68	73	211	201
Right-of-use-assets obtained in exchange for lease obligations:				
Operating leases	695	19	1,091	125
Finance leases	-	86	307	4,757
Weighted average remaining lease term (years):				
Operating leases			8.8	10.5
Finance lease			11.4	12.2
Weighted average discount rate:				
Operating leases			7.1%	7.4%
Finance leases			5.1%	5.2%

Approximate future minimum rental commitments under non-cancellable leases as of March 25, 2022 were as follows:

	Operating Leases	Finance Leases
2022	$ 794	$ 204
2023	2,981	807
2024	2,489	772
2025	1,625	555
2026	1,488	492
Thereafter	9,458	4,263
Total future lease payments	18,835	7,093
Less: Amount representing interest	(5,124)	(1,994)
Present value of future payments	$ 13,711	$ 5,099

The following table provides a summary of leases recorded on the condensed consolidated balance sheet.

	Balance Sheet Location	March 25, 2022	June 30, 2021
Lease Assets			
Operating lease right-of-use assets	Right-of-use assets operating leases	$ 13,692	$ 14,736
Finance lease right-of-use assets	Property, plant and equipment, net	4,904	5,244
Lease Liabilities			
Operating lease liabilities	Accrued liabilities	$ 2,168	$ 1,870
Operating lease liabilities	Lease obligations	11,543	12,887
Finance lease liabilities	Accrued liabilities	567	541
Finance lease liabilities	Other long-term liabilities	4,532	4,836

O. Derivative Financial Instruments

From time to time, the Company enters into derivative instruments to manage risks relating to interest rate and foreign exchange rate volatility. The Company does not purchase, hold or sell derivative financial instruments for trading purposes. The Company's practice is to terminate derivative transactions if the underlying asset or liability matures or is sold or terminated, or if it determines the underlying forecasted transaction is no longer probable of occurring.

The Company reports all derivative instruments on its consolidated balance sheets at fair value and establishes criteria for designation and effectiveness of transactions entered into for hedging purposes.

Interest Rate Swap Contracts

The Company has one outstanding interest rate swap contract as of March 25, 2022, with a notional amount of $14,500. It has been designated as a cash flow hedge in accordance with ASC 815, Derivatives and Hedging.

The primary purpose of the Company's cash flow hedging activities is to manage the potential changes in value associated with interest payments on the Company's SOFR-based (formerly LIBOR-based) indebtedness. The Company records gains and losses on interest rate swap contracts qualifying as cash flow hedges in accumulated other comprehensive loss to the extent that these hedges are effective and until the Company recognizes the underlying transactions in net earnings, at which time these gains and losses are recognized in interest expense on its consolidated statements of operations and comprehensive income. Cash flows from derivative financial instruments are classified as cash flows from financing activities on the consolidated statements of cash flows. These contracts generally have original maturities of greater than twelve months.

Net unrealized after-tax gain (loss) related to cash flow hedging activities that were included in accumulated other comprehensive income were $178 and $(678) as of March 25, 2022, and June 30, 2021, respectively. The unrealized amounts in accumulated other comprehensive loss will fluctuate based on changes in the fair value of open contracts during each reporting period.

The Company estimates that $98 of net unrealized losses related to cash flow hedging activities included in accumulated other comprehensive loss will be reclassified into earnings within the next twelve months.

Derivatives Designated as Net Investment Hedges

The Company is exposed to foreign currency exchange risk related to its investment in net assets in foreign countries. As discussed in Note J, Long-term Debt, during the fourth quarter of fiscal 2021, the Company designated its euro denominated Revolving Loan, with a notional amount of €6,500, as a net investment hedge to mitigate the risk of variability in its euro denominated net investments in wholly-owned foreign subsidiaries. All changes in the fair value of the euro revolver were then recorded in accumulated other comprehensive income along with the foreign currency translation adjustments on those foreign investments. Net unrealized after-tax gain related to net investment hedging activities that were included in accumulated other comprehensive income were $1,227 and $334 as of March 25, 2022 and June 30, 2021, respectively.

Fair Value of Derivative Instruments

The fair value of derivative instruments included in the condensed consolidated balance sheets were as follows:

	Balance Sheet Location	March 25, 2022	June 30, 2021
Derivative designated as hedge:			
Interest rate swap	Accrued liabilities	$ 100	$ 346
Interest rate swap	Other long-term liabilities	$ -	$ 542

The impact of the Company's derivative instruments on the condensed consolidated statements of operations and comprehensive (loss) income for the quarter and three quarters ended March 25, 2022 and March 26, 2021, respectively, was as follows:

	Statement of Comprehensive Income Location	For the Quarter Ended March 25, 2022	For the Quarter Ended March 26, 2021	For the Three Quarters Ended March 25, 2022	For the Three Quarters Ended March 26, 2021
Derivative designated as hedge:					
Interest rate swap	Interest expense	$ 81	$ 98	$ 268	$ 297
Interest rate swap	Unrealized gain (loss) on cash flow hedge	556	193	855	372
Net investment hedge	Unrealized gain on hedges	254	-	893	-
Derivatives not designated as hedges:					
Foreign currency forward contracts	Other income (expense), net	$ -	$ -	$ -	$ (13)

Item 2. Management Discussion and Analysis

In the financial review that follows, we discuss our results of operations, financial condition and certain other information. This discussion should be read in conjunction with our consolidated financial statements as of March 25, 2022, and related notes, as reported in Item 1 of this Quarterly Report.

Some of the statements in this Quarterly Report on Form 10-Q are "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements include the Company's description of plans and objectives for future operations and assumptions behind those plans. The words "anticipates," "believes," "intends," "estimates," and "expects," or similar anticipatory expressions, usually identify forward-looking statements. In addition, goals established by the Company should not be viewed as guarantees or promises of future performance. There can be no assurance the Company will be successful in achieving its goals.

In addition to the assumptions and information referred to specifically in the forward-looking statements, other factors, including but not limited to those factors discussed under Item 1A, Risk Factors, of the Company's Annual Report filed on Form 10-K for June 30, 2021, as supplemented in this Quarterly Report, could cause actual results to be materially different from what is expressed or implied in any forward-looking statement.

Results of Operations

(In thousands)

	Quarter Ended March 25, 2022	% of Net Sales	Quarter Ended March 26, 2021	% of Net Sales	Three Quarters Ended March 25, 2022	% of Net Sales	Three Quarters Ended March 26, 2021	% of Net Sales
Net sales	$ 59,289		$ 57,640		$ 166,939		$ 152,377	
Cost of goods sold	41,598		43,678		122,319		119,835	
Gross profit	17,691	29.8%	13,962	24.2%	44,620	26.7%	32,542	21.4%
Marketing, engineering and administrative expenses	14,396	24.3%	13,196	22.9%	42,753	25.6%	39,000	25.6%
Restructuring of operations	303	0.5%	251	0.4%	1,542	0.9%	777	0.5%
Other operating income	(63)	-0.1%		0.0%	(2,957)	-1.8%		0.0%
Income (loss) from operations	$ 3,055	5.2%	$ 515	0.9%	$ 3,282	2.0%	$ (7,235)	-4.7%

Comparison of the Third Quarter of Fiscal 2022 with the Third Quarter of Fiscal 2021

Net sales for the third quarter increased 2.9%, or $1.6 million, to $59.3 million from $57.6 million in the same quarter a year ago. The Company continues to experience improving market conditions across most markets served, although demand for new units in the North American oil and gas market has not shown meaningful improvement. The Company's ability to ship product was significantly hampered by a variety of supply chain challenges. These include supplier capacity constraints, extended supplier lead times and a global shortage of electronic components. The supply chain disruptions had a negative impact on fiscal 2022 third quarter net sales of approximately $7 million - $10 million. Global sales of industrial products improved 45.0% from the prior year and off-highway transmission sales increased 5.4%, while sales of marine and propulsion products decreased by 1.7% compared with the prior year third quarter. The North American region enjoyed the most significant sales improvement ($4.2 million or 26.4%) due to generally improving market conditions and increased aftermarket demand in the North American energy market. The European region saw sales decrease ($2.4 million or 9.9%), with project delays and supply chain challenges hampering volume. Similarly, sales into the Asia Pacific region decreased ($2.0 million or 13.8%) due to the supply chain challenges noted above. Currency translation had an unfavorable impact on third quarter fiscal 2022 sales compared to the third quarter of the prior year totaling $3.0 million primarily due to the weakening of the euro against the U.S. dollar.

Sales at our manufacturing segment increased 8.2%, or $4.3 million, versus the same quarter last year. The U.S. manufacturing operations experienced a 25.9%, or $6.0 million, increase in sales versus the third fiscal quarter of 2021, with recovering markets following the significant impact of the COVID-19 pandemic, partially offset by the supply chain challenges noted above. The Company’s operation in the Netherlands was up $0.5 million (3.8%) compared to the third fiscal quarter of 2021, with many boat construction projects being delayed due to the COVID-19 crisis. The Company’s Belgian operation saw a decrease compared to the prior year third quarter (24.2% or $1.7 million), with supply chain challenges combined with a negative translation impact. The Company’s Italian manufacturing operations, also impacted by supply chain disruptions across their product offering, were down $0.4 million (5.9%) compared to the third quarter of fiscal 2021. The Company’s Swiss manufacturing operation, which supplies customized propellers for the global mega yacht and patrol boat markets, was down $0.2 million (15.5%) compared to the prior year third quarter.

Our distribution segment experienced a decrease in sales of $2.6 million (9.8%) compared to the third quarter of fiscal 2021. Despite continued strong demand, the Company’s Asian distribution operations in Singapore, China and Japan were down 6.4% from the prior year due to lack of product deliveries from the manufacturing entities noted above. The Company’s North America distribution operation saw a decrease of 5.0%, while the Company’s European distribution operation saw flat revenue in the quarter. The Company’s distribution operation in Australia, which provides boat accessories, propulsion and marine transmission systems for the pleasure craft market, saw continued strong demand, but reported a revenue decline (25.6% decrease from the prior year third fiscal quarter), due to supply chain challenges, primarily electronic components.

Gross profit as a percentage of sales for the third quarter of fiscal 2022 improved to 29.8%, compared to 24.2% for the same period last year. The current quarter result reflects the benefit of improved volume for the quarter ($0.4 million) and a favorable mix impact ($2.2 million – primarily due to strong aftermarket and global energy demand), along with the positive impact of pricing actions taken early in the quarter. We remain sensitive to the inflationary environment we are currently operating in, and are prepared to react with additional pricing actions as required.

For the fiscal 2022 third quarter, marketing, engineering and administrative (“ME&A”) expenses, as a percentage of sales, were 24.3%, compared to 22.9% for the fiscal 2021 third quarter. ME&A expenses increased $1.2 million (9.1%) versus the same period last fiscal year. The increase in ME&A spending for the quarter was comprised of the accrual for the global bonus program ($0.8 million), professional fees ($0.3 million), marketing activities ($0.1 million), increased travel costs ($0.2 million) and other net spending increases of $0.9 million (largely inflation). These increases were partially offset by a Dutch COVID-19 subsidy recorded in the quarter, which reduced ME&A expense by $0.7 million, and a currency driven reduction of $0.4 million.

The Company incurred restructuring charges of approximately $0.3 million during the third quarter of fiscal 2022, primarily associated with an adjustment to the carrying value of an asset held for sale. The Company has accepted an offer to sell the corporate headquarters building for a price slightly below previous estimates.

Interest expense was down slightly to $0.5 million for the third fiscal quarter of 2022 compared to $0.6 million for the prior year third fiscal quarter.

Other income of $0.5 million for the third fiscal quarter was primarily attributable to translation gains related to the Company’s euro-denominated liabilities.

The fiscal 2022 third quarter effective tax rate was negative 24.6% compared to 64.3% in the prior fiscal year third quarter. The current year rate was impacted by the fact that the domestic entity recognized a full valuation allowance in the fourth quarter of fiscal 2021, resulting in no tax benefits being recognized for current domestic losses.

Comparison of the First Three Quarters of Fiscal 2022 with the First Three Quarters of Fiscal 2021

Net sales for the first three quarters increased 9.6%, or $14.6 million, to $166.9 million from $152.4 million in the same period a year ago. The Company experienced a broad-based recovery in demand across most of the markets served, as the impact of the COVID-19 crisis on the Company’s global markets begins to subside. Global sales of industrial products improved by 34.8% from the prior year, while off-highway transmission sales increased by 6.1% and marine and propulsion grew by 5.8%. The North American region experienced the most significant sales improvement ($11.3 million or 25.0%) due to a broad-based market recovery and extremely strong aftermarket demand in the North American oil and gas segment. The North American region improved from 30% of total sales in the prior year first three quarters to 34% in the fiscal 2022 comparable period. The European region saw a moderate decline ($1.3 million and 2.2%), with strengthening market conditions more than offset by supply chain challenges. Sales into the Asia Pacific region decreased ($1.1 million or 2.8%), due to the noted supply chain challenges despite stable demand for oil and gas units in China and an improving marine market in Australia. Currency translation had an unfavorable impact on the first three quarters of fiscal 2022 sales compared to the same period of the prior year totaling $3.5 million primarily due to the weakening of the euro against the U.S. dollar.

Sales at our manufacturing segment increased 11.1%, or $14.8 million, versus the first three quarters of last fiscal year. The U.S. manufacturing operation experienced a 24.0%, or $14.7 million, increase in sales versus the first three quarters of fiscal 2021, with market recovery seen across all product lines, hampered somewhat by supply chain challenges, during the recent nine-month period. The Company's operation in the Netherlands was essentially flat (up 0.5% or $0.2 million) compared to the first three quarters of fiscal 2021, with many boat construction projects delayed due to the COVID-19 crisis. The Company's Belgian operation also saw a decrease compared to the prior year (11.6% or $2.0 million), with supply chain difficulties offsetting improving market conditions. The Company's Italian manufacturing operations were up $1.3 million (7.5%) compared to the first three quarters of fiscal 2021, with most of the improvement coming in the second quarter thanks to a resurgent pleasure craft market. The Company's Swiss manufacturing operation, which supplies customized propellers for the global mega yacht and patrol boat markets, was up $0.6 million (20.0%) compared to the prior year comparable period.

Our distribution segment experienced an increase in sales of $0.7 million (1.0%) compared to the first three quarters of fiscal 2021. The Company's Asian distribution operations in Singapore, China and Japan were down 5.4% from the prior year as supply chain challenges during the recent nine month period delayed delivery from the manufacturing operations. The Company's North America distribution operation saw an increase of 2.0% on an improving overall market demand. The Company's distribution operation in Australia, which provides boat accessories, propulsion and marine transmission systems for the pleasure craft market, saw strong growth (13.6% increase from the prior year first three quarters), on improving pleasure craft marine market trends in the region. The Company's European distribution operation saw a slight increase of $0.2 million (1.4%) on improving market conditions.

Gross profit as a percentage of sales for the first three quarters of fiscal 2022 improved to 26.7%, compared to 21.4% for the same period last year. The improvement is attributable to increased volume ($3.1 million), a more favorable mix ($6.5 million – primarily due to increased aftermarket volume), the net positive impact of government subsidies ($1.4 million) and favorable pricing and cost reduction actions ($1.1 million). The Company was able to offset significant inflationary cost increases in the first three quarters with pricing actions and targeted cost reduction efforts.

For the fiscal 2022 first three quarters, marketing, engineering and administrative ("ME&A") expenses, as a percentage of sales, were 25.6%, compared to 25.6% for the fiscal 2021 comparable period. ME&A expenses increased $3.8 million (9.6%) versus the same period last fiscal year. The increase in ME&A spending for the first three quarters was comprised of increases to salaries and benefits ($0.7 million), global bonus expense ($2.0 million), professional fees ($0.7 million), marketing expenses ($0.3 million), business insurance ($0.2 million), corporate travel ($0.4 million) and other net spending increases ($1.7 million, largely inflation). These increases were partially offset by COVID-19 subsidies, which reduced ME&A expense by $1.8 million and a currency driven reduction of $0.4 million.

The Company incurred restructuring charges of approximately $1.5 million during the first three quarters of fiscal 2022, primarily associated with final negotiated settlement related to the Belgian restructuring program announced in June 2021 ($1.2 million). The total cost of this program is now estimated at $3.2 million, and the Company anticipated annual pre-tax savings of approximately $1.6 million upon completion of this program. The Company continues to focus on actively managing its cost structure and reducing fixed costs in light of the ongoing market challenges.

Interest expense was down slightly from the prior year comparable period, reflecting slightly lower borrowing levels and consistent average interest rates.

Other income of $0.6 million for the first three fiscal quarters was primarily attributable to translation gains related to the Company's euro denominated liabilities.

The effective income tax rate for the first three quarters of fiscal 2022 was 76.5% compared to 28.9% for the comparable period in fiscal 2021. The current year rate was impacted by the fact that the domestic entity recognized a full valuation allowance in the fourth quarter of fiscal 2021, resulting in no tax benefits being recognized for current domestic losses.

Financial Condition, Liquidity and Capital Resources

Comparison between March 25, 2022 and June 30, 2021

As of March 25, 2022, the Company had net working capital of $116.4 million, which represents an increase of $3.0 million, or 2.7%, from the net working capital of $113.4 million as of June 30, 2021.

Cash increased $0.5 million to $12.8 million as of March 25, 2022, versus $12.3 million as of June 30, 2021. The majority of the cash as of March 25, 2022, is at the Company's overseas operations in Europe ($4.9 million) and Asia-Pacific ($6.2 million).

Trade receivables of $39.0 million were down just $0.5 million, or approximately 1.3%, when compared to last fiscal year-end. The impact of foreign currency translation was to decrease accounts receivable by $1.2 million versus June 30, 2021. As a percent of sales, trade receivables finished at 65.7% in the third quarter of fiscal 2022 compared to 54.3% for the comparable period in fiscal 2021 and 59.6% for the fourth quarter of fiscal 2021.

Inventories increased by $16.1 million, or 14.0%, versus June 30, 2021 to $131.1 million. The impact of foreign currency translation was to decrease inventories by $3.4 million versus June 30, 2021. The remaining increase was seen primarily at the Company's operations in North America ($10.5 million), the Netherlands ($2.7 million) and Australia ($5.2 million). These increases were primarily driven by an imbalance in the supply chain, resulting in a growth in past due backlog and excess inventory waiting for missing components to finish assembly. On a consolidated basis, as of March 25, 2022, the Company's backlog of orders to be shipped over the next six months approximates $108.9 million, compared to $70.3 million at June 30, 2021 and $71.4 million at March 26, 2021. As a percentage of six-month backlog, inventory has decreased from 163% at June 30, 2021 to 120% at March 25, 2022.

Net property, plant and equipment decreased $2.7 million (6.0%) to $42.8 million versus $45.5 million at June 30, 2021. The Company spent $2.4 million on capital equipment in the first three quarters, offset by an unfavorable exchange impact ($0.8 million) and depreciation ($4.9 million). The capital spending in the first three quarters reflects primarily maintenance capital. In total, the Company expects to invest between $4 and $6 million in capital assets in fiscal 2022. The Company continues to review its capital plans based on overall market conditions and availability of capital, and may make changes to its capital plans accordingly. The Company's capital program is focused on modernizing key core manufacturing, assembly and testing processes and improving efficiencies at its facilities around the world.

Accounts payable as of March 25, 2022, of $34.2 million was up $3.2 million, or 10.3%, from June 30, 2021. The impact of foreign currency translation was to reduce accounts payable by $1.1 million versus June 30, 2021. The remaining increase is primarily related to the increased purchasing activities in light of increased demand in the quarter.

Total borrowings and long-term debt as of March 25, 2022, increased $2.0 million to $34.1 million versus $32.1 million at June 30, 2021. This increase is primarily attributable to the increase in inventory driven by supply chain imbalances, partially offset by the repatriation of cash from Switzerland following the sale of our Swiss facility in the first fiscal quarter. During the first nine months, the Company reported negative free cash flow of $9.6 million (defined as operating cash flow less acquisitions of fixed assets), which excludes the sale of the Swiss facility for $9.1 million. The Company ended the quarter with total debt, net of cash, of $21.2 million, compared to $19.7 million at June 30, 2021, for a net increase of $1.5 million.

Total equity decreased $1.2 million, or 0.9%, to $129.5 million as of March 25, 2022. The net profit during the first three quarters increased equity by $0.5 million, offset by an unfavorable foreign currency translation of $6.4 million. The net change in common stock and treasury stock resulting from the accounting for stock-based compensation increased equity by $1.4 million. The net remaining increase in equity of $3.3 million primarily represents the amortization of net actuarial loss and prior service cost on the Company's defined benefit pension plans, along with the unrealized gain on cash flow hedges.

On June 29, 2018, the Company entered into a Credit Agreement (the “Credit Agreement”) with BMO Harris Bank N.A. (“BMO”) that provided for the assignment and assumption of the previously existing loans between the Company and Bank of Montreal (the “2016 Credit Agreement”) and subsequent amendments into a term loan (the “Term Loan”) and revolving credit loans (each a “Revolving Loan” and, collectively, the “Revolving Loans,” and, together with the Term Loan, the “Loans”). Pursuant to the Credit Agreement, BMO agreed to make the Term Loan to the Company in a principal amount not to exceed $35.0 million and the Company may, from time to time prior to the maturity date, enter into Revolving Loans in amounts not to exceed, in the aggregate, $50.0 million (the “Revolving Credit Commitment”). The Credit Agreement also allows the Company to obtain Letters of Credit from BMO, which if drawn upon by the beneficiary thereof and paid by BMO, would become Revolving Loans. Under the Credit Agreement, the Company may not pay cash dividends on its common stock in excess of $3.0 million in any fiscal year.

On March 4, 2019, the Company entered into a second amendment (the “Second Amendment”) to the Credit Agreement. The Second Amendment reduced the principal amount of the term loan commitment under the Credit Agreement from $35.0 million to $20.0 million. In connection with the Second Amendment, the Company issued an amended and restated term note in the amount of $20.0 million to the Bank, which amended the original $35.0 million note provided under the Credit Agreement.

Prior to entering into the Second Amendment, the outstanding principal amount of the term loan (the “Term Loan”) under the Credit Agreement was $10.8 million. On the date of the Second Amendment, the Bank made an additional advance on the Term Loan to the Company in the amount of $9.2 million. The Second Amendment also extended the maturity date of the Term Loan from January 2, 2020 to March 4, 2026, and added a requirement that the Company make principal installments of $0.5 million per quarter starting with the quarter ending June 30, 2019.

The Second Amendment also reduced the applicable margin for purposes of determining the interest rate applicable to the Term Loan. Previously, the applicable margin was 3.00%, which was added to the Monthly Reset LIBOR Rate or the Adjusted LIBOR, as applicable. Under the Second Amendment, the applicable margin was between 1.375% and 2.375%, depending on the Company’s total funded debt to EBITDA ratio.

The Second Amendment also adjusted certain financial covenants made by the Company under the Credit Agreement. Specifically, the Company covenanted (i) not to allow its total funded debt to EBITDA ratio to be greater than 3.00 to 1.00 (the cap had previously been 3.50 to 1.00 for quarters ending on or before September 30, 2019 and 3.25 to 1.00 for quarters ending on or about December 31, 2019 through September 30, 2020), and (ii) that its tangible net worth will not be less than $100.0 million plus 50% of net income for each fiscal year ending on and after June 30, 2019 for which net income is a positive number (the $100.0 million figure had previously been $70.0 million).

On January 28, 2020, the Company entered into a third amendment (the “Third Amendment”) to the Credit Agreement. The Third Amendment restated the financial covenant provisions related to the maximum allowable ratio of total funded debt to EBITDA from 3.00 to 1.00 to 4.00 to 1.00 for the quarter ended December 27, 2019, 5.00 to 1.00 for the quarter ending March 27, 2020, 4.00 to 1.00 for the quarter ending June 30, 2020, 3.50 to 1.00 for the quarter ending September 25, 2020, and 3.00 to 1.00 for quarters ending on or after December 25, 2020. For purposes of determining EBITDA, the Third Amendment added back extraordinary expenses (not to exceed $3.9 million) related to the previously reported isolated product performance issue on one of the Company’s oil and gas transmission models at certain installations. Under the Third Amendment, the applicable margin for revolving loans, letters of credit, and term loans was between 1.25% and 3.375%, depending on the Company’s total funded debt to EBITDA ratio.

On July 22, 2020, the Company entered into a fifth amendment (the “Fifth Amendment”) to the Credit Agreement that amends the Credit Agreement dated as of June 29, 2018, as amended, between the Company and BMO. The Fifth Amendment reduced BMO’s Revolving Credit Commitment from $50.0 million to $45.0 million. The Fifth Amendment also gives the Company the option to make interest-only payments on the Term Loan for quarterly payments occurring on September 30, 2020 and December 31, 2020, and limits the Company’s Capital Expenditures for the fiscal year ending June 30, 2021 to $10.0 million.

The Fifth Amendment provides the Company with relief from its Total Funded Debt to EBITDA ratio financial covenant under the Credit Agreement through (and including) the earlier of June 30, 2021 or a date selected by the Company. During the financial covenant relief period:

- The “Applicable Margin” to be applied to Revolving Loans, the Term Loan, and the Commitment/Facility Fee will be increased to 3.25%, 3.875%, and 0.20%, respectively.

- The Company may not make certain restricted payments (specifically, cash dividends, distributions, purchases, redemptions or other acquisitions of or with respect to shares of its common stock or other common equity interests).

- The Company must maintain liquidity (as defined in the Fifth Amendment) of at least $15.0 million.

- The Company must maintain minimum EBITDA of at least (1) $1.0 million for the fiscal quarter ending June 30, 2020 and the two fiscal quarters ending on or about September 30, 2020; (2) $2.5 million for the three fiscal quarters ending on or about December 31, 2020; (3) $6.0 million for the four fiscal quarters ending on or about March 31, 2021; and (4) $10.0 million for the four fiscal quarters ending June 30, 2021.

For purposes of the minimum EBITDA covenant and the Total Funded Debt to EBITDA ratio, the Fifth Amendment clarified that EBITDA shall exclude any gain that is realized on the forgiveness of the Small Business Administration Paycheck Protection Program loan that the Company previously received.

The Fifth Amendment also changed the definition of “LIBOR” (used in calculating interest on Eurodollar Loans), “Monthly Reset LIBOR Rate” (used in calculating interest on LIBOR Loans), and “LIBOR Quoted Rate” (used in the definition of “Base Rate,” which is used in calculating interest on Letters of Credit that are drawn upon and not timely reimbursed).

The Company also entered into a Deposit Account Control Agreement with the Bank, reflecting the Bank’s security interest in deposit accounts the Company maintains with the Bank. Under the Fifth Amendment, the Bank may not provide a notice of exclusive control of a deposit account (thereby obtaining exclusive control of the account) prior to the occurrence or existence of a Default or an Event of Default under the Credit Agreement or otherwise upon the occurrence or existence of an event or condition that would, but for the passage of time or the giving of notice, constitute a Default or an Event of Default under the Credit Agreement.

On January 27, 2021, the Company entered into a Forbearance Agreement and Amendment No. 6 to the Credit Agreement (the “Forbearance Agreement”) that further amended the Credit Agreement.

The Company entered into the Forbearance Agreement because the Company was not in compliance with its financial covenant to maintain a minimum EBITDA of at least $2.5 million for the three fiscal quarters ended as of December 25, 2020. In the Forbearance Agreement, the Bank has agreed to forbear from exercising its rights and remedies against the Company under the Credit Agreement with respect to the Company’s noncompliance with the minimum EBITDA covenant during the period (the “Forbearance Period”) commencing January 27, 2021 and ending on the earlier of (i) September 30, 2021, and (ii) the date on which a default under the Forbearance Agreement or Credit Agreement occurs. During the Forbearance Period, the Bank may continue to honor requests of the Company for draws on the revolving note provided by the Bank under the Credit Agreement, except that the revolving credit commitment is reduced from $45.0 million to $42.5 million during the Forbearance Period.

The Forbearance Agreement also added to the Company’s financial reporting requirements under the Credit Agreement by requiring the Company to provide the Bank with monthly forecasts of the Company’s financial statements, and monthly reports on the Company’s six-month backlog.

On September 30, 2021, the Company entered into a First Amended and Restated Forbearance Agreement and Amendment No. 7 to Credit Agreement (the “Amended and Restated Forbearance Agreement”) that amends the Credit Agreement dated as of June 29, 2018, as amended between the Company and the Bank.

The Amended and Restated Forbearance Agreement extended the Forbearance Period through February 28, 2022, or if earlier, through the date on which a default under the Amended and Restated Forbearance Agreement or Credit Agreement occurs. During the extended Forbearance Period, the Bank will continue to forbear from exercising its rights and remedies against the Company under the Credit Agreement with respect to the Company’s noncompliance with its minimum EBITDA covenants. The Amended and Restated Forbearance Agreement also made certain adjustments to the Credit Agreement, including:

- Permitting the Company to sell its manufacturing facility in Novazzano, Switzerland for a gross sales price of approximately $10 million, resulting in Net Cash Proceeds of approximately $8.7 million (the “Rolla Disposition”).
- Requiring the Company to promptly repatriate approximately $7 million of the Net Cash Proceeds from the Rolla Disposition (the “Rolla Repatriation”), and to apply $1 million of such Net Cash Proceeds to the Term Loan and the remainder to the revolving Loans under the Credit Agreement.

- Upon completion of the Rolla Repatriation: (1) reducing the portion of the Borrowing Base that is based on Eligible Inventory from the lesser of $35 million or 50% of the value of Eligible Inventory to the lesser of $30 million or 50% of the value of Eligible Inventory; and (2) reducing the Revolving Credit Commitment from a maximum of $42.5 million to a maximum of $40 million.

On February 28, 2022, the Company entered into a Second Amended and Restated Forbearance Agreement and Amendment No. 8 to Credit Agreement (the "Second Amended and Restated Forbearance Agreement") that amends the Credit Agreement dated as of June 29, 2018, as amended between the Company and the Bank.

The Second Amended and Restated Forbearance Agreement extends the Forbearance Period through June 30, 2022, or if earlier, through the date on which a default under the Amended and Restated Forbearance Agreement or Credit Agreement occurs. During the extended Forbearance Period, the Bank will continue to forbear from exercising its rights and remedies against the Company under the Credit Agreement with respect to the Company's noncompliance with its minimum EBITDA covenants. The Second Amended and Restated Forbearance Agreement also makes certain adjustments to the Credit Agreement, including:

- Reducing the portion of the Borrowing Base that is based on Eligible Inventory from the lesser of $35,000,000 or 50% of the value of Eligible Inventory to the lesser of $30,000,000 or 50% of the value of Eligible Inventory. This change was already in effect under the terms of the Amended and Restated Forbearance Agreement, due to the Company's previously reported sale of its manufacturing facility in Novazzano, Switzerland for a gross sales price of approximately $10,000,000, resulting in Net Cash Proceeds (as defined in the Amended and Restated Forbearance Agreement) of approximately $8,700,000 (the "Rolla Disposition") and repatriation of approximately $7,000,000 of those Net Cash Proceeds (the "Rolla Repatriation").

- Reducing the Revolving Credit Commitment from a maximum of $42,500,000 to a maximum of $40,000,000. This change was also already in effect under the terms of the Amended and Restated Forbearance Agreement due to the Rolla Disposition and Rolla Repatriation.

The Company also executed a Third Amended and Restated Revolving Note with the Bank, reflecting the maximum Revolving Credit Commitment of $40,000,000.

When the Forbearance Period ends, the Bank's forbearance under the Forbearance Agreement will cease, and the Company is subject to the Total Funded Debt to EBITDA ratio financial covenant of 3.00 to 1.00. Further, upon an event of default and upon notice from the Bank, the Company's obligations under the Loan Documents would be accelerated and become due at the default rate, and the Bank may exercise its rights and remedies under the Credit Agreement for any occurrence and continuation of default under the Credit Agreement.

For the quarter ended March 25, 2022, as a result of the Forbearance Agreement, the Company was not required to meet the minimum EBITDA financial covenant. The Company expects to be in compliance with the terms of the Credit Agreement following the forbearance period, and therefore continues to classify its debt as long term.

The Company remains in compliance with its liquidity and other covenants, and has agreed to provide additional financial reports to BMO.

Borrowings under the Credit Agreement are secured by substantially all of the Company's personal property, including accounts receivable, inventory, machinery and equipment, and intellectual property. The Company has also pledged 100% of its equity interests in certain domestic subsidiaries and 65% of its equity interests in certain foreign subsidiaries. The Company also entered into a Collateral Assignment of Rights under Purchase Agreement for its acquisition of Veth Propulsion. To effect these security interests, the Company entered into various amendment and assignment agreements that consent to the assignment of certain agreements previously entered into between the Company and the Bank of Montreal in connection with the 2016 Credit Agreement. The Company also amended and assigned to BMO a Negative Pledge Agreement that it has previously entered into with Bank of Montreal, pursuant to which it agreed not to sell, lease or otherwise encumber real estate that it owns except as permitted by the Credit Agreement and the Negative Pledge Agreement.

Upon the occurrence of an Event of Default, BMO may take the following actions upon written notice to the Company: (1) terminate its remaining obligations under the Credit Agreement; (2) declare all amounts outstanding under the Credit Agreement to be immediately due and payable; and (3) demand the Company to immediately Cash Collateralize L/C Obligations in an amount equal to 105% of the aggregate L/C Obligations or a greater amount if BMO determines a greater amount is necessary. If such Event of Default is due to the Company's bankruptcy, BMO may take the three actions listed above without notice to the Company.

There are no material off-balance-sheet arrangements, and the Company continues to have sufficient liquidity for near-term needs. The Company had approximately $15.9 million of available borrowings under the Credit Agreement as of March 25, 2022. The Company expects to continue to generate enough cash from operations, as well as have sufficient capacity under its credit facilities, to meet its operating and investing needs. As of March 25, 2022, the Company also had cash of $12.8 million, primarily at its overseas operations. These funds, with some restrictions and tax implications, are available for repatriation as deemed necessary by the Company. In fiscal 2022, the Company expects to contribute $0.7 million to its defined benefit pension plans, the minimum contribution required.

Net working capital increased $3.0 million, or 2.7%, during the first three quarters of fiscal 2022, and the current ratio declined remained level at 2.4 for March 25, 2022 and June 30, 2021. The increase in net working capital was primarily driven by an increase to inventory driven by substantial supply chain imbalances across the Company's operations.

The Company expects capital expenditures to be approximately $4 million - $6 million in fiscal 2022. These anticipated expenditures reflect the Company's plans to modernize its equipment and facilities, enhance its global sourcing program and drive new product development.

Management believes that available cash, the BMO credit facility, and potential access to debt markets will be adequate to fund the Company's capital requirements for the foreseeable future.

The Company has approximately $0.8 million of unrecognized tax benefits, including related interest and penalties, as of March 25, 2022, which, if recognized, would favorably impact the effective tax rate. See Note H, Income Taxes, of the Condensed Consolidated Financial Statements for disclosures surrounding uncertain income tax positions.

The Company maintains defined benefit pension plans for some of its operations in the United States and Europe. The Company has established the Benefits Committee (a non-Board management committee) to oversee the operations and administration of the defined benefit plans. The Company estimates that fiscal 2022 contributions to all defined benefit plans will total $0.7 million. As of March 25, 2022, $0.7 million in contributions have been made.

New Accounting Releases

See Note A, Basis of Presentation, to the condensed consolidated financial statements for a discussion of recently issued accounting standards.

Critical Accounting Policies

The preparation of this Quarterly Report requires management's judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting period. There can be no assurance that actual results will not differ from those estimates.

The Company's critical accounting policies are described in Item 7 of the Company's Annual Report filed on Form 10-K for June 30, 2021. There have been no significant changes to those accounting policies subsequent to June 30, 2021.

Item 3. Quantitative and Qualitative Disclosure About Market Risk

The Company is electing not to provide this disclosure due to its status as a Smaller Reporting Company.

Item 4. Controls and Procedures

(a) *Evaluation of Disclosure Controls and Procedures*

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("the Exchange Act") as of the end of the period covered by this report. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in recording, processing, summarizing, and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act, and that such information is accumulated and communicated to the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely discussions regarding required disclosure.

(b) *Changes in Internal Control Over Financial Reporting*

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). During the most recent fiscal quarter, no changes were made which have materially affected, or which are reasonably likely to materially affect, our internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is a defendant in several product liability or related claims which are considered either adequately covered by appropriate liability insurance or involving amounts not deemed material to the business or financial condition of the Company.

Item 1A. Risk Factors

There have been no material changes to the risk factors previously disclosed in response to Item 1A to Part I of our 2021 Annual Report on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) *Unregistered Sales of Equity Securities*

There were no securities of the Company sold by the Company during the quarter ended March 25, 2022, which were not registered under the Securities Act of 1933, in reliance upon an exemption from registration provided by Section 4 (2) of the Act.

(b) *Use of Proceeds*

Not applicable.

(c) *Issuer Purchases of Equity Securities*

Issuer Purchases of Equity Securities

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
January 1 – January 28, 2022	0	NA	0	315,000
January 29 – February 25, 2022	0	NA	0	315,000
February 26 – March 25, 2022	0	NA	0	315,000
Total	0	NA	0	315,000

Under authorizations granted by the Board of Directors on February 1, 2008 and July 27, 2012, the Company was authorized to purchase 500,000 shares of its common stock. This authorization has no expiration, and as of March 25, 2022, 315,000 may yet be purchased under these authorizations. The Company did not purchase any shares of its common stock pursuant to these authorizations during the quarter ended March 25, 2022.

The discussion of limitations upon the payment of dividends as a result of the Credit Agreement between the Company and BMO Harris Bank, N.A., as discussed in Part I, Item 2, "Management's Discussion and Analysis " under the heading "Financial Condition, Liquidity and Capital Resources," is incorporated herein by reference.

Item 3. Defaults Upon Senior Securities

None.

Item 5. Other Information

None.

Item 6. Exhibits

31a	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31b	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32a	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32b	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	Inline XBRL Instance Document
101.SCH	Inline XBRL Schema
101.CAL	Inline XBRL Calculation Linkbase
101.DEF	Inline XBRL Definition Linkbase
101.LAB	Inline XBRL Label Linkbase
101.PRE	Inline XBRL Presentation Linkbase
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101).

SIGNATURE

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.

TWIN DISC, INCORPORATED
(Registrant)

Date: May 4, 2022

/s/ JEFFREY S. KNUTSON
Jeffrey S. Knutson
Vice President – Finance, Chief Financial Officer, Treasurer and Secretary
Chief Accounting Officer

Exhibit 31a

CERTIFICATION

I, John H. Batten, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Twin Disc, Incorporated;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 4, 2022

/s/ JOHN H. BATTEN
John H. Batten
President and Chief Executive Officer

Exhibit 31b
CERTIFICATION

I, Jeffrey S. Knutson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Twin Disc, Incorporated;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 4, 2022

/s/ JEFFREY S. KNUTSON
Jeffrey S. Knutson
Vice President – Finance, Chief Financial Officer, Treasurer and Secretary

EXHIBIT 32a

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Twin Disc, Incorporated (the “Company”) on Form 10-Q for the fiscal quarter ending March 25, 2022, as filed with the Securities and Exchange Commission as of the date hereof (the “Report”), I, John H. Batten, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 4, 2022

/s/ JOHN H. BATTEN
John H. Batten
President and Chief Executive Officer

EXHIBIT 32b

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Twin Disc, Incorporated (the “Company”) on Form 10-Q for the fiscal quarter ending March 25, 2022, as filed with the Securities and Exchange Commission as of the date hereof (the “Report”), I, Jeffrey S. Knutson, Vice President – Finance, Chief Financial Officer, Treasurer and Secretary of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 4, 2022

/s/ JEFFREY S. KNUTSON
Jeffrey S. Knutson
Vice President – Finance, Chief Financial Officer, Treasurer and Secretary