TOPPS CO INC
Form 10-Q
October 07, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the quarterly period ended August 28, 2004

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from _______________ to __________________

Commission File Number: 0-15817

THE TOPPS COMPANY, INC.
(Exact name of registrant as specified in its charter)

Delaware	11-2849283
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One Whitehall Street, New York, NY 10004
(Address of principal executive offices, including zip code)

(212) 376-0300
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes _X_ No .

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 126-2 of the Act). Yes _X_ No .

The number of outstanding shares of Common Stock as of October 1, 2004 was 40,414,831.

THE TOPPS COMPANY, INC.
AND SUBSIDIARIES

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PART II - OTHER INFORMATION

THE TOPPS COMPANY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	(Unaudited) August 28, 2004	February 28, 2004
	(amounts in thousands,	

	except share data)	
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 110,599	$ 93,837
Accounts receivable - net	19,391	30,109
Inventories	30,953	33,009
Income tax receivable	1,542	2,697
Deferred tax assets	951	1,505
Prepaid expenses and other current assets	9,775	11,691
TOTAL CURRENT ASSETS	173,211	172,848
PROPERTY, PLANT AND EQUIPMENT	33,414	32,349
Less: accumulated depreciation and amortization	20,392	18,563
NET PROPERTY, PLANT AND EQUIPMENT	13,022	13,786
GOODWILL	67,566	67,586
INTANGIBLE ASSETS, net of accumulated amortization	9,575	10,474
OTHER ASSETS	10,765	10,769
TOTAL ASSETS	$ 274,169	$ 275,463
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 10,312	$ 10,946
Accrued expenses and other liabilities	23,902	26,249
Income taxes payable	3,378	2,354
TOTAL CURRENT LIABILITIES	37,592	39,549
DEFERRED INCOME TAXES	1,719	1,956
OTHER LIABILITIES	23,254	22,681
TOTAL LIABILITIES	62,565	64,186
STOCKHOLDERS' EQUITY:		
Preferred stock, par value $.01 per share; authorized 10,000,000 shares, none issued	--	--
Common stock, par value $.01 per share; authorized 100,000,000 shares; issued 49,244,000 shares as of August 28, 2004 and February 28, 2004	492	492
Additional paid-in capital	27,829	27,829
Treasury stock, 8,846,000 shares and 8,632,000 shares as of August 28, 2004 and February 28, 2004, respectively	(84,840)	(82,287)
Retained earnings	275,207	270,704
Accumulated other comprehensive loss, net of income taxes	(7,084)	(5,461)
TOTAL STOCKHOLDERS' EQUITY	211,604	211,277
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 274,169	$ 275,463

See Notes to Condensed Consolidated Financial Statements.

THE TOPPS COMPANY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	(Unaudited)			
	Thirteen weeks ended		Twenty-six weeks ended	
	August 28, 2004	August 30, 2003	August 28, 2004	August 30, 2003
	(amounts in thousands, except share date)			
Net sales	$ 68,781	$ 73,319	$ 156,870	$ 149,311
Cost of sales	42,501	44,560	96,791	92,428
Gross profit on sales	26,280	28,759	60,079	56,883
Selling, general and administrative expenses	21,879	21,543	50,472	45,886
Other income, net	411	342	844	944
Income from operations	4,812	7,558	10,451	11,941
Interest income, net	557	450	1,041	1,484
Income before provision for income taxes	5,369	8,008	11,492	13,425
Provision for income taxes	1,714	2,736	3,735	4,632
Net income	$ 3,655	$ 5,272	$ 7,757	$ 8,793
Net income per share - basic	$ 0.09	$ 0.13	$ 0.19	$ 0.22
- diluted	$ 0.09	$ 0.13	$ 0.19	$ 0.21
Weighted average shares outstanding - basic	40,459,000	40,605,000	40,513,000	40,650,000
-diluted	41,511,000	41,386,000	41,565,000	41,433,000

See Notes to Condensed Consolidated Financial Statements.

THE TOPPS COMPANY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF
COMPREHENSIVE INCOME

	(Unaudited) Thirteen weeks ended August 28, 2004	August 30, 2003	Twenty-six weeks ended August 28, 2004	August 30, 2003
	(amounts in thousands, except share date)			
Net income	$ 3,655	$ 5,272	$ 7,757	$ 8,793
Currency translation adjustment	(756)	(1,340)	(1,623)	970
Comprehensive income	$ 2,899	$ 3,932	$ 6,134	$ 9,763

See Notes to Condensed Consolidated Financial Statements.

THE TOPPS COMPANY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Unaudited) Twenty-six weeks ended August 28, 2004	August 30, 2003
	(amounts in thousands)	

Cash flows from operating activities:		
Net income	$ 7,757	$ 8,793
Add non-cash items included in net income:		
Depreciation and amortization	3,161	2,844
Deferred income taxes	317	83
Changes in operating assets and liabilities:		
Accounts receivable	10,718	6,239
Inventories	2,007	(2,573)
Income tax receivable/payable	2,178	921
Prepaid expenses and other current assets	1,916	(433)
Payables and other current liabilities	2,982	(5,624)
Other assets and liabilities	(218)	566
Cash provided by operating activities	24,854	10,816
Cash flows from investing activities:		
Acquisition of business, net of cash acquired	--	(27,923)
Additions to property, plant and equipment	(1,065)	(1,063)
Cash used in investing activities	(1,065)	(28,986)
Cash flows from financing activities:		
Dividends paid to stockholders	(3,254)	(1,631)
Purchase of treasury stock and exercise of stock options	(2,553)	(1,591)
Cash used in by financing activities	(5,807)	(3,222)
Effect of exchange rates on cash and cash equivalents	(1,220)	305
Net increase (decrease) in cash and cash equivalents	$16,762	$(21,087)
Cash and cash equivalents at beginning of period	$ 93,837	$114,259
Cash and cash equivalents at end period	$110,599	$ 93,172
Supplemental disclosure of cash flow information:		
Interest paid	$ 137	$ 70
Income taxes paid	$ 1,792	$ 3,718

See Notes to Condensed Consolidated Financial Statements.

THE TOPPS COMPANY, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF AUGUST 28, 2004 AND FEBRUARY 28, 2004
AND FOR THE THIRTEEN AND TWENTY-SIX WEEK PERIODS
ENDED AUGUST 28, 2004 AND AUGUST 30, 2003

1. Summary of Significant Accounting Policies

Basis of Presentation: The accompanying unaudited condensed interim consolidated financial statements have been prepared by The Topps Company, Inc. and its subsidiaries (the "Company") pursuant to the rules and regulations of the Securities and Exchange Commission and reflect all adjustments which are, in the opinion of management, considered necessary for a fair presentation. Operating results for the thirteen-week periods ended August 28, 2004 and August 30, 2003 are not necessarily indicative of the results that may be expected for the year. For further information, refer to the consolidated financial statements and notes thereto in the Company's annual report for the year ended February 28, 2004.

Employee Stock Options: The Company accounts for stock-based employee compensation based on the intrinsic value of stock options granted in accordance with the provisions of Accounting Principles Board ("APB") Opinion 25, "Accounting for Stock Issued to Employees." Information relating to stock-based employee compensation, including the pro forma effects, had the Company accounted for stock-based employee compensation based on the fair value of stock options granted (net of tax) in accordance with SFAS 123, "Accounting for Stock-Based Compensation," is shown below:

	For the thirteen weeks ended			
	August 28, 2004		August 30, 2003	
	As reported	Pro forma	As reported	Pro forma
Net income, as reported	$ 3,655	$ 3,655	$ 5,272	$ 5,272
Less: Stock-based employee compensation		(170)		(349)
Pro forma net income		$ 3,485		$ 4,923
Earnings per share:				
Basic	$ 0.09	$ 0.09	$ 0.13	$ 0.12
Diluted	$ 0.09	$ 0.09	$ 0.13	$ 0.12

	For the twenty-six weeks ended			
	August 28, 2004		August 30, 2003	
	As reported	Pro forma	As reported	Pro forma
Net income, as reported	$ 7,757	$ 7,757	$ 8,793	$ 8,793
Less: Stock-based employee compensation		(311)		(549)
Pro forma net income		$ 7,446		$ 8,244
Earnings per share:				
Basic	$ 0.19	$ 0.18	$ 0.22	$ 0.20
Diluted	$ 0.19	$ 0.18	$ 0.21	$ 0.20

Options have an exercise price equal to the market price on the date prior to the grant date and typically vest over a three-year period. In determining the preceding pro forma amounts under Statement of Financial Accounting Standards ("SFAS") 123, the fair value of each option grant is estimated as of the date of grant using the Black-Scholes option pricing model with the following assumptions: $0.16 per share dividend on fiscal 2005 and fiscal 2004 options, but no dividend on fiscal 2003 options; risk-free interest rate, estimated volatility and expected life as follows: fiscal 2005 options - 4.4%, 32% and 6.0 years, respectively; fiscal 2004 options - 4.4%, 38% and 6.5 years, respectively; fiscal 2003 options - 4.5%, 35% and 6.5 years, respectively.

2. Quarterly Comparison

Management believes that quarter-to-quarter comparisons of sales and operating results are affected by a number of factors, including, but not limited to, the timing of sports and entertainment releases, new product introductions, seasonal products, the timing of various expenses such as advertising and variations in shipping and factory scheduling requirements. Thus, quarterly results may vary.

3. Accounts Receivable

	(Unaudited) August 28, 2004	February 28, 2004
	(amounts in thousands)	
Gross receivables	$ 46,229	$ 52,843
Reserve for returns	(23,028)	(19,516)
Other reserves	(3,810)	(3,218)
Net receivables	$ 19,391	$ 30,109

Other reserves consist of allowances for discounts, doubtful accounts and customer deductions for promotional marketing programs.

4. Inventories

	(Unaudited) August 28, 2004	February 28, 2004
	(amounts in thousands)	
Raw materials	$ 7,627	$ 5,571
Work in process	4,961	2,824
Finished products	18,365	24,614
Total inventories	$ 30,953	$ 33,009

5. Segment Information

Following is the breakdown of industry segments as required by SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information." The Company has two reportable business segments: Confectionery and Entertainment.

The Confectionery segment consists of a variety of candy products including Ring Pop, Push Pop and Baby Bottle Pop, Juicy Drop Pop, the Bazooka bubble gum line and, from time to time, confectionery products based on licensed characters, such as Pokemon and Yu-Gi-Oh!.

The Entertainment segment primarily consists of cards and sticker album products featuring sports and non-sports subjects. Trading cards feature players from Major League Baseball, the National Basketball Association, the National Football League, and the National Hockey League (although our contract with the NHL has expired), as well as characters from popular films, television shows and other entertainment properties. Sticker album products feature players from the English Premier League and characters from entertainment properties such as Pokemon and Yu-Gi-Oh! This segment also includes results from WizKids, a designer and marketer of strategy games acquired in July 2003.

The Company's chief decision-maker regularly evaluates the performance of each segment based upon its contributed margin, which is profit after cost of goods, product development, advertising and promotional costs and obsolescence, but before unallocated general and administrative expenses and manufacturing overhead, depreciation and amortization, other income (expense), net interest and income taxes.

The majority of the Company's assets are shared across both segments, and the Company's chief decision-maker does not evaluate the performance of each segment utilizing asset-based measures. Therefore, the Company does not include a breakdown of assets or depreciation and amortization by segment.

	Thirteen weeks ended		Twenty-six weeks ended	
	August 28, 2004	August 30, 2003	August 28, 2004	August 30, 2003
	(amounts in thousands)			
Net Sales				
Confectionery	$ 39,982	$ 42,008	$ 84,189	$ 87,538
Entertainment	28,799	31,311	72,681	61,773
Total	$ 68,781	$ 73,319	$156,870	$149,311
Contributed Margin				
Confectionery	$ 15,777	$ 15,491	$ 28,779	$ 29,260
Entertainment	8,998	10,276	22,426	17,399
Total	$ 24,775	$ 25,767	$ 51,205	$ 46,659

Reconciliation of Contributed Margin to Income Before Provision for Income Taxes:				
Total contributed margin	$ 24,775	$ 25,767	$ 51,205	$ 46,659
Unallocated general and administrative expense and manufacturing overhead	(18,805)	(16,986)	(38,437)	(32,818)
Depreciation and amortization	(1,569)	(1,565)	(3,161)	(2,844)
Other income, net	411	342	844	944
Income from operations	4,812	7,558	10,451	11,941
Interest income, net	557	450	1,041	1,484
Income before provision for income taxes	$ 5,369	$ 8,008	$ 11,492	$ 13,425

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6. Dividend and Share Repurchase Programs

In June 2003, the Board of Directors of the Company initiated a quarterly dividend of $0.04 per share.

On July 1, 2004, the Board of Directors declared its second quarter cash dividend of $0.04 per share payable on August 2, 2004 to shareholders of record on July 19, 2004.

In October 1999, the Company's Board of Directors authorized the repurchase of up to 5 million shares of the Company's common stock. In October 2001, the Company completed the authorization and the Board approved the purchase of another 5 million shares. As of August 28, 2004, under these two programs, the Company has purchased 8,296,700 common shares.

7. Credit Agreement

On June 26, 2000, the Company entered into a credit agreement with Chase Manhattan Bank and LaSalle Bank National Association for a term of four years, which ended on June 26, 2004. On June 25, 2004, the credit agreement was amended, however, to extend the expiration date for 90 days in order to provide the Company sufficient time to complete refinancing arrangements. This credit agreement has now expired.

On September 14, 2004, the Company entered into a new credit agreement with JPMorgan Chase Bank. The agreement provides for a $30.0 million unsecured facility to cover revolver and letter of credit needs and expires on September 13, 2007. Interest rates are variable and a function of market rates and the Company's EBITDA. The credit agreement contains restrictions and prohibitions of a nature generally found in loan agreements of this type and requires the Company, among other things, to comply with certain financial covenants, limits the Company's ability to sell or acquire assets or borrow additional money and places certain restrictions on the purchase of Company shares and the payment of dividends. The credit agreement may be terminated by the Company at any point over the three-year term (provided the Company repays all outstanding amounts thereunder) without penalty.

There was no debt outstanding under either credit agreement as of February 28, 2004 or August 28, 2004.

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8. Reclassifications

Certain items in the prior years' financial statements have been reclassified to conform with the current year's presentation.

9. Goodwill and Intangible Assets

On March 3, 2002, the Company adopted SFAS 141 "Business Combinations" and SFAS 142 "Goodwill and Other Intangible Assets" which require the Company to prospectively cease amortization of goodwill and instead conduct periodic tests of goodwill for impairment.

As a result of the acquisition of WizKids in July 2003, goodwill increased by $18.7 million, and other intangibles increased by $6.2 million (included in intellectual property) (see Note 11). Intangible assets as of August 28, 2004 and February 28, 204 were as follows:

	(amounts in thousands)					
	August 28, 2004 (Unaudited)			February 28, 2004		
	Gross Carrying Value	Accumulated Amortization	Net	Gross Carrying Value	Accumulated Amortization	
Licenses and Contracts	$ 21,569	$(17,607)	$ 3,962	$ 21,569	$(17,272)	$
Intellectual Property	18,784	(13,767)	5,017	18,784	(13,251)	
Software and Other	2,953	(2,765)	188	2,953	(2,717)	
Min. Pension Liab	408	--	408	408	--	
Total Intangibles	$ 43,714	$(34,139)	$ 9,575	$ 43,714	$(33,240)	$

Useful lives of the Company's intangible assets have been established based on the Company's intended use of such assets and their estimated period of future benefit, which are reviewed periodically. Useful lives are as follows:

Category	Useful Life	Weighted Average Remaining Useful Life
Licenses and Contracts	15 years	5.9 years
Intellectual Property	6 years	4.9 years
Software and Other	5 years	2.0 years

The weighted average remaining useful life for the Company's intangible assets in aggregate is 5.2 years. Over the next five years, the Company estimates amortization of the intangible assets detailed above to be as follows:

Fiscal Year	Amount (in thousands)
2005	$ 1,797
2006	$ 1,797
2007	$ 1,750
2008	$ 1,703
2009 and thereafter	$ 2,528

In addition to the amortization of intangibles listed above, reported amortization expense, which was $1,268,000 and $894,000 for the twenty-six weeks ended August 28, 2004 and August 30, 2003, respectively, included amortization of deferred financing fees and deferred compensation costs.

10. Legal Proceedings

In November 2000, the Commission of the European Communities (the "Commission") began an investigation into whether Topps Europe's past distribution arrangements for the sale of Pokemon products complied with European law (the "EU investigation"). On June 17, 2003, the Commission filed a Statement of Objections against The Topps Company, Inc. and its

European subsidiaries, therein coming to a preliminary conclusion that these entities infringed Article 81 of the EC treaty during 2000 by preventing parallel trade between member states of the European Union. A hearing in front of the European Commission Tribunal took place on October 23, 2003, and on May 27, 2004, the Commission found The Topps Company, Inc. and its European subsidiaries jointly and severally liable for infringement of Article 81(1) of the EC treaty. The Commission imposed a total fine of 1.6 million euros ($1.9 million) which was included in accrued expenses in the condensed consolidated balance sheet as of May 29, 2004 and in SG&A expense for the thirteen weeks ended May 29, 2004. The fine has now been paid.

On February 17, 2000, Telepresence, Inc. sued Topps and nine other manufacturers of trading cards (the "Defendants") in the Federal District Court for the Central District of California for infringement of U.S. Patent No. 5,803,501 which was issued on September 8, 1998 (the "501 Patent"). In its suit, Telepresence contended that the patent covers all types of "relic" cards that contain an authentic piece of equipment, i.e., a piece of sporting equipment or jersey. After initial discovery, on November 15, 2000, the Defendants jointly moved for summary judgment on the grounds that the named Plaintiff (Telepresence, Inc.) did not have standing to sue for infringement of the 501 Patent. The motion was granted and the Telepresence litigation was dismissed with prejudice on March 28, 2001.

After the dismissal, the 501 Patent was assigned to a company called Media Technologies, Inc. Media Technologies is under the control of the same person (the inventor, Adrian Gluck) who brought the Telepresence action. On November 19, 2001, Media Technologies sued essentially the same group of defendants in the same court for infringement of the 501 Patent. On March 13, 2002, the Defendants again moved for summary judgment based on the fact that the Telepresence action was dismissed with prejudice. That motion was granted by the District Court on April 22, 2002. Plaintiff (Media Technologies, Inc.) appealed on May 2, 2002. The Court of Appeals for the Federal Circuit reversed the judgment on July 11, 2003, and the case has been returned to Judge Stotler in the Central District of California for trial.

Discovery in the case commenced September 29, 2003 and was stayed pending the outcome of two summary judgment motions filed by defendants. On March 17, 2004, Topps filed a motion for summary judgment based on non-infringement while other defendants filed a motion for summary judgment based on patent invalidity because of prior art. Both motions were denied on July 26, 2004 and discovery has now resumed. On September 15th, 2004, defendant Upper Deck Company, LLC moved for a separate trial on the issues of infringement, damages, willfulness and counterclaims.

The trial is currently scheduled for February 2005. An adverse outcome in the litigation could result in a substantial liability for the Company. It is still too early in the matter to determine the likelihood of damages or to estimate the range of loss, if any, and, accordingly, no provision has been recorded for this matter in the accompanying condensed consolidated financial statements.

The Company is a defendant in several other civil actions which are routine and incidental to its business. In management's opinion, after consultation with legal counsel, these other actions are not likely to have a material adverse effect on the Company's consolidated financial statements.

11. Acquisition of Wizkids, LLC

On July 9, 2003, the Company acquired Wizkids, LLC ("WizKids"), a designer and marketer of collectible strategy games, for a cash purchase price of approximately $28.4 million. It is believed that the acquisition will serve to enhance and accelerate the expansion of the Company's entertainment business. The acquisition is being accounted for using the purchase method of accounting. The financial statements of WizKids have been consolidated into the financial statements of the Company subsequent to the acquisition. The allocation of the purchase price is reflected in the financial statements contained herein.

The total consideration paid by the Company to WizKids' shareholders was comprised of $29,500,000 in cash, net of a working capital adjustment of $1,123,500. The purchase price also reflected a $1,326,130 payment to a third party for associated licenses and legal, accounting, and investment banking fees of $679,075. The purchase price was determined based on discounted cash flow projections, which reflected expected synergies with the Company.

The purchase price includes a $6.2 million allocation for intellectual property rights associated with the WizKids product line, which is being amortized over an estimated useful life of 6 years. There were no contingent payments with the purchase price.

Contemporaneous with the acquisition, the Company entered into an employment agreement with Jordan Weisman, the majority shareholder and founder of WizKids, for a forty-eight month period following the closing. As part of this employment agreement, $2 million of the consideration paid to Mr. Weisman as a shareholder is being accounted for as deferred compensation and is being amortized over four years. If Mr. Weisman does not remain a WizKids employee for the full four years of the agreement, he will be required to pay the Company the unamortized balance of his deferred compensation. As an additional part of his employment agreement, Mr. Weisman is entitled to contingent payments during the forty-eight months subsequent to the closing equal to 2% of WizKids' annual net revenue in excess of $35 million, assuming that certain operating margin targets are met. In addition, Mr. Weisman was granted 165,000 options to acquire the Company's common stock, which were granted at fair market value on the date of grant and vest over a four-year period.

The following table sets forth the components of the purchase price:

Total consideration	$ 29,500,000
Less: Working capital adjustment	(1,123,500)
Deferred compensation agreement	(2,000,000)
Add: Purchase of license	1,326,130
Transaction costs	679,075
Total purchase price	$ 28,381,705

The following table provides the fair value of the acquired assets and liabilities assumed based upon WizKids' July 9, 2003 balance sheet:

Current assets	$ 8,201,851
Property and equipment	564,743
Other assets	115,000
Liabilities assumed, current	(5,426,072)

Fair value of net assets acquired	3,455,522
Intangible assets	6,200,000
Goodwill	18,726,183
Total estimated fair value of net assets acquired and estimated goodwill	$ 28,381,705

The goodwill of $18.7 million is included in the Entertainment business segment and is deductible for tax purposes over a fifteen-year period.

The impact of including WizKids in the condensed consolidated statements of operations on a pro forma basis as if the acquisition had occurred on March 2, 2003 is as follows:

	(Unaudited) Thirteen weeks ended August 30, 2003	Twenty-six weeks ended August 30, 2003
	(amounts in thousands,	except share data)
Net sales	$ 78,152	$162,699
Income from operations	5,965	10,138
Net income	4,280	7,682
Net income per share - basic	$ 0.11	$ 0.19
- diluted	$ 0.10	$ 0.19

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12. Employee Benefit Plans

The components of net periodic benefit costs for the thirteen and twenty-six weeks ended August 28, 2004 and August 30, 2003 are as follows:

	Pension		Postretirement Healthcare	
Thirteen weeks	August 28, 2004	August 30, 2003	August 28, 2004	August 30, 2003
	(amounts in thousands)			
Service Cost	$ 345	$ 346	$ 82	$ 71
Interest cost	593	597	163	150
Expected return on plan assets	(535)	(363)	-	-
Amortization of:				
Initial transition obligation	(15)	(12)	50	50
Prior service cost	33	33	-	-
Actuarial (gains) losses	179	279	27	12
Net periodic benefit cost	$ 600	$ 880	$ 322	$ 283

Postretirement

Twenty-six weeks	Pension August 28, 2004	Pension August 30, 2003	Healthcare August 28, 2004	Healthcare August 30, 2003
	(amounts in thousands)			
Service Cost	$ 690	$ 692	$ 164	$ 142
Interest cost	1,187	1,195	324	300
Expected return on plan assets	(1,069)	(726)	-	-
Amortization of:				
Initial transition obligation	(30)	(25)	100	100
Prior service cost	66	66	-	-
Actuarial (gains) losses	358	558	54	24
Net periodic benefit cost	$ 1,202	$ 1,760	$ 642	$ 566

The fiscal 2005 costs are estimated based on actuarial assumptions, and actual costs will be adjusted accordingly during the year.

13. Recently Issued Accounting Pronouncements

In January 2004, the Financial Accounting Standards Board ("FASB") issued FSP 106-1, which allows companies to elect a one-time deferral of the recognition of effects of the Medicare Prescription Drug Act and disclosures related to the postretirement healthcare plan. The FASB allows the one-time deferral due to a lack of clarification regarding its accounting and uncertainties regarding the effects of the Medicare Prescription Drug Act on plan participants. For companies electing the one-time deferral, the deferral remains in effect until guidance on the accounting for the federal subsidy is issued, or until certain other events, such as a plan amendment, settlement or curtailment, occur. The Company is currently evaluating the effects of the Medicare Prescription Drug Act on the postretirement benefit plan and its participants, and has elected the one-time deferral. In May 2004, the FASB issued FSP No. 106-2 ("FSP 106-2"), which superseded FSP 106-1. FSP 106-2 provides authoritative guidance on the accounting for the Act and specifies the disclosure requirements for employers who have adopted FSP 106-2. FSP 106-2 is effective for the interim or annual period beginning after June 15, 2004. The Company's accumulated post-retirement benefit obligation and net post-retirement benefit cost for fiscal 2004 and fiscal 2005 do not reflect the effects of the Medicare Prescription Drug Act. Once specific guidance on the accounting for the federal subsidy is issued, anticipated by the Company's third quarter of fiscal 2005, it could result in a change to previously reported information.

14. Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements and, therefore, there is no effect on its financial condition, changes in financial condition, revenue or expenses, results of operations, liquidity, capital expenditures or capital resources from this type of arrangement.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders of
The Topps Company, Inc.

We have reviewed the accompanying condensed consolidated balance sheet of The Topps Company, Inc. and subsidiaries (the "Company") as of August 28, 2004, and the related condensed consolidated statements of operations and comprehensive income for the thirteen and twenty-six week periods ended August 28, 2004 and August 30, 2003 and of cash flows for the twenty-six week periods ended August 28, 2004 and August 30, 2003. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of February 28, 2004, and the related consolidated statements of operations, stockholders' equity, comprehensive income, and cash flows for the year then ended (not presented herein); and in our report dated May 4, 2004, we expressed an unqualified opinion on those consolidated financial statements and included an explanatory paragraph relating to the Company's change in method of accounting for goodwill and other intangible assets to conform to Statement of Financial Accounting Standard 142. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of February 28, 2004 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

s/ DELOITTE & TOUCHE LLP

October 7, 2004
New York, New York

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Second Quarter Fiscal Year 2005 (thirteen weeks ended August 28, 2004) versus
Second Quarter Fiscal Year 2004 (thirteen weeks ended August 30, 2003)

The following table sets forth, for the periods indicated, net sales by key business segment:

	Thirteen weeks ended August 28, 2004	Thirteen weeks ended August 30, 2003	Twenty-six weeks ended August 28, 2004	Twenty-six weeks ended August 30, 2003
	(amounts in thousands)			
Net Sales				
Confectionery	$ 39,982	$ 42,008	$ 84,189	$ 87,538
Entertainment	28,799	31,311	72,681	61,773
Total	$ 68,781	$ 73,319	$156,870	$149,311

Net sales for the second quarter of fiscal 2005 were $68.8 million, a decrease of $4.5 million, or 6.2%, from $73.3 million in the same period last year. Stronger foreign currencies versus the dollar increased sales in the quarter this year by $1.3 million.

Net sales of confectionery products, which include, among other things, Ring Pop, Push Pop, Baby Bottle Pop, Bazooka brand bubble gum and licensed candy products, were $40.0 million in the second quarter of this year, a decrease of $2.0 million, or 4.8%, from $42.0 million in fiscal 2004. Stronger foreign currencies contributed $0.6 million. Confectionery sales in the second quarter continued to be impacted by industry issues such as retail consolidation, increased promotional spending by competitors (including price discounting) and childhood nutritional concerns. Partially offsetting these factors was a favorable contribution from the growing sales of Juicy Drop Pop and the further roll-out of two new Topps chewy products--Juicy Drop Chews and Juicy Bugs.

Net sales of entertainment products, which include cards, stickers, sticker albums and the WizKids line of strategy games, were $28.8 million in the second quarter of fiscal 2005, a decrease of $2.5 million, or 8.0%, from $31.3 million in the same period last year. Stronger foreign currencies provided a $0.7 million benefit. The decline was a function of the decision not to release hockey cards due to an uncertain NHL season and difficult comparisons to last year's basketball sales, which benefited from a highly anticipated rookie class. Additionally, net sales were impacted by higher returns provisions for European sports and publishing products. Sales at WizKids, acquired in July of last year, were higher due to the full quarter of ownership this year. Worldwide publishing sales increased slightly year-over-year driven by Pokemon, Wacky Packages, Garbage Pail Kids and Yu-Gi-Oh! releases.

Gross profit as a percentage of net sales in the second quarter of fiscal 2005 was 38.2% as compared with last year's level of 39.2%. This decline was primarily the result of the higher returns provisions in the European entertainment business, which reduced net sales. Lower autograph and relic costs on U.S. sports products partly offset the impact of increased provisions.

Other income/expense in the quarter was $411,000 as compared with last year's figure of $342,000. This was largely the result of the absence of exchange losses on foreign cash balances recorded last year, and, to a lesser degree, increased licensing income from confectionery brands and WizKids.

SG&A expense was $21.9 million in the quarter this year, up from $21.5 million in fiscal 2004. As a percentage of net sales, SG&A was 31.8% this year versus 29.4% a year ago. The modest increase in SG&A dollar spending was the result of costs associated with a strategic planning project and higher selling-related expenses in the U.S. and Europe, in part offset by reduced advertising and marketing costs behind U.S. confectionery products and etopps.

Net interest income of $557,000 in the second quarter this year was higher than a year-ago due to higher interest rates.

The effective tax rate reflects provisions for federal, state and local income taxes in accordance with statutory income tax rates. The Company`s tax rate of 31.9% in the second quarter this year versus 34.2% last year reflects the adjustment necessary to reduce the full year forecasted rate to 32.5% from 33.0%.

Net income for the second quarter of fiscal 2005 was $3.7 million, or $0.09 per diluted share, compared with $5.3 million, or $0.13 per diluted share last year.

First Half Fiscal 2005 (twenty-six weeks ended August 28, 2004) compared to First Half Fiscal 2004 (twenty-six weeks ended August 30, 2003)

Net sales in the first half of fiscal 2005 were $156.9 million, an increase of $7.6 million, or 5.1%, from $149.3 million in the same period last year. Stronger foreign currencies versus the dollar served to increase sales by $4.1 million.

Net sales of confectionery products were $84.2 million in the first half this year, a decrease of $3.3 million, or 3.8%, from $87.5 million in fiscal 2004. Stronger foreign currencies contributed $1.7 million. Confectionery sales this year were impacted largely by industry issues in the U.S. and reduced demand for Yu-Gi-Oh! confectionery products in Europe. Newer items, particularly Juicy Drop Pop, as well as Juicy Drop Chews and Juicy Bugs, added incrementally to sales in the first half this year.

Net sales of entertainment products in the first half of this year were $72.7 million, an increase of $10.9 million, or 17.7%, from $61.8 million last year. Stronger foreign currencies added $2.4 million this year. Year-over-year first half growth was attributable to sales of sticker album collections featuring the European Championship, a soccer tournament held every four years, as well as to higher sales of English Premier League products, more than offseting lower sales of U.S. sports cards and internet products in the period. In addition, sales at WizKids, acquired in July of last year, added an incremental $6.4 million in sales in the six months of ownership this year.

Gross profit as a percentage of net sales in the first half of fiscal 2005 was 38.3% as compared with 38.1% for the same period last year. Lower sports autograph and relic costs, the absence of expenses associated with Cool Junk last year and a reduction in product development costs associated with the U.S. sports business offset the impact of higher returns provisions on the sale of European entertainment products.

Other income was $844,000 this year versus $944,000 last year. This reduction was largely due to the recent relative stabilization of the U.S. dollar which resulted in lower mark-to-market gains this year on foreign exchange contracts.

SG&A expense was $50.5 million for the first half of fiscal 2005 compared with $45.9 million in fiscal 2004. As a percent of net sales, SG&A of 32.2% was 1.5% points higher than last year. The increase in dollar costs was primarily a function of a full six months of WizKids ownership, as well as a $1.9 million fine levied by the European Commission in the first quarter of this year. (see

Note 10 - Legal Proceedings.) Cost savings initiatives instituted last year in the U.S. sports, Internet and WizKids operations helped offset higher consulting and selling expenses, salary inflation and the impact of stronger European currencies. Advertising and marketing costs were below last year for the six-month period due to reduced spending on the U.S. confectionery business and etopps, partially offset by higher spending behind new product launches overseas.

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Net interest income for the first half of fiscal 2005 decreased to $1.0 million from $1.5 million in fiscal 2004 due to interest received from the IRS on a tax refund in the first quarter of last year.

The tax rate for the first half this year was 32.5%, reflecting the current full-year tax rate outlook, versus 34.5% for the same period last year.

Net income in the first half of fiscal 2005 was $7.8 million, or $0.19 per diluted share, compared with $8.8 million, or $0.21 per diluted share last year. Excluding the impact of the European Commission fine, net income in the first half this year was $9.7 million, or $0.23 per diluted share.

Liquidity and Capital Resources

Management believes that the Company has adequate means to meet its liquidity and capital resource needs over the foreseeable future as a result of the combination of cash on hand, anticipated cash from operations and credit line availability.

At August 28, 2004, the Company had $110.6 million in cash and cash equivalents.

On June 26, 2000, the Company entered into a credit agreement with Chase Manhattan Bank and LaSalle Bank National Association for a term of four years, which ended on June 26, 2004. On June 25, 2004, the credit agreement was amended to extend the expiration date for 90 days in order to provide the Company sufficient time to complete refinancing arrangements. This credit agreement has now expired.

On September 14, 2004, the Company entered into a new credit agreement with JPMorgan Chase Bank. The agreement provides for a $30.0 million unsecured facility to cover revolver and letter of credit needs and expires on September 13, 2007. Interest rates are variable and a function of market rates and the Company's EBITDA. The credit agreement contains restrictions and prohibitions of a nature generally found in loan agreements of this type and requires the Company, among other things, to comply with certain financial covenants, limits the Company's ability to sell or acquire assets or borrow additional money and places certain restrictions on the purchase of Company shares and the payment of dividends. The credit agreement may be terminated by the Company at any point over the three-year term (provided the Company repays all outstanding amounts thereunder) without penalty.

In October 2001, the Board of Directors authorized the purchase of up to 5 million shares of stock. During the first half of fiscal 2005, the Company purchased 350,400 shares at an average price of $9.11 per share. The Company has repurchased a total of 3.3 million shares under this authorization.

In the six months ended August 28, 2004, the Company's net increase in cash and cash equivalents was $16.8 million versus a decrease of $21.1 million in the comparable period of fiscal 2004. The cash use last year was largely a function of the purchase of WizKids net of cash acquired of $27.9 million.

Cash provided by operating activities this year was $24.9 million versus $10.8 million last year. This improvement was primarily due to a $10.7 million reduction in receivables resulting from the collection of seasonal confectionery and European sports billings and the increase in the returns reserve related to sales of European entertainment products. Additionally, better management of confectionery stocks resulted in a reduction in inventories in the first half this year.

Cash used in investing activities was $1.1 million this year for the Company's capital spending. Last year's figure of $29.0 million includes the WizKids net purchase price of $27.9 million and $1.1 million in capital spending. Fiscal 2005 full year capital spending is projected to be in the $3 million to $4 million range, driven by investments in Ring Pop production equipment and computer software and hardware. Capital spending dividend payments and treasury stock purchases are being funded out of cash flow from operating activities.

Cash used in financing activities of $5.8 million this year reflects $3.2 million in cash dividends and $2.6 million in treasury stock purchases (net of $0.6 million options exercised). This spending compares with an outlay of $3.2 million last year, comprised of $1.6 million in cash dividends and $1.6 million in net treasury stock purchases. Dividend payments and treasury stock purchases are being funded out of cash flow from operating activities.

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There are no material changes outside the ordinary course of business with respect to Company's purchase obligations as presented in the Commitments table included in its Annual Report on Form 10-K for the year ended February 28, 2004.

The Company does not have any off-balance sheet arrangements and, therefore, there is no effect on its financial condition, changes in financial condition, revenue or expenses, results of operations, liquidity, capital expenditures or capital resources from this type of arrangement.

Cautionary Statements

In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 (the "Reform Act"), the Company is hereby filing cautionary statements identifying important factors that could cause actual results to differ materially from those projected in any forward-looking statements of the Company made by or on behalf of the Company, whether oral or written. Among the factors that could cause the Company's actual results to differ materially from those indicated in any such forward-looking statements are: (i) the failure of certain of the Company's principal products, particularly sports cards, entertainment cards, WizKids strategy games, confectionery products and sticker album collections, to achieve expected sales levels; (ii) the Company's inability to produce timely, or at all, certain new planned confectionery products; (iii) quarterly fluctuations in results; (iv) the Company's loss of important licensing arrangements; (v) the Company's loss of important supply arrangements with third parties; (vi) the loss of any of the Company's key customers or distributors; (vii) further material contraction in the trading card industry as a whole; (viii) excessive returns of the Company's products; (ix) civil unrest, currency devaluation, health-related issues, or political upheaval in certain foreign countries in which the Company conducts business; and other risks detailed from time to time in the Company's reports and registration statements filed with the Securities and Exchange Commission.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires Topps management to make estimates and judgments that affect the reported amounts of revenue, expenses, assets, liabilities and the disclosure of contingent assets and liabilities. Actual results may differ from these estimates.

Note 1 to the Company's consolidated financial statements, included in its Annual Report on Form 10-K for the year ended February 28, 2004, "Summary of Significant Accounting Policies," summarizes its significant accounting policies. Following is a summary of the critical policies and methods used.

Revenue Recognition: Revenue related to sales of the Company's products is generally recognized when products are shipped, the title and risk of loss has passed to the customer, the sales price is fixed or determinable and collectibility is reasonably assured. Sales made on a returnable basis are recorded net of a provision for estimated returns. These estimates are revised, as necessary, to reflect actual experience and market conditions.

Returns Provisions: In determining the provision for returns, the Company performs an in-depth review of wholesale and retail inventory levels for each product sold, trends in product sell-through by sales channel, and other factors. The provision for returns was $11.2 million in the first twenty-six weeks of fiscal 2005 and $5.8 million in 2004, which equates to 7.1% and 3.9% of higher net sales, respectively. The increase in the provision this year the result of anticipated returns of sticker album products featuring the European Championship, which occurs once every four years, as well as other entertainment properties. An increase or decrease in the provision for returns by 1% of net sales would decrease or increase operating income by approximately $1.6 million.

Intangible Assets: Intangible assets include trademarks and the value of sports, entertainment and proprietary product rights. Amortization is by the straight-line method over estimated lives which range between three and fifteen years. Management evaluates the recoverability of finite-lived intangible assets under the provisions of SFAS No. 144 "Accounting for the Impairment or Disposal of Long-lived Assets" based on the projected undiscounted cash flows attributable to the individual assets, among other methods.

Accrual for Obsolete Inventory: The Company's accrual for obsolete inventory reflects the cost of items in inventory not anticipated to be sold. This accrual is deemed necessary as a result of discontinued items and packaging or a reduction in forecasted sales and is adjusted periodically based on a review of inventory stocks and sales projections. The provision for obsolete inventory was $1.9 million in the twenty-six weeks of fiscal 2005 and $2.0 million in fiscal 2004, which equates to 1.2% and 1.3% of net sales, respectively. An increase or decrease in the provision for obsolescence by 1% of net sales would decrease or increase operating income by approximately $1.6 million.

ITEM 3. DISCLOSURES ABOUT MARKET RISK

The Company's exposure to market risk associated with activities in derivative financial instruments (e.g., hedging or currency swap agreements), other financial instruments and derivative commodity instruments is confined to the impact of mark-to-market changes in foreign currency rates on the Company's forward contracts and options. The Company has no debt outstanding and does not engage in any commodity-related derivative transactions. As of August 28, 2004, the Company had contracts and options which were entered into for the purpose of hedging forecasted receipts and disbursements in various foreign currencies.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our 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 quarterly report. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act.

Changes in internal controls

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. There were no significant deficiencies or material weaknesses, and therefore there were no corrective actions taken.

PART II

ITEM 1. LEGAL PROCEEDINGS

In November 2000, the Commission of the European Communities (the "Commission") began an investigation into whether Topps Europe's past distribution arrangements for the sale of Pokemon products complied with European law (the "EU investigation"). On June 17, 2003, the Commission filed a Statement of Objections against The Topps Company, Inc. and its European subsidiaries, therein coming to a preliminary conclusion that these entities infringed Article 81 of the EC treaty during 2000 by preventing parallel trade between member states of the European Union. A hearing in front of the European Commission Tribunal took place on October 23, 2003, and on May 27, 2004, the Commission found The Topps Company, Inc. and its European subsidiaries jointly and severally liable for infringement of Article 81(1) of the EC treaty. The Commission imposed a total fine of 1.6 million euros ($1.9 million) which was included in accrued expenses in the condensed consolidated balance sheet as of May 29, 2004 and in SG&A expense for the thirteen weeks ended May 29, 2004. The fine has now been paid.

On February 17, 2000, Telepresence, Inc. sued Topps and nine other manufacturers of trading cards (the "Defendants") in the Federal District Court for the Central District of California for infringement of U.S. Patent No. 5,803,501 which was issued on September 8, 1998 (the "501 Patent"). In its suit, Telepresence contended that the patent covers all types of "relic" cards that contain an authentic piece of equipment, i.e., a piece of sporting equipment or jersey. After initial discovery, on November 15, 2000, the Defendants jointly moved for summary judgment on the grounds that the named Plaintiff (Telepresence, Inc.) did not have standing to sue for infringement of the 501 Patent. The motion was granted and the Telepresence litigation was dismissed with prejudice on March 28, 2001.

After the dismissal, the 501 Patent was assigned to a company called Media Technologies, Inc. Media Technologies is under the control of the same person (the inventor, Adrian Gluck) who brought the Telepresence action. On November 19, 2001, Media Technologies sued essentially the same group of defendants in the same court for infringement of the 501 Patent. On March 13, 2002, the Defendants again moved for summary judgment based on the fact that the Telepresence action was dismissed with prejudice. That motion was granted by the District Court on April 22, 2002. Plaintiff (Media Technologies, Inc.) appealed on May 2, 2002. The Court of Appeals for the Federal Circuit reversed the judgment on July 11, 2003, and the case has been returned to Judge Stotler in the Central District of California for trial.

Discovery in the case commenced September 29, 2003 and was stayed pending the outcome of two summary judgment motions filed by defendants. On March 17, 2004, Topps filed a motion for summary judgment based on non-infringement while other defendants filed a motion for summary judgment based on patent invalidity because of prior art. Both motions were denied on July 26, 2004 and discovery has now resumed. On September 15th, 2004 defendant Upper Deck Company, LLC moved for a separate trial on the issues of infringement, damages, willfulness and counterclaims.

The trial is currently scheduled for February 2005. An adverse outcome in the litigation could result in a substantial liability for the Company. It is still too early in the matter to determine the likelihood of damages or to estimate the range of loss, if any, and, accordingly, no provision has been recorded for this matter in the accompanying condensed consolidated financial statements.

The Company is a defendant in several other civil actions which are routine and incidental to its business. In management's opinion, after consultation with legal counsel, these other actions are not likely to have a material adverse effect on the Company's consolidated financial statements.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits as required by Item 601 of Regulation S-K filed herewith:

10.22 Credit agreement, dated September 14, 2004, between the Company and JPMorgan Chase Bank.

10.23 The Topps Company, Inc. Bonus Plan for Scott Silverstein, effective August 4, 2004.

10.24 License Agreement between the Football Association Premier League Limited and Topps Europe, LTD dated September 30, 2003.

31.1 Certification of Principal Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934.

31.2 Certification of Principal Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934.

32.1 Certification of Arthur T. Shorin, Chairman and Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Catherine K. Jessup, Vice-President-Chief Financial Officer and Treasurer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K

1. Form 8-K, dated August 4, 2004, with press release, reporting the appointment of Scott Silverstein as President and Chief Operating Officer.

2. Form 8-K, dated September 24, 2004, with press release, dated September 23, 2004, reporting the Company's fiscal 2005 second quarter earnings.

3. Form 8-K, dated October 7, 2004, with press release, dated October 6, 2004, reporting the Company's fiscal 2005 third quarter dividend declaration.

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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.

THE TOPPS COMPANY, INC.

REGISTRANT

s/ Catherine K. Jessup

Catherine K. Jessup
Duly Authorized Officer

October 7, 2004

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