VERSAR INC
Form 10-Q
May 11, 2009

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 March 27, 2009

[ ] 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 1-9309

VERSAR, INC.
(Exact name of registrant as specified in its charter)

DELAWARE	54-0852979
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
6850 Versar Center Springfield, Virginia	22151
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (703) 750-3000

Not Applicable

(Former name, former address and former fiscal year, if changed since last report.)

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

Yes [ ] No [ ]

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

Large accelerated filer [ ]	Accelerated filer [ ]
Non-accelerated filer [ ] (Do not check if a smaller reporting company)	Smaller reporting company [X]

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

Yes [ ]   No [X]

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date.

Class of Common Stock	Outstanding at May 1, 2009
$.01 par value	9,102,169

VERSAR, INC. AND SUBSIDIARIES

INDEX TO FORM 10-Q

VERSAR, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
(In Thousands)

	March 27, 2009	June 27, 2008
ASSETS	(Unaudited)	
Current assets		
Cash and cash equivalents	$ 5,248	$ 11,938
Accounts receivable, net	31,006	21,596
Prepaid expenses and other current assets	1,633	1,080
Deferred income taxes	821	1,015
Total current assets	38,708	35,629
Property and equipment, net	2,487	2,152
Deferred income taxes	556	517
Goodwill	776	776
Other assets	639	754
Total assets	$ 43,166	$ 39,828
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 8,579	$ 7,731
Billings in excess of revenue	---	156
Accrued salaries and vacation	2,571	1,719
Accrued bonus	1,150	2,066
Other liabilities	1,863	1,686
Total current liabilities	14,163	13,358
Other long-term liabilities	1,403	1,417
Total liabilities	15,566	14,775
Commitments and contingencies		
Stockholders' equity		
Common stock, $.01 par value; 30,000,000 shares authorized; 9,193,635 shares and		

9,059,135 shares issued; 9,074,300 shares and 8,975,101 shares outstanding at March 27, 2009 and June 27, 2008, respectively	92	91
Retained earnings		
Capital in excess of par value	27,650	27,115
Retained earnings (accumulated deficit)	660	(1,554)
Treasury stock	(706)	(578)
Accumulated other comprehensive loss	(96)	(21)
Total stockholders' equity	27,600	25,053
Total liabilities and stockholders' equity	$ 43,166	$ 39,828

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

3

VERSAR, INC. AND SUBSIDIARIES
Consolidated Statements of Income
(Unaudited - in thousands, except per share amounts)

	For the Three-Month Periods Ended		For the Nine-Month Periods Ended	
	March 27, 2009	March 28, 2008	March 27, 2009	March 28, 2008
GROSS REVENUE	$ 31,851	$ 28,874	$ 84,816	$ 87,111
Purchased services and materials, at cost	17,470	16,212	46,670	52,348
Direct costs of services and overhead	10,026	8,866	27,408	24,401
GROSS PROFIT	4,355	3,796	10,738	10,362
Selling, general and administrative Expenses	2,525	2,250	6,759	5,882
OPERATING INCOME	1,830	1,546	3,979	4,480
OTHER EXPENSE				
(Gain) loss on marketable securities	(20)	---	326	---
Interest expense (income)	21	(35)	40	(151)
INCOME BEFORE INCOME TAXES	1,829	1,581	3,613	4,631

Income tax expense	704	668	1,399	1,956
NET INCOME	$ 1,125	$ 913	$ 2,214	$ 2,675
NET INCOME PER SHARE - BASIC	$ 0.12	$ 0.10	$ 0.24	$ 0.30
NET INCOME PER SHARE - DILUTED	$ 0.12	$ 0.10	$ 0.24	$ 0.29
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING - BASIC	9,170	8,985	9,099	8,890
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING - DILUTED	9,199	9,257	9,131	9,246

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

4

VERSAR, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
(Unaudited - in thousands)

	For the Nine-Month Periods Ended	
	March 27, 2009	March 28, 2008
Cash flows from operating activities		
Net income	$ 2,214	$ 2,675
Adjustments to reconcile net income to net cash used in operating activities		
Depreciation and amortization	750	658
Provision for doubtful accounts receivable	125	(1)
Loss on marketable securities	326	---
Loss on life insurance policy cash surrender value	167	28
Share based compensation	594	688
Deferred taxes	155	1,824
Tax benefit on restricted stock	(33)	(551)
Changes in assets and liabilities		
(Increase) decrease in accounts receivable	(9,539)	211
Increase in prepaids and other assets	(673)	(948)
Increase (decrease) in accounts payable	905	(4,554)
Increase in accrued salaries and vacation	854	644
(Decrease) increase in other liabilities	(1,021)	103
Net cash (used in) provided by operating activities	(5,176)	777

Cash flows used in investing activities		
Purchase of property and equipment	(1,102)	(622)
Purchase of marketable securities	(3,000)	---
Proceeds from sale of marketable securities	2,674	---
Premium paid on life insurance policies	(37)	(38)
Net cash used in investing activities	(1,465)	(660)
Cash flows from financing activities		
Proceeds from issuance of common stock	48	946
Purchase of treasury stock	(128)	(179)
Tax benefit on restricted stock	33	551
Net cash (used in) provided by financing activities	(47)	1,318
Effect of exchange rate changes	(2)	26
Net (decrease) increase in cash and cash equivalents	(6,690)	1,461
Cash and cash equivalents at the beginning of the period	11,938	6,296
Cash and cash equivalents at the end of the period	$ 5,248	$ 7,757
Supplementary disclosure of cash flow information:		
Cash paid during the period for		
Interest	$ 43	$ 39
Income taxes	1,501	135

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

VERSAR, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements

(A) Basis of Presentation

The accompanying consolidated condensed financial statements are presented in accordance with the requirements of Form 10-Q and consequently do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America or those normally made in Versar, Inc.'s Annual Report on Form 10-K filed with the United States Securities and Exchange Commission. These financial statements should be read in conjunction with the Company's Annual Report filed on Form 10-K for the year ended June 27, 2008 for additional information.

The accompanying consolidated financial statements include the accounts of Versar, Inc. and its wholly-owned subsidiaries ("Versar" or the "Company"). All significant intercompany balances and transactions have been eliminated in consolidation. The financial information has been prepared in accordance with the Company's customary accounting practices. Certain adjustments to the financial statements are necessary for fair presentation and are of a normal recurring nature as part of the operations of the business. In the opinion of management, the information reflects all adjustments necessary for a fair presentation of the Company's consolidated financial position as of March 27, 2009, and the results of operations for the nine-month periods ended March 27, 2009 and March 28, 2008. The results of operations for such periods, however, are not necessarily indicative of the results to be expected for a full fiscal year.

(B) Accounting Estimates

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

(C) Contract Accounting

The Company records income from major fixed-price construction and engineering contracts, extending over more than one accounting period, using the percentage-of-completion method. During performance of such contracts, estimated final contract prices and costs are periodically reviewed and revisions are made as required. The effects of these revisions are included in the periods in which the revisions are made. On cost-plus-fee contracts, revenue is recognized to the extent of costs incurred plus a proportionate amount of fee earned, and on time-and-material contracts, revenue is recognized to the extent of billable rates times hours delivered plus material and other reimbursable costs incurred. Losses on contracts are recognized when they become known. Disputes arise in the normal course of the Company's business on projects where the Company is contesting with customers for collection of funds because of events such as delays, changes in contract specifications and questions of cost allowability or collectibility. Such disputes, whether claims or unapproved change orders in the process of negotiation, are recorded at the lesser of their estimated net realizable value or actual costs incurred and only when realization is probable and can be reliably estimated. Claims against the Company are recognized where loss is considered probable and reasonably determinable in amount. Management reviews outstanding receivables on a regular basis and assesses the need for reserves taking into consideration past collection history and other events that bear on the collectibility of such receivables.

(D) Income Taxes

At March 27, 2009, the Company had approximately $1.4 million in deferred tax assets, which primarily relate to temporary differences between financial statement and income tax reporting. Such differences include depreciation, deferred compensation, accruals and reserves. Given the Company's continued improved financial performance and funded backlog over the last three years, management believes the Company will be able to utilize the full benefit of the tax asset.

(E) Debt

The Company has a line of credit facility with United Bank (the Bank) that provides for advances up to $7.5 million based upon qualifying receivables. Interest on borrowings is based upon the prime rate of interest minus 0.5%

(2.75% as of March 27, 2009). In October 2006, the Company obtained a letter of credit of approximately $1.6 million under the line of credit facility which serves as collateral for surety bond coverage provided by the Company's insurance carrier against project construction work. The letter of credit was reduced to $455,147 in January 2009. The letter of credit reduces the Company's availability on the line of credit. Availability under the line of credit at March 27, 2009 was approximately $7 million. Obligations under the credit facility are guaranteed by Versar and each subsidiary individually and are secured by accounts receivable, equipment and intangibles, plus all insurance policies on property constituting collateral of Versar and its subsidiaries. The line of credit matures in November 2009 and is subject to certain covenants related to the maintenance of financial ratios. These covenants require a minimum tangible net worth of $15 million; a maximum total liabilities to tangible net worth ratio not to exceed 2.5 to 1; and a minimum current ratio of at least 1.25 to 1. The Company was in compliance with such covenants as of March 27, 2009. The Company had no borrowings outstanding under the line of credit as of March 27, 2009.

(F) Goodwill and Other Intangible Assets

The carrying value of goodwill is approximately $776,000 relating to prior acquisitions. Goodwill is reported in the Company's Program Management business segment. The Company began reporting the Program Management business segment separately in fiscal year 2007, primarily due to the increase in business volume in Iraq and in United States construction related work. In performing its goodwill impairment analysis, management has utilized a market-based valuation approach to determine the estimated fair value of the Program Management business segment. Management engages outside professionals and valuation experts, as necessary, to assist in performing this analysis. An analysis was performed on public companies and company transactions to prepare a market-based valuation. Based upon the analysis, the estimated fair value of the Program Management business segment substantially exceeded the carrying value of the net assets of $6.5 million as of June 27, 2008. Should the Program Management business segment's financial performance not meet estimates, then impairment of goodwill would have to be further assessed to determine whether a write down of goodwill value would be warranted. If such a write down were to occur, it would negatively impact the Company's financial position and results of operations. However, it would not impact the Company's cash flow or financial debt covenants.

(G) Net Income Per Share

Basic net income per common share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per common share also includes common stock equivalents outstanding during the period, if dilutive. The Company's common stock equivalents consist of stock options and restricted stock awards.

	For the Three-Month Periods Ended		For the Nine-Month Periods Ended	
	March 27, 2009	March 28, 2008	March 27, 2009	March 28, 2008
Weighted average common shares outstanding - basic	9,169,668	8,984,653	9,099,276	8,890,338
Effect of assumed exercise of options and vesting of restricted stock awards (treasury stock method)	29,716	271,963	32,128	355,962
Weighted average common shares outstanding - diluted	9,199,384	9,256,616	9,131,404	9,246,300

For fiscal year 2009, options to purchase approximately 27,000 shares of common stock were not included in the computation of diluted earnings per share because the effect would be anti-dilutive.

VERSAR, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements (continued)

(H) Common Stock

The Company has implemented an Employee Stock Purchase Plan (ESPP) to allow eligible employees of Versar the opportunity to acquire an ownership interest in the Company's common stock. As amended, the ESPP permits employees to purchase shares of Versar common stock from the open market at 95% of its fair market value. The ESPP qualifies as an "employee stock purchase plan" under Section 423 of the Internal Revenue Code.

(I) Stock-Based Compensation

In September 2008, the Company awarded 90,000 shares of restricted stock to executive officers and employees. The awards vest over a period of 4.5 months to 16.5 months. Stock-based compensation expense relating to restricted stock and option awards totaled $594,000 and $688,000 for the nine months ended March 27, 2009 and March 28, 2008, respectively. Stock-based compensation expense relating to restricted stock and option awards for the three-month periods ending March 27, 2009 and March 28, 2008 were $80,000 and $226,000, respectively. These expenses were included in the direct costs of services and overhead lines of the Consolidated Statements of Income. During the nine months ended March 27, 2009, incentive stock options to purchase 6,000 shares of common stock and non-qualified stock options to purchase 20,000 shares of common stock with intrinsic value of approximately $7,300 and $18,000, respectively, were exercised.

In November 2005, the stockholders approved the Versar, Inc.

2005 Stock Incentive Plan (the "2005 Plan"). The 2005 Plan provides for grants of incentive awards, including stock options, SARS, restricted stock, restricted stock units and performance based awards, to directors, officers and employees of the Company and its affiliates as approved from time to time by the Company's Compensation Committee. Only employees may receive stock options classified as "incentive stock options", also known as "ISO's". The per share exercise price for options and SARS granted under the 2005 Plan may not be less than the fair market value of the common stock on the date of grant. A maximum of 400,000 shares of common stock may be awarded under the 2005 Plan. No single director, officer, or employee may receive awards of more than 100,000 shares of common stock during the term of the 2005 Plan. The ability to make awards under the 2005 Plan will terminate in November 2015. As of March 27, 2009, approximately 128,000 shares are available for future grant under the 2005 Plan.

The Company also maintains the Versar 2002 Stock Incentive Plan (the "2002 Plan"), the Versar 1996 Stock Option Plan (the "1996 Plan") and the Versar 1992 Stock Option Plan (the "1992 Plan").

Under the 2002 Plan, restricted stock and other types of stock-based awards were granted to any employee, service provider or director to whom a grant was approved from time to time by the Company's Compensation Committee. A "service provider" is defined for purposes of the 2002 Plan as an individual who is neither an employee nor a director of the Company or any of its affiliates but who provides the Company or one of its affiliates substantial and important services. No shares remain for future grant under the 2002 Plan. The Company will continue to maintain the plan until all previously granted securities have vested and been exercised, forfeited or retired. As of March 27, 2009, there were vested stock options to purchase 283,970 shares of common stock outstanding under the 2002 Plan.

Under the 1996 Plan, options were granted to key employees, directors and service providers at the fair market value on the date of grant. Each option expires on the earlier of the last day of the tenth year after the date of grant or after expiration of a period designated in the option agreement. The 1996 Plan has expired and no additional options may be granted under this plan. The Company will continue to maintain the plan until all previously granted options have been exercised, forfeited or expire. As of March 27, 2009, there were vested stock options to purchase 153,761 shares of common stock outstanding under the 1996 Plan.

Under the 1992 Plan, options were granted to key employees at the fair market value on the date of grant and became exercisable during the five-year period from the date of the grant at 20% per year. Options were granted with a ten year term and expire if not exercised by the tenth anniversary of the grant date. The 1992 Plan has expired and no additional options may be granted under this plan. The Company will continue to maintain the plan until all previously granted options have been exercised, forfeited or expire. As of March 27, 2009, there were vested stock options to purchase 83,500 shares of common stock outstanding under the 1992 Plan.

A summary of activity under the Company's stock incentive plans as of March 27, 2009, and changes during the first nine months of fiscal year 2009 are presented below:

Options	Shares (in thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value ($000)
Outstanding at June 28, 2008	571	$ 3.05		
Exercised	(26)	2.85		
Cancelled	(2)	3.43		
Outstanding at March 27, 2009	543	$ 3.10	4.44 yrs.	$ 962
Exercisable at March 27, 2009	533	$ 3.01	4.23 yrs.	$ 921

As of March 27, 2009, there were unvested options to purchase approximately 10,000 shares outstanding under the plans. Vesting of these options is conditioned on the Company's stock price reaching certain thresholds over a fixed period. The Company expects to recognize estimated compensation costs of $42,000 if the pricing and service conditions of these options are met in the future.

At March 27, 2009, there were approximately 56,000 shares of un-vested restricted stock to be vested within twelve months. A summary of the restricted stock plan activity is presented below:

Restricted Stock	Shares (in thousands)	Weighted-Average Award Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value ($000)
Outstanding at June 28, 2008	69	$ 7.93		
Granted	95	5.66		
Vested	(108)	7.17		
Outstanding at March 27, 2009	56	$ 5.39	11.4 mos.	$ 299

(J) New Accounting Pronouncements

In September 2006, the Financial Accounting Standard Board ("FASB") issued SFAS No. 157, Fair Value Measurements ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November

15, 2007, and interim periods within those fiscal years. In February 2008, FASB issued FASB Staff Position ("FSP") No. FAS 157-2, Effective Dates of FASB Statement No. 157, which deferred the effective date of SFAS 157 for all nonrecurring fair value measurements of nonfinancial assets and liabilities until fiscal years beginning after November 15, 2008. In October 2008, the FASB also issued FSP No. FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active, which clarifies the application of SFAS 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market of that financial asset is not active. The FSP observes that revisions resulting from a change in valuation technique or its application should be accounted for as a change in accounting estimate, and any effects on fair-value measurement would be recognized in the period of adoption. Our adoption of SFAS 157 on December 29, 2008 was limited to financial assets and liabilities and had no impact on our condensed consolidated financial statements in the first

nine months of fiscal 2009. We are currently evaluating the anticipated effect of this statement on the non-financial assets and non-financial liabilities in our consolidated financial statements.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an Amendment of FASB Statement No. 115 ("SFAS 159"). SFAS 159 permits entities to measure many financial instruments and certain other items at fair value to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting. Most of the provisions in SFAS 159 are elective and may be applied prospectively. Early adoption is permitted, provided the Company also elects to apply the provisions of SFAS 157. The Company has adopted the provisions of SFAS 159 in fiscal year 2009 and determined that there was no material impact on its financial position, results of operations or cash flows.

In April 2008, the Financial Accounting Standards board issued FASB Staff Position (FSP) FAS 142-3, "Determination of the Useful Life of Intangible Assets," to provide guidance for determining the useful life of recognized intangible assets and to improve consistency between the period of expected cash flows used to measure the fair value of a recognized intangible asset and the useful life of the intangible asset as determined under FASB Statement 142, Goodwill and Other Intangible Assets. The FSP requires that an entity consider its own historical experience in renewing or extending similar arrangements. However, the entity must adjust that experience based on entity-specific factors included in Statement 142. If the Company lacks historical experience to consider for similar arrangements, it would consider assumptions that market participants would use about renewal or extension, as adjusted for the entity-specific factors under Statement 142. The Company will adopt FSP FAS 142-3 in fiscal year 2010. The Company believes that upon adoption, FSP FAS 142-3 will not have an effect on the Company's financial statements.

In November 2008, the Financial Accounting Standards Board ratified a consensus opinion reached by the Emerging Issues Task Force (EITF) on EITF Issue 08-6, "Equity Method Investment Accounting Considerations," to clarify accounting and impairment considerations involving equity method investments after the effective date of both FASB Statement 141 (revised 2007), Business Combinations, and FASB Statement 160, Noncontrolling Interests in Consolidated Financial Statements. EITF Issue 08-6 includes the Task Force's conclusions on how an equity method investor should (1) initially measure its equity method investment, (2) account for impairment charges recorded by its investee, and (3) account for shares issued by the investee. EITF Issue 08-6 is effective for fiscal years beginning on or after December 15, 2008. The Company intends to adopt EITF Issue 08-6 effective January 1, 2009 on a prospective basis. The Company does not currently have any investments that are accounted for under the equity method and as a result, does not believe the adoption of EITF Issue 08-6 will have a significant effect on its financial statements.

(K) Business Segments

The Company's business is operated through four business segments as follows: Program Management, Compliance and Environmental Programs, Professional Services, and National Security. The Company evaluates and measures the performance of its business segments based on gross revenue, gross profit and operating income. As such, selling, general and administrative expenses, interest and income taxes have not been allocated to the Company's business segments. These segments were segregated based on the nature of the work, business processes, customer base and business environment in which each of the segments operates.

The Program Management business segment manages larger, more complex projects whose business processes and management are unique to the rest of the Company. The Compliance and Environmental Programs business segment provides consulting support to several federal government and municipal agencies. The Professional Services business segment provides outsourced personnel to various government agencies providing our clients with cost-effective resources. The National Security business segment provides unique solutions to the federal government including testing and evaluation and personal protective solutions to meet our clients' needs.

Summary of financial information for each of the Company's segments follows:

	For the Three-Month Periods Ended		For the Nine-Month Periods Ended	
	March 27, 2009	March 28, 2008	March 27, 2009	March 28, 2008

GROSS REVENUE				
Program Management	$ 21,580	$ 17,823	$ 54,310	$ 51,627
Compliance and Environmental Programs	4,682	6,859	15,146	23,784
Professional Services	3,050	2,160	8,012	5,938
National Security	2,539	2,032	7,348	5,762
	$ 31,851	$ 28,874	$ 84,816	$ 87,111
GROSS PROFIT(A)				
Program Management	$ 3,515	$ 2,608	$ 7,986	$ 6,980
Compliance and Environmental Programs	106	490	641	1,650
Professional Services	411	346	1,220	960
National Security	323	352	891	772
	$ 4,355	$ 3,796	$ 10,738	$ 10,362
Selling, general and administrative expenses	(2,525)	(2,250)	(6,759)	(5,882)
OPERATING INCOME	$ 1,830	$ 1,546	$ 3,979	$ 4,480

(A) Gross profit is defined as gross revenue less purchased services and materials and direct costs of services and overhead.

	Periods Ended	
	March 27, 2009	June 27, 2008
	(In thousands)	
IDENTIFIABLE ASSETS		
Program Management	$ 21,922	$ 11,405
Compliance and Environmental Programs	5,467	8,762
Professional Services	4,112	1,554
National Security	2,334	2,693
Corporate and Other	9,331	15,414
Total Assets	$ 43,166	$ 39,828

(L) Marketable Securities

During the first quarter of fiscal year 2009, the Company recorded a $352,000 loss on marketable securities the Company was holding in the FISCO Income Plus Funds. The FISCO fund received an immediate demand margin call from its broker, UBS. Rather than allow the fund the customary time to satisfy the margin call at the end of the day, UBS demanded the fund cover all calls and puts at high premiums immediately or indicated it would take control of the fund and start liquidating the fund itself. The fund has terminated its relationship with UBS and transferred the assets to a new custodian. The fund has taken legal action against UBS to cover its losses. The Company will participate in any recovery from any such action. The Company has reallocated its remaining assets from marketable securities to its primary bank due to the volatile nature of the market. During the three months ended March 27, 2009, the Company recovered $26,000 of the initial loss before the funds were liquidated from the FISCO fund. A loss on marketable securities of $326,000 is reflected in the consolidated statement of income for the nine months ended March 27, 2009, as a result of the liquidation of the FISCO fund.

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

This report contains certain forward-looking statements which are based on current expectations. Actual results may differ materially. The forward-looking statements include without limitation, those regarding the continued award of future work or task orders from government and private clients, cost controls and reductions, the expected resolution of delays in billing of certain projects, and the possible impact of current and future claims against the Company based upon negligence and other theories of liability. Forward-looking statements involve numerous risks and uncertainties that could cause actual results to differ materially, including, but not limited to, the possibility that the demand for the Company's services may decline as a result of possible changes in general and industry specific economic conditions and the effects of competitive services and pricing; the possibility that the Company will not be able to perform work within budget or contractual limitations; one or more current or future claims made against the Company may result in substantial liabilities; the possibility that the Company will not be able to attract and retain key professional employees; changes to or failure of the Federal government to fund certain programs in which the Company participates; delays in project funding; and such other risks and uncertainties, described in our Form 10-K for fiscal year ended June 27, 2008 and in other reports and other documents filed by the Company from time to time with the Securities and Exchange Commission.

Financial Trends

During fiscal year 2008, backlog continued to grow, increasing by 12% to $64 million at June 27, 2008. In the first nine months of fiscal year 2009, the Company was awarded $97 million in additional work, which resulted in an increase in funded backlog to $76 million as of March 27, 2009. However, during the first nine months of fiscal year 2009, the Company experienced a 3% decline in gross revenues. This decline was primarily attributable to a decrease in the award of additional municipal aquatic facility work and the impact on our commercial and municipal work as a result of the poor economic conditions that have been in effect throughout in our Compliance and Environmental Programs business segment in fiscal year 2009. Several awards of new, larger projects for the Program Management business segment were received late during the first quarter of fiscal year 2009 and have resulted in additional construction work during the third and fourth quarters of fiscal year 2009. The Company continues to experience a decline in the award of aquatic facility work and the Company expects the Compliance and Environmental Programs business segment to continue to experience a decline in revenues during the balance of fiscal year 2009 as a result of the lack of commercial and municipal project funding due to the overall poor U.S. economy.

Approximately 55% of the Company's business volume was related to the reconstruction efforts in Iraq and Afghanistan for fiscal year 2009. However, the Company has continued to take steps during fiscal year 2009 to further diversify its business to prepare for a time when opportunities in Iraq may be reduced or eliminated. The Company has focused primarily on BRAC efforts and requirements which have been delayed as a result of the war in Iraq. We continue to follow the funding shifts in Iraq to Afghanistan, and a new business initiative in the United Arab Emirates, to maintain and expand our international business basis. We believe the funding of BRAC work world-wide represents our greatest opportunity for growth in the balance of fiscal year 2009. We are also pursuing federal stimulus funded projects which are in line with our federal and municipal business base.

There are a number of risk factors or uncertainties that could significantly impact our future financial performance including the following:

* General economic or political conditions;
* Threatened or pending litigation;
* The timing of expenses incurred for corporate initiatives;
* Employee hiring, utilization, and turnover rates;
* The seasonality of spending in the federal government and for commercial clients;
* Delays in project contracted engagements;
* Unanticipated contract changes impacting profitability;

* Increased pricing competition due to reductions in prices by our competitors;
* The ability to obtain follow-on project work;
* Failure to properly manage projects resulting in additional costs;
* The cost of compliance for the Company's laboratories;
* The results of a negative government audit potentially impacting our costs, reputation and ability to work with the federal government;
* Loss of key personnel;
* The ability to compete in a highly competitive environment; and
* Federal funding delays due to the war in Iraq and Afghanistan.

Results of Operations

Third Quarter Comparison of Fiscal Year 2009 and 2008

	For the Three-Month Periods Ended	
	March 27, 2009	March 28, 2008
GROSS REVENUE		
Program Management	$ 21,580	$ 17,823
Compliance and Environmental Programs	4,682	6,859
Professional Services	3,050	2,160
National Security	2,539	2,032
	$ 31,851	$ 28,874

Gross revenue for the third quarter of fiscal year 2009 was $31,851,000, an increase of $2,977,000 (10%) over that reported in the third quarter of fiscal year 2008. Gross revenue for the Program Management business segment was $21,580,000, an increase of $3,757,000 (21%) compared to that reported in the third quarter of fiscal year 2008. The increase is attributable to our efforts to support both the Air Force and the Army in Iraq as part of the reconstruction support efforts. Gross revenue for the Compliance and Environmental Programs business segment for the third quarter of fiscal year 2009 was $4,682,000, a decrease of $2,177,000 (32%) compared to that reported in the third quarter of fiscal year 2008. The decrease is attributable to a decline in follow on work for municipal aquatic facilities as a result of the overall poor U.S. economy. Gross revenue for the Professional Services business segment was $3,050,000, an increase of $890,000 (41%) compared to that reported in the third quarter of fiscal year 2008. The increase was attributable to increased revenues from the Company's U.S. Army's contracts. Gross revenue for the National Security business segment for the third quarter of fiscal year 2009 was $2,539,000, an increase of $507,000 (25%) compared to that reported in the third quarter of fiscal year 2008. The increase is attributable to increased chemical laboratory testing work during the quarter.

Purchased services and materials increased by $1,258,000 (8%) in the third quarter of fiscal year 2009 compared to that reported in the third quarter of fiscal year 2008. The increase was attributable to increases in subcontracted work in the Program Management business segment, the Professional Services business segment and the National Security business segment, which was, in turn, offset, in part by a reduction of approximately $1.6 million of purchased services and materials in the Compliance and Environmental business segment as a result of the lack of follow on municipal aquatic work and current economic conditions which has resulted in a reduction in municipal and commercial business activity.

Direct costs of services and overhead include the cost to Versar of direct and overhead staff, including recoverable and unallowable costs that are directly attributable to contracts. Direct costs of services and overhead increased by $1,160,000 (13%) in the third quarter of fiscal year 2009 compared to that reported in the third quarter of fiscal year 2008. The increase is primarily due to the business growth in the Program Management, Professional Services, and National Security business segments, offset, in part, by the necessary overhead cost reductions in the Compliance and Environmental business segment because of its reduced business volume as discussed above.

ITEM 2 Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Gross profit for the third quarter of fiscal year 2009 was $4,355,000, a $559,000 (15%) increase over that reported in the third quarter of fiscal year 2008. The increase is primarily attributable to the increased gross revenues and improved operating margins during the third quarter of fiscal year 2009.

	For the Three-Month Periods Ended	
	March 27, 2009	March 28, 2008
GROSS PROFIT		
Program Management	$ 3,515	$ 2,608
Compliance and Environmental Programs	106	490
Professional Services	411	346
National Security	323	352
	$ 4,355	$ 3,796

Gross profit for the Program Management business segment was $3,515,000, an increase of $907,000 (35%) over that reported in the third quarter of fiscal year 2008. The increase is due to the increased gross revenues and improved operating margins as a result of cost reduction efforts and improved project profit margins. Gross profit for the Compliance and Environmental Programs business segment for the third quarter of fiscal year 2009 was $106,000, a decrease of $384,000 (78%) compared to that reported in the third quarter of fiscal year 2008. The decrease is due to the economic slow down, the lack of follow on municipal aquatic renovation work and project reserves of approximately $150,000 during the third quarter. Gross profit for the Professional Services business segment was $411,000, an increase of $65,000 (19%) compared to that reported in the third quarter in fiscal year 2008. The increase is attributable to the increased gross revenues as mentioned above. Gross profit for the National Security business segment for the third quarter of fiscal year 2009 was $323,000, a decrease of $29,000 compared to that reported in the third quarter of fiscal year 2008. The decrease is due to delays in executing personal protective suit orders which were primarily caused by third party manufacturing delays.

Selling, general and administrative expenses increased by $275,000 during the third quarter of fiscal year 2009 compared to that reported in the third quarter of fiscal year 2008. The increase is primarily due to increased business development activity supporting all business segments to continue the business growth of the Company.

Operating income for the third quarter of fiscal year 2009 was $1,830,000, an increase of $284,000 (18%) compared to that reported in the third quarter of fiscal year 2008. The increase is primarily due to the improved financial performance of the Program Management business segment during the quarter, which was, partially, offset by reduced profitability in the Compliance and Environmental Programs business segment as mentioned above.

Interest expense for the third quarter of fiscal year 2009 was

$21,000, a decrease of $56,000 over that reported in the third quarter of fiscal year 2008. The decrease was due to the lower federal prime interest rate and the fact that there was no off setting interest income received on funds held by the Company in its bank account.

Income tax expense for the third quarter of fiscal year 2009 was $704,000, an increase of $36,000 compared to that reported in the third quarter of fiscal year 2008. The effective tax rates were 38% and 42% for the third quarters of fiscal years 2009 and 2008, respectively.

Versar's net income for the third quarter of fiscal year 2009 was $1,125,000 compared to $913,000 in the third quarter of fiscal year 2008, a 23% increase compared to that reported in the same period last year.

ITEM 2 Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Nine Month Comparison of Fiscal Year 2009 and 2008

	For the Nine-Month Periods Ended	
	March 27, 2009	March 28, 2008
GROSS REVENUE		
Program Management	$ 54,310	$ 51,627
Compliance and Environmental Programs	15,146	23,784
Professional Services	8,012	5,938
National Security	7,348	5,762
	$ 84,816	$ 87,111

Gross revenue for the first nine months of fiscal year 2009 was $84,816,000, a decrease of $2,295,000 (3%) over that reported in the first nine months of fiscal year 2008. Gross revenue for the first nine months of fiscal year 2009 in the Program Management business segment was $54,310,000, an increase of $2,683,000 (5%) compared to that reported in the first nine months of fiscal year 2008. The increase is attributable to our efforts to support both the Air Force and the Army in Iraq and Afghanistan as well as the Company's new business initiative in the United Arab Emirates of approximately $1.6 million. Gross revenue for the first nine months of fiscal year 2009 in the Compliance and Environmental Programs business segment was $15,146,000, a decrease of $8,638,000 (36%) compared to that reported in the first nine months of fiscal year 2008. The decrease is primarily attributable to a decline throughout fiscal year 2009 in the availability of work for municipal aquatic facilities due to the current economic conditions. Gross revenue for the first nine months of fiscal year 2009 in the Professional Services business segment was $8,012,000, an increase of $2,074,000 (35%) compared to that reported in the first nine months of fiscal year 2008. The increase was attributable to a contract award received in the fourth quarter of fiscal year 2008 with the U.S. Army to provide additional professional services. Gross revenue for the first nine months of fiscal year 2009 in the National Security business segment was $7,348,000, an increase of $1,586,000 (28%) compared to that reported in the first nine months of fiscal year 2008. The increase is attributable to increased laboratory testing work during the first nine months of fiscal year 2009.

Purchased services and materials decreased by $5,678,000 (11%) in the first nine months of fiscal year 2009 compared to that reported in the first nine months of fiscal year 2008. The decrease was attributable to the decline in subcontracted work in the Compliance and Environmental Programs business segment as a result of the decreased work for municipal aquatic facilities as mentioned above.

Direct costs of services and overhead include the cost to Versar of direct and overhead staff, including recoverable and unallowable costs that are directly attributable to contracts. Direct costs of services and overhead increased by $3,007,000 (12%) in the first nine months of fiscal year 2009 compared to that reported in the first nine months of fiscal year 2008. The increase is due increased marketing and sales costs, staffing and recruiting costs in support of the Company's business growth during the third quarter of fiscal year 2009.

Gross profit for the first nine months of fiscal year 2009 was $10,738,000, a $376,000 (4%) increase over that reported in the first nine months of fiscal year 2008. The increase is attributable to the increased gross revenues in the Program Management, Professional Services and National Security business segments, which was, partially, offset, by the poor operating performance in the Compliance and Environmental Programs business segment.

ITEM 2 Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

	For the Nine-Month Periods Ended	
	March 27, 2009	March 28, 2008
GROSS PROFIT		
Program Management	$ 7,986	$ 6,980
Compliance and Environmental Programs	641	1,650
Professional Services	1,220	960
National Security	891	772
	$ 10,738	$ 10,362

Gross profit for the Program Management business segment for the first nine months of fiscal year 2009 was $7,986,000, an increase of $1,006,000 (14%) compared to that reported in the first nine months of fiscal year 2008. The increase is due to the increased gross revenues and as a result of cost reduction efforts and improved project profit margins. Gross profit for the Compliance and Environmental Programs business segment for the first nine months of fiscal year 2009 was $641,000, a decrease of

$1,009,000 (61%) compared to that reported in the first nine months of fiscal year 2008. The decrease is due to poor operating performance resulting from the impact of current economic conditions on the municipal aquatic work previously done by this segment. Gross profit for the Professional Services business segment was $1,220,000, an increase of $260,000 (27%) compared to that reported in the first nine months of fiscal year 2008. The increase is attributable to the increased gross revenues as mentioned above. Gross profit for the National Security business segment for the first nine months of fiscal year 2009 was $891,000, an increase of $119,000 (15%) compared to that reported in the first nine months of fiscal year 2008. The increase is due to increased laboratory work and improved operating margins during the period.

Selling, general and administrative expenses increased by $877,000 during the first nine months of fiscal year 2009 compared to that reported in the first nine months of fiscal year 2008. The increase is primarily due to increased business development activity in support of all business segments to continue the business growth of the Company as well as Sarbanes Oxley compliance costs.

Operating income for the first nine months of fiscal year 2009 was $3,979,000, a $501,000 (11%) decrease compared to that reported in the first nine months of fiscal year 2008. The decrease is due to the reduced revenues and operating performance in the Company's Compliance and Environmental Programs business segment and increased selling, general and administrative costs.

During the first quarter of fiscal year 2009, the Company recorded a $326,000 loss on marketable securities the Company was holding in the FISCO Income Plus Funds. The FISCO fund received an immediate demand margin call from its broker, UBS. Rather than allow the fund the customary time to satisfy the margin call at the end of the day, UBS demanded the fund cover all calls and puts at high premiums immediately or indicated it would take control of the fund and start liquidating the fund itself. The fund has terminated its relationship with UBS and transferred the assets to a new custodian. The fund currently is taking legal action against UBS to cover its losses. The Company will participate in any recovery from any such action. The Company has reallocated its remaining assets from marketable securities to its primary bank due to the volatile nature of the market.

Interest expense for the first nine months of fiscal year 2009 was $40,000, a decrease of $191,000 compared to that reported in the first nine months of fiscal year 2008. The decrease was due to lower interest rates and a decline in cash balances maintained with the Company's bank.

Income tax expense for the first nine months of fiscal year 2009 was $1,399,000, a decrease of $557,000 compared to that reported in the first nine months of fiscal year 2008. The effective tax rates were 39% and 42%, for the first nine months of fiscal years 2009 and 2008, respectively.

Versar's net income for the first nine months of fiscal year 2009 was $2,214,000 compared to $2,675,000 in the first nine months of fiscal year 2008. The decrease is due to the reduced revenues and operating performance in the Company's Compliance and Environmental business segment, increased selling, general and administrative costs and the loss on marketable securities discussed above.

Liquidity and Capital Resources

The Company's working capital as of March 27, 2009 approximated $24,545,000, an increase of $2,274,000 (10%) from June 27, 2008. In addition, at March 27, 2009, the Company's current ratio was 2.73, an improvement over the 2.67 current ratio reported on June 27, 2008. The increase was due to increases in current assets during the first nine months of fiscal year 2009.

The Company has a line of credit facility with United Bank (the Bank) that provides for advances up to $7.5 million based upon qualifying receivables. Interest on borrowings is based upon the prime rate of interest minus 0.5% (2.75% as of March 27, 2009). In October 2006, the Company obtained a letter of credit of approximately $1.6 million which serves as collateral for surety bond coverage provided by the Company's insurance carrier against project construction work. The letter of credit was reduced to $455,147 in January 2009. The letter of credit reduces the Company's availability on the line of credit. Availability under the line of credit at March 27, 2009 was approximately $7.0 million. There are no borrowings outstanding under the line of credit as of March 27, 2009. Obligations under the credit facility are guaranteed by Versar and each subsidiary individually and are secured by accounts receivable, equipment and intangibles, plus all insurance policies on property constituting collateral of Versar and its subsidiaries. The line of credit matures in November 2009 and is subject to certain covenants related to the maintenance of financial ratios. These covenants require a minimum tangible net worth of $15 million; a maximum total liabilities to tangible net worth ratio not to exceed 2.5 to 1; and a minimum current ratio of at least 1.25 to 1. The Company was in compliance with such covenants as of March 27, 2009.

Management believes that the current cash balance of over $5.2 million along with anticipated cash from operations and existing availability under the line of credit, are sufficient to meet its liquidity needs within the next year. Expected capital requirements for the remainder of fiscal year 2009 are approximately $200,000 primarily to maintain our existing information technology systems and software applications. Such capital requirements will be funded through existing working capital.

The global economic business downturn has primarily impacted our commercial and state and municipal work in our Compliance and Environmental Programs business segment. As such, we are adjusting the Company's cost structure to minimize the impact to the overall Company financial performance.

The Company's cash balances held with United Bank have decreased by approximately $6.7 million, primarily a result of increased receivables of $9.4 million. The increase in receivables resulted from a change in certain contract vehicles, which resulted in an increase in the number of days our invoices remain outstanding for payment. The Company also paid approximately $1.5 million in taxes for fiscal year 2008 and estimated taxes for fiscal year 2009. We do not anticipate that this trend will continue.

Critical Accounting Policies and Related Estimates That Have a Material Effect on Versar's Consolidated Financial Statements

Below is a discussion of the accounting policies and related estimates that we believe are the most critical to understanding the Company's consolidated financial position and results of operations, which require management judgments and estimates, or involve uncertainties. Information regarding our other accounting policies is included in the notes to our consolidated financial statements included elsewhere in this report on Form 10-Q and in our annual report on Form 10-K filed for the 2008 fiscal year.

Revenue recognition: Contracts in process are stated at the lower of actual costs incurred plus accrued profits or incurred costs reduced by progress billings. On cost-plus fee contracts, revenue is recognized to the extent of costs incurred plus a proportionate amount of fee earned, and on time-and-material contracts, revenue is recognized to the extent of billable rates times hours delivered plus material and other reimbursable costs incurred. The Company records income from major fixed-price contracts, extending over more than one accounting period, using the percentage-of-completion method. During the performance of such contracts, estimated final contract prices and costs are periodically reviewed and revisions are made as required. Fixed price contracts can be significantly impacted by changes in contract performance, contract delays, liquidated damages and penalty provisions and contract change orders, which may affect the revenue recognition on a project. Revisions to such estimates are made when they become known.

There is the possibility that there will be currently unforeseeable adjustments to our estimated contract revenues, costs and margins for fixed price contracts in the future, particularly in the later stages of these contracts. Such adjustments are common in the construction industry given the nature of the contracts. These adjustments could either positively or negatively impact our estimates due to the circumstances surrounding the negotiations of change orders, the impact of schedule slippage, subcontractor claims and contract disputes which are normally resolved at the end of the contract.

Allowance for doubtful accounts: Disputes arise in the normal course of the Company's business on projects where the Company is contesting with customers for collection of funds because of events such as delays, changes in contract specifications and questions of cost allowability and collectibility. Such disputes, whether claims or unapproved change orders in process of negotiation, are recorded at the lesser of their estimated net realizable value or actual costs incurred and only when realization is probable and can be reliably estimated. Management reviews outstanding receivables on a regular basis and assesses the need for reserves, taking into consideration past collection history and other events that bear on the collectibility of such receivables.

Asset retirement obligation: The Company has recorded an asset retirement obligation associated with the estimated clean-up costs for its chemical laboratory in its National Security business segment. In accordance with SFAS 143, the Company estimated the costs to clean up the laboratory and return it to its original state at a present value of approximately $497,000. The Company currently estimates the amortization and accretion expense to be approximately $180,000 to $190,000 per year over the next 2 1/2 years. The Company is rigorously pursuing reimbursement for such costs and other costs from the U.S. Army as a significant portion of the chemical agent that was used in the chemical laboratory was government owned. If the Company determines that the estimated clean up cost is higher than expected or the likelihood of recovery from the U.S. Army is remote, such adjustments will be reflected when they become known in accordance with SFAS 143. At March 27, 2009, the Company has accrued approximately $574,000 long-term liability to clean up the chemical laboratory.

Goodwill and other intangible assets: The carrying value of goodwill is approximately $776,000. In performing its goodwill impairment analysis, management has utilized a market-based valuation approach to determine the estimated fair value of the Program Management business segment. Management engages outside professionals and valuation experts, as necessary, to assist in performing this analysis on an annual basis. An analysis is performed on public companies and company transactions to prepare a market-based valuation. Based upon the latest analysis as of June 27, 2008, the estimated fair value of the Program Management business segment exceeded the carrying value of the net assets of $6.5 million on an enterprise value basis by a substantial margin. Should the Program Management business segment's financial performance not meet estimates, then impairment of goodwill would have to be further assessed to determine whether a write down of goodwill value would be warranted. If such a write down were to occur, it would negatively impact the Company's financial position and results of operations. However, it would not impact the Company's cash flow or financial debt covenants.

New accounting pronouncements: In September 2006, the Financial Accounting Standard Board ("FASB") issued SFAS No. 157, Fair Value Measurements ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. In February 2008, FASB issued FASB Staff Position ("FSP") No. FAS 157-2, Effective Dates of FASB Statement No. 157, which deferred the effective date of SFAS 157 for all nonrecurring fair value measurements of nonfinancial assets and liabilities until fiscal

years beginning after November 15, 2008. In October 2008, the FASB also issued FSP No. FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active, which clarifies the application of SFAS 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market of that financial asset is not active. The FSP observes that revisions resulting from a change in valuation technique or its application should be accounted for as a change in accounting estimate, and any effects on fair-value measurement would be recognized in the period of adoption. Our adoption of SFAS 157 on December 29, 2008 was limited to financial assets and liabilities and had no impact on our condensed consolidated financial statements in the first nine months of fiscal 2009. We are currently evaluating the anticipated effect of this statement on the non-financial assets and non-financial liabilities in our consolidated financial statements.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an Amendment of FASB Statement No. 115 ("SFAS 159"). SFAS 159 permits entities to measure many financial instruments and certain other items at fair value to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting. Most of the provisions in SFAS 159 are elective and may be applied prospectively. Early adoption is permitted, provided the Company also elects to apply the provisions of SFAS 157. The Company has adopted the provisions of SFAS 159 in fiscal year 2009 and determined that there was no material impact on its financial position, results of operations or cash flows.

In April 2008, the Financial Accounting Standards board issued FASB Staff Position (FSP) FAS 142-3, "Determination of the Useful Life of Intangible Assets," to provide guidance for determining the useful life of recognized intangible assets and to improve consistency between the period of expected cash flows used to measure the fair value of a recognized intangible asset and the useful life of the intangible asset as determined under FASB Statement 142, Goodwill and Other Intangible Assets. The FSP requires that an entity consider its own historical experience in renewing or extending similar arrangements. However, the entity must adjust that experience based on entity-specific factors included in Statement 142. If the Company lacks historical experience to consider for similar arrangements, it would consider assumptions that market participants would use about renewal or extension, as adjusted for the entity-specific factors under Statement 142. The Company will adopt FSP FAS 142-3 in fiscal year 2010. The Company believes that upon adoption, FSP FAS 142-3 will not have an effect on the Company's financial statements.

In November 2008, the Financial Accounting Standards Board ratified a consensus opinion reached by the Emerging Issues Task Force (EITF) on EITF Issue 08-6, "Equity Method Investment Accounting Considerations," to clarify accounting and impairment considerations involving equity method investments after the effective date of both FASB Statement 141 (revised 2007), Business Combinations, and FASB Statement 160, Noncontrolling Interests in Consolidated Financial Statements. EITF Issue 08-6 includes the Task Force's conclusions on how an equity method investor should (1) initially measure its equity method investment, (2) account for impairment charges recorded by its investee, and (3) account for shares issued by the investee. EITF Issue 08-6 is effective for fiscal years beginning on or after December 15, 2008. The Company intends to adopt EITF Issue 08-6 effective January 1, 2009 on a prospective basis. The Company does not currently have any investments that are accounted for under the equity method and as a result, does not believe the adoption of EITF Issue 08-6 will have a significant effect on its financial statements.

Impact of Inflation

Versar seeks to protect itself from the effects of inflation. The majority of contracts the Company performs are for a period of a year or less or are cost-plus-fixed-fee type contracts and, accordingly, are less susceptible to the effects of inflation. Multi-year contracts include provisions for projected increases in labor and other costs.

Contingencies

Versar and its subsidiaries are parties to various legal actions arising in the normal course of business. The Company believes that the ultimate resolution of these legal actions will not have a material adverse effect on its consolidated financial position and results of operations. (See Part II, Item 1 - Legal Proceedings).

ITEM 2 Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Business Segments

Versar currently has four business segments: Program Management, Compliance and Environmental Programs, Professional Services, and National Security. See Note J of the Notes to the Consolidated Financial Statements for details regarding these segments.

Item 3 - Quantitative and Qualitative Disclosures About Market Risk

The Company has not entered into any transactions using derivative financial instruments or derivative commodity instruments and believes that its exposure to interest rate risk and other relevant market risk is not material.

Item 4T - Controls and Procedures

As of the last day of the period covered by this report, the Company carried out an evaluation, under the supervision of the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective, as of such date, to ensure that required information will be disclosed on a timely basis in its reports under the Exchange Act.

Further, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures have been designed to ensure that information required to be disclosed in reports filed by us under the Exchange Act is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, in a manner to allow timely decisions regarding the required disclosure.

There were no changes in the Company's internal control over financial reporting during the last quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1 - Legal Proceedings

Versar and its subsidiaries are parties from time to time to various legal actions arising in the normal course of business. The Company believes that any ultimate unfavorable resolution of these legal actions will not have a material adverse effect on its consolidated financial condition and results of operations.

Item 1A - Risk Factors

The risk factors discussed in Part 1, "Item 1A. Risk Factors," in our Annual Report on Form 10-K for the year ended June 27, 2008, should be considered in conjunction with the other information set forth in this quarterly report on Form 10-Q.

If our partners fail to perform their contractual obligations on a project, we could be exposed to legal liability, loss of reputation or reduced profits.

We, from time to time, enter joint venture agreements and other contractual arrangements with outside partners to jointly bid on and execute a particular project. The success of these joint projects depends in part on the satisfactory performance of the contractual obligations of our partners. If any of our partners fail to satisfactorily perform their contractual obligations, we may be required to make additional investments and provide additional services to complete projects, increasing our cost on those projects. If we are unable to adequately address a partner's performance issues, then our client could terminate the joint project, exposing us to legal liability, loss of reputation or reduced profits.

Item 6 - Exhibits

(a) Exhibits

Exhibit No.	Description	Reference
10.1*	Employment Agreement between Charles S. Cox and Versar, Inc. entered into on February 2, 2009 and effective as of January 3, 2009.	(A)
31.1 and 31.2	Certification pursuant to Securities Exchange Act Section 13a-14.	
32.1 and 32.2	Certification under Section 906 of the Sarbanes-Oxley Act of 2002.	

---

* Indicates management contract or compensatory plan or arrangement.

(A) Incorporated by reference to the similarly numbered exhibit to the Registrant's Form 8-K Current Report dated February 2, 2009 filed with the Commission on February 4, 2009.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

VERSAR, INC.
(Registrant)

By: /S/ Theodore M. Prociv

Theodore M. Prociv
Chief Executive Officer,
President, and Director

By: /S/ Lawrence W. Sinnott

Lawrence W. Sinnott
Executive Vice President,
Chief Operating Officer,
Chief Financial Officer,
Treasurer, and Principal
Accounting Officer

Date: May 11, 2009