

Compass Diversified Holdings
Form 10-Q
May 07, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended March 31, 2014

Or

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

For the transition period from _____ to _____

COMPASS DIVERSIFIED HOLDINGS

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of

001-34927
(Commission

57-6218917
(I.R.S. employer

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Non-accelerated filer

Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of May 1, 2014, there were 48,300,000 shares of Compass Diversified Holdings outstanding.

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COMPASS DIVERSIFIED HOLDINGS
QUARTERLY REPORT ON FORM 10-Q
For the period ended March 31, 2014
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NOTE TO READER

In reading this Quarterly Report on Form 10-Q, references to:

the Trust and Holdings refer to Compass Diversified Holdings;

businesses, operating segments, subsidiaries and reporting units refer to, collectively, the businesses controlled by the Company;

the Company refer to Compass Group Diversified Holdings LLC;

the Manager refer to Compass Group Management LLC (CGM);

the initial businesses refer to, collectively, Staffmark Holdings, Inc. (Staffmark), Crosman Acquisition Corporation, Compass AC Holdings, Inc. (ACI or Advanced Circuits) and Silvue Technologies Group, Inc.;

the 2012 acquisition refer to the acquisition of Arnold Magnetic Technologies Holdings Corporation (Arnold or Arnold Magnetics);

the Trust Agreement refer to the amended and restated Trust Agreement of the Trust dated as of November 1, 2010;

the Credit Facility refer to a credit agreement (as amended) with a group of lenders led by Toronto Dominion (Texas) LLC, as agent, which provides for the Revolving Credit Facility and the Term Loan Facility;

the Revolving Credit Facility refer to the \$320 million Revolving Credit Facility provided by the Credit Facility that matures in April 2017;

the Term Loan Facility refer to the \$279.0 million Term Loan Facility, as of March 31, 2014, provided by the Credit Facility that matures in October 2017;

the LLC Agreement refer to the fourth amended and restated operating agreement of the Company dated as of January 1, 2012; and

we, us and our refer to the Trust, the Company and the businesses together.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, contains both historical and forward-looking statements. We may, in some cases, use words such as project, predict, believe, anticipate, plan, expect, estimate, intend, should, potentially, or may, or other words that convey uncertainty of future events or outcomes to identify these forward-looking statements. Forward-looking statements in this Quarterly Report on Form 10-Q are subject to a number of risks and uncertainties, some of which are beyond our control, including, among other things:

our ability to successfully operate our businesses on a combined basis, and to effectively integrate and improve future acquisitions;

our ability to remove CGM and CGM's right to resign;

our organizational structure, which may limit our ability to meet our dividend and distribution policy;

our ability to service and comply with the terms of our indebtedness;

our cash flow available for distribution and reinvestment and our ability to make distributions in the future to our shareholders;

our ability to pay the management fee and profit allocation if and when due;

our ability to make and finance future acquisitions;

our ability to implement our acquisition and management strategies;

the regulatory environment in which our businesses operate;

trends in the industries in which our businesses operate;

changes in general economic or business conditions or economic or demographic trends in the United States and other countries in which we have a presence, including changes in interest rates and inflation;

environmental risks affecting the business or operations of our businesses;

our and CGM's ability to retain or replace qualified employees of our businesses and CGM;

costs and effects of legal and administrative proceedings, settlements, investigations and claims; and

extraordinary or force majeure events affecting the business or operations of our businesses.

Our actual results, performance, prospects or opportunities could differ materially from those expressed in or implied by the forward-looking statements. Additional risks of which we are not currently aware or which we currently deem immaterial could also cause our actual results to differ.

In light of these risks, uncertainties and assumptions, you should not place undue reliance on any forward-looking statements. The forward-looking events discussed in this Quarterly Report on Form 10-Q may not occur. These forward-looking statements are made as of the date of this Quarterly Report on Form 10-Q. We undertake no obligation to publicly update or revise any forward-looking statements to reflect subsequent events or circumstances, whether as a result of new information, future events or otherwise, except as required by law.

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PART I

FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Compass Diversified Holdings

Condensed Consolidated Balance Sheets

<i>(in thousands)</i>	March 31, 2014 (unaudited)	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	\$ 86,622	\$ 113,229
Accounts receivable, less allowances of \$3,758 at March 31, 2014 and \$3,424 at December 31, 2013	129,563	111,736
Inventories	168,598	152,948
Prepaid expenses and other current assets	22,630	21,220
Total current assets	407,413	399,133
Property, plant and equipment, net	71,477	68,059
Goodwill	259,982	246,611
Intangible assets, net	336,334	310,359
Deferred debt issuance costs, less accumulated amortization of \$4,731 at March 31, 2014 and \$4,161 at December 31, 2013	7,918	8,217
Other non-current assets	13,058	12,534
Total assets	\$ 1,096,182	\$ 1,044,913
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	\$ 66,623	\$ 62,539
Accrued expenses	50,845	55,590
Due to related party	4,330	4,528
Current portion, long-term debt	5,350	2,850
Other current liabilities	4,050	4,623
Total current liabilities	131,198	130,130
Deferred income taxes	59,192	60,024
Long-term debt, less original issue discount	319,471	280,389
Other non-current liabilities	23,831	5,435
Total liabilities	533,692	475,978

Stockholders' equity

Trust shares, no par value, 500,000 authorized; 48,300 shares issued and outstanding at March 31, 2014 and December 31, 2013	725,453	725,453
Accumulated other comprehensive income	684	693
Accumulated deficit	(265,333)	(252,761)
Total stockholders' equity attributable to Holdings	460,804	473,385
Noncontrolling interest	101,686	95,550
Total stockholders' equity	562,490	568,935
Total liabilities and stockholders' equity	\$ 1,096,182	\$ 1,044,913

See notes to condensed consolidated financial statements.

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Compass Diversified Holdings
Condensed Consolidated Statements of Operations
(unaudited)

	Three months ended	
	March 31,	
	2014	2013
<i>(in thousands, except per share data)</i>		
Net sales	\$ 246,048	\$ 241,567
Cost of sales	169,696	165,194
Gross profit	76,352	76,373
Operating expenses:		
Selling, general and administrative expense	46,173	41,209
Supplemental put expense		6,396
Management fees	4,735	4,316
Amortization expense	7,349	7,630
Operating income	18,095	16,822
Other income (expense):		
Interest income	9	2
Interest expense	(4,581)	(5,341)
Amortization of debt issuance costs	(570)	(485)
Other income, net	184	327
Income before income taxes	13,137	11,325
Provision for income taxes	5,764	7,699
Net income	7,373	3,626
Less: Net income attributable to noncontrolling interest	2,714	2,032
Net income attributable to Holdings	\$ 4,659	\$ 1,594
Basic and fully diluted net income per share attributable to Holdings (refer to Note J)	\$ 0.08	\$ 0.03
Weighted average number of shares of trust stock outstanding basic and fully diluted	48,300	48,300
Cash distributions declared per share (refer to Note J)	\$ 0.36	\$ 0.36

See notes to condensed consolidated financial statements.

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Compass Diversified Holdings
Condensed Consolidated Statements of Comprehensive Income
(unaudited)

	Three months ended	
	March 31,	
	2014	2013
<i>(in thousands)</i>		
Net income	\$ 7,373	\$ 3,626
Other comprehensive income (loss)		
Foreign currency translation and other	(9)	(718)
Total comprehensive income, net of tax	\$ 7,364	\$ 2,908

See notes to condensed consolidated financial statements.

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Compass Diversified Holdings

Condensed Consolidated Statement of Stockholders' Equity

(unaudited)

<i>(in thousands)</i>	Number of Shares	Amount	Accumulated Deficit	Accum. Other Comprehensive Income (Loss)	Stockholders Equity Attrib. to Holdings	Non- Controlling Interest	Total Stockholders Equity
Balance January 1, 2014	48,300	\$ 725,453	\$ (252,761)	\$ 693	\$ 473,385	\$ 95,550	\$ 568,935
Net income			4,659		4,659	2,714	7,373
Other comprehensive loss - foreign currency translation and other				(9)	(9)		(9)
Option activity attributable to noncontrolling shareholders						3,579	3,579
Effect of subsidiary stock option exercise			157		157	(157)	
Distributions paid			(17,388)		(17,388)		(17,388)
Balance March 31, 2014	48,300	\$ 725,453	\$ (265,333)	\$ 684	\$ 460,804	\$ 101,686	\$ 562,490

See notes to condensed consolidated financial statements.

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Compass Diversified Holdings
Condensed Consolidated Statements of Cash Flows
(unaudited)

<i>(in thousands)</i>	Three months ended March 31,	
	2014	2013
Cash flows from operating activities:		
Net income	\$ 7,373	\$ 3,626
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	4,636	3,981
Amortization expense	7,349	7,630
Amortization of debt issuance costs and original issue discount	864	845
Supplemental put expense		6,396
Unrealized (gain) loss on interest rate and foreign currency derivatives	92	(385)
Noncontrolling stockholder stock based compensation	1,365	1,301
Excess tax benefit from subsidiary stock options	(1,061)	
Deferred taxes	(594)	(857)
Other	(53)	(71)
Changes in operating assets and liabilities, net of acquisition:		
Increase in accounts receivable	(15,652)	(18,130)
Increase in inventories	(7,063)	(2,010)
Increase in prepaid expenses and other current assets	(3,274)	(187)
Increase (decrease) in accounts payable and accrued expenses	(22)	17,987
Net cash (used in) provided by operating activities	(6,040)	20,126
Cash flows from investing activities:		
Acquisitions, net of cash acquired	(42,297)	
Purchases of property and equipment	(3,631)	(3,328)
Proceeds from sale of businesses		93
Payment of interest rate swap	(495)	
Other investing activities	7	
Net cash used in investing activities	(46,416)	(3,235)
Cash flows from financing activities:		
Borrowings under credit facility	59,000	15,000
Repayments under credit facility	(17,713)	(12,637)
Distributions paid	(17,388)	(17,388)
Net proceeds provided by noncontrolling shareholders	1,156	
Distributions paid to noncontrolling shareholders		