FORWARD AIR CORP
Form 10-Q
October 26, 2012

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

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended September 30, 2012
Commission File No. 000-22490

FORWARD AIR CORPORATION
(Exact name of registrant as specified in its charter)

Tennessee	62-1120025
(State or other jurisdiction of incorporation)	(I.R.S. Employer Identification No.)
430 Airport Road Greeneville, Tennessee	37745
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code: (423) 636-7000

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 x 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 definition of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer o Non-accelerated filer o Smaller reporting company o

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

Yes o No x

The number of shares outstanding of the registrant's common stock, $0.01 par value, as of October 23, 2012 was 29,377,437.

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Forward Air Corporation

Part I. Financial Information

Item 1. Financial Statements (Unaudited).
Forward Air Corporation
Condensed Consolidated Balance Sheets
(Dollars in thousands, except share and per share amounts)
(Unaudited)

	September 30, 2012	December 31, 2011
Assets		
Current assets:		
Cash	$92,988	$58,801
Accounts receivable, less allowance of $1,478 in 2012 and $1,503 in 2011	74,878	70,922
Other current assets	13,607	9,994
Total current assets	181,473	139,717
Property and equipment	238,704	223,135
Less accumulated depreciation and amortization	101,941	93,267
Total property and equipment, net	136,763	129,868
Goodwill and other acquired intangibles:		
Goodwill	43,332	43,332
Other acquired intangibles, net of accumulated amortization of $24,905 in 2012 and $21,462 in 2011	23,225	26,668
Total net goodwill and other acquired intangibles	66,557	70,000
Other assets	1,825	1,566
Total assets	$386,618	$341,151
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	$12,896	$12,392
Accrued expenses	16,475	20,986
Current portion of debt and capital lease obligations	386	552
Total current liabilities	29,757	33,930
Long-term debt and capital lease obligations, less current portion	88	333
Other long-term liabilities	6,805	8,860
Deferred income taxes	12,991	11,126
Shareholders' equity:		
Preferred stock	—	—
Common stock, $0.01 par value: Authorized shares - 50,000,000, Issued and outstanding shares - 29,190,036 in 2012 and 28,553,286 in 2011	292	285
Additional paid-in capital	62,971	42,212
Retained earnings	273,714	244,405
Total shareholders' equity	336,977	286,902
Total liabilities and shareholders' equity	$386,618	$341,151

The accompanying notes are an integral part of the financial statements.

Forward Air Corporation
Condensed Consolidated Statements of Comprehensive Income
(In thousands, except per share data)
(Unaudited)

	Three months ended		Nine months ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
Operating revenue:				
Forward Air				
Airport-to-airport	$96,914	$92,966	$290,006	$266,606
Logistics	20,878	18,409	63,315	52,909
Other	6,528	7,250	19,498	20,524
Forward Air Solutions				
Pool distribution	19,194	17,124	56,102	48,104
Total operating revenue	143,514	135,749	428,921	388,143
Operating expenses:				
Purchased transportation				
Forward Air				
Airport-to-airport	40,150	36,142	119,546	104,411
Logistics	15,954	14,041	47,756	40,214
Other	1,822	1,797	5,252	4,929
Forward Air Solutions				
Pool distribution	5,176	4,109	14,989	11,067
Total purchased transportation	63,102	56,089	187,543	160,621
Salaries, wages and employee benefits	31,698	33,402	97,408	95,336
Operating leases	6,895	6,672	20,826	20,083
Depreciation and amortization	5,425	5,429	15,940	15,734
Insurance and claims	3,098	2,120	8,132	6,140
Fuel expense	2,318	2,406	7,271	7,357
Other operating expenses	11,352	9,311	32,303	29,390
Total operating expenses	123,888	115,429	369,423	334,661
Income from operations	19,626	20,320	59,498	53,482
Other income (expense):				
Interest expense	(111)	(131)	(241)	(468)
Other, net	(21)	10	(6)	57
Total other expense	(132)	(121)	(247)	(411)
Income before income taxes	19,494	20,199	59,251	53,071
Income taxes	7,227	7,287	22,544	20,321
Net income and comprehensive income	$12,267	$12,912	$36,707	$32,750
Net income per share:				
Basic	$0.42	$0.44	$1.27	$1.12
Diluted	$0.41	$0.44	$1.24	$1.11
Weighted average shares outstanding:				
Basic	29,088	29,237	28,895	29,236

Diluted	29,660	29,552	29,484	29,591
Dividends per share:	$0.10	$0.07	$0.24	$0.21

The accompanying notes are an integral part of the financial statements.

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Forward Air Corporation
Condensed Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine months ended September 30, 2012	September 30, 2011
Operating activities:		
Net income	$36,707	$32,750
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	15,940	15,734
Share-based compensation	4,550	4,457
Loss (gain) on disposal of property and equipment	259	(76)
Provision for loss on receivables	226	17
Provision for revenue adjustments	1,417	1,480
Deferred income taxes	2,460	6,079
Tax benefit for stock options exercised	(354)	(232)
Changes in operating assets and liabilities		
Accounts receivable	(5,599)	(8,308)
Prepaid expenses and other current assets	(1,629)	(1,828)
Accounts payable and accrued expenses	(8,298)	4,757
Net cash provided by operating activities	45,679	54,830
Investing activities:		
Proceeds from disposal of property and equipment	867	997
Purchases of property and equipment	(20,499)	(20,292)
Other	(267)	316
Net cash used in investing activities	(19,899)	(18,979)
Financing activities:		
Payments of debt and capital lease obligations	(411)	(488)
Proceeds from exercise of stock options	15,740	7,721
Payments of cash dividends	(7,009)	(6,187)
Repurchase of common stock (repurchase program)	—	(24,294)
Common stock issued under employee stock purchase plan	119	128
Cash settlement of share-based awards for minimum tax withholdings	(386)	—
Tax benefit for stock options exercised	354	232
Net cash provided by (used in) financing activities	8,407	(22,888)
Net increase in cash	34,187	12,963
Cash at beginning of period	58,801	74,504
Cash at end of period	$92,988	$87,467

The accompanying notes are an integral part of the financial statements.

1. Basis of Presentation

Forward Air Corporation's ("the Company") services can be classified into two principal reporting segments: Forward Air, Inc. ("Forward Air") and Forward Air Solutions, Inc. ("FASI").

Through the Forward Air segment, the Company is a leading provider of time-definite transportation and related logistics services to the North American deferred air freight market and its activities can be classified into three categories of service: airport-to-airport, logistics, and other. Forward Air's airport-to-airport service operates a comprehensive national network for the time-definite surface transportation of expedited ground freight. The airport-to-airport service offers customers local pick-up and delivery and scheduled surface transportation of cargo as a cost effective, reliable alternative to air transportation. Forward Air's logistics services provide expedited truckload brokerage and dedicated fleet services. Forward Air's other services include shipment consolidation and deconsolidation, warehousing, customs brokerage, and other handling. The Forward Air segment primarily provides its transportation services through a network of terminals located at or near airports in the United States and Canada.

FASI provides pool distribution services throughout the Mid-Atlantic, Southeast, Midwest and Southwest continental United States. Pool distribution involves managing high-frequency handling and distribution of time-sensitive product to numerous destinations in specific geographic regions. FASI's primary customers for this service are regional and nationwide distributors and retailers, such as mall, strip mall and outlet based retail chains.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by United States generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The Company's operating results are subject to seasonal trends when measured on a quarterly basis; therefore operating results for the three and nine months ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. For further information, refer to the consolidated financial statements and notes thereto included in the Forward Air Corporation Annual Report on Form 10-K for the year ended December 31, 2011.

The balance sheet at December 31, 2011, as presented in this filing, has been derived from the audited financial statements at that date, but does not include all of the financial information and notes required by United States generally accepted accounting principles for complete financial statements.

The accompanying unaudited condensed consolidated financial statements of the Company include Forward Air Corporation and its subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

2. Recent Accounting Pronouncements

In May 2011, the FASB issued additional amendments to its fair value guidance in order to improve comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. GAAP and International Financial Reporting Standards ("IFRS"). These new amendments were not intended to establish valuation standards or affect valuation practices outside of financial reporting, but to explain how to measure fair value. These amendments require additional disclosures for transfer between Level 1 and Level 2 of the fair value hierarchy, sensitivity of Level 3 fair value measurements to changes in unobservable inputs and categorization by level of the fair value hierarchy for items required to be disclosed. These amendments are effective for interim and annual periods beginning after December 15, 2011. The adoption of the new amendments did not have a material effect on the Company's financial statement disclosures.

In September 2011, the FASB issued amendments to its goodwill and intangible asset guidance to permit an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether to perform the two-step goodwill impairment test. Under these new amendments, an entity is not required to calculate the fair value of a reporting unit unless the entity determines that is more likely than not that its fair value is less than its carrying amount. These amendments are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The adoption of these amendments does impact how the Company assesses goodwill impairment, but the adoption of the amendments did not have a significant effect on the Company's financial statement results or disclosures.

In 2011, the FASB issued amendments to require that all non-owner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-statement approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. These amendments eliminate the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. The amendments do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. As the Company does not currently have any items of comprehensive income, these amendments did not significantly impact the Company's financial statement presentation or disclosures.

3. Goodwill and Long-Lived Assets

The Company conducts an annual (or more frequently if circumstances indicate possible impairment) impairment test of goodwill for each reporting unit at June 30 of each year. The first step of the goodwill impairment test is the Company assesses qualitative factors to determine whether it is more likely than not that the fair value of either of its reporting units is less than its carrying amount, including goodwill. When performing the qualitative assessment, the Company considers the impact of factors including, but not limited to, macroeconomic and industry conditions, overall financial performance of each reporting unit, litigation and new legislation. If based on the qualitative assessments, the Company believes it more likely than not that the fair value of either reporting unit is less than the reporting unit's carrying amount the Company will prepare an estimation of the respective reporting unit's fair value. If this estimation of fair value indicates that impairment potentially exists, the Company will then measure the amount of the impairment, if any. Goodwill impairment exists when the calculated implied fair value of goodwill is less than its carrying value. Changes in strategy or market conditions could significantly impact these fair value estimates and require adjustments to recorded asset balances.
The Company conducted its annual impairment assessments and tests of goodwill for each reporting unit as of June 30, 2012 and no impairment charges were required. If a fair value estimation is required, the Company calculates the fair value of the applicable reportable units, using a combination of discounted projected cash flows and market valuations for comparable companies as of the valuation date. The Company's inputs into the fair value calculations for goodwill are classified within level 3 of the fair value hierarchy as defined in the FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles ("the FASB Codification").
As of September 30, 2012, the carrying value of goodwill related to the Forward Air and FASI segments was $37,926 and $5,406, respectively. Based on the Company's qualitative assessment we did not perform an estimation of Forward Air's fair value, but did perform a fair value estimation for FASI. The estimation of fair value related to the impairment test for goodwill is particularly sensitive to projected financial information used in the calculations. The FASI segment is currently facing the challenges of building, expanding and diversifying its revenue base. If FASI's efforts are significantly delayed, future estimates of projected financial information may be reduced, and the Company may be required to record an impairment charge against the carrying value of FASI's goodwill. There were no changes in the carrying amount of goodwill during the three and nine months ended September 30, 2012.

4. Share-Based Payments

The Company's general practice has been to make a single annual grant of share-based compensation to key employees and to make other employee grants only in connection with new employment or promotions. Forms of share-based compensation granted to employees by the Company include stock options, non-vested shares of common stock ("non-vested share"), and performance shares. The Company also typically makes a single annual grant of non-vested shares to non-employee directors in conjunction with the annual election of non-employee directors to the Board of

Directors. Share-based compensation is based on the grant date fair value of the instrument and is recognized, net of estimated forfeitures, ratably over the requisite service period, or vesting period. The Company estimates forfeitures based upon historical experience. All share-based compensation expense is recognized in salaries, wages and employee benefits.

Employee Activity - Stock Options

Stock option grants to employees typically expire seven years from the grant date and vest ratably over a three-year period. The Company used the Black-Scholes option-pricing model to estimate the grant-date fair value of options granted. The weighted-average fair value of options granted and assumptions used to calculate their fair value during the nine months ended September 30, 2012 and 2011 were as follows:

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Notes to Condensed Consolidated Financial Statements

	Nine months ended September 30, 2012	September 30, 2011
Expected dividend yield	0.9 %	1.0 %
Expected stock price volatility	46.6 %	44.9 %
Weighted average risk-free interest rate	0.8 %	2.4 %
Expected life of options (years)	4.2	4.6
Weighted average grant date fair value	$ 13	$ 11

The following tables summarize the Company’s employee stock option activity and related information:

	Three months ended September 30, 2012			
	Options (000)	Weighted-Average Exercise Price	Aggregate Intrinsic Value (000)	Weighted-Average Remaining Contractual Term
Outstanding at June 30, 2012	3,138	$ 27		
Granted	—	—		
Exercised	(252)	28		
Forfeited	(11)	29		
Outstanding at September 30, 2012	2,875	$ 26	$ 20,497	2.8
Exercisable at September 30, 2012	2,487	$ 26	$ 17,994	2.4

	Three months ended September 30, 2012	September 30, 2011
Shared-based compensation for options	$ 575	$ 959
Tax benefit for option compensation	$ 167	$ 252
Unrecognized compensation cost for options, net of estimated forfeitures	$ 2,052	$ 3,769

	Nine months ended September 30, 2012			
	Options (000)	Weighted-Average Exercise Price	Aggregate Intrinsic Value (000)	Weighted-Average Remaining Contractual Term
Outstanding at December 31, 2011	3,363	$ 26		
Granted	93	37		
Exercised	(570)	27		
Forfeited	(11)	$ 29		
Outstanding at September 30, 2012	2,875	$ 26	$ 20,497	2.8

Exercisable at September 30, 2012	2,487	$ 26	$ 17,994	2.4

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	Nine months ended September 30, 2012	September 30, 2011
Shared-based compensation for options	$ 1,994	$ 3,023
Tax benefit for option compensation	$ 546	$ 803
Unrecognized compensation cost for options, net of estimated forfeitures	$ 2,052	$ 3,769

Employee Activity - Non-vested Shares

Non-vested share grants to employees vest ratably over a three-year period. The non-vested shares' fair values were estimated using closing market prices on the day of grant. The following tables summarize the Company's employee non-vested share activity and related information:

	Three months ended September 30, 2012		
	Non-vested Shares (000)	Weighted-Average Grant Date Fair Value	Aggregate Grant Date Fair Value (000)
Outstanding and non-vested at June 30, 2012	174	$ 33	
Granted	—	—	
Vested	—	—	
Forfeited	(6)	$ 33	
Outstanding and non-vested at September 30, 2012	168	$ 33	$ 5,579

	Three months ended September 30, 2012	September 30, 2011
Shared-based compensation for non-vested shares	$ 506	$ 253
Tax benefit for non-vested share compensation	$ 196	$ 100
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	$ 4,035	$ 2,348

	Nine months ended September 30, 2012		
	Non-vested Shares (000)	Weighted-Average Grant Date Fair Value	Aggregate Grant Date Fair Value (000)
Outstanding and non-vested at December 31, 2011	108	$ 29	
Granted	103	37	
Vested	(36)	29	
Forfeited	(7)	33	
Outstanding and non-vested at September 30, 2012	168	$ 33	$ 5,579

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	Nine months ended September 30, 2012	September 30, 2011
Shared-based compensation for non-vested shares	$ 1,502	$ 641
Tax benefit for non-vested share compensation	$ 581	$ 252
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	$ 4,035	$ 2,348

Employee Activity - Performance Shares

In 2011 and 2012, the Company granted performance shares to key employees. Under the terms of the performance share agreements, on the third anniversary of the grant date, the Company will issue to the employees a calculated number of common stock shares based on the three year performance of the Company's common stock share price as compared to the share price performance of a selected peer group. No shares may be issued if the Company share price performance outperforms 30% or less of the peer group, but the number of shares issued may be doubled if the Company share price performs better than 90% of the peer group. The fair value of the performance shares was estimated using a Monte Carlo simulation. The weighted average assumptions used in the Monte Carlo calculation were as follows:

	Nine months ended September 30, 2012		September 30, 2011	
Expected stock price volatility	40.8	%	47.7	%
Weighted average risk-free interest rate	0.4	%	1.4	%

The following tables summarize the Company's employee performance share activity, assuming median share awards, and related information:

	Three months ended September 30, 2012		
	Performance Shares (000)	Weighted-Average Grant Date Fair Value	Aggregate Grant Date Fair Value (000)
Outstanding and non-vested at June 30, 2012	62	$ 36	
Granted	—	—	
Vested	—	—	
Outstanding and non-vested at September 30, 2012	62	$ 36	$ 2,205

	Three months ended September 30, 2012	September 30, 2011
Shared-based compensation for performance shares	$ 185	$ 95
Tax benefit for performance share compensation	$ 72	$ 37
Unrecognized compensation cost for performance shares, net of estimated forfeitures	$ 1,356	$ 893

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	Nine months ended September 30, 2012		
	Performance Shares (000)	Weighted-Average Grant Date Fair Value	Aggregate Grant Date Fair Value (000)
Outstanding and non-vested at December 31, 2011	38	$ 30	
Granted	24	45	
Vested	—	—	
Outstanding and non-vested at September 30, 2012	62	$ 36	$ 2,205

	Nine months ended	
	September 30, 2012	September 30, 2011
Shared-based compensation for performance shares	$ 515	$ 240
Tax benefit for performance share compensation	$ 199	$ 94
Unrecognized compensation cost for performance shares, net of estimated forfeitures	$ 1,356	$ 893

Employee Activity - Employee Stock Purchase Plan

Under the 2005 Employee Stock Purchase Plan (the "ESPP"), which has been approved by shareholders, the Company is authorized to issue up to a remaining 425,848 shares of common stock to employees of the Company. These shares may be issued at a price equal to 90% of the lesser of the market value on the first day or the last day of each six-month purchase period. Common stock purchases are paid for through periodic payroll deductions and/or up to two large lump sum contributions. For the nine months ended September 30, 2012, participants under the plan purchased 4,121 shares at an average price of $29.04 per share. For the nine months ended September 30, 2011, participants under the plan purchased 4,941 shares at an average price of $25.82 per share. The weighted-average fair value of each purchase right under the ESPP granted for the nine months ended September 30, 2012, which is equal to the discount from the market value of the common stock at the end of each six month purchase period, was $3.23 per share. The weighted-average fair value of each purchase right under the ESPP granted for the nine months ended September 30, 2011, which is equal to the discount from the market value of the common stock at the end of each six month purchase period, was $7.97 per share. Share-based compensation expense of $13 and $40 was recognized during the nine months ended September 30, 2012 and 2011, respectively.

Non-employee Director Activity - Non-vested Shares

Grants of non-vested shares to non-employee directors vest ratably over the elected term to the Board of Directors, or one year. The following tables summarize the Company's non-employee non-vested share activity and related information:

	Three months ended September 30, 2012		
	Non-vested Shares (000)	Weighted-Average Grant Date Fair Value	Aggregate Grant Date Fair Value (000)
Outstanding and non-vested at June 30, 2012	20	$ 32	

Granted	—	—	
Vested	—	—	
Outstanding and non-vested at September 30, 2012	20	$ 32	$ 640

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	Three months ended September 30, 2012	September 30, 2011
Shared-based compensation for non-vested shares	$ 161	$ 195
Tax benefit for non-vested share compensation	$ 62	$ 76
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	$ 385	$ 465

	Nine months ended September 30, 2012		
	Non-vested Shares (000)	Weighted-Average Grant Date Fair Value	Aggregate Grant Date Fair Value (000)
Outstanding and non-vested at December 31, 2011	24	$ 33	
Granted	20	32	
Vested	(24)	33	
Outstanding and non-vested at September 30, 2012	20	$ 32	$ 640

	Nine months ended September 30, 2012	September 30, 2011
Shared-based compensation for non-vested shares	$ 526	$ 513
Tax benefit for non-vested share compensation	$ 204	$ 201
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	$ 385	$ 465

Non-employee Director Activity - Stock Options

In addition to the above activity, each May from 1995 to 2005 options were granted to the non-employee directors of the Company. The options have terms of ten years and are fully exercisable. At September 30, 2012, 29,375 options were outstanding and will expire between May 2014 and May 2015. At September 30, 2012, the weighted average exercise price per share and remaining contractual term for the outstanding options of non-employee directors were $23 and 2.2 years, respectively.

5. Senior Credit Facility

In February 2012, the Company entered into a new $150,000 credit facility. This facility has a term of five years and matures in February 2017. The Company entered into this larger credit facility in order to fund potential acquisitions, the repurchase of its common stock and the financing of other general business purposes. Interest rates for advances under the facility are LIBOR plus 1.1% based upon covenants related to total indebtedness to earnings (1.3% at September 30, 2012). The agreement contains certain covenants and restrictions, none of which are expected to significantly affect the Company's operations or ability to pay dividends. No assets are pledged as collateral against the credit facility. As of September 30, 2012, the Company had no borrowings outstanding under the senior credit facility. At September 30, 2012, the Company had utilized $9,316 of availability for outstanding letters of credit and had $140,684 of available borrowing capacity outstanding under the senior credit facility.

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6. Net Income Per Share

The following table sets forth the computation of basic and diluted net income per share:

	Three months ended		Nine months ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
Numerator:				
Numerator for basic and diluted income per share - net income	$12,267	$12,912	$36,707	$32,750
Denominator (in thousands):				
Denominator for basic income per share - weighted-average shares	29,088	29,237	28,895	29,236
Effect of dilutive stock options and non-vested shares	572	315	589	355
Denominator for diluted income per share - adjusted weighted-average shares	29,660	29,552	29,484	29,591
Basic net income per share	$0.42	$0.44	$1.27	$1.12
Diluted net income per share	$0.41	$0.44	$1.24	$1.11

The number of options and non-vested shares that could potentially dilute net earnings per share in the future, but that were not included in the computation of income per diluted share because to do so would have been anti-dilutive for the periods presented, were approximately 251,000 and 912,000 at September 30, 2012 and 2011, respectively.

7. Income Taxes

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, various states and Canada. With a few exceptions, the Company is no longer subject to U.S. federal, state and local, or Canadian examinations by tax authorities for years before 2007.

For the nine months ended September 30, 2012 and 2011, the effective income tax rates varied from the statutory federal income tax rate of 35.0%, primarily as a result of the effect of state income taxes, net of the federal benefit and permanent differences between book and tax net income.

8. Financial Instruments

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash and trade accounts receivable. The Company does not generally require collateral from its customers. Concentrations of credit risk with respect to trade accounts receivable on a consolidated basis are limited due to the large number of entities comprising the Company’s customer base and their dispersion across many different industries. However, while not significant to the Company on a consolidated basis, three customers accounted for approximately 60.2% and 60.9% of FASI’s operating revenue for the three and nine months ended September 30, 2012, respectively.

Fair Value of Financial Instruments

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

Accounts receivable and accounts payable: The carrying amounts reported in the balance sheet for accounts receivable and accounts payable approximate their fair value based on their short-term nature.

The Company's senior credit facility bears interest at LIBOR plus 1.1% based upon covenants related to total indebtedness to earnings. Using interest rate quotes and discounted cash flows, the Company estimated the fair value of its outstanding debt and capital lease obligations as follows:

	September 30, 2012	
	Carrying Value	Fair Value
Other debt and capital leases	$474	$521

The Company's fair value calculations for the above financial instruments are classified within level 3 of the fair value hierarchy.

9. Shareholders' Equity

During the first and second quarters of 2012 and each quarter of 2011, the Company’s Board of Directors declared a cash dividend of $0.07 per share of common stock. On July 24, 2012, the Company’s Board of Directors declared a cash dividend of $0.10 per share of common stock payable on September 7, 2012 to shareholders of record at the close of business on August 23, 2012. The Company expects to continue to pay regular quarterly cash dividends, though each subsequent quarterly dividend is subject to review and approval by the Board of Directors.

In July 2007, the Company’s Board of Directors approved a stock repurchase program (“Repurchase Plan”) for up to two million shares of the Company’s common stock. As of September 30, 2012, 815,059 shares remain that may be repurchased under the Repurchase Plan.

10. Commitments and Contingencies

From time to time, the Company is party to ordinary, routine litigation incidental to and arising in the normal course of business. The Company does not believe that any of these pending actions, individually or in the aggregate, will have a material adverse effect on its business, financial condition or results of operations.

The primary claims in the Company’s business relate to workers’ compensation, property damage, vehicle liability and medical benefits. Most of the Company’s insurance coverage provides for self-insurance levels with primary and excess coverage which management believes is sufficient to adequately protect the Company from catastrophic claims. In the opinion of management, adequate provision has been made for all incurred claims up to the self-insured limits, including provision for estimated claims incurred but not reported.

The Company estimates its self-insurance loss exposure by evaluating the merits and circumstances surrounding individual known claims and by performing hindsight and actuarial analysis to determine an estimate of probable losses on claims incurred but not reported. Such losses could be realized immediately as the events underlying the claims have already occurred as of the balance sheet dates.

Because of the uncertainty of the ultimate resolution of outstanding claims, as well as uncertainty regarding claims incurred but not reported, it is possible that management’s provision for these losses could change materially in the near term. However, no estimate can currently be made of the range of additional loss that is at least reasonably possible.

11. Segment Reporting

The Company operates in two reportable segments based on differences in services provided. Forward Air provides time-definite transportation and logistics services to the deferred air freight market. FASI provides pool distribution services primarily to regional and national distributors and retailers.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies disclosed in Note 1 to the Consolidated Financial Statements included in the Company's 2011 Annual Report on Form 10-K. Segment data includes intersegment revenues. Assets and costs of the corporate headquarters are allocated to the segments based on usage. The Company evaluates the performance of its segments based on net income (loss). The Company's business is conducted in the U.S. and Canada.

The following tables summarize segment information about net income (loss) and assets used by the chief operating decision maker of the Company in making decisions regarding allocation of assets and resources as of and for the three and nine months ended September 30, 2012 and 2011.

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Forward Air Corporation
Notes to Condensed Consolidated Financial Statements

	Three months ended September 30, 2012			
	Forward Air	FASI	Eliminations	Consolidated
External revenues	$ 124,320	$ 19,194	$ —	$ 143,514
Intersegment revenues	186	274	(460)	—
Depreciation and amortization	4,242	1,183	—	5,425
Share-based compensation expense	1,412	16	—	1,428
Interest expense	106	5	—	111
Interest income	5	—	—	5
Income tax expense	7,133	94	—	7,227
Net income	12,106	161	—	12,267
Total assets	386,462	36,279	(36,123)	386,618
Capital expenditures	1,343	838	—	2,181

	Three months ended September 30, 2011			
	Forward Air	FASI	Eliminations	Consolidated
External revenues	$ 118,625	$ 17,124	$ —	$ 135,749
Intersegment revenues	315	129	(444)	—
Depreciation and amortization	4,373	1,056	—	5,429
Share-based compensation expense	1,421	81	—	1,502
Interest expense	122	9	—	131
Interest income	40	—	—	40
Income tax expense (benefit)	7,420	(133)	—	7,287
Net income (loss)	13,123	(211)	—	12,912
Total assets	378,552	36,099	(39,838)	374,813
Capital expenditures	4,607	244	—	4,851

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Forward Air Corporation
Notes to Condensed Consolidated Financial Statements

	Nine months ended September 30, 2012			
	Forward Air	FASI	Eliminations	Consolidated
External revenues	$372,819	$56,102	$—	$428,921
Intersegment revenues	939	572	(1,511)	—
Depreciation and amortization	12,455	3,485	—	15,940
Share-based compensation expense	4,399	151	—	4,550
Interest expense	223	18	—	241
Interest income	29	—	—	29
Income tax expense (benefit)	22,689	(145)	—	22,544
Net income (loss)	36,993	(286)	—	36,707
Total assets	386,462	36,279	(36,123)	386,618
Capital expenditures	15,310	5,189	—	20,499

	Nine months ended September 30, 2011			
	Forward Air	FASI	Eliminations	Consolidated
External revenues	$340,039	$48,104	$—	$388,143
Intersegment revenues	577	292	(869)	—
Depreciation and amortization	12,601	3,133	—	15,734
Share-based compensation expense	4,208	249	—	4,457
Interest expense	435	33	—	468
Interest income	144	—	—	144
Income tax expense (benefit)	21,009	(688)	—	20,321
Net income (loss)	33,914	(1,164)	—	32,750
Total assets	378,552	36,099	(39,838)	374,813
Capital expenditures	17,550	2,742	—	20,292

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

Overview and Executive Summary

Our operations can be broadly classified into two principal segments: Forward Air, Inc. (“Forward Air”) and Forward Air Solutions, Inc. (“FASI”).

Through our Forward Air segment, we are a leading provider of time-definite surface transportation and related logistics services to the North American expedited ground freight market. We offer our customers local pick-up and delivery (Forward Air Complete™) and scheduled surface transportation of cargo as a cost-effective, reliable alternative to air transportation. We transport cargo that must be delivered at a specific time, but is less time-sensitive than traditional air freight. This type of cargo is frequently referred to in the transportation industry as deferred air freight. We operate our Forward Air segment through a network of terminals located on or near airports in 85 cities in the United States and Canada, including a central sorting facility in Columbus, Ohio and 12 regional hubs serving key markets. We also offer our customers an array of logistics and other services including: expedited truckload brokerage (“TLX”); dedicated fleets; warehousing; customs brokerage; and shipment consolidation, deconsolidation and handling.

FASI provides pool distribution services throughout the Mid-Atlantic, Southeast, Midwest and Southwest continental United States. Pool distribution involves managing high-frequency handling and distribution of time-sensitive product to numerous destinations in specific geographic regions. Our primary customers for this service are regional and nationwide distributors and retailers, such as mall, strip mall and outlet based retail chains. We service these customers through a network of terminals and service centers located in 20 cities.

Our operations, particularly our network of hubs and terminals, represent substantial fixed costs. Consequently, our ability to increase our earnings depends in significant part on our ability to increase the amount of freight and the revenue per pound for the freight shipped through our networks and to grow other lines of businesses, such as TLX, which will allow us to maintain revenue growth in challenging shipping environments.

Trends and Developments

Results from Operations

During the three months ended September 30, 2012, we experienced a 5.7% increase in our consolidated revenues compared to the three months ended September 30, 2011. The increase in revenue is attributable to a 4.7% and 13.4% revenue increase in our Forward Air and FASI segments, respectively, during the three months ended September 30, 2012 as compared to the three months ended September 30, 2011. Forward Air revenue increases were driven by the airport-to-airport and logistics service lines. Airport-to-airport increased on higher utilization of Forward Air Complete™ ("Complete") and increases in our price per pound. Our airport-to-airport price per pound increased on a general rate increase initiated in September 2012. Volumes or tonnage shipped through our airport-to-airport business were flat during the third quarter of 2012 and this trend has continued into the fourth quarter of 2012. The logistics revenue increase was attributable to higher TLX revenue on an increase miles driven partially offset by a decline in our TLX revenue per mile.

FASI revenue increased 13.4% for the three months ended September 30, 2012, compared to the same period in 2011. The FASI revenue increase was primarily the result of new business wins. The increase in revenue drove the

$0.6 million, improvement in FASI’s results from operations during the three months ended September 30, 2012, compared to the three months ended September 30, 2011.

Our net fuel surcharge revenue is the result of our fuel surcharge rates, which are set weekly using the national average for diesel price per gallon, and the tonnage transiting our network. A change in business mix combined with the decreasing diesel fuel prices did negatively impact our total net fuel surcharge revenue during the three month ended September 30, 2012. During the three months ended September 30, 2012, total net fuel surcharge revenue decreased 9.9% as compared to the same period in 2011. Net fuel surcharge revenue was flat for the nine months ended September 30, 2012, as compared to the same period in 2011.

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Goodwill

In accordance with our accounting policy, we conducted our annual impairment assessments and tests of goodwill for each reporting unit as of June 30, 2012 and no impairment charges were required. As of September 30, 2012, the carrying value of goodwill related to the Forward Air and FASI segments was $37.9 million and $5.4 million, respectively. Based on our qualitative assessment of Forward Air we believed it was more likely than not that the fair value of the reporting unit continued to exceed the reporting unit's carrying value. During the second quarter of 2012, we prepared an estimation of the FASI reporting unit's fair value. The estimation of fair value related to the impairment test for goodwill is particularly sensitive to projected financial information used in the calculations. Our FASI segment is currently facing the challenges of building, expanding and diversifying its revenue base. If FASI's efforts are significantly delayed, future estimates of projected financial information may be reduced, and we may be required to record an impairment charge against the carrying value of FASI's goodwill.

Results of Operations

The following table sets forth our consolidated historical financial data for the three months ended September 30, 2012 and 2011 (in millions):

	Three months ended							
	September 30, 2012		September 30, 2011		Change		Percent Change	
Operating revenue	$143.5		$135.7		$7.8		5.7	%
Operating expenses:								
Purchased transportation	63.1		56.1		7.0		12.5	
Salaries, wages, and employee benefits	31.7		33.4		(1.7	)	(5.1	)
Operating leases	6.9		6.6		0.3		4.5	
Depreciation and amortization	5.5		5.4		0.1		1.9	
Insurance and claims	3.1		2.2		0.9		40.9	
Fuel expense	2.3		2.4		(0.1	)	(4.2	)
Other operating expenses	11.3		9.3		2.0		21.5	
Total operating expenses	123.9		115.4		8.5		7.4	
Income from operations	19.6		20.3		(0.7	)	(3.4	)
Other expense:								
Interest expense	(0.1	)	(0.1	)	—		—	
Total other expense	(0.1	)	(0.1	)	—		—	
Income before income taxes	19.5		20.2		(0.7	)	(3.5	)
Income taxes	7.2		7.3		(0.1	)	(1.4	)
Net income	$12.3		$12.9		$(0.6	)	(4.7	)%

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The following table sets forth our historical financial data by segment for the three months ended September 30, 2012 and 2011 (in millions):

	Three months ended September 30, 2012	Percent of Revenue	September 30, 2011	Percent of Revenue	Change	Percent Change
Operating revenue						
Forward Air	$124.5	86.8 %	$118.9	87.6 %	$5.6	4.7 %
FASI	19.5	13.6	17.2	12.7	2.3	13.4
Intercompany eliminations	(0.5)	(0.4)	(0.4)	(0.3)	(0.1)	25.0
Total	143.5	100.0	135.7	100.0	7.8	5.7
Purchased transportation						
Forward Air	58.1	46.7	52.1	43.8	6.0	11.5
FASI	5.4	27.7	4.4	25.6	1.0	22.7
Intercompany eliminations	(0.4)	80.0	(0.4)	100.0	—	—
Total	63.1	44.0	56.1	41.3	7.0	12.5
Salaries, wages and employee benefits						
Forward Air	24.3	19.5	26.4	22.2	(2.1)	(8.0)
FASI	7.4	37.9	7.0	40.7	0.4	5.7
Total	31.7	22.1	33.4	24.6	(1.7)	(5.1)
Operating leases						
Forward Air	5.2	4.2	4.9	4.1	0.3	6.1
FASI	1.7	8.7	1.7	9.9	—	—
Total	6.9	4.8	6.6	4.9	0.3	4.5
Depreciation and amortization						
Forward Air	4.3	3.4	4.4	3.7	(0.1)	(2.3)
FASI	1.2	6.2	1.0	5.8	0.2	20.0
Total	5.5	3.8	5.4	4.0	0.1	1.9
Insurance and claims						
Forward Air	2.6	2.1	1.8	1.5	0.8	44.4
FASI	0.5	2.6	0.4	2.3	0.1	25.0
Total	3.1	2.1	2.2	1.6	0.9	40.9
Fuel expense						
Forward Air	1.0	0.8	1.0	0.9	—	—
FASI	1.3	6.7	1.4	8.1	(0.1)	(7.1)
Total	2.3	1.6	2.4	1.8	(0.1)	(4.2)
Other operating expenses						
Forward Air	9.7	7.8	7.7	6.5	2.0	26.0

FASI	1.7	8.7	1.6	9.3	0.1	6.3
Intercompany eliminations	(0.1)	20.0	—	—	(0.1)	NM
Total	11.3	7.9	9.3	6.8	2.0	21.5
Income (loss) from operations						
Forward Air	19.3	15.5	20.6	17.3	(1.3)	(6.3)
FASI	0.3	1.5	(0.3)	(1.7)	0.6	(200.0)
Total	$19.6	13.7 %	$20.3	15.0 %	$(0.7)	(3.4)%

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The following table presents the components of the Forward Air segment's operating revenue and purchased transportation for the three months ended September 30, 2012 and 2011 (in millions):

	Three months ended September 30, 2012	Percent of Revenue		September 30, 2011	Percent of Revenue		Change		Percent Change	
Forward Air revenue										
Airport-to-airport	$97.0	77.9	%	$93.1	78.3	%	$3.9		4.2	%
Logistics	20.9	16.8		18.6	15.6		2.3		12.4	
Other	6.6	5.3		7.2	6.1		(0.6	)	(8.3	)
Total	$124.5	100.0	%	$118.9	100.0	%	$5.6		4.7	%
Forward Air purchased transportation										
Airport-to-airport	$40.3	41.5	%	$36.2	38.9	%	$4.1		11.3	%
Logistics	16.0	76.6		14.1	75.8		1.9		13.5	
Other	1.8	27.3		1.8	25.0		—		—	
Total	$58.1	46.7	%	$52.1	43.8	%	$6.0		11.5	%

Three Months Ended September 30, 2012 compared to Three Months Ended September 30, 2011

Revenues

Operating revenue increased by $7.8 million, or 5.7%, to $143.5 million for the three months ended September 30, 2012 from $135.7 million in the same period of 2011.

Forward Air

Forward Air operating revenue increased $5.6 million, or 4.7%, to $124.5 million from $118.9 million, accounting for 86.8% of consolidated operating revenue for the three months ended September 30, 2012 compared to 87.6% for the same period in 2011. Airport-to-airport revenue, which is the largest component of our consolidated operating revenue, increased $3.9 million, or 4.2%, to $97.0 million from $93.1 million, accounting for 77.9% of the segment's operating revenue during the three months ended September 30, 2012 compared to 78.3% during the three months ended September 30, 2011. As tonnage shipped through our airport-to-airport network was flat, the increase in revenue was attributable to improved linehaul pricing and increased Complete revenue. A 0.1% increase in tonnage and an increase in our base revenue per pound, excluding net fuel surcharge revenue and Complete revenue, accounted for $0.9 million of the increase in airport-to-airport revenue. Our airport-to-airport business is priced on a per pound basis and the average revenue per pound, excluding the impact of fuel surcharges and Complete, increased 1.1% for the three months ended September 30, 2012 versus the three months ended September 30, 2011. Average base revenue per pound increased as a result of a general rate increase that we implemented in September 2012. The remaining increase in airport-to-airport revenue is the result of increased revenue from our Complete pick-up and delivery service. Complete revenue increased $3.5 million, or 33.0%, during the three months ended September 30, 2012 compared to the same period of 2011. The increase in Complete revenue was attributable to higher customer utilization of our Complete service. Partially offsetting the revenue increases from Complete utilization and improved linehaul pricing was a $0.5 million, or 5.7%, decline in net fuel surcharge revenue during the three months ended September 30, 2012 compared to the same period in 2011. Net fuel surcharge revenue declined on the flat tonnage growth discussed above and reduced rates charged to customers in conjunction with lower year-over-year average diesel prices for most of the third quarter of 2012.

Logistics revenue, which is primarily TLX, increased $2.3 million, or 12.4%, to $20.9 million in the third quarter of 2012 from $18.6 million in the same period of 2011. TLX revenue, which is priced on a per mile basis, increased $2.3 million as miles driven to support our TLX revenue increased by approximately 15.9% during the three months ended September 30, 2012 compared to the same period in 2011. However, the increase in miles was offset by an approximate 2.0% decrease in TLX's average revenue per mile. The change in miles and average revenue per mile is mainly attributable to a change in customer mix during the third quarter of 2012 as compared to the same period in 2011.

Other revenue, which includes warehousing services and terminal handling, accounted for the final component of Forward Air operating revenue. Other revenue decreased $0.6 million, or 8.3%, to $6.6 million in the third quarter of 2012 from $7.2 million in the same period of 2011. The decrease in revenue was primarily due to ceasing certain dedicated local pick up and delivery services early in the fourth quarter of 2012. Also, as tonnage shipped through our airport-to-airport network began to slow we have experienced a decline in other terminal based revenues.

FASI

FASI operating revenue increased $2.3 million, or 13.4%, to $19.5 million for the three months ended September 30, 2012 from $17.2 million for the same period in 2011. The increase in revenue was mostly attributable to new business wins for new and previously existing customers. Approximately $0.4 million of the new business was from new customers, including non-specialty retailers. Another $0.6 million of revenue was attributable to truckload direct to store business for a previously existing customer. The remainder of the FASI revenue increase was attributable to higher volumes as well as new market wins from existing customers.

Intercompany Eliminations

Intercompany eliminations increased $0.1 million, or 25.0%, to $0.5 million in the third quarter of 2012 from $0.4 million in the same period of 2011. The intercompany eliminations are the result of truckload, airport-to-airport, and handling services Forward Air provided to FASI and FASI cartage and handling services provided to Forward Air during the three months ended September 30, 2012 and 2011.

Purchased Transportation

Purchased transportation increased by $7.0 million, or 12.5%, to $63.1 million in the third quarter of 2012 from $56.1 million in the same period of 2011. As a percentage of total operating revenue, purchased transportation was 44.0% during the three months ended September 30, 2012 compared to 41.3% for the same period in 2011.

Forward Air

Forward Air's purchased transportation increased by $6.0 million, or 11.5%, to $58.1 million for the three months ended September 30, 2012 from $52.1 million for the three months ended September 30, 2011. The increase in purchased transportation is primarily attributable to a 6.4% increase in miles driven and a 4.9% increase in the total cost per mile for the third quarter of 2012 versus the same period in 2011. As a percentage of segment operating revenue, Forward Air purchased transportation was 46.7% during the three months ended September 30, 2012 compared to 43.8% for the same period in 2011.

Purchased transportation costs for our airport-to-airport network increased $4.1 million, or 11.3%, to $40.3 million for the three months ended September 30, 2012 from $36.2 million for the three months ended September 30, 2011. For the three months ended September 30, 2012, purchased transportation for our airport-to-airport network increased to 41.5% of airport-to-airport revenue from 38.9% for the same period in 2011. The $4.1 million increase is partially attributable to a 2.5% increase in miles driven by our network of owner-operators or third party transportation providers and a 2.0% increase in the cost per mile paid to our network of owner-operators or third party transportation providers. The increase in miles increased purchased transportation by $0.7 million while the higher cost per mile increased purchased transportation by $0.6 million. Miles driven by our network of owner-operators or third party transportation providers increased in conjunction with a shift in our customer mix. The cost per mile increase was attributable to higher rates from third party transportation providers as well as increased rates paid to our network of owner-operators. The increase in owner-operator pay per mile was mainly due to a shift in business and customer mix and the impact on routes driven. The remaining increase was attributable to a $2.8 million increase in third party transportation costs associated with the higher Complete shipment volumes discussed above.

Purchased transportation costs for our logistics revenue increased $1.9 million, or 13.5%, to $16.0 million for the three months ended September 30, 2012 from $14.1 million for the three months ended September 30, 2011. For the three months ended September 30, 2012, logistics' purchased transportation costs represented 76.6% of logistics revenue compared to 75.8% for the same period in 2011. The increase in logistics' purchased transportation was mostly attributable to a $2.0 million increase in TLX purchased transportation. Miles driven to support our TLX revenue increased 15.9% while our TLX cost per mile decreased 0.3% during the three months ended September 30, 2012 compared to the same period in 2011. The improvement in cost per mile was mostly attributable to slightly lower utilization of third party transportation providers. The increase in TLX purchased transportation was partially offset by a decrease in various other non-mileage based costs, such as drayage services.

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Purchased transportation costs related to our other revenue were $1.8 million for the three months ended September 30, 2012 and 2011. Other purchased transportation costs as a percentage of other revenue increased to 27.3% of other revenue for the three months ended September 30, 2012 from 25.0% for the same period in 2011. The increase in other purchased transportation costs as a percentage of revenue is primarily attributable to the cessation of certain, dedicated local pick up and delivery business early in the fourth quarter of 2012. This business was primarily serviced by Company-employed drivers so revenues were reduced without a corresponding decrease in other purchased transportation. Also, contributing to the increase as a percentage of revenue was the adverse impact on other terminal revenue of the slowing airport-to-airport tonnage growth.

FASI

FASI purchased transportation increased $1.0 million, or 22.7%, to $5.4 million for the three months ended September 30, 2012 from $4.4 million for the three months ended September 30, 2011. FASI purchased transportation as a percentage of revenue was 27.7% for the three months ended September 30, 2012 compared to 25.6% for the three months ended September 30, 2011. The increase in FASI purchased transportation in total dollars and as a percentage of revenue was mostly attributable to certain new business having an increased linehaul component which increased the utilization of owner-operators and third-party transportation providers.

Intercompany Eliminations

Intercompany eliminations increased were $0.4 million for the three months ended September 30, 2012 and 2011. The intercompany eliminations are the result of truckload and airport-to-airport services Forward Air provided to FASI and FASI cartage services provided to Forward Air during the three months ended September 30, 2012.

Salaries, Wages, and Benefits

Salaries, wages and employee benefits decreased by $1.7 million, or 5.1%, to $31.7 million