

Armstrong Flooring, Inc.
Form 10-Q
November 06, 2017

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, 2017

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

Commission File Number 001-37589

ARMSTRONG FLOORING, INC.

(Exact name of Registrant as specified in its charter)

Delaware 47-4303305
(State or other jurisdiction of incorporation or organization) (I.R.S. employer Identification number)

2500 Columbia Avenue, PO Box 3025, Lancaster, Pennsylvania 17604
(Address of principal executive offices)

(717) 672-9611
(Registrant's telephone number, including area code).

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 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, a smaller reporting company or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company) Emerging growth company

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

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

The Registrant had 25,725,206 shares of common stock, \$0.0001 par value, outstanding at October 30, 2017.

Armstrong Flooring, Inc.

Table of Contents

	Page Number
<u>Cautionary Statement Concerning Forward-Looking Statements</u>	1
PART I <u>FINANCIAL INFORMATION</u>	
Item 1. <u>Financial Statements</u>	
<u>Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) (Unaudited)</u>	2
<u>Condensed Consolidated Balance Sheets (Unaudited)</u>	3
<u>Condensed Consolidated Statements of Stockholders' Equity (Unaudited)</u>	4
<u>Condensed Consolidated Statements of Cash Flows (Unaudited)</u>	5
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	6
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	21
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	30
Item 4. <u>Controls and Procedures</u>	30
PART II <u>OTHER INFORMATION</u>	
Item 1. <u>Legal Proceedings</u>	31
Item 1A. <u>Risk Factors</u>	31
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	31
Item 3. <u>Defaults Upon Senior Securities</u>	31
Item 4. <u>Mine Safety Disclosures</u>	31
Item 5. <u>Other Information</u>	31
Item 6. <u>Exhibits</u>	32
<u>SIGNATURES</u>	33

CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS

Certain statements in this Quarterly Report on Form 10-Q ("Form 10-Q") and the documents incorporated by reference may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Those forward-looking statements are subject to various risks and uncertainties and include all statements that are not historical statements of fact and those regarding our intent, belief or expectations, including, but not limited to, our expectations concerning our residential and commercial markets and their effect on our operating results, and our ability to increase revenues, earnings and EBITDA (as such terms are defined by documents incorporated by reference herein). Words such as "anticipate," "expect," "intend," "plan," "target," "project," "predict," "believe," "will," "would," "could," "should," "seek," "estimate" and similar expressions are intended to identify such forward-looking statements. These statements are based on management's current expectations and beliefs and are subject to a number of factors that could lead to actual results materially different from those described in the forward-looking statements. Although we believe that the assumptions underlying the forward-looking statements are reasonable, we can give no assurance that our expectations will be attained. Factors that could have a material adverse effect on our financial condition, liquidity, results of operations or future prospects or which could cause actual results to differ materially from our expectations include, but are not limited to:

- global economic conditions;
- construction activity;
- competition;
- key customers;
- availability and costs of raw materials and energy;
- recent plant construction;
- international operations;
- intellectual property rights;
- cost saving and productivity initiatives;
- strategic transactions;
- labor;
- information systems;
- claims and litigation;
- defined-benefit plan obligations;
- liquidity;
- debt covenants;
- debt;
- negative tax consequences;
- outsourcing;
- environmental matters; and

other risks detailed from time to time in our filings with the Securities and Exchange Commission, press releases, and other communications, including those set forth under "Risk Factors" included in our Annual Report on Form 10-K and in the documents incorporated by reference.

Such forward-looking statements speak only as of the date they are made. We expressly disclaim any obligation to release publicly any updates or revisions to any forward-looking statements to reflect any change in our expectations with regard thereto or change in events, conditions or circumstances on which any statement is based.

PART I: FINANCIAL INFORMATION

Item 1. Financial Statements

Armstrong Flooring, Inc. and Subsidiaries

Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) (Unaudited)

(Dollars in millions, except per share data)

	Three Months Ended September 30, 2017		Nine Months Ended September 30, 2016	
Net sales	\$308.5	\$313.4	\$871.0	\$921.5
Cost of goods sold	276.8	243.4	735.1	736.4
Gross profit	31.7	70.0	135.9	185.1
Selling, general and administrative expenses	49.3	53.8	153.2	157.0
Intangible asset impairment	12.5	—	12.5	—
Operating (loss) income	(30.1)	16.2	(29.8)	28.1
Interest expense	0.8	0.6	2.0	1.3
Other expense, net	0.1	0.3	0.1	2.1
(Loss) income from continuing operations before income taxes	(31.0)	15.3	(31.9)	24.7
Income tax (benefit) expense	(12.3)	6.0	(10.8)	10.9
(Loss) income from continuing operations	(18.7)	9.3	(21.1)	13.8
Gain on disposal of discontinued operations, net of tax	—	—	—	1.7
Net (loss) income	(18.7)	9.3	(21.1)	15.5
Other comprehensive (loss) income, net of tax:				
Foreign currency translation adjustments	2.3	0.1	5.7	(6.6)
Derivatives loss	(0.6)	(0.3)	(1.5)	(2.2)
Pension and postretirement adjustments	(2.6)	1.1	(0.2)	2.0
Total other comprehensive (loss) income	(0.9)	0.9	4.0	(6.8)
Total comprehensive (loss) income	\$(19.6)	\$10.2	\$(17.1)	\$8.7
Basic (loss) earnings per share of common stock:				
Basic (loss) earnings per share of common stock from continuing operations	\$(0.70)	\$0.33	\$(0.76)	\$0.50
Basic earnings per share of common stock from discontinued operations	—	—	—	0.06
Basic (loss) earnings per share of common stock	\$(0.70)	\$0.33	\$(0.76)	\$0.56
Diluted (loss) earnings per share of common stock:				
Diluted (loss) earnings per share of common stock from continuing operations	\$(0.70)	\$0.33	\$(0.76)	\$0.49
Diluted earnings per share of common stock from discontinued operations	—	—	—	0.06
Diluted (loss) earnings per share of common stock	\$(0.70)	\$0.33	\$(0.76)	\$0.55

See accompanying notes to Condensed Consolidated Financial Statements.

Armstrong Flooring, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(Dollars in millions, except par value)

	September 30, 2017	December 31, 2016
	(Unaudited)	
Assets		
Current assets:		
Cash	\$ 43.6	\$ 30.6
Accounts and notes receivable, net	85.1	76.0
Inventories, net	264.5	272.1
Income tax receivable	4.3	2.4
Prepaid expenses and other current assets	21.5	23.8
Total current assets	419.0	404.9
Property, plant, and equipment, less accumulated depreciation and amortization of \$392.1 and \$336.8, respectively	421.1	445.2
Prepaid pension costs	0.1	0.2
Intangible assets, net	62.1	42.6
Deferred income taxes	5.8	4.5
Other noncurrent assets	6.9	7.0
Total assets	\$ 915.0	\$ 904.4
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 156.5	\$ 163.0
Income tax payable	0.9	0.4
Total current liabilities	157.4	163.4
Long-term debt	96.1	21.2
Postretirement benefit liabilities	72.1	75.5
Pension benefit liabilities	4.0	1.6
Other long-term liabilities	9.7	9.1
Noncurrent income taxes payable	0.5	1.7
Deferred income taxes	6.2	8.4
Total liabilities	346.0	280.9
Stockholders' equity:		
Common stock with par value \$.0001 per share: 100,000,000 shares authorized; 28,173,681 issued and 25,724,685 outstanding shares as of September 30, 2017 and 27,895,671 issued and outstanding shares as of December 31, 2016	—	—
Preferred stock with par value \$.0001 per share: 15,000,000 shares authorized; none issued	—	—
Treasury stock, at cost, 2,448,996 shares as of September 30, 2017	(39.9) —
Additional paid-in capital	675.8	673.3
(Accumulated deficit) retained earnings	(11.1) 10.0
Accumulated other comprehensive loss	(55.8) (59.8
Total stockholders' equity	569.0	623.5
Total liabilities and stockholders' equity	\$ 915.0	\$ 904.4

See accompanying notes to Condensed Consolidated Financial Statements.

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Armstrong Flooring, Inc. and Subsidiaries

Condensed Consolidated Statements of Stockholders' Equity (Unaudited)

(Dollars in millions)

	Common Stock		Treasury Stock		Net AWI Investment	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	(Accumulated Deficit) Retained Earnings	Total Equity
	Shares	Amount	Shares	Amount					
December 31, 2016	27,895,671	\$ —	\$—	\$—	\$—	\$ 673.3	\$ (59.8)	\$ 10.0	\$ 623.5
Net (loss)	—	—	—	—	—	—	—	(21.1)	(21.1)
Repurchase of common stock	(2,455,604)	—	2,455,604	(40.0)	—	—	—	—	(40.0)
Stock-based compensation, net	284,618	—	(6,608)	0.1	—	3.3	—	—	3.4
Net transfers to Armstrong World Industries ("AWI")	—	—	—	—	(0.8)	—	—	—	(0.8)
Reclassification of net parent investment to additional paid-in capital	—	—	—	—	0.8	(0.8)	—	—	—
Other comprehensive income	—	—	—	—	—	—	4.0	—	4.0
September 30, 2017	25,724,685	\$ —	2,448,996	\$(39.9)	\$—	\$ 675.8	\$ (55.8)	\$ (11.1)	\$ 569.0
December 31, 2015	—	\$ —	\$—	\$—	\$ 622.0	\$—	\$ 2.0	\$—	\$ 624.0
Net (loss) income	—	—	—	—	(0.8)	—	—	16.3	15.5
Net transfers from (to) AWI	—	—	—	—	102.3	—	(54.2)	—	48.1
Cash distribution paid to AWI	—	—	—	—	(50.0)	—	—	—	(50.0)
Reclassification of net parent investment to additional paid-in capital	—	—	—	—	(673.5)	673.5	—	—	—
Issuance of common stock at separation	27,738,779	—	—	—	—	—	—	—	—
Stock-based compensation, net	74,860	—	—	—	—	3.9	—	—	3.9
Other comprehensive (loss)	—	—	—	—	—	—	(6.8)	—	(6.8)
September 30, 2016	27,813,639	\$ —	\$—	\$—	\$—	\$ 677.4	\$ (59.0)	\$ 16.3	\$ 634.7

See accompanying notes to Condensed Consolidated Financial Statements.

Armstrong Flooring, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)
(Dollars in millions)

	Nine Months Ended September 30,	
	2017	2016
Cash flows from operating activities:		
Net (loss) income	\$(21.1)	\$15.5
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	59.9	34.2
Intangible asset impairment	12.5	—
Deferred income taxes	(5.2)	(2.6)
Stock-based compensation	3.8	3.8
U.S. pension expense	6.7	4.3
Other non-cash adjustments, net	(1.0)	1.8
Changes in operating assets and liabilities:		
Receivables	(7.8)	(11.1)
Inventories	9.9	(13.9)
Accounts payable and accrued expenses	(2.8)	17.1
Income taxes payable	(3.1)	4.1
Other assets and liabilities	(5.6)	2.0
Net cash provided by operating activities	46.2	55.2
Cash flows from investing activities:		
Purchases of property, plant and equipment	(33.5)	(28.1)
Cash paid for acquisition	(36.1)	—
Other investing activities	0.3	0.6
Net cash used for investing activities	(69.3)	(27.5)
Cash flows from financing activities:		
Proceeds from revolving credit facility	90.0	100.0
Payments on revolving credit facility	(15.0)	(90.0)
Financing costs	—	(1.4)
Payments of long-term debt	—	(10.0)
Payments on capital lease	(0.1)	—
Purchases of treasury stock	(40.0)	—
Cash distribution paid to AWI	—	(50.0)
Proceeds from exercised stock options	1.4	0.2
Value of shares withheld related to employee tax withholding	(1.8)	—
Net transfers from AWI	—	55.6
Net cash provided by financing activities	34.5	4.4
Effect of exchange rate changes on cash and cash equivalents	1.6	0.1
Net increase in cash and cash equivalents	13.0	32.2
Cash and cash equivalents at beginning of year	30.6	—
Cash and cash equivalents at end of period	\$43.6	\$32.2
Supplemental Cash Flow Disclosure:		
Amounts in accounts payable for capital expenditures	\$6.2	\$3.7
Interest paid	1.9	1.2
Income taxes (refunded) paid, net	(3.1)	7.5

See accompanying notes to Condensed Consolidated Financial Statements.

Armstrong Flooring, Inc. and Subsidiaries
Notes to Unaudited Condensed Consolidated Financial Statements
(Dollars in millions, except per share data)

NOTE 1. BUSINESS AND BASIS OF PRESENTATION

Background

Armstrong Flooring, Inc. ("AFI") is a leading global producer of flooring products for use primarily in the construction and renovation of residential, commercial and institutional buildings. AFI designs, manufactures, sources and sells resilient and wood flooring products in North America and the Pacific Rim. When we refer to "AFI," "the Company," "we," "our," and "us" in this report, we are referring to Armstrong Flooring, Inc., a Delaware corporation, and its consolidated subsidiaries.

On April 1, 2016, we became an independent company as a result of the separation by Armstrong World Industries, Inc. ("AWI"), a Pennsylvania corporation, of its Resilient Flooring and Wood Flooring segments from its Building Products segment (the "Separation"). The Separation was effected by allocating the assets and liabilities related primarily to the Resilient Flooring and Wood Flooring segments to AFI and then distributing the common stock of AFI to AWI's shareholders (the "Distribution"). The Separation and Distribution (together, the "Spin-off") resulted in AFI and AWI becoming two independent, publicly traded companies, with AFI owning and operating the Resilient Flooring and Wood Flooring segments and AWI continuing to own and operate a ceilings business.

Basis of Presentation

Prior to April 1, 2016, AFI operated as a part of AWI. The financial information for periods prior to April 1, 2016 was prepared on a combined basis from AWI's historical accounting records and is presented herein on a stand-alone basis as if the operations had been conducted independently of AWI. Beginning April 1, 2016, the financial information was prepared on a consolidated basis. The Condensed Consolidated Financial Statements of AFI presented are not indicative of our future performance, and, for periods prior to April 1, 2016, do not necessarily reflect what our historical results of operations, financial position and cash flows would have been if we had operated as a separate, stand-alone entity during those periods.

For periods prior to April 1, 2016, AFI was comprised of certain stand-alone legal entities for which discrete financial information was available, as well as portions of legal entities for which discrete financial information was not available ("Shared Entities"). For the Shared Entities for which discrete financial information was not available, such as shared utilities, taxes, and other shared costs, allocation methodologies were applied to allocate amounts to AFI. The Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) for these periods include all revenues and costs attributable to AFI, including costs for facilities, functions and services used by AFI. The results of operations for those periods also include allocations of costs for administrative functions and services performed on behalf of AFI by centralized staff groups within AWI, AWI's general corporate expenses, and certain pension and other retirement benefit costs for those periods. All of the allocations and estimates in the Condensed Consolidated Financial Statements are based on assumptions that AFI management believes are reasonable.

All charges and allocations of cost for facilities, functions and services performed by AWI prior to the Spin-off were deemed paid by AFI to AWI in cash, in the period in which the cost was recorded in the Condensed Consolidated Statements of Operations and Comprehensive Income (Loss). Prior to the Spin-off, transactions between AWI and AFI were accounted for through Net AWI investment.

Prior to the Spin-off, AFI's portion of current income taxes payable was deemed to have been remitted to AWI in the period the related tax expense was recorded. AFI's portion of current income taxes receivable was deemed to have been remitted to AFI by AWI in the period to which the receivable applies only to the extent that a refund of such taxes could have been recognized by AFI on a stand-alone basis under the law of the relevant taxing jurisdiction. These Condensed Consolidated Financial Statements are prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP"). The statements include management estimates and judgments, where appropriate. Management uses estimates to record many items including certain asset values,

Armstrong Flooring, Inc. and Subsidiaries
Notes to Unaudited Condensed Consolidated Financial Statements
(Dollars in millions, except per share data)

allowances for bad debts, inventory obsolescence, lower of cost or market or net realizable value charges, warranty reserves, workers compensation, general liability and environmental claims and income taxes. When preparing an estimate, management determines the amount based upon the consideration of relevant information. Management may confer with outside parties, including outside counsel. Actual results may differ from these estimates. In the opinion of management, all adjustments of a normal, recurring nature have been included to provide a fair statement of the results for the reporting periods presented. Operating results for the three and nine months ended September 30, 2017 and 2016 included in this report are unaudited. Quarterly results are not necessarily indicative of annual earnings, primarily due to the different level of sales in each quarter of the year and the possibility of changes in economic conditions between periods.

Certain amounts in the prior year's Condensed Consolidated Financial Statements and related notes thereto have been recast to conform to the 2017 presentation. Otherwise, the accounting policies used in preparing the Condensed Consolidated Financial Statements in this Form 10-Q are the same as those used in preparing the Consolidated Financial Statements for the year ended December 31, 2016. These statements should therefore be read in conjunction with the Consolidated Financial Statements and notes that are included in the Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

During the fourth quarter of 2016, we changed the method of accounting for our Wood Flooring inventories from the last-in, first-out ("LIFO") method to the first-in, first-out ("FIFO") method. As a result of this accounting change, comparative financial statements of prior periods have been adjusted to apply the new method retrospectively. See additional disclosure regarding this change within the notes to the Consolidated Financial Statements included in the Annual Report on Form 10-K for the fiscal year ended December 31, 2016. The change from LIFO to FIFO decreased Cost of goods sold for the three months ended September 30, 2016 by \$2.1 million and increased Income tax expense by \$1.1 million, resulting in an increase in Net income of \$1.0 million from \$8.3 million to \$9.3 million. Cost of goods sold for the nine months ended September 30, 2016 decreased by \$6.8 million and income tax expense increased by \$2.7 million, resulting in an increase in Net income of \$4.1 million from \$11.4 million to \$15.5 million. This accounting change also increased Additional paid-in capital at September 30, 2016 by \$7.9 million from \$669.5 million to \$677.4 million. Retained earnings at September 30, 2016 increased by \$2.3 mi