CECO ENVIRONMENTAL CORP
Form 10-Q
November 09, 2015

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 September 30, 2015

or

¨ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from __________ to __________

Commission File No. 0-7099

CECO ENVIRONMENTAL CORP.

(Exact name of registrant as specified in its charter)

Delaware	**13-2566064**
(State or other jurisdiction of Incorporation or organization)	**(IRS Employer Identification No.)**
4625 Red Bank Road, Cincinnati, Ohio	**45227**
(Address of principal executive offices)	**(Zip Code)**

(513) 458-2600

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (check one)

Large Accelerated Filer	¨	Accelerated Filer	x
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 x

The number of shares outstanding of each of the issuer s classes of common equity, as of the latest practical date: 34,048,024 shares of common stock, par value $0.01 per share, as of November 6, 2015.

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CECO ENVIRONMENTAL CORP. AND SUBSIDIARIES

QUARTERLY REPORT ON FORM 10-Q

For the quarter ended September 30, 2015

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CECO ENVIRONMENTAL CORP. AND SUBSIDIARIES

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CONDENSED CONSOLIDATED BALANCE SHEETS

(dollars in thousands, except per share data)	(unaudited) SEPTEMBER 30, 2015	DECEMBER 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 30,763	$ 18,162
Restricted cash	5,350	1,200
Accounts receivable, net	100,758	58,394
Costs and estimated earnings in excess of billings on uncompleted contracts	58,686	24,371
Inventories, net	29,850	23,416
Prepaid expenses and other current assets	11,812	9,046
Prepaid income taxes	4,990	4,190
Assets held for sale	2,500	4,188
Total current assets	244,709	142,967
Property, plant and equipment, net	47,489	18,961
Goodwill	232,240	167,547
Intangible assets-finite life, net	83,975	58,398
Intangible assets-indefinite life	30,249	19,766
Deferred charges and other assets	8,158	6,154
	$ 646,820	$ 413,793
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current portion of debt	$ 19,699	$ 8,887
Accounts payable and accrued expenses	104,949	51,462
Billings in excess of costs and estimated earnings on uncompleted contracts	23,341	14,597
Income taxes payable	646	405
Total current liabilities	148,635	75,351
Other liabilities	29,416	27,884
Debt, less current portion	174,584	102,969
Deferred income tax liability, net	43,561	26,365

Total liabilities	396,196	232,569
Commitments and contingencies		
Shareholders equity:		
Preferred stock, $.01 par value; 10,000 shares authorized, none issued		
Common stock, $.01 par value; 100,000,000 shares authorized, 34,048,024 and 26,404,869 shares issued in 2015 and 2014, respectively	340	264
Capital in excess of par value	242,571	168,886
Accumulated earnings	10,794	19,051
Accumulated other comprehensive loss	(8,725)	(6,621)
	244,980	181,580
Less treasury stock, at cost, 137,920 shares in 2015 and 2014	(356)	(356)
Total CECO shareholders equity	244,624	181,224
Noncontrolling interest	6,000	
Total shareholders equity	250,624	181,224
	$ 646,820	$ 413,793

The notes to the condensed consolidated financial statements are an integral part of the above statements.

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CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)

(unaudited)

(dollars in thousands, except per share data)	THREE MONTHS ENDED SEPTEMBER 30, 2015	THREE MONTHS ENDED SEPTEMBER 30, 2014	NINE MONTHS ENDED SEPTEMBER 30, 2015	NINE MONTHS ENDED SEPTEMBER 30, 2014
Net sales	$ 98,230	$ 63,300	$ 266,176	$ 187,111
Cost of sales	67,435	42,242	187,778	124,875
Gross profit	30,795	21,058	78,398	62,236
Selling and administrative expenses	18,054	13,038	46,158	36,402
Acquisition and integration expenses	5,685	81	6,978	321
Amortization and earn-out expenses	9,250	2,394	19,989	7,288
Legal reserves		300		300
(Loss) income from operations	(2,194)	5,245	5,273	17,925
Other expense, net	(282)	(1,459)	(1,456)	(1,686)
Interest expense	(1,711)	(767)	(3,845)	(2,255)
(Loss) income before income taxes	(4,187)	3,019	(28)	13,984
Income tax expense (benefit)	638	(684)	2,495	2,767
Net (loss) income	$ (4,825)	$ 3,703	$ (2,523)	$ 11,217
(Loss) earnings per share:				
Basic	$ (0.17)	$ 0.14	$ (0.09)	$ 0.44
Diluted	$ (0.17)	$ 0.14	$ (0.09)	$ 0.43
Weighted average number of common shares outstanding:				
Basic	28,617,589	25,691,884	27,066,072	25,647,561
Diluted	28,617,589	26,129,427	27,066,072	26,105,415

The notes to the condensed consolidated financial statements are an integral part of the above statements.

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CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(unaudited)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
(dollars in thousands)	2015	2014	2015	2014
Net (loss) income	$ (4,825)	$ 3,703	$ (2,523)	$ 11,217
Other comprehensive loss:				
Foreign currency translation	(1,575)	(1,069)	(2,104)	(1,181)
Other comprehensive loss	(1,575)	(1,069)	(2,104)	(1,181)
Comprehensive (loss) income	$ (6,400)	$ 2,634	$ (4,627)	$ 10,036

The notes to the condensed consolidated financial statements are an integral part of the above statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(dollars in thousands)	NINE MONTHS ENDED SEPTEMBER 30, 2015	2014
Cash flows from operating activities:		
Net (loss) income	$ (2,523)	$ 11,217
Adjustment to reconcile net (loss) income to net cash (used in) provided by operating activities:		
Depreciation and amortization	11,217	8,103
Unrealized foreign currency loss	1,689	
Loss (gain) on sale of property and equipment	222	(13)
Non-cash interest expense included in net income	791	411
Share-based compensation expense	1,318	1,221
Bad debt expense	504	111
Inventory reserve expense	463	461
Deferred income taxes	(657)	
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable	(16,635)	(2,772)
Costs and estimated earnings in excess of billings on uncompleted contracts	(10,522)	(2,889)
Inventories	170	(253)
Prepaid expense and other current assets	286	(4,164)
Deferred charges and other assets	201	478
Accrued litigation settlement		(2,536)
Accounts payable and accrued expenses	2,354	(1,554)
Billings in excess of costs and estimated earnings on uncompleted contracts	(252)	(674)
Income taxes payable	274	(414)
Other liabilities	479	(436)
Net cash (used in) provided by operating activities	(10,621)	6,297
Cash flows from investing activities:		
Acquisitions of property and equipment	(526)	(801)
Proceeds from sale of property and equipment	2,396	7,475
Net cash paid for acquisitions	(37,130)	(8,214)
Net used in investing activities	(35,260)	(1,540)
Cash flows from financing activities:		
Decrease in restricted cash	100	
Net (repayments) borrowings on revolving credit lines	(1,242)	1,557
Borrowings of long-term debt	170,000	
Repayments of debt	(101,966)	(6,637)
Financing fees paid	(2,923)	

Proceeds from employee stock purchase plan and exercise of stock options	298	1,048
Repurchases of common stock		(973)
Dividends paid to common shareholders	(5,734)	(4,374)
Net cash provided by (used in) financing activities	58,533	(9,379)
Effect of exchange rate changes on cash and cash equivalents	(51)	
Net increase (decrease) in cash and cash equivalents	12,601	(4,622)
Cash and cash equivalents at beginning of period	18,162	22,661
Cash and cash equivalents at end of period	$ 30,763	$ 18,039
Supplemental Schedule of Non-Cash Activities:		
Common stock issued in business acquisition	$ 72,145	$ 500
Cash paid during the period for:		
Interest	$ 2,965	$ 2,061
Income taxes	$ 1,812	$ 7,171

The notes to the condensed consolidated financial statements are an integral part of the above statements.

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CECO ENVIRONMENTAL CORP. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. Basis of Reporting for Consolidated Financial Statements

The accompanying unaudited condensed consolidated financial statements of CECO Environmental Corp. and its subsidiaries (the Company , we , us , or our) have been prepared pursuant to the rules and regulations of the Securitie and Exchange Commission (the SEC). Certain information and footnote disclosures normally included in annual financial statements have been condensed or omitted pursuant to those rules and regulations. In the opinion of management, the accompanying unaudited condensed consolidated financial statements of the Company contain all adjustments (consisting only of normal recurring adjustments) necessary to present fairly the financial position as of September 30, 2015 and the results of operations and cash flows for the three-month and nine-month periods ended September 30, 2015 and 2014. The results of operations for the three-month and nine-month periods ended September 30, 2015 are not necessarily indicative of the results to be expected for the full year. The balance sheet as of December 31, 2014 has been derived from the audited consolidated financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2014 filed with the SEC.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) 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 could differ from those estimates.

These financial statements and accompanying notes should be read in conjunction with the audited financial statements and the notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2014 filed with the SEC.

Unless otherwise indicated, all balances within tables are in thousands, except per share amounts.

During the third quarter of 2015, the Company completed the acquisition of PMFG, Inc. (PMFG). During 2014, the Company completed four acquisitions, including i) in August 2014, HEE Environmental Engineering (HEE), ii) in September 2014, SAT Technology, Inc. (SAT), iii) in November 2014, Emtrol LLC (Emtrol), and iv) in December 2014, Jiangyin Zhongli Industrial Technology Co. Ltd. (Zhongli). The results of their operations have been consolidated with our results following the acquisition dates. For a more complete discussion of the transactions, refer to Note 16.

The Company s consolidated financial statements include the accounts of all wholly-owned and majority-owned subsidiaries for all periods presented. All significant inter-company accounts and transactions have been eliminated in consolidation. The Company is the majority owner of Peerless Propulsys China Holdings LLC (Peerless Propulsys). The Company s 60% equity investment in Peerless Propulsys entitles it to 80% of the earnings. Peerless Propulsys is the sole owner of Peerless China Manufacturing Co. Ltd. (PCMC). The noncontrolling interest of Peerless Propulsys is reported as a separate component on the Consolidated Balance Sheets.

2. New Financial Accounting Pronouncements

In September 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-16, Simplifying the Accounting for Measurement-Period Adjustments. ASU 2015-16 requires adjustments to provisional amounts that are identified during the measurement period to be recognized in the reporting period in which the adjustment amounts are determined. This includes any effect on earnings of changes in depreciation, amortization, or other income effects as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. In addition, the amendments in the ASU would require an entity to disclose (either on the face of the income statement or in the notes) the nature and amount of measurement-period adjustments recognized in the current period, including separately the amounts in current-period income statement line items that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. ASU 2015-16 is effective for annual periods beginning after December 15, 2015, and interim periods within those annual periods. The Company is currently evaluating the potential impact of the adoption of ASU 2015-16 on the Company s consolidated financial statements.

In August 2015, the FASB issued ASU 2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements. ASU 2015-15 codifies the SEC staff announcement that entities are permitted to defer and present debt issuance costs related to line-of-credit arrangements as assets. Given the absence of authoritative guidance within ASU 2015-03 for debt issuance costs related to line-of-credit arrangements, ASU 2015-15 clarifies that the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The Company adopted this ASU, and it did not have a significant impact on the Company s consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, Simplifying the Measurement of Inventory. ASU 2015-11 requires inventory within the scope of the ASU (e.g. first-in, first-out (FIFO) or average cost) to be measured using the lower of cost and net realizable value. Inventory excluded from the scope of the ASU (i.e., last-in, first-out (LIFO) or the retail inventory method) will continue to be measured at the lower of cost or market. The ASU also amends some of the other guidance in Topic 330, Inventory, to more clearly articulate the requirements for the measurement and disclosure of inventory. However, those amendments are not intended to result in any changes to current practice. ASU 2015-11 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The adoption of this standard is not expected to have a significant impact on the Company s consolidated financial statements.

In May 2015, FASB issued ASU 2015-07, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent). ASU 2015-07 requires investments for which fair value is measured at net asset value per share (or its equivalent) using the practical expedient should not be categorized in the fair value hierarchy as defined under FASB Topic 820, Fair Value Measurements. The FASB issued the ASU to eliminate the diversity in practice resulting from the way in which investments measured at net asset value per share (or its equivalent) with future redemption dates are classified, and also to ensure that all investments categorized in the fair value hierarchy are classified using a consistent approach. ASU 2015-07 is effective for annual periods beginning after December 15, 2015, and interim periods within those annual periods. The adoption of this standard is not expected to have a significant impact on the Company s consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs. ASU 2015-03 requires that debt issuance costs rela