BEACON ROOFING SUPPLY INC
Form 10-Q
February 06, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended December 31, 2016

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 Number 000-50924

BEACON ROOFING SUPPLY, INC.

(Exact name of registrant as specified in its charter)

Delaware **36-4173371**

(State or other jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

505 Huntmar Park Drive, Suite 300, Herndon, VA 20170

(Address of Principal Executive Offices) (Zip Code)

(571) 323-3939

(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 and 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 x	Accelerated filer ¨
Non-accelerated filer ¨ (do not check if a smaller reporting company)	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

As of February 1, 2017, 60,076,778 shares of common stock, par value $0.01 per share, of the registrant were outstanding.

BEACON ROOFING SUPPLY, INC.

FORM 10-Q

For the Quarter Ended December 31, 2016

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BEACON ROOFING SUPPLY, INC.

Consolidated Balance Sheets

(Unaudited; In thousands, except share and per share amounts)

	December 31, 2016	September 30, 2016	December 31, 2015
Assets			
Current assets:			
Cash and cash equivalents	$ 73,271	$ 31,386	$ 32,210
Accounts receivable, less allowance of $16,711, $14,812 and $8,871 as of December 31, 2016, September 30, 2016 and December 31, 2015, respectively	489,898	626,965	489,172
Inventories, net	528,709	480,736	466,063
Prepaid expenses and other current assets	209,651	163,103	150,384
Total current assets	1,301,529	1,302,190	1,137,829
Property and equipment, net	147,340	148,569	145,607
Goodwill	1,197,550	1,197,565	1,162,111
Intangibles, net	444,210	464,024	487,477
Other assets, net	1,511	1,511	1,270
Total Assets	$ 3,092,140	$ 3,113,859	$ 2,934,294
Liabilities and Stockholders' Equity			
Current liabilities:			
Accounts payable	$ 336,837	$ 360,915	$ 347,205
Accrued expenses	166,479	161,113	151,547
Current portions of long-term debt	14,610	14,811	14,287
Total current liabilities	517,926	536,839	513,039
Borrowings under revolving lines of credit, net	332,679	359,661	343,225
Long-term debt, net	722,516	722,929	722,888
Deferred income taxes, net	136,260	135,482	100,667
Long-term obligations under equipment financing and other, net	32,915	35,121	43,322
Total liabilities	1,742,296	1,790,032	1,723,141
Commitments and contingencies			
Stockholders' equity:			
Common stock (voting); $.01 par value; 100,000,000 shares authorized; 60,030,516 issued and outstanding as of December 31, 2016; 59,890,885 issued and outstanding as of September 30, 2016; 59,192,132 issued and outstanding at December 31, 2015	600	598	591

Undesignated preferred stock; 5,000,000 shares authorized, none issued or outstanding	-	-	-
Additional paid-in capital	701,542	694,564	668,828
Retained earnings	667,752	647,322	564,523
Accumulated other comprehensive loss	(20,050)	(18,657)	(22,789)
Total stockholders' equity	1,349,844	1,323,827	1,211,153
Total Liabilities and Stockholders' Equity	$ 3,092,140	$ 3,113,859	$ 2,934,294

See accompanying Notes to Condensed Consolidated Financial Statements

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BEACON ROOFING SUPPLY, INC.

Consolidated Statements of Operations

(Unaudited; In thousands, except share and per share amounts)

	Three Months Ended December 31,	
	2016	2015
Net sales	$1,002,184	$976,480
Cost of products sold	751,117	743,292
Gross profit	251,067	233,188
Operating expense	204,110	206,344
Income from operations	46,957	26,844
Interest expense, financing costs, and other	13,574	16,256
Income before provision for income taxes	33,383	10,588
Provision for income taxes	12,953	3,470
Net income	$20,430	$7,118
Weighted-average common stock outstanding:		
Basic	59,943,264	58,972,913
Diluted	60,993,080	59,962,033
Net income per share:		
Basic	$0.34	$0.12
Diluted	$0.33	$0.12

See accompanying Notes to Condensed Consolidated Financial Statements

BEACON ROOFING SUPPLY, INC.

Consolidated Statements of Comprehensive Income

(Unaudited; In thousands)

	Three Months Ended December 31,	
	2016	2015
Net income	$ 20,430	$ 7,118
Other comprehensive income (loss):		
Foreign currency translation adjustment	(1,652)	(2,469)
Total other comprehensive loss	(1,652)	(2,469)
Comprehensive income	$ 18,778	$ 4,649

See accompanying Notes to Condensed Consolidated Financial Statements

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BEACON ROOFING SUPPLY, INC.

Consolidated Statements of Cash Flows

(Unaudited; In thousands)

	Three Months Ended December 31,	
	2016	2015
Operating Activities		
Net income	$20,430	$7,118
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	28,425	23,671
Stock-based compensation	3,816	7,179
Certain interest expense and other financing costs	1,418	2,425
Gain on sale of fixed assets	(312)	(300)
Deferred income taxes	788	(333)
Other, net	-	426
Changes in operating assets and liabilities, net of the effects of businesses acquired:		
Accounts receivable	136,895	95,715
Inventories	(48,019)	43,514
Prepaid expenses and other assets	(46,594)	(1,773)
Accounts payable and accrued expenses	(18,724)	(132,967)
Net cash provided by operating activities	78,123	44,675
Investing Activities		
Purchases of property and equipment	(7,280)	(2,153)
Acquisition of businesses, net	(1,850)	(941,156)
Proceeds from the sale of assets	400	229
Net cash used in investing activities	(8,730)	(943,080)
Financing Activities		
Borrowings under revolving lines of credit	355,057	890,128
Repayments under revolving lines of credit	(382,395)	(549,378)
Borrowings under term loan	-	450,000
Repayments under term loan	(1,125)	(186,750)
Borrowings under Senior Notes	-	300,000
Borrowings under equipment financing facilities and other	1,010	-
Repayments under equipment financing facilities and other	(3,415)	(1,367)
Payment of deferred financing costs	-	(27,813)
Proceeds from issuance of common stock	3,460	8,984
Taxes paid related to net share settlement of equity awards	(297)	-
Excess tax benefit from stock-based compensation	-	1,501
Net cash provided by (used in) financing activities	(27,705)	885,305

Effect of exchange rate changes on cash and cash equivalents	197	(351)
Net increase (decrease) in cash and cash equivalents	41,885	(13,451)
Cash and cash equivalents, beginning of period	31,386	45,661
Cash and cash equivalents, end of period	$73,271	$32,210
Supplemental cash flow information		
Cash paid during the period for:		
Interest	$19,335	$10,827
Income taxes, net of tax refunds	13,906	7,621

During the period ended December 31, 2015, the Company issued Common Stock with a value of $302 million and replacement awards with a value of $5 million in connection with the acquisition of Roofing Supply Group, LLC, which are accounted for as a non-cash investing activity.

See accompanying Notes to Condensed Consolidated Financial Statements

BEACON ROOFING SUPPLY, INC.

Notes to Condensed Consolidated Financial Statements

(Unaudited; In thousands, except share and per share data or otherwise indicated)

1. Company Overview

Beacon Roofing Supply, Inc. (the “Company”) was incorporated in the state of Delaware on August 22, 1997 and is the largest publicly traded distributor of residential and non-residential roofing materials and complementary building products in the United States and Canada. The Company operates its business under regional and local trade names and services customers in 47 states within the United States and 6 provinces in Canada. The Company’s current material subsidiaries are Beacon Sales Acquisition, Inc., Beacon Canada, Inc. and Beacon Roofing Supply Canada Company.

2. Summary of Significant Accounting Policies

Basis of Presentation

Beacon Roofing Supply, Inc. (the “Company”) prepared the condensed consolidated financial statements in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and the requirements of the Securities and Exchange Commission (SEC). As permitted under those rules, certain footnotes or other financial information have been condensed or omitted. The balance sheet as of December 31, 2015 has been presented for a better understanding of the impact of seasonal fluctuations on the Company's financial condition.

In management's opinion, the financial statements include all normal and recurring adjustments that are considered necessary for the fair presentation of the Company's financial position and operating results. The results for the three-month period ended December 31, 2016 are not necessarily indicative of the results to be expected for the twelve months ending September 30, 2017 (fiscal year 2017 or “2017”).

The three-month periods ended December 31, 2016 and 2015 had 61 and 62 business days, respectively.

These interim Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto contained in the Company's fiscal year 2016 ("2016") Annual Report on Form 10-K for the year ended September 30, 2016.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in these consolidated financial statements and accompanying notes. Significant items subject to such estimates include inventories, purchase price allocations, recoverability of goodwill and intangibles, and income taxes. Actual amounts could differ from those estimates.

Recent Accounting Pronouncements- Adopted

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-03, "*Simplifying the Presentation of Debt Issuance Costs*" to simplify the presentation of debt issuance costs. This guidance requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the associated debt liability, consistent with the required presentation for debt discounts. This update is effective for financial statements issued for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years and early adoption is permitted. Upon adoption, an entity must apply the new guidance retrospectively to all prior periods presented in the financial statements. The Company elected to early adopt this new guidance effective October 1, 2015. The adoption of this standard changed the Company's previous practice of presenting debt issuance costs as an asset and resulted in the reduction of total assets and total liabilities in an amount equal to the balance of unamortized debt issuance costs at each balance sheet date presented. Debt issuance costs that are now presented as a direct reduction from the carrying amount of the associated debt liability amounted to $24.1 million as of December 31, 2016, $25.2 million as of September 30, 2016, and $30.0 million as of December 31, 2015.

In September 2015, the FASB issued ASU 2015-16, "*Simplifying the Accounting for Measurement-Period Adjustments*." This guidance eliminates the requirement to restate prior period financial statements for measurement period adjustments related to business combinations. It requires that the cumulative impact of a measurement period adjustment, including the impact on prior periods, be recognized in the reporting period in which the adjustment is identified. In addition, the portion of the adjustment recorded in the current period that would have been recognized in prior periods had the adjustment been identified at that time must be presented, by line item, either on the face of the income statement or in the accompanying notes. This guidance is effective for annual and interim reporting periods beginning after December 15, 2015 and early adoption is permitted. The Company elected to early adopt this new guidance effective January 1, 2016 and the impact on the financial statements through the quarter ended December 31, 2016 was immaterial.

In November 2015, the FASB issued ASU 2015-17, "*Balance Sheet Classification of Deferred Taxes*." This guidance requires entities to present deferred tax assets and deferred tax liabilities as noncurrent in a classified balance sheet. This ASU is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period, and early adoption is permitted. Entities are permitted to apply this guidance either prospectively or retrospectively. The Company adopted the guidance as of March 31, 2016 and applied it retrospectively to all prior periods. As a result, the Company reclassified its current deferred tax balances of $31.9 million to non-current deferred taxes as of September 30, 2015.

Recent Accounting Pronouncements- Not Yet Adopted

In May 2014, the FASB issued ASU 2014-09, "*Revenue from Contracts with Customers*." This guidance requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers, and will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for public business entities for fiscal years beginning on or after January 1, 2018, and early adoption is permitted for annual periods beginning after December 31, 2016. The standard permits the use of either the retrospective or cumulative effect transition method. The Company has not selected a transition method and is currently evaluating the impact this guidance may have on its financial statements and related disclosures.

In July 2015, the FASB issued ASU 2015-11, "*Inventory: Simplifying the Measurement of Inventory.*" This guidance applies to inventory valued at first-in, first-out (FIFO) or average cost and requires inventory to be measured at the lower of cost and net realizable value, rather than at the lower of cost or market. ASU 2015-11 is effective on a prospective basis for annual periods, including interim reporting periods within those periods, beginning after December 15, 2016. The Company reports inventory on an average-cost basis and thus will be required to adopt the standard. The Company is currently evaluating the impact that this guidance may have on its financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, "*Leases*." The ASU will replace most existing accounting for lease guidance when it becomes effective. This guidance is effective for the Company beginning on October 1, 2019 and early adoption is permitted. The standard must be adopted using the modified retrospective approach. The standard will require the Company to record a right to use asset and a lease liability for most of the Company's leases including the Company's leases currently treated as operating leases. The Company is currently evaluating the impact that this guidance may have on its financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, "*Compensation - Stock Compensation: Improvements to Employee Share-Based Payment Accounting.*" This ASU is intended to simplify several aspects of the accounting for share-based payment transactions, including the accounting for income taxes, forfeitures and statutory tax withholding requirements, as well as classification in the statement of cash flows. The provisions of this standard are effective for reporting periods beginning after December 15, 2016 and early adoption is permitted. The provisions of this standard contain specific transition guidance for each amendment. The Company is currently evaluating the impact that this guidance may have on its financial statements and related disclosures.

In June 2016, the FASB issued ASU 2016-13, “*Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments.”* This ASU is intended to introduce a revised approach to the recognition and measurement of credit losses, emphasizing an updated model based on expected losses rather than incurred losses. The provisions of this standard are effective for reporting periods beginning after December 15, 2019 and early adoption is permitted. The Company is currently evaluating the impact that this guidance may have on its financial statements and related disclosures.

3. Acquisitions

Roofing Supply Group

On October 1, 2015, the Company acquired 100% of the equity of Roofing Supply Group, LLC ("RSG”), a leading roofing products distributor owned by investment firm Clayton, Dubilier & Rice ("CD&R"). RSG’s results of operations have been included with Company’s consolidated results beginning October 1, 2015. RSG distributed roofing supplies and related materials from 85 locations across 25 states as of October 1, 2015.

Total consideration paid for RSG was approximately $1.17 billion, out of which $288.2 million was in cash, $306.8 million of Company’s common stock and option replacement awards, and $574.4 million in refinancing of RSG’s debt. The RSG long-term debt was repaid simultaneously with the proceeds of a new ABL Revolver, Term Loan and Senior Notes (see Note 8).

In connection with the RSG acquisition, the Company was required to issue equity awards to certain RSG employees in replacement of RSG equity awards that were cancelled at closing. The replacement awards consisted of options to purchase 661,349 shares of the Company’s common stock. The terms and fair value of these awards approximated the cancelled RSG awards on the issuance date. The fair value of the replacement awards associated with services rendered through the date of the RSG acquisition was recognized as a component of the total acquisition consideration, and the remaining fair value of the replaced awards associated with post RSG acquisition services will be recognized as an expense on a straight-line basis over the remaining service period.

The RSG acquisition has been accounted for as a business combination in accordance with the requirements of *ASC 805 Business Combinations*. The acquisition price has been allocated among assets acquired and liabilities assumed at fair value based on information currently available, with the excess recorded as goodwill. The goodwill recognized is attributable primarily to expected synergies and the assembled workforce of RSG. These come from the synergies that are obtained in operating the branches as part of a larger network, and from an experienced employee base skilled at managing a distribution business. As of September 30, 2016, the Company had finalized the acquisition accounting entries for the RSG acquisition, detailed as follows (in thousands):

Cash	$ 16,451
Accounts receivable	177,251
Inventory	179,651
Other current assets	50,000
Property, plant, and equipment	55,159
Other intangible assets	382,600
Goodwill	617,477
Current liabilities	(252,190)
Non-current liabilities	(56,949)
Total purchase price	$ 1,169,450

RSG's future growth attributable to new customers, geographic market presence and assembled workforce are additional assets that are not separable and which contributed to recorded goodwill, of which $86.1 million was tax deductible as of the October 1, 2015 RSG acquisition date. All of the Company's goodwill plus the indefinite-lived trade name are tested for impairment annually, and all acquired goodwill and intangible assets are subject to review for impairment should future indicators of impairment develop. The fair value of acquired RSG accounts receivables was $177.3 million, with the gross contractual amount being $185.9 million.

Other Acquisitions – Fiscal Year 2017

On December 16, 2016, the Company purchased certain assets of BJ Supply Company, a distributor of roofing and related building products with 1 branch serving Pennsylvania and New Jersey and annual sales of approximately $4 million.

Other Acquisitions – Fiscal Year 2016

During fiscal year 2016, the Company acquired 42 branches from the following seven additional acquisitions:

- On December 1, 2015, the Company purchased certain assets of RCI Roofing Supply, a distributor of residential and commercial roofing and related products with 5 branches operating in Nebraska, Iowa and Colorado and annual sales of approximately $23 million. As of December 31, 2016, the Company had finalized the acquisition accounting entries for this acquisition.

- On December 18, 2015, the Company acquired 100% of the equity interests of Roofing and Insulation Supply, a distributor primarily of residential and commercial insulation along with roofing and related products with 20 branches spanning 13 states operating across New England, the Mid-Atlantic, the Southeast, the Upper Midwest, Texas and Colorado and annual sales of approximately $70 million. As of December 31, 2016, the Company had finalized the acquisition accounting entries for this acquisition.

- On December 29, 2015, the Company purchased certain assets of Statewide Wholesale, a distributor of residential and commercial roofing and related products with 1 branch located in Denver, Colorado and annual sales of approximately $15 million. As of December 31, 2016, the Company had finalized the acquisition accounting entries for this acquisition.

- On April 1, 2016, the Company purchased certain assets of Atlantic Building Products, a distributor of decking, windows, siding, and related products with 2 branches operating in eastern Pennsylvania and annual sales of approximately $5 million.

- On April 1, 2016, the Company purchased certain assets of Lyf-Tym Building Products, a distributor of siding, windows, gutters, vinyl railings, and related products with 6 branches operating in North Carolina and Virginia and annual sales of approximately $20 million.

- On May 2, 2016, the Company purchased certain assets of Fox Brothers Company, a distributor of roofing, siding, windows, doors, and related products with 4 branches operating in Michigan and annual sales of approximately $35 million.

- On June 1, 2016, the Company acquired 100% of the equity interests of Woodfeathers, Inc., a distributor of primarily residential roofing and related products with 4 branches operating in Oregon and Washington and annual sales of approximately $30 million.

The Company recorded the acquired assets and liabilities related to these transactions at their estimated fair values as of the respective acquisition dates, with resulting goodwill of $84.8 million ($59.8 million of which is deductible for tax purposes) and $60.8 million in intangible assets associated with these other acquisitions as of December 31, 2016.

Other Acquisitions – Additional Information

For those acquisitions where the acquisition accounting entries have yet to be finalized, the Company's allocation of the purchase price is subject to change on receipt of additional information, including, but not limited to, the finalization of asset valuations (intangible and fixed) and income tax accounting.

The Company has not provided pro forma results of operations for any acquisitions in fiscal years 2017 or 2016 herein, as the Company included the results of operations of each acquisition in its consolidated statement of income from the date of each acquisition.

4. Net Income per Share

Basic net income per common share is computed by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted net income per common share is computed by dividing net income by the weighted-average number of common shares and dilutive common share equivalents then outstanding using the treasury stock method. Common equivalent shares consist of the incremental common shares issuable upon the exercise of stock options and vesting of restricted stock awards.

The following table presents the basic and diluted weighted-average shares outstanding for each period presented:

	Three Months Ended December 31,	
	2016	2015
Weighted-average common shares outstanding, basic	59,943,264	58,972,913

Effect of dilutive securities: &nbs