CECO ENVIRONMENTAL CORP
Form 10-Q
May 11, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2006

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)	**(I.R.S. Employer Identification No.)**

3120 Forrer Street, Cincinnati, Ohio 45209

(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 and (2) has been subject to such filing requirements for the past 90 days. x Yes ¨ No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Act).

Large Accelerated Filer ¨ Accelerated Filer ¨ Non-Accelerated Filer x

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of latest practical date.

Class: Common, par value $.01 per share outstanding at May 4, 2006 - 11,217,780

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CECO ENVIRONMENTAL CORP.

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

MARCH 31, 2006

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CECO ENVIRONMENTAL CORP.

CONSOLIDATED BALANCE SHEETS

Dollars in thousands, except per share data

	MARCH 31, 2006 (unaudited)	DECEMBER 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 322	$ 310
Accounts receivable, net	18,742	13,151
Costs and estimated earnings in excess of billings on uncompleted contracts	4,887	4,681
Inventories	2,294	1,981
Prepaid expenses and other current assets	2,129	1,672
Total current assets	28,374	21,795
Property and equipment, net	8,861	8,796
Goodwill, net	9,527	9,527
Intangibles finite life, net	638	658
Intangibles indefinite life	1,395	1,395
Deferred charges and other assets	515	729
	$49,310	$ 42,900
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current portion of debt	$ 8,174	$ 568
Current portion of subordinated notes		1,000
Accounts payable and accrued expenses	12,194	12,017
Billings in excess of costs and estimated earnings on uncompleted contracts	7,307	3,766
Detachable stock warrants	1,946	842
Total current liabilities	29,621	18,193
Other liabilities	1,861	1,934
Debt, less current portion		6,214
Deferred income tax liability	3,143	3,143
Subordinated notes (related party - $5,715 and $6,633, respectively)	6,715	6,633
Total liabilities	41,340	36,117
Shareholders equity:		
Common stock, $0.01 par value; 100,000,000 shares authorized, 11,202,780 and 10,168,479 shares issued in 2006 and 2005	112	102
Capital in excess of par value	16,810	15,017
Accumulated deficit	(7,808)	(7,072)
Accumulated other comprehensive loss	(789)	(791)
	8,325	7,256
Less treasury stock, at cost, 137,920 shares in 2006 and 175,220 in 2005	(355)	(473)

Total shareholders equity	7,970	6,783
	$49,310	$ 42,900

The notes to consolidated financial statements

are an integral part of the above statements.

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CECO ENVIRONMENTAL CORP.

CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

Dollars in thousands, except per share data

	THREE MONTHS ENDED MARCH 31, 2006	THREE MONTHS ENDED MARCH 31, 2005
Net sales	$ 24,382	$ 15,055
Costs and expenses:		
Cost of sales, exclusive of items shown separately below	20,249	12,882
Selling and administrative	3,145	2,841
Depreciation and amortization	292	292
	23,686	16,015
Income (loss) from operations	696	(960)
Other (expense) income	(1,080)	50
Interest expense (including related party interest of $232 and $259, respectively)	(571)	(597)
Loss before income taxes	(955)	(1,507)
Income tax benefit	(219)	(875)
Net loss	$ (736)	$ (632)
Per share data:		
Basic and diluted net loss	$ (.07)	$ (.06)
Weighted average number of common shares outstanding:		
Basic and diluted	10,913,503	9,993,260

The notes to consolidated financial statements are

an integral part of the above statements.

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CECO ENVIRONMENTAL CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

Dollars in thousands

	THREE MONTHS ENDED MARCH 31, 2006	2005
Cash flows from operating activities:		
Net loss	$ (736)	$ (632)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	292	292
Non cash interest expense included in net loss	118	89
Non cash warrant valuation expense (gains) included in net loss	1,104	(31)
Non cash gains included in net loss	(22)	(19)
Changes in operating assets and liabilities:		
Accounts receivable	(5,591)	3,631
Inventories	(313)	(176)
Costs and estimated earnings in excess of billings on uncompleted contracts	(206)	3
Prepaid expenses and other current assets	(457)	(831)
Deferred charges and other assets	163	133
Accounts payable and accrued expenses	177	(3,182)
Billings in excess of costs and estimated earnings on uncompleted contracts	3,541	1,167
Other	(48)	3
Net cash (used in) provided by operating activities	(1,978)	447
Net cash used in investing activities - acquisition of property and equipment	(335)	(228)
Cash flows from financing activities:		
Proceeds from exercise of warrants & options not under plan	1,769	
Proceeds from exercise of stock options	137	
Compensation expense stock options	15	
Subordinated debt repayments	(988)	
Short-term debt borrowings (repayments)	1,392	(156)
Net cash provided by (used in) financing activities	2,325	(156)
Net increase in cash	12	63
Cash and cash equivalents at beginning of the period	310	339
Cash and cash equivalents at end of the period	$ 322	$ 402
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the period for:		
Interest	$ 1,136	$ 495
Income taxes	$ 152	$ 95

The notes to consolidated financial statements are

an integral part of the above statement

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CECO ENVIRONMENTAL CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. Basis of reporting for consolidated financial statements and significant accounting policies.

The accompanying unaudited consolidated financial statements of CECO Environmental Corp. and subsidiaries (the Company , we , us , or our) have been prepared in accordance with accounting principles generally accepted in the United States of America. In the opinion of management, the accompanying unaudited consolidated financial statements of the Company contain all adjustments (consisting only of normal recurring accruals) necessary to present fairly the financial position as of March 31, 2006 and the results of operations and of cash flows for the three-month periods ended March 31, 2006 and 2005. The results of operations for the three-month period ended March 31, 2006 are not necessarily indicative of the results to be expected for the full year. The balance sheet as of December 31, 2005 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, 2005.

These financial statements should be read in conjunction with the audited financial statements and notes thereto in the Company s Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Stock Based Compensation

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), Share-Based Payment, effective January 1, 2006. SFAS No. 123(R) requires public entities to measure the cost of employee services received in exchange for an award of equity instruments and recognize this cost over the period during which an employee is required to provide the services. The Company has adopted SFAS No. 123(R) using the modified prospective application as defined in the Statement, and therefore financial statements from periods ending prior to January 1, 2006 have not been restated. As a result of adopting SFAS No. 123(R) on January 1, 2006, the Company s income before income taxes and net income for the quarter ended March 31, 2006 are $14,600 and $9,600 lower, respectively, than if it had continued to account for share-based compensation under APB No. 25. Basic and diluted earnings per share for the quarter ended March 31, 2006 would have been unchanged if the Company had not adopted SFAS No. 123(R). See further discussion in Note 8.

Prior to January 1, 2006, the company applied the provisions of Accounting Principles Board Opinion No. 25 (APB No. 25), Accounting for Stock Issued to Employees. Accordingly, no compensation expense was reflected in the financial statements as the exercise price of options granted to employees and non-employee directors equaled the fair market value of the Company s common shares on the date of grant. The Company had adopted the disclosure-only provisions of SFAS No. 123, Accounting for Stock Based Compensation.

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CECO ENVIRONMENTAL CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

If the Company had adopted the expense recognition provisions of SFAS No. 123 prior to January 1, 2006, net income and earnings per share for the three month period ended March 31, 2005 would have been as follows:

(In thousands except earnings per share)	Three months ended March 31, 2005
Net loss as reported	$ (632)
Add: Stock-based compensation expense included in reported net income, net of related tax effects	
Deduct: Total stock-based compensation determined under the fair value based method for all awards, net of tax effects	(8)
Pro forma net loss	(640)
Earnings per common share	
Basic and diluted	
As reported	$ (0.06)
Pro forma	$ (0.06)

2. New Accounting Standards

None

3. Inventories

$ *in thousands*	March 31, 2006	December 31, 2005
Raw materials and subassemblies	$ 1,196	$ 1,107
Finished goods	298	160
Parts for resale	800	814
Reserve for obsolescence		(100)
	$2,294	$ 1,981

4. Business Segment Information

Our structure and operational integration results in one segment that focuses on engineering, designing, building and installing systems that remove airborne contaminants from industrial facilities, as well as equipment that controls emissions from such facilities. Accordingly, the consolidated financial statements herein reflect the operating results of the segment.

5. Earnings Per Share

For the three months ended March 31, 2006 and 2005, both basic weighted average common shares outstanding and diluted average common shares outstanding were 10,913,503 and 9,993,260, respectively. We consider outstanding options and warrants in computing diluted net loss per share only when they are dilutive. Options and warrants to purchase 2,482,100 and 3,553,700 shares for the three months ended March 31, 2006 and 2005, respectively, were not included in the computation of diluted earnings per share due to their having an anti-dilutive effect. There were no adjustments to net loss for the basic or diluted earnings per share computations.

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CECO ENVIRONMENTAL CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

6. Debt

Total bank debt at March 31, 2006 was $8.2 million and $6.8 million at December 31, 2005. Unused credit availability under our $13.0 million revolving line of credit at March 31, 2006 was $7.0 million. Availability is limited as determined by a borrowing base formula contained in the credit agreement.

In December 2005, we refinanced our bank credit facility aggregating $16.1 million consisting of $3.1 million in term loans and a $13.0 million revolving credit line. Interest is charged based on the bank s prime rate plus 2.0 percentage points on the credit facility and plus 2.25 points on the term loan (9.75% and 10.0% at March 31, 2006).

7. Employee Benefit Plans

We sponsor a non-contributory defined benefit pension plan for certain union employees. The plan is funded in accordance with the funding requirements of the Employee Retirement Income Security Act of 1974.

We also sponsor a post-retirement health care plan for office employees retiring before January 1, 1990. The plan allows retirees who have attained the age of 65 to elect the type of coverage desired.

Retirement and health care plan expense is based on valuations performed by plan actuaries as of the beginning of each fiscal year. The components of the expense consisted of the following:

	Three Months Ended March 31,	
$ *in thousands*	**2006**	**2005**
Retirement plan:		
Service cost	$ 32	$ 33
Interest cost	71	69
Expected return on plan assets	(84)	(76)
Amortization of prior service cost	2	2
Amortization of net actuarial (gain)/loss	23	22
Net periodic benefit cost	$ 44	$ 50
Health care plan:		
Interest cost	$ 6	$ 7

We made contributions to our defined benefit plans in the first quarter of 2006 totalling $90,000. We anticipate contributing $393,000 to fund the pension plan and $69,000 for the retiree health care plan during the remainder of fiscal of 2006.

8. Equity Compensation

On January 1, 2006, the Company adopted SFAS No. 123(R), Share-Based Payment, which requires the Company to measure the cost of employee services received in exchange for an award of equity instruments and to recognize this cost in the financial statements over the period during which an employee is required to provide services. The Company has adopted SFAS No. 123(R) using the modified prospective application as defined in the Statement, and therefore financial statements for periods ending prior to January 1, 2006 have not been restated. Prior to January 1, 2006, the Company had

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CECO ENVIRONMENTAL CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

applied provisions of Accounting Principles Board Opinion No. 25, (Accounting for Stock Issued to Employees) and booked no compensation expense in the financial statements. The Company adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123 (SFAS No. 123), Accounting for Stock Based Compensation.

Stock Options

The Company has an equity compensation plan that was approved by shareholders whic