SKYWORKS SOLUTIONS, INC.
Form 8-K
December 05, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the

Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): November 29, 2011

Skyworks Solutions, Inc.

(Exact Name of Registrant as Specified in Charter)

Delaware	1-5560	04-2302115
(State or Other Jurisdiction of Incorporation)	(Commission File Number)	(IRS Employer Identification No.)

20 Sylvan Road, Woburn, MA	**01801**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant s telephone number, including area code: (781) 376-3000

Not applicable.

(Former name or former address, if changed since last report.)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (*see* General Instruction A.2. below):

¨ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

¨ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

x Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

¨ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 1.01. Entry into a Material Definitive Agreement.
Settlement Agreement and Mutual Release

On November 29, 2011, Skyworks Solutions, Inc., a Delaware corporation (Skyworks), and Advanced Analogic Technologies Incorporated, a Delaware corporation (AATI), entered into a Settlement Agreement and Mutual Release (the Settlement Agreement), settling the arbitration claims they had asserted under their May 26, 2011 Agreement and Plan of Merger (a copy of which was heretofore filed as an exhibit to the now-withdrawn Registration Statement of Skyworks on Form S-4, File No. 333-174953, and which is hereby re-filed as Exhibit 2.2 hereto) (the Merger Agreement). Pursuant to the Settlement Agreement, each company agreed to (i) enter into an amendment to the Merger Agreement (described below), (ii) voluntarily dismiss with prejudice the claims asserted against each other that were the subject of arbitration proceedings pending in the Delaware Court of Chancery, No. 004-A-CS and 005-A-CS (the Arbitration Proceedings), (iii) jointly issue the press release filed as Exhibit 99.1 to the Schedule TO-C filed with the SEC by Skyworks on November 30, 2011, (iv) release the other party and its respective officers, directors, stockholders, employees, advisors, representatives and other related parties from all claims, demands, rights, actions or causes of actions, liabilities, damages, losses, obligations, judgments, suits, fees, expenses, costs, matters and issues of any kind or nature whatsoever, including any claims which could form the basis of a termination for cause, in existence prior to the execution of the Settlement Agreement, and (v) agreed to bear its own legal fees and costs incurred in connection with the arbitration proceedings. On November 30, 2011, the Hon. Leo E. Strine, Jr., Chancellor of the Delaware Court of Chancery, acting as arbitrator in the Arbitration Proceedings, entered an order dismissing the petitions in the Arbitration Proceedings and the claims asserted therein with prejudice.

The foregoing description of the Settlement Agreement is only a summary, does not purport to be complete and is qualified in its entirety by reference to the Settlement Agreement, a copy of which is filed as Exhibit 99.1 hereto and is incorporated herein by reference.

Amendment No. 1 to Agreement and Plan of Merger

On November 30, 2011, Skyworks, PowerCo Acquisition Corp., a Delaware corporation and a wholly owned subsidiary of Skyworks (Merger Sub), and AATI entered into Amendment No. 1 to the Merger Agreement (the Amendment) , modifying the price, structure, conditions and other terms of Skyworks pending proposed acquisition of AATI. Pursuant to the Amendment, the one-step merger transaction at $6.13 per share in cash and stock contemplated by the May 26, 2011 Merger Agreement has been restructured as an all-cash two-step transaction at $5.80 per share.

In the first step of the transaction, upon the terms and subject to the conditions set forth in the Amendment, Skyworks has agreed to commence within seven business days (i.e., by December 9, 2011) a cash tender offer for any and all outstanding shares of AATI common stock (the Offer) at a purchase price of $5.80 per share in cash (the Offer Price). The consummation of the Offer will be conditioned on (i) at least a majority of the outstanding shares of AATI s common stock having been validly tendered and not properly withdrawn pursuant to the Offer prior to the expiration date of the Offer, (ii) the Merger Agreement having not been terminated in accordance with its terms, (iii) AATI having complied with certain interim covenants regarding conduct of its business, (iv) the representations and warranties of AATI concerning certain capitalization matters being true and correct as of the date of the Amendment, and (v) no governmental authority enacting, issuing, promulgating, enforcing or entering any order, executive order, stay, decree, judgment or injunction (preliminary or permanent) prohibiting the consummation of the Offer or the Merger (as defined below). The Offer will not be subject to financing.

In the second step of the transaction, following (and subject to) the consummation of the Offer and subject to certain further customary conditions (specifically, receipt of the requisite approval of AATI s stockholders (if required under applicable law), and no governmental authority having enacted, issued, promulgated, enforced or entered any order, executive order, stay, decree, judgment or injunction (preliminary or permanent) prohibiting consummation of the merger), Merger Sub will be merged with and into AATI (the Merger) and AATI will become a wholly owned subsidiary of Skyworks. In the Merger, each share of AATI s common stock then outstanding (other than shares already purchased in the Offer and other than shares for which appraisal rights have been properly exercised under Delaware law) will be converted into the right to receive an amount equal to the Offer Price. Skyworks may, but is not required to, provide for a subsequent offering period under federal securities law following the expiration of the Offer. In addition, AATI has granted Skyworks a top-up option to acquire shares of AATI s common stock in order to facilitate the consummation of the Merger using such short form merger procedures. The top-up option is exercisable any time after the first time at which Skyworks accepts for payment any shares of AATI common stock pursuant to the Offer. If Skyworks acquires 90% or more of the outstanding shares of AATI s common stock pursuant the Offer, the subsequent offering period (if any) and the top-up option, then Skyworks will consummate the Merger pursuant to the short form merger procedures under Delaware law as soon as practicable following the consummation of the Offer without a vote or any further action by the holders of AATI s common stock. If Skyworks does not acquire at least 90% of AATI s outstanding common stock, a majority of the outstanding shares of common stock must be voted to adopt the Merger Agreement before the Merger can be completed. In this event, AATI will call and convene a stockholder meeting to obtain this approval, and Skyworks will vote all shares of AATI common stock it holds in favor of adoption of the Merger Agreement, thereby assuring approval.

Other than as expressly modified pursuant to the Amendment, the Merger Agreement remains in full force and effect as originally executed on May 26, 2011. The foregoing description of the Amendment is only a summary, does not purport to be complete and is qualified in its entirety by reference to the Amendment, a copy of which is filed as Exhibit 2.1 hereto and is incorporated herein by reference.

Item 9.01 Financial Statements and Exhibits.

(d) Exhibits

2.1 Amendment No. 1 to Agreement and Plan of Merger, dated November 30, 2011 by and among Skyworks Solutions, Inc., PowerCo Acquisition Corp., and Advanced Analogic Technologies Incorporated

2.2 Agreement and Plan of Merger, dated as of May 26, 2011, by and among Skyworks Solutions, Inc., PowerCo Acquisition Corp., and Advanced Analogic Technologies Incorporated

99.1 Settlement Agreement, dated November 29, 2011, by and among Skyworks Solutions, Inc., PowerCo Acquisition Corp., and Advanced Analogic Technologies Incorporated

Additional Information and Where to Find It

Skyworks will file a Tender Offer Statement on Schedule TO and AATI will file a Solicitation/Recommendation Statement on Schedule 14D-9 with the Securities and Exchange Commission (SEC) in connection with the amended merger agreement and tender offer. Security holders are advised to read the Tender Offer Statement (and the exhibits thereto) and the Solicitation/Recommendation Statement when they are available because they will contain important information. Investors can obtain the Tender Offer Statement (including exhibits) when it is filed by Skyworks, the Solicitation/Recommendation Statement when it is filed by AATI, and other documents filed by Skyworks and/or AATI for free at the web site of the U.S. Securities and Exchange Commission at http://www.sec.gov. In addition, investors and security holders can obtain free copies of the documents filed by Skyworks with the SEC from Skyworks by contacting Skyworks Investor Relations at (949) 231-4700 or by accessing Skyworks investor relations website at http://www.skyworksinc.com, and free copies of the documents filed by AATI with the SEC from AATI by contacting AATI s Investor Relations at The Blueshirt Group, Lisa Laukkanen, at (415) 217-4967 or by accessing Advanced Analogic Technologies investor relations website at http://www.analogictech.com.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

SKYWORKS SOLUTIONS, INC.

Date: December 5, 2011

/s/ Mark V. B. Tremallo
Mark V. B. Tremallo
Vice President, General Counsel and Corporate Secretary

EXHIBIT INDEX

Exhibit Number	Description
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bution facilities. The fair value of the distribution reporting unit was determined using the present value of expected future cash flows and other valuation measures. The $1,272,000 ($789,000 net of related tax benefit) non-cash charge was reflected as a cumulative effect of an accounting change in the Consolidated Statements of Operations for the quarter ended March 31, 2002. In accordance with SFAS 142 and SFAS 3, "Reporting Accounting Changes in Interim Financial Statements" ("SFAS 3"), when a transitional impairment loss for goodwill (cumulative effect type accounting change) is measured in other than the first interim reporting period, it is recognized in the 10 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES Notes to Consolidated Financial Statements -continued- (4) Goodwill and Other Intangible Assets (continued) ----------------------------------- first interim period irrespective of the period in which it is measured. (5) Notes Payable ------------- At March 31, 2003 and December 31, 2002, notes payable represent amounts outstanding under a $6,000,000 line of credit (increased to $7,000,000 effective April 22, 2003) from a commercial lender to the Company's subsidiaries. The line of credit is collateralized by the subsidiaries' accounts receivable and inventory, bears interest at prime rate plus 1/2% (5.25% at March 31, 2003), expires June 19, 2004, and is subject to annual renewal. At March 31, 2003, the line of credit limit available for borrowing based on eligible receivables and inventory aggregated $5,383,000, of which $4,757,000 was outstanding. The average amounts outstanding for the three month periods ended March 31, 2003 and 2002 were $4,754,000 and $4,583,000, respectively. (6) Long-Term Debt and Current Installments of Long-Term Debt --- Included in long-term debt at March 31, 2003, are four mortgage loans, collateralized by real property, in the aggregate amount of $834,000, less current installments aggregating $254,000. Subsequent to March 31, 2003 the Company sold a property no longer utilized in operations and satisfied a mortgage in the approximate amount of $199,000 classified as a current liability. During 2000, the Company acquired certain assets and assumed certain liabilities of seven building materials distributors in which it issued $850,000 uncollateralized 8% promissory notes as partial consideration. At March 31, 2003, the aggregate remaining notes of $128,000 were classified as a current liability. Other long-term debt in the aggregate amount of $659,000, less current installments of $274,000, relates principally to equipment financing. The notes bear interest at various rates ranging from 3.10% to 11.4%. 11 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES Notes to Consolidated Financial Statements -continued- (7) Income Taxes ------------ At March 31, 2003, the net deferred tax asset of approximately $913,000 consisted primarily of the tax effect of net operating loss carryforwards and the goodwill written off. The operating loss carryforwards of approximately $769,000 expire in varying amounts from 2005 through 2009. In the three months ended March 31, 2003 and 2002, the Company recognized income tax benefit of $21,000 and tax expense of $66,000, respectively. (8) Capital Stock ------------- (a) Common Stock ------------ At March 31, 2003, the Company had outstanding 9,235,434 shares of common stock with a $.01 par value per share ("Common Stock"). The holders of common stock are entitled to one vote per share on all matters, voting together with the holders of preferred stock, if any. In the event of liquidation, holders of common stock are entitled to share ratably in all the remaining assets of the Company, if any, after satisfaction of the liabilities of the Company and the preferential rights of the holders of outstanding preferred stock, if any. On July 19, 2002 at the Company's Annual Meeting of Shareholders, the Company's Shareholders approved a proposal for a one for five reverse common stock split ("Reverse Stock Split"). Pursuant to the terms of the proposal, the Reverse Stock Split was to become effective upon filing an appropriate certificate with the Secretary of State of Delaware. Notwithstanding the approval of the Reverse Stock Split, the Board of Directors reserved the right, without further action by the Shareholders, to elect not to proceed with the Reverse Stock Split if at any time prior to the filing of such certificate with the State of Delaware, the Board of Directors, in its sole discretion, determined that it was no longer in the best interests of the Company and its stockholders. In addition, the Board of Directors reserved the right to delay the Reverse Stock Split for up to twelve months following the stockholder approval. The Board of Directors determined it was in the best interest of the Company to postpone the implementation of the Reverse Stock Split until a future date to be determined by the Board and as a result the Reverse Stock Split has not been implemented. (b) Preferred Stock --------------- The authorized preferred stock of the Company consists of 5,000,000 shares, $.01 par value per share. The preferred stock is issuable in series, each of which may vary, as determined by 12 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES Notes to Consolidated Financial Statements -continued- (8) Capital Stock (continued) ------------ the Board of Directors, as to the designation and number of shares in such series, the voting power of the holders thereof, the dividend rate, redemption terms and prices, the voluntary and involuntary liquidation preferences, and the conversion rights and sinking fund requirements, if any, of such series. At March 31, 2003 and December 31, 2002, there were no shares of preferred stock outstanding. (c) Warrants -------- At March 31, 2003, the Company had warrants outstanding to purchase 150,000 shares of the Company's common stock (the "Warrants"). Each Warrant entitles the holder to purchase one share at $.38 per share until December 31, 2003. (d) Stock Option Plans ------------------ The Company has two stock option plans, the Directors' Stock Option Plan and the 1999 Employee Stock Option Plan (collectively, the "1999 Plans"). The 1999 Plans provide for options to be granted at generally no less than the fair market value of the Company's Common stock at the grant date. Options granted under the 1999 Plans have a term of up to 10 years and are exercisable six months form the grant date. The 1999 Plans are administered by the Compensation and Stock Option Committee (the "Committee"), which is comprised of three outside directors. The Committee determines who is eligible to participate and the number of shares for which options are to be granted. A total of 600,000 and 200,000 shares are reserved for issuance under the Employee and Directors' Plans, respectively. As of March 31, 2003, options for 360,000 shares were available for future grants under the Employee Plan. No shares are currently available for future grant under the Directors' Plan. (9) Earnings Per Share ------------------ Below is a reconciliation between basic and diluted earnings per common share under FAS 128 for the three months ended March 31, 2003 and 2002 (in thousands except per share amounts): 2003 2002 --------------------- ------------------------ Per Per Loss Shares Share Loss Shares Share ----- ----- ----- ----- ----- ------- Net (loss) income $ (33) -- -- $(667) -- -- Basic earnings per share $ (33) 9,235 $ -- $(667) 9,220 $ (.07) ----- ----- ----- ----- ----- ------- Effect of dilutive securities: Options/Warrants -- -- -- -- -- -- ----- ----- ----- ----- ----- ------- Diluted earnings per common share $ (33) 9,235 $ -- $(667) 9,220 $ (.07) ----- ----- ----- ----- ----- ------- 13 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES Notes to Consolidated Financial Statements -continued- (9) Earnings Per Share (continued) ------------------ For the three months ended March 31, 2003 and 2002, 590,000 and 510,000 options and warrants were excluded from the diluted earnings per share computations, respectively, because they were anti-dilutive. (10) Commitments and Contingencies ----------------------------- (a) Contingencies ------------- As of May 1, 2003, the Company's subsidiary, Acrocrete, Inc., together with other parties are defendants in 41 lawsuits pending in various Southeastern states, brought by homeowners, homeowners associations, contractors and subcontractors, or their insurance companies, claiming moisture intrusion damages on single and multi-family residences. The Company's insurance carriers have accepted coverage under a reservation of rights for 35 of these claims and are providing a defense. The Company expects its insurance carriers will accept coverage for the other 6 recently filed lawsuits. Acrocrete is vigorously defending all of these cases and believes it has meritorious defenses, counter-claims and claims against third parties. Acrocrete is unable to determine the exact extent of its exposure or outcome of this litigation. The allegations of defects in synthetic stucco wall systems are not restricted to Acrocrete products, but rather are an industry-wide issue. There has never been any defect proven against Acrocrete. The alleged failure of these products to perform has generally been linked to improper application and the failure of adjacent building materials such as windows, roof flashing, decking and the lack of caulking. On June 15, 1999, Premix was served with a complaint captioned Mirage Condominium Association, Inc. v. Premix, In the Eleventh Judicial Circuit In and For Miami-Dade County, Florida, Case No: 97-27544 (CA-11). The lawsuit raises a number of allegations against 12 separate defendants involving alleged construction defects. The lawsuit originally alleged a claim against Premix for third-party beneficiary breach of contract. This claim was voluntarily dismissed on the eve of a hearing on Premix's dispositive Motion for Summary Judgment. A Third Amended Complaint was filed against Premix for breach of a statutory implied warranty. Plaintiff has alleged that certain materials, purportedly provided by Premix to the Developers/Contractor and used to anchor balcony railings to the structure were defective. After the Third Amended Complaint was filed, the contractor filed a cross claim against Premix for indemnification, breach of implied warranty and product liability. 14 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES Notes to Consolidated Financial Statements -continued- (10) Commitments and Contingencies (continued) ---------------------------- (a) Contingencies (continued) ------------ Premix has meritorious defenses to these claims. The Company's insurance carrier has not made a decision regarding coverage to date. In the interim, the insurance carrier has retained defense counsel on behalf of Premix and is paying defense costs. Premix expects the insurance carriers to eventually accept coverage. As discovery is not yet completed, Premix is unable to determine the exact extent of its exposure or the outcome of this litigation. The Company's subsidiaries are engaged in other legal actions and claims arising in the ordinary course of its business, none of which are believed to be material to the Company. On April 23, 1999, certain Dissenting Shareholders owning shares of the Company's formerly issued preferred stock filed a petition for appraisal in the Delaware Chancery Court to determine the fair value of their shares at the effective date of Merger, which would require the Company to pay the holders the fair value of their stock in cash as determined by the Delaware Chancery Court. A trial for the appraisal rights was held in the Chancery Court of Delaware in June 2002. In February 2003, the Company and the Dissenting Stockholders reached a settlement in principle prior to the trial court issuing a ruling. On April 30, 2003 the Company consummated the settlement with its Dissenting Stockholders. As of March 31, 2003, the Company has recorded $1,541,000 in the accompanying balance sheet as an estimate for appraisal rights based on the estimated fair value of settlement. (See Note 11) (b) Lease Commitments ---------------- At March 31, 2003, certain property, plant and equipment were under lease by the Company under long-term leases. The Company will pay aggregate annual rent of approximately $1,091,000 for its current operating leases. The leases expire at various dates ranging from August 31, 2003 to August 31, 2009. Comparable properties at equivalent rentals are available for replacement of these facilities if any leases are not extended. The Company does not expect to incur any material relocation expenses. (11) Recent Events ------------ In February 2003, the Company and former holders of 81,100 shares of Preferred Stock who elected appraisal rights in connection with the Company's 1998 Merger ("Dissenting Stockholders") reached a settlement in principle prior to the trial court issuing a ruling (the "Settlement"). On April 30, 2003, the Settlement was completed and the Company paid the 15 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES Notes to Consolidated Financial Statements -continued- (11) Recent Events (continued) ------------ Dissenting Stockholders $12.00 per share in cash ($973,200) and issued a 5.6% Promissory Note for $10.00 per share ($811,000) due May 1, 2006, with such Note reduced to $7.00 per share ($567,700) in the event the Company prepays the Note in full prior to November 1, 2004. If the note is not paid in full prior to November 1, 2004, the interest rate will increase from 5.6% to 8.0%. The Company satisfied the cash due at closing from cash on hand and borrowings from its amended line of credit with it commercial lender based on an increase to its inventory borrowing base. At March 31, 2003 and December 31, 2002, based on management's intention to prepay the Note in full prior to November 1, 2004, the appraisal rights obligation was recorded at $1,541,000. As a result of the completion of the settlement on April 30, 2003, $567,700 of the Obligation for Appraisal Rights was classified as long-term liability at March 31, 2003. On April 22, 2003 the Company amended its line of credit to provide for an increase to $7,000,000 from $6,000,000 based on eligible receivables and inventory and increased the amount of inventory eligible for borrowings. 16 Item 2 Management's Discussion and Analysis of Financial Condition and Results --- of Operations ------------ General ------- The Company's business is related primarily to the level of construction activity in the Southeastern United States, particularly the states of Florida, Georgia, Mississippi and Alabama. The majority of the Company's products are sold to contractors, subcontractors and building materials dealers located principally in these states who provide building materials for the construction of residential, commercial and industrial buildings and swimming pools. The level of construction activity is subject to population growth, inventory of available housing units, government growth policies and construction funding, among other things. Although general construction activity has remained strong in the Southeastern United States during the last several years, the duration of recent economic conditions and the magnitude of their effect on the construction industry are uncertain and cannot be predicted. Special Note Regarding Forward-Looking Statements --- This Form 10-Q contains certain forward looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to the financial condition, results of operations and business of the Company, and its subsidiaries, including statements made under Management's Discussion and Analysis of Financial Condition and Results of Operations. These forward looking statements involve certain risks and uncertainties. No assurance can be given that any of such matters will be realized. Factors that may cause actual results to differ materially from those contemplated by such forward looking statements include, among others, the following: realization of tax benefits; impairment of long-lived assets, including goodwill; the ability to collect our account or note receivables when due or within a reasonable period of time after they become due and payable; the outcome of litigation; the competitive pressure in the industry; general economic and business conditions; the ability to implement and the effectiveness of business strategy and development plans; quality of management; business abilities and judgment of personnel; there may be changes in accounting policies and practices, as may be adopted by regulatory agencies as well as the Financial Accounting Standards Board; availability of qualified personnel; and labor and employee benefit costs. These risks may not be exhaustive. The Company operates in a continually changing business environment, and new risks emerge from time to time. The Company cannot predict such risks nor can the Company assess the impact, if any, of such risks on its business or the extent to which any risk, or combination of risks may cause actual results to differ from those projected in any forward-looking statements. 17 Item 2 Management's Discussion and Analysis of Financial Condition and Results --- of Operations (continued) ------------ Special Note Regarding Forward-Looking Statements (continued) -- These forward-looking statements speak only as of the date of this document. The Company does not undertake any obligation to update or revise any of these forward-looking statements to reflect events or circumstance occurring after the date of this document or to reflect the occurrence of unanticipated events. Results of Operations -------------------- Three Months Ended March 31, 2003 Compared to 2002 --- Net Sales for the three months ended March 31, 2003 increased $253,000 or approximately 2.9% compared to 2002. Net sales derived from a new distribution facility opened in the third quarter of 2002 in Port St. Lucie, Florida, offset by the reduction in sales realized from the Pensacola distribution facility closed in the third quarter of 2002, accounted for $97,000 of the $253,000 increase in sales. The balance of the increase in sales came from internally generated growth from the sales of the Company's manufactured products and increased sales from the Company's distribution facilities offset by a reduction of approximately $225,000 decrease in sales from the Company's Gulfport, Mississippi distribution facility. The decrease in sales at the Gulfport facility is believed to be primarily because of increased competition due to the alleged violation of a non-compete agreement of a former employee at that location. The Company has instituted litigation against the former employee to enjoin further violations and for damages resulting from such actions. Gross profit as a percentage of net sales for the first quarter of 2003 was approximately 30.4% compared to 31.3% in 2002. The decrease in gross profit margins was principally due to lower gross profit margins realized from sales generated from the Company's distribution facilities in 2003 compared to the same period in 2002. The lower gross profit margins are primarily attributable to more intense competitive conditions in several of the Company's trade areas in 2003, particularly the Gulfport, Mississippi trade area. The Company is continuing to emphasize the sales of its higher gross profit margin manufactured products through its distribution facilities and other distributors and to decrease reliance on sales of products purchased from other manufacturers. The Company increased its sales force during 2002 to further promote the sales of its manufactured products to the end-user. Selling, general and administrative expenses as a percentage of net sales for the first quarter of 2003 were approximately 30.7% compared to 28.3% in 2002. Selling, general and administrative expenses increased $285,000 or approximately 11.6% in 2003, compared to 2002. Of this 18 Item 2 Management's Discussion and Analysis of Financial Condition and Results --- of Operations (continued) ------------ Three Months Ended March 31, 2003 Compared to 2002 (continued) -- increase, approximately $138,000 is believed to be attributed to inflationary cost pressures on certain expenses and costs associated with the Company's attention on improving customer service and the opening of a new distribution facility in August 2002. Insurance premiums accounted for approximately $18,000 of the increase in expenses. Delivery charges and fuel costs increased approximately $53,000. Maintenance costs increased $27,000 and payroll costs were up approximately $40,000. (The Company's total payroll costs increased approximately 2.8% in the first quarter of 2003 compared to 2002). In addition, during the first quarter of 2003 the Company elected to settle several customer complaints to maintain customer goodwill that resulted in a $39,000 increase in expenses compared to the same period in 2002. Based on historical experience, the Company is not expecting to incur a similar amount of expenses in subsequent quarters. Also, the Company incurred a $49,000 increase in legal fees in the first quarter of 2003 compared to 2002, primarily as a result of the commencement of litigation against a former employee for violations of his non-compete agreement as discussed above. Increases in various other operating expenses accounted for the remaining $59,000 increase in expenses. Interest expense decreased $35,000 in the first quarter of 2003, or approximately 26.5%, compared to 2002. The decrease in interest expense in the first three months of 2003 was primarily due to a reduced level of interest bearing obligations in 2003 compared to 2002, principally the appraisal rights obligations as a result of a settlement completed on April 30, 2003. In the first quarter of 2003, the Company recognized an income tax benefit of $21,000, compared to a $66,000 expense for the first three months of 2002. After giving effect to the above factors, the Company generated a loss before taxes and the write-off of goodwill, as discussed below, for the first three months of 2003 of $54,000, compared to income of $122,000 for 2002. The first quarter 2002 results were adversely impacted by $1,272,000 ($789,000 net of related deferred tax benefit) non-cash goodwill impairment charge. The charge was related to the Company's required adoption of Statement of Financial Accounting Standards (SFAS) No. 142 "Goodwill and Other Intangible Assets". The goodwill impairment charge did not affect the operating results of the Company. The Company doesn't have any remaining goodwill on its balance sheet which may be impaired for future periods. The impairment of goodwill was attributable to the under-performance of the Company's distribution operations associated with the acquisition of 19 Item 2 Management's Discussion and Analysis of Financial Condition and Results -- of Operations (continued) ------------- Three Months Ended March 31, 2003 Compared to 2002 (continued) -- certain building materials distributors in 2000. In accordance with SFAS No. 142, the Company has reflected this impairment charge in the first quarter 2002 financial results as a cumulative change in accounting principle. As a result of the above factors, the Company incurred a net loss of $33,000 or $.00 per fully diluted share for the first quarter of 2003, compared to a loss of $667,000 or $.07 per share for 2002. Liquidity and Capital Resources ------------------------------ Sources and Uses of Cash ----------------------- The Company generated approximately $356,000 and $228,000 of net cash from operations for the first three months of 2003 and 2002, respectively, due primarily to the following items. In the first quarter of 2003, net cash provided by operating activities included a $501,000 increase in accounts payables compared to a $361,000 increase in the same quarter in 2002. Also, in the first three months of 2003 inventory decreased by $4,000, compared to a $206,000 increase in the first quarter of 2002, due to improved working capital management. During the first quarter of 2003, the net expenditures for investing activities were $106,000 compared to $85,000 in 2002. The purchase of equipment to up-grade the Company's manufacturing equipment and distribution capabilities accounted for the majority of the expenditures for each period. During the three months ended March 31, 2003, the line of credit balance decreased approximately $157,000 as a result of improvements in the Company's cash management program. The Company also made a net reduction on long-term debt totaling $30,000 during the quarter. Future Commitments and Funding Sources ------------------------------------ As of March 31, 2003, the Company had cash and cash equivalents of $1,672,000, which included customer payments in the amount of $470,000 that are required to be remitted to the Company's commercial lender upon their bank clearance under the terms of the Company's line of credit. Upon remittance of such amount, the outstanding balance of the line of credit will be reduced by such amount and will increase the availability for future borrowing under the line. The Company has implemented a cash management program in an attempt to gain a more rapid clearance of customer payments deposited in its bank accounts. At March 31, 2003, the Company's contractual cash obligations, with initial or remaining terms in excess of one 20 Item 2 Management's Discussion and Analysis of Financial Condition and Results -- of Operations (continued) ------------- Liquidity and Capital Resources (continued) ------------------------------ year, remained generally unchanged compared to December 31, 2002. See Notes 6 and 10 in the accompanying financial statements for additional information regarding the Company's commitments. At March 31, 2003, the Company had working capital of approximately $1,925,000 compared to working capital of $1,432,000 at December 31, 2002. The increase in working capital was primarily attributable to the reclassification of $568,000 of the appraisal rights obligation from a short-term liability at December 31, 2002 to a long-term liability at March 31, 2003. Subsequent to March 31, 2003, the Company sold a former distribution facility property and repaid a $199,000 mortgage obligation classified as a short-term liability at March 31, 2003. The Company's principal source of short-term liquidity is existing cash on hand and the utilization of a line of credit with its commercial lender. The maturity date of the line of credit is June 19, 2004, subject to annual renewal. Premix, Acrocrete and Just-Rite borrow on the line of credit, based upon and collateralized by, their eligible accounts receivable and inventory. Generally, accounts not collected within 120 days are not eligible accounts receivable under the Company's borrowing agreement with its commercial lender. At March 31, 2003, $4,757,000 had been borrowed against the line of credit. Based on eligible receivables and inventory, the Company had, under its line of credit, total available borrowing, (including the amount outstanding of $4,757,000) of approximately $5,383,000 at March 31, 2003. On April 22, 2003 the line of credit was amended to increase the maximum borrowings from $6,000,000 to $7,000,000 and increase the amount of eligible borrowings based on inventory. Trade accounts receivable represent amounts due from subcontractors, contractors and building materials dealers located principally in Florida, Mississippi and Georgia who have purchased products on an unsecured open account basis and through Company owned warehouse distribution outlets. As of March 31, 2003, the Company owned and operated eleven distribution facilities. Accounts receivable, net of allowance, at March 31, 2003 was $5,093,000 compared to $4,880,000 at December 31, 2002. The increase in receivables of $213,000, or approximately 4.4%, was primarily related to slower payments by certain customers in the first quarter of 2003 compared to the fourth quarter of 2002. As a result of the consummation of the December 31, 1998 merger, the Company agreed to pay $733,000 in cash to its former preferred stockholders. As of March 31, 2003, the Company had paid $685,000 of such cash amount. Amounts payable to such stockholders at March 31, 2003 results from their non-compliance with the condition for payments. 21 Item 2 Management's Discussion and Analysis of Financial Condition and Results -- of Operations (continued) ------------- Liquidity and Capital Resources (continued) ------------------------------ Holders representing 81,100 preferred shares elected dissenters' rights, which, under Delaware law, require cash payments equal to the fair value of their stock, as of the date of the merger, to be determined in accordance with Section 262 of the Delaware General Corporation Law. The Company recorded a liability for each share based on the fair value of $2.25 in cash, and $8.00 Subordinated Debenture and five shares of the Company's common stock since that is the consideration the dissenting holders would have received if they did not perfect their dissenters' rights under the law. Dissenting stockholders filed a petition for appraisal rights in the Delaware Chancery Court on April 23, 1999. A trial for the appraisal rights was held in the Chancery Court of Delaware in June 2002. In February 2003, the Company and the dissenting stockholders reached a settlement in principal prior to the trial court issuing a ruling. On April 30, 2003 the Company completed its settlement and paid the holders of appraisal rights $12.00 per share in cash ($973,200) and issued a 5.6% Promissory Note for $10.00 per share ($811,000) due May 1, 2006, with such Note to be reduced to $7.00 per share ($567,700) in the event the Company prepays the Note in full prior to November 1, 2004. The Company satisfied the cash due at closing from cash on hand and borrowings from its amended line of credit with its commercial lender. At March 31, 2003, based on management's intention to prepay the Note in full prior to November 1, 2004, the appraisal rights obligation was recorded in the amount of $1,541,000, of which $567,700 was classified as a long-term liability. As of March 31, 2003, the Company has paid the holders of the Subordinated Debentures tendering their bonds $808,000. Amounts payable to stockholders at March 31, 2003 on the Company's consolidated balance sheets includes $214,000 payable to former debenture holders who have not yet tendered their Debentures as required by the terms of such instrument. The Company presently is focusing its efforts on enhancing customer service, increasing operating productivity through reducing costs and expenses and improving working capital. The Company expects to incur various capital expenditures aggregating approximately $300,000 during the next twelve months to upgrade and maintain its equipment and delivery fleet to support operations and improve customer service. The Company expects to finance approximately $200,000 of these expenditures from various lenders with the balance funded by cash derived from operations. The Company believes its cash on hand, the maintenance of its amended line of credit and new equipment financing arrangements will provide sufficient cash to meet its current 22 Item 2 Management's Discussion and Analysis of Financial Condition and Results -- of Operations (continued) ------------- Liquidity and Capital Resources (continued) ------------------------------ obligations for its operations and support the cash requirements of it capital expenditure programs in 2003. The ability of the Company to maintain and improve its long-term liquidity is primarily dependent on the Company's ability to successfully achieve and maintain profitable operations. Item 3 Market Risks ------------ Residential and Commercial Construction Activity -- The Company's sales depend heavily on the strength of residential and commercial construction activity in the Southeastern United States. The strength of these markets depends on many factors beyond the Company's control. Some of these factors include interest rates, employment levels, availability of credit, prices of raw materials and consumer confidence. Downturns in the markets that the Company serve or in the economy generally could have a material adverse effect on the Company's operating results and financial condition. Reduced levels of construction activity may result in intense price competition among building materials suppliers, which may adversely affect the Company's gross margins. The Company's first quarter revenues and, to a lesser extent, its fourth quarter revenues are typically adversely affected by winter construction cycles and weather patterns in colder climates as the level of activity in the new construction and home improvement markets decreases. Because much of the Company's overhead and expense remains relatively fixed throughout the year, Company profits also tend to be lower during the first and fourth quarters. Exposure to Interest Rates ------------------------- The Company has two variable rate mortgages totaling $359,000 at March 31, 2003. The mortgages bear interest at prime plus 1% and are due October 2004. In addition, the Company's $7,000,000 line of credit from a commercial lender bears an interest rate of prime plus 1/2%. A significant increase in the prime rate could have a material adverse effect on the Company's operating results and financial condition. Item 4 Controls and Procedures ---------------------- Evaluation of Disclosure Controls and Procedures --- Within 90 days prior to the filing date of this Quarterly Report, the Company carried out an evaluation, under the 23 Item 4 Controls and Procedures Evaluation of Disclosure Controls and Procedures (continued) --- supervision and with the participation of the Company's management, including the Company's Chief Executive Officer/Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-14(c) and 15d-14(c) under the Securities Exchange Act of 1934). Based upon that evaluation, the Chief Executive Officer/Chief Financial Officer concluded that the Company's disclosure controls and procedure are effective in ensuring that information required to be disclosed in the reports the Company files and submits under the Securities Exchange Act of 1934 are recorded, processed, summarized and reported as and when required. Changes in Internal Controls --------------------------- There were no significant changes in the Company's internal controls or in other factors that could significantly affect such internal controls subsequent to the date of the evaluation described in the paragraph above, including any corrective action with regard to significant deficiencies and material weaknesses. 24 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES PART II. Other Information Item 1. Legal Proceedings See notes to Consolidated Financial Statements, Note 10 (a), set forth in Part I Financial Information. Item 4. Submission of Matters to a Vote of Security Holders None. 25 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES PART II. Other Information - continued Item 6. Exhibits and Reports on Form 8-K ------------------------------- Exhibit No. Description ----------- ----------- 2.1 Agreement and Plan of Merger, by and between Imperial Industries, Inc. and Imperial Merger Corp. dated October 12, 1998 (Incorporated by reference to Form S-4 Registration Statement, Exhibit 2). 3.1 Certificate of Incorporation of the Company, (Incorporated by reference to Form S-4 Registration Statement, Exhibit 3.1). 3.2 Amendment to Certificate of Incorporation of the Company (Incorporated by reference to Form 10-K dated December 31, 2001, Exhibit 3.2). 3.3 By-Laws of the Company, (Incorporated by reference to Form S-4 Registration Statement, Exhibit 3.2). 10.1 Consolidating, Amended and Restated Financing Agreement by and between Congress Financial Corporation and Premix-Marbletite Manufacturing Co., Acrocrete, Inc. and Just-Rite Supply, Inc. dated January 28, 2000. (Incorporated by reference to Form 10-K dated December 31, 1999, File No. 1-7190, Exhibit 10-1). 10.2 Employee Stock Option Plan (Incorporated by reference to Form 10-K dated December 31, 2000, Exhibit 10.4). 10.3 Directors Stock Option Plan (Incorporated by reference to Form 10-K dated December 31, 2000, Exhibit 10.5). 10.4 Form of Promissory Note issued in Settlement of Preferred Stock Dissenters Rights. 10.5 Amendment No. 3 to Consolidating, Amended and Restated Financing Agreement by and between Congress Financial Corporation and Premix-Marbletite Manufacturing Co., Acrocrete, Inc. and Just-Rite Supply, Inc. dated April 22, 2003. 99.1 Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002. (b) Reports on Form 8-K None. 26 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES SIGNATURES Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on it behalf by the undersigned thereunto duly authorized. IMPERIAL INDUSTRIES, INC. By: /S/ Howard L. Ehler, Jr. ------------------------- Howard L. Ehler, Jr. Principal Executive Officer/ Chief Financial Officer By: /S/ Betty Jean Murchison ------------------------- Betty Jean Murchison Chief Accounting Officer/ Assistant Vice President May 13, 2003 27 IMPERIAL INDUSTRIES, INC. AND SUBSIDIARIES CERTIFICATE I, Howard L. Ehler, Jr., certify that: 1. I have reviewed this quarterly report on Form 10-Q of Imperial Industries, Inc; 2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstance under which such statements were made, not misleading; 3. Based on my knowledge, the financial statements, and other financial information include in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report; 4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and I have: a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this quarterly report is being prepared. b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and c) Presented in this quarterly report my conclusions about the effectiveness of the disclosure controls and procedures based on my evaluation as of the Evaluation Date; 5. I have disclosed, based on my most recent evaluation, to the registrant's auditors and the Audit Committee of the Company's Board of Directors: a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and 6. I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of my most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses. Imperial Industries, Inc. By: /S/ Howard L. Ehler, Jr. ------------------------ Howard L. Ehler, Jr. Chief Executive Officer/ May 13, 2003 Chief Financial Officer 28