CHART INDUSTRIES INC
Form 10-Q
April 26, 2012
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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 March 31, 2012

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 1-11442

CHART INDUSTRIES, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware	34-1712937
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

One Infinity Corporate Centre Drive, Suite 300, Garfield Heights, Ohio 44125
(Address of Principal Executive Offices) (ZIP Code)

Registrant's Telephone Number, Including Area Code: (440) 753-1490

NOT APPLICABLE
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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.

Large accelerated filer x	Accelerated filer ¨
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

At April 26, 2012, there were 29,900,660 outstanding shares of the Company's Common Stock, par value $0.01 per share.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.
CHART INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except per share amounts)

	March 31, 2012 (Unaudited)	December 31, 2011
ASSETS		
Current Assets		
Cash and cash equivalents	$242,520	$256,861
Accounts receivable, net	127,254	131,904
Inventories, net	167,855	149,822
Unbilled contract revenue	26,735	25,247
Prepaid expenses	9,199	7,088
Other current assets	32,194	26,707
Total Current Assets	605,757	597,629
Property, plant and equipment, net	141,952	137,301
Goodwill	289,436	288,770
Identifiable intangible assets, net	137,334	140,553
Other assets, net	9,908	10,222
TOTAL ASSETS	$1,184,387	$1,174,475
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current Liabilities		
Short-term debt	$4,761	$4,758
Accounts payable	72,304	84,297
Customer advances and billings in excess of contract revenue	109,894	102,996
Accrued salaries wages, and benefits	21,284	29,108
Warranty reserve	12,197	13,181
Current portion of long-term debt	6,500	6,500
Other current liabilities	28,210	24,653
Total Current Liabilities	255,150	265,493
Long-term debt	223,837	223,224
Long-term deferred tax liability, net	45,841	43,945
Accrued pension liabilities	15,457	15,905
Other long-term liabilities	7,998	12,357
Equity		
Chart Industries’ shareholders’ equity:		
Common stock, par value $.01 per share – 150,000,000 shares authorized, 29,899,189 and 29,612,684 shares issued and outstanding at March 31, 2012 and December 31, 2011, respectively	299	296
Additional paid-in capital	339,145	333,034
Retained earnings	288,799	274,716
Accumulated other comprehensive income	5,257	2,993
Total Chart Industries, Inc. shareholders’ equity	633,500	611,039
Noncontrolling interest	2,604	2,512
Total equity	636,104	613,551
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$1,184,387	$1,174,475

The balance sheet at December 31, 2011 has been derived from the audited financial statements at that date, but does not include all of the information and notes required by U.S. generally accepted accounting principles for complete financial statements.

See accompanying notes to these unaudited condensed consolidated financial statements. The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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CHART INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (UNAUDITED)
(Dollars and shares in thousands, except per share amounts)

	Three Months Ended March 31,	
	2012	2011
Sales	$216,106	$162,941
Cost of sales	148,549	110,455
Gross profit	67,557	52,486
Selling, general and administrative expenses	40,626	34,862
Amortization expense	3,070	3,317
	43,696	38,179
Operating income	23,861	14,307
Other expenses (income):		
Interest expense, net	3,962	3,934
Financing costs amortization	321	325
Foreign currency gains	(352)	(759)
	3,931	3,500
Income before income taxes	19,930	10,807
Income tax expense	5,778	3,404
Net income	14,152	7,403
Noncontrolling interest, net of tax	69	(127)
Net income attributable to Chart Industries, Inc.	$14,083	$7,530
Net income attributable to Chart Industries, Inc. per common share – basic	$0.48	$0.26
Net income attributable to Chart Industries, Inc. per common share – diluted	$0.47	$0.25
Weighted average number of common shares outstanding – basic	29,593	28,768
Weighted average number of common shares outstanding – diluted	30,061	29,678
Comprehensive income, net of tax	$16,416	$13,468
Less: Comprehensive income attributable to noncontrolling interest, net of tax	69	(127)
Comprehensive income attributable to Chart Industries, Inc., net of tax	$16,347	$13,595

See accompanying notes to these unaudited condensed consolidated financial statements. The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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CHART INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(Dollars in thousands)

	Three Months Ended March 31,	
	2012	2011
OPERATING ACTIVITIES		
Net income	$14,152	$7,403
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	7,223	6,652
Interest accretion of convertible notes discount	2,238	—
Employee stock and stock option related compensation expense	2,505	1,401
Financing costs amortization	321	325
Foreign currency gains	(352)	(759)
Other non-cash operating activities	243	(291)
Increase (decrease) in cash resulting from changes in operating assets and liabilities:		
Accounts receivable	5,391	(2,648)
Inventory	(17,074)	(12,911)
Unbilled contract revenues and other current assets	(1,662)	(255)
Accounts payable and other current liabilities	(27,619)	(12,548)
Customer advances and billings in excess of contract revenue	5,462	(7,207)
Net Cash Used In Operating Activities	(9,172)	(20,838)
INVESTING ACTIVITIES		
Capital expenditures	(6,345)	(4,266)
Other investing activities	—	388
Net Cash Used In Investing Activities	(6,345)	(3,878)
FINANCING ACTIVITIES		
Principal payments on long-term debt	(1,625)	(1,625)
Proceeds from exercise of options	1,725	2,238
Tax benefit from exercise of stock options	6,355	2,452
Common stock repurchases	(4,473)	(1,090)
Net Cash Provided By Financing Activities	1,982	1,975
Effect of exchange rate changes on cash	(806)	4,625
Net decrease in cash and cash equivalents	(14,341)	(18,116)
Cash and cash equivalents at beginning of period	256,861	165,112
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$242,520	$146,996

See accompanying notes to these unaudited condensed consolidated financial statements. The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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CHART INDUSTRIES, INC. AND SUBSIDIARIES
Notes to Unaudited Condensed Consolidated Financial Statements – March 31, 2012
(Dollars and shares in thousands, except per share amounts)
NOTE A — Basis of Preparation
The accompanying unaudited condensed consolidated financial statements of Chart Industries, Inc. and its subsidiaries (the "Company" or "Chart") have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for annual financial statements. These financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012.
Principles of Consolidation: The unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiaries. Intercompany accounts and transactions are eliminated in consolidation. Investments in affiliates where the Company's ownership is between 20 percent and 50 percent, or where the Company does not have control, but has the ability to exercise significant influence over operations or financial policy, are accounted for under the equity method.
Use of Estimates: The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.
Nature of Operations: The Company is a leading global manufacturer of standard and custom-engineered products and systems serving a wide variety of low-temperature and cryogenic applications. The Company has developed an expertise in cryogenic systems and equipment, which operate at low temperatures sometimes approaching absolute zero. The majority of the Company's products, including vacuum insulated containment vessels, heat exchangers, cold boxes and other cryogenic components, are used throughout the liquid-gas supply chain for the purification, liquefaction, distribution, storage and end-use of industrial gases and hydrocarbons. The Company has domestic operations located across the United States, including the principal executive offices located in Ohio, and an international presence in Asia, Australia and Europe.
Reclassification: Certain reclassifications have been made to the 2011 condensed consolidated statement of cash flow in order to conform to the 2012 presentation.
Cost of Sales: Manufacturing expenses associated with sales are included in cost of sales. Cost of sales include all materials, direct and indirect labor, inbound freight, purchasing and receiving, inspection, internal transfers and distribution and warehousing of inventory. In addition, shop supplies, facility maintenance costs, manufacturing engineering, project management and depreciation expense for assets used in the manufacturing process are included in cost of sales.
Selling, general and administrative costs ("SG&A"): SG&A includes selling, marketing, customer service, product management, design engineering, and other administrative costs not directly supporting the manufacturing process as well as depreciation expense associated with non-manufacturing assets. In addition, SG&A includes corporate operating expenses for executive management, accounting, tax, treasury, human resources, information technology, legal, internal audit, risk management and stock-based compensation expense.
Cash and Cash Equivalents: The Company considers all investments with an initial maturity of three months or less when purchased to be cash equivalents. The March 31, 2012 and December 31, 2011 balances include money market investments, certificates of deposit, and commercial paper. Chart Cryogenic Distribution Equipment (Changzhou) Company, Limited, a joint venture of the Company, held $988 in restricted cash on deposit to cover guarantees.
Short-Term Investments: From time to time, the Company invests in short-term, highly liquid, variable rate instruments, which have stated maturities of greater than three months but less than six months. These short term investments are recorded at cost which approximates fair value. The Company has determined that its investment securities are available and intended for use in current operations and, accordingly, classifies investment securities as

current assets. There are no short term investments at March 31, 2012 or December 31, 2011.

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CHART INDUSTRIES, INC. AND SUBSIDIARIES
Notes to Unaudited Condensed Consolidated Financial Statements – March 31, 2012
(Dollars and shares in thousands, except per share amounts) – Continued

Inventories: Inventories are stated at the lower of cost or market with cost being determined by the first-in, first-out (“FIFO”) method. The components of inventory are as follows:

	March 31, 2012	December 31, 2011
Raw materials and supplies	$69,833	$64,832
Work in process	41,093	36,045
Finished goods	56,929	48,945
	$167,855	$149,822

Revenue Recognition: For the majority of the Company’s products, revenue is recognized when products are shipped, title has transferred and collection is reasonably assured. For these products, there is also persuasive evidence of an arrangement and the selling price to the buyer is fixed or determinable. For brazed aluminum heat exchangers, cold boxes, liquefied natural gas fueling stations and engineered tanks, the Company uses the percentage of completion method of accounting. Earned revenue is based on the percentage of incurred costs to date compared to total estimated costs at completion after giving effect to the most current estimates. The cumulative impact of revisions in total cost estimates during the progress of work is reflected in the period in which these changes become known. Earned revenue reflects the original contract price adjusted for agreed upon claims and change orders, if any. Losses expected to be incurred on contracts in process, after consideration of estimated minimum recoveries from claims and change orders, are charged to operations as soon as such losses are known. Pre-contract costs relate primarily to salaries and benefits incurred to support the selling effort are expensed as incurred. Change orders resulting in additional revenue and profit are recognized upon approval by the customer based on the percentage of incurred costs to date compared to total estimated costs at completion. Certain contracts include incentive-fee arrangements. The incentive fees in such contracts can be based on a variety of factors but the most common are the achievement of target completion dates, target costs, and/or other performance criteria. Incentive fee revenue is not recognized until it is earned. Timing of amounts billed on contracts varies from contract to contract and could cause a significant variation in working capital requirements. The Company reports sales net of tax assessed by qualifying governmental authorities.

Product Warranties: The Company provides product warranties with varying terms and durations for the majority of its products. The Company calculates its warranty reserve by considering historical warranty experience and specifically identified warranty issues. The Company records warranty expense in cost of sales. The changes in the Company’s consolidated warranty reserve during the three months ended March 31, 2012 and 2011 are as follows:

	Three Months Ended March 31, 2012	2011
Beginning balance	$13,181	$13,372
Warranty expense	989	2,171
Warranty usage	(1,973)	(1,982)
Ending balance	$12,197	$13,561

Goodwill and Other Intangible Assets: The Company does not amortize goodwill or other indefinite-lived intangible assets, but reviews them at least annually for impairment, and on an interim basis if necessary, using a measurement date of October 1st. The Company amortizes intangible assets that have finite lives over their useful lives.

With respect to goodwill, the Company assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. The reporting units are the same as our operating segments, which are also the reportable segments: Energy & Chemicals, Distribution & Storage, and BioMedical. The Company first evaluates relevant events and circumstances, such as macroeconomic conditions and the Company's overall financial performance to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill. The Company then evaluates how significant each of the identified factors could be to the fair value or carrying amount of a reporting unit and weighs these factors in totality in forming a conclusion whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the Company determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, the first and second steps of the goodwill impairment test are not necessary. Otherwise, the Company would perform the first step of the two-step goodwill impairment test. As of October 1, 2011 and based on the Company's qualitative assessment, the Company determined that it was not more likely than not that the fair value is less than the carrying amount of each reporting unit and, therefore, the two-step goodwill impairment test was not necessary.

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CHART INDUSTRIES, INC. AND SUBSIDIARIES
Notes to Unaudited Condensed Consolidated Financial Statements – March 31, 2012
(Dollars and shares in thousands, except per share amounts) – Continued

With respect to other indefinite-lived intangible assets, the Company determines the fair value of any indefinite-lived intangible assets using an income approach, compares the fair value to its carrying amount and records an impairment loss if the carrying amount exceeds its fair value. The Company uses the relief from royalty method to develop fair value estimates for trade names and trademarks. This method focuses on the level of royalty payments that the user of an intangible asset would be willing to pay for the use of the asset if it were not owned by the user. This method has been consistently applied between years. As of October 1, 2011, the Company determined that the fair values of trademarks, trade names, and in-process research and development exceeded their carrying amounts.
The following table displays the gross carrying amount and accumulated amortization for all intangible assets:

		March 31, 2012		December 31, 2011	
	Estimated Useful Life	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Finite-lived assets:					
Unpatented technology	9 years	$18,229	$(9,562)	$18,113	$(9,024)
Patents	10 years	8,978	(6,482)	9,080	(5,434)
Product names	14 years	5,674	(1,858)	5,638	(1,818)
Customer relations	13 years	130,614	(50,634)	130,488	(48,840)
		$163,495	$(68,536)	$163,319	$(65,116)
Indefinite-lived intangible assets:					
Trademarks and trade names		$39,305		$39,280	
In-process research and development		3,070		3,070	
		$42,375		$42,350	

The following table represents the changes in goodwill:

Balance as of January 1, 2012	$288,770
Foreign currency adjustments	666
Balance as of March 31, 2012	$289,436

Amortization expense for intangible assets subject to amortization was $3,070 and $3,317 for the three months ended March 31, 2012 and 2011, respectively, and is estimated to be approximately $13,300 for 2012 and an average of $10,800 for years 2013 through 2017.
Stock-based Compensation: The Company records stock-based compensation according to current accounting guidance which requires all share-based payments to employees and directors, including grants of employee stock options, to be measured at fair value on the date of grant.
During the three months ended March 31, 2012, the Company granted 104 stock options, 31 shares of restricted stock and stock unit awards and 34 performance stock units and leveraged restricted stock units. The stock options vest over a four year period. Restricted stock and stock unit awards vest over a three year period and performance stock units and leveraged restricted stock units vest at the end of three years based on the achievement of certain performance and market conditions.
During the three months ended March 31, 2012, participants in the Company's stock option plans exercised options to purchase 184 shares of the Company's common stock.
Stock-based compensation expense was $2,505 and $1,401 for the three months ended March 31, 2012 and 2011, respectively. As of March 31, 2012, the total stock-based compensation expected to be recognized over the weighted average period of approximately 2.1 years is $9,077.

Convertible Debt: The Company determines if the embedded conversion feature within the Convertible Senior Subordinated Notes (the “Convertible Notes”) is clearly and closely related to the Company’s common stock and therefore exempt from separate accounting treatment under ASC 815, “Accounting for Derivative Instruments and

Hedging Activities.” Convertible Notes exempt from derivative accounting are recognized according to ASC 470-20, “Debt with Conversion and

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Other Options" by bifurcating the principal balance into a liability component and an equity component where the fair value of the liability component is estimated by calculating the present value of its cash flows discounted at an interest rate that the Company would have received for similar debt instruments that have no conversion rights (the "straight-debt rate"), and the equity component is the residual amount, net of tax, which creates a discount on the Convertible Notes. The Company subsequently recognizes non-cash interest expense as the carrying value of the Convertible Notes is accreted back to its principal amount.

Recently Issued Accounting Pronouncements: In December 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2011-12, "Comprehensive Income – Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05 (Topic 220)." The amendments were made to allow the FASB time to consider whether there should be additional presentation and disclosure requirements for reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. All other requirements in ASU 2011-05 are not affected by this update. This ASU is effective for fiscal years beginning after December 15, 2011. The adoption of this guidance did not have a material impact on the financial statements of the Company.

In September 2011, the FASB issued ASU 2011-09, "Compensation – Retirement Benefits – Multiemployer Plans (Subtopic 715-80)." The Company has historically participated in the multiemployer plan for union employees at the Company's La Crosse, Wisconsin facility. The amendments in the ASU require the Company to provide additional separate disclosures for multiemployer pension plans and multiemployer other postretirement benefit plans. The amendments are effective for fiscal years ending after December 15, 2011 and are applied retrospectively for all prior periods presented. The adoption of this guidance did not have a material impact on the Company's financial position, results of operations or cash flows.

In September 2011, the FASB issued ASU 2011-08, "Intangibles – Goodwill and Other (Topic 350)." The amendments in the ASU permit an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a bas