WATER PIK TECHNOLOGIES INC
Form 10-Q
August 10, 2005

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2005

o	**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 1-15297

WATER PIK TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**25-1843384** (IRS Employer Identification No.)

23 Corporate Plaza, Suite 246
Newport Beach, CA 92660
(Address of principal executive offices, including zip code)

Registrant s telephone number, including area code: **(949) 719-3700**

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 ý No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2): Yes ý No o

The number of shares of Common Stock outstanding on August 5, 2005 was 12,217,657 shares.

WATER PIK TECHNOLOGIES, INC.

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PART I FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS

Water Pik Technologies, Inc.

Consolidated Balance Sheets

(In thousands, except for share and per-share amounts)

	June 30, 2005 (Unaudited)	September 30, 2004
Assets		
Current assets:		
Cash and cash equivalents	$ 25,084	$ 11,036
Accounts receivable, less allowances of $1,955 at June 30, 2005 and $2,122 at September 30, 2004	66,209	51,682
Inventories	40,286	38,497
Deferred income taxes	9,036	8,736
Prepaid expenses and other current assets	3,309	2,580
Assets of discontinued operations		25,646
Total current assets	143,924	138,177
Property, plant and equipment, net	36,286	40,333
Goodwill, net	28,924	28,572
Deferred income taxes		225
Other assets, net	4,825	3,893
Total assets	$ 213,959	$ 211,200
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 23,561	$ 24,027
Accrued income taxes	1,756	27
Accrued liabilities	29,048	30,443
Current portion of long-term debt	749	3,838
Liabilities of discontinued operations		4,883
Total current liabilities	55,114	63,218
Long-term debt, less current portion	14,937	20,839
Other accrued liabilities	6,149	4,603
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $0.01 par value: 5,000,000 shares authorized; none issued		
Common stock, $0.01 par value: 50,000,000 shares authorized; 12,203,575 and 12,282,527 shares issued and outstanding at June 30, 2005 and September 30, 2004, respectively	128	128
Additional paid-in capital	82,846	82,625
Equity adjustments due to stock plans	(135)	(996)
	(7,380)	(7,130)

Treasury stock at cost, 708,738 and 541,343 shares at June 30, 2005 and September 30, 2004, respectively				
Retained earnings		59,381		45,474
Accumulated comprehensive income		2,919		2,439
Total stockholders equity		137,759		122,540
Total liabilities and stockholders equity	$	213,959	$	211,200

See accompanying notes

Water Pik Technologies, Inc.

Consolidated Statements of Operations

(In thousands, except for share and per share amounts)

(Unaudited)

	Three Months Ended June 30, 2005	Three Months Ended June 30, 2004	Nine Months Ended June 30, 2005	Nine Months Ended June 30, 2004
Sales	$ 93,270	$ 80,952	$ 231,323	$ 225,467
Cost and expenses:				
Cost of sales	64,159	56,963	160,122	158,416
Selling expenses	10,864	10,437	30,764	32,134
General and administrative expenses	7,985	5,616	19,036	17,024
Research and development expenses	1,282	1,414	3,998	4,526
	84,290	74,430	213,920	212,100
Operating income	8,980	6,522	17,403	13,367
Interest expense	418	348	1,309	1,352
Other income	(241)	(90)	(545)	(226)
Income from continuing operations before income taxes	8,803	6,264	16,639	12,241
Income tax provision	3,495	2,412	6,605	4,434
Income from continuing operations	5,308	3,852	10,034	7,807
Discontinued operations:				
Income (loss) from operations of discontinued product line	429	(309)	2,540	1,624
Income tax provision (benefit)	145	(243)	865	555
Gain on sale of discontinued operations, net of tax of $1,238	2,198		2,198	
Income (loss) on discontinued operations	2,482	(66)	3,873	1,069
Net income	$ 7,790	$ 3,786	$ 13,907	$ 8,876
Basic net income (loss) per common share				
Continuing operations	$ 0.44	$ 0.33	$ 0.83	$ 0.65
Discontinued operations	0.21	(0.01)	0.32	0.09
Net income	$ 0.65	$ 0.32	$ 1.16	$ 0.74
Diluted net income (loss) per common share				
Continuing operations	$ 0.42	$ 0.31	$ 0.79	$ 0.62
Discontinued operations	0.19	(0.01)	0.31	0.08
Net income	$ 0.61	$ 0.30	$ 1.10	$ 0.71
Shares used in per share calculation basic	12,063,000	11,851,000	12,019,000	11,933,000
Shares used in per share calculation diluted	12,765,000	12,592,000	12,689,000	12,585,000

Water Pik Technologies, Inc.

Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Nine Months Ended June 30, 2005	Nine Months Ended June 30, 2004
Operating activities:		
Net income	$ 13,907	$ 8,876
Income from discontinued operations	(3,873)	(1,069)
Income from continuing operations	10,034	7,807
Adjustments to reconcile income from continuing operations to net cash provided by operating activities:		
Depreciation and amortization	6,480	7,001
Deferred income taxes	793	(81)
Tax benefit of pre-spin-off foreign tax losses		18
Compensation expense arising from stock awards	508	682
Tax benefit from restricted stock awards	129	547
Interest income from stockholder notes		(142)
Loss on sale of property, plant and equipment	60	29
Change in operating assets and liabilities, net of effects of business acquisitions and dispositions:		
Accounts receivable	(14,580)	(14,127)
Inventories	(1,552)	7,859
Accounts payable	(552)	1,812
Accrued liabilities	(1,420)	3,398
Accrued income taxes	845	(673)
Other assets and liabilities	(1,089)	(1,731)
Cash (used in) provided by operating activities	(344)	12,399
Investing activities:		
Purchase of business net of cash acquired		(10,128)
Purchases of property, plant and equipment	(2,619)	(4,026)
Disposals of property, plant and equipment	92	11
Proceeds from sale of discontinued operations	24,300	
Cash provided by (used in) investing activities	21,773	(14,143)
Financing activities:		
Net borrowings on revolving credit facilities	(4)	1,243
Principal payments on promissory notes	(8,972)	(2,850)
Proceeds from exercise of stock options	399	2,273
Acquisition of treasury stock	(250)	
Principal payment on capital leases	(15)	(10)
Cash (used in) provided by financing activities	(8,842)	656
Effect of exchange rate changes on cash	181	(150)
Cash provided by discontinued operations	1,280	622
Increase (decrease) in cash	14,048	(616)

Cash and cash equivalents at beginning of period		11,036		3,888
Cash and cash equivalents at end of period	$	25,084	$	3,272

See accompanying notes

Water Pik Technologies, Inc.

Notes to Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation

DESCRIPTION OF BUSINESS

In accordance with the Securities and Exchange Commission s Plain English guidelines, this Quarterly Report on Form 10-Q has been written in the first person. In this document, the words we , our , and us refer to Water Pik Technologies, Inc. and not any other person.

We are a leader in designing, manufacturing and marketing a broad range of well-recognized swimming pool and personal healthcare products. We operate in two business segments: the Pool Products segment and the Personal Health Care segment. The Pool Products segment designs, manufactures and markets swimming pool and spa heaters, heat pumps, electronic controls, valves, pumps, filters, automatic salt chlorine generators, titanium heat exchangers, water features, and accessories. Our pool products are sold through contractors and wholesale distributors. The Personal Health Care segment designs, manufactures and markets personal healthcare products including showerheads, consumer and professional oral health products and water filtration products. Our personal healthcare products are sold through a variety of channels, including home centers, mass-merchandisers, drug store chains and specialty retailers.

On June 6, 2005, we entered into an asset purchase agreement to sell substantially all of the assets and liabilities of our Laars® Heating Systems business (Heating Systems), a component of our former Pool Products and Heating Systems segment, to Bradford White Corporation (BWC). See Note 11, Discontinued Operations . The sale was completed on June 30, 2005. As a result, we have restated our financial statements for all periods presented in this report to reflect the discontinued operations. All discussions and amounts in this report for all years and periods presented relate to continuing operations only unless otherwise noted.

FISCAL YEAR

In January 2004, we changed our fiscal year end from the Sunday nearest December 31 to the Sunday nearest September 30. As a result of this change, we reported a nine-month transition period ended September 30, 2004. We operate on a 52- or 53- week fiscal year with fiscal quarters ending on the Sunday nearest to the end of the applicable thirteen-week period. The fiscal quarter and year-to-date periods presented in our consolidated financial statements are presented as of the last day of the calendar quarter for convenience. This Form 10-Q is for the three month period ended July 3, 2005, but for presentation purposes, is described as the three month period ended June 30, 2005.

SEASONALITY

Our business is highly seasonal, with operating results varying from quarter to quarter. The Personal Health Care segment has generally experienced higher sales in the quarter ending in December of each fiscal year due to stronger retail demand during the holiday season. The Pool Products segment has historically experienced higher sales in the quarter ending in June of each fiscal year as customers purchase products in anticipation of the warm spring and summer months during which the level of new pool construction increases. As a result of the seasonality of sales, the Pool Products segment offers incentive programs and extended payment terms to encourage pool product customers to purchase products from September through December, as is consistent with industry practice. The extended payment term receivables are collected during the spring and summer months, which creates a seasonal peak in working capital and borrowing levels during the winter months. Variations in operating results can also occur due to short-term trends such as changes in the economic environment, consumer spending, product sourcing arrangements and weather patterns.

UNAUDITED INTERIM FINANCIAL INFORMATION

Our consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States 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 accounting principles generally accepted in the United States for complete financial statements. In management s opinion, all adjustments, consisting primarily of normal recurring accruals, considered necessary for a fair presentation have been included. Certain prior year amounts have been reclassified to conform to the current year financial statement presentation. These reclassifications had no effect on reported results of operations or stockholders equity. The information included in this Form 10-Q should be read in conjunction with our Transition Report on Form 10-KT, as amended, for the transition period from January 1, 2004 through September 30, 2004, including information regarding our critical accounting policies and estimates. Operating results for the interim periods presented are not necessarily indicative of the results to be expected for the twelve months ending September 30, 2005.

RECENT ACCOUNTING PRONOUNCEMENTS

In May 2005, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 154, Accounting Changes and Error Corrections, which, under most circumstances, requires retrospective application of a change in accounting principle. SFAS No. 154 also requires the restatement of previously issued financial statements when reporting the correction of an error. SFAS No. 154 is effective for fiscal years beginning after December 15, 2005. We do not believe the adoption will have a material impact on our financial statements.

In December 2004, the FASB finalized SFAS No. 123R, Share-Based Payment, which requires companies to measure and recognize compensation costs for all share-based payments (including employee stock options) at fair value, effective for interim or annual periods beginning after June 15, 2005. On April 15, 2005, the U.S. Securities and Exchange Commision (the SEC) announced a deferral of the effective date of SFAS No. 123R until the first interim or annual reporting period of the first fiscal year beginning on or after June 15, 2005. We expect to adopt SFAS No. 123R for the quarter ending December 31, 2005. The impact of adoption of SFAS No. 123R cannot be predicted at this time because it will depend on levels of share-based payments granted in the future. However, had we adopted SFAS No. 123R in prior periods, the impact on our results of operations would have been similar to the amounts reported historically in our footnotes under the pro forma disclosure provisions of SFAS No. 123, Accounting for Stock-Based Compensation .

In December 2004, the FASB issued FASB Staff Position No. 109-1, Application of FASB Statement No. 109 (SFAS 109), Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004 (FSP 109-1). FSP 109-1 clarifies that the manufacturer s deduction provided for under the American Jobs Creation Act of 2004 (the Act) should be accounted for as a special deduction in accordance with SFAS 109 and not as a tax rate reduction. The adoption of FSP 109-1 will have no impact on our results of operations or financial position for fiscal year 2005, as the manufacturer s deduction is not available to us until fiscal year 2006. We are currently evaluating the effect that the manufacturer s deduction will have in subsequent years.

In December 2004, the FASB also issued FASB Staff Position No. 109-2, Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004 (FSP 109-2). The Act introduces a special one-time dividends received deduction on the repatriation of certain foreign earnings to a U.S. taxpayer (repatriation provision), provided certain criteria are met. FSP 109-2, which was effective for the quarter ended December 2004, provides accounting and disclosure guidance for the repatriation provision. We are currently evaluating our alternatives under the provision of the Act, which had no impact on our consolidated results of operations or financial position for the periods presented.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs, an amendment of ARB No. 43, Chapter 4. SFAS 151 clarifies that abnormal inventory costs such as costs of idle facilities, excess freight and handling costs, and wasted materials (spoilage) are required to be recognized as current period charges. The provisions of SFAS 151 are effective for the fiscal year beginning after June 15, 2005. We are currently evaluating the impact that this statement will have on our financial statements.

2. Inventories

We value our inventory at the lower of its cost to purchase or manufacture (last-in, first-out (LIFO) and first-in, first-out (FIFO) cost methods) or its current estimated market value. Inventories consist of the following:

	June 30, 2005	September 30, 2004
	(In thousands)	
Raw materials and supplies	$ 15,507	$ 12,184

Work-in-process		2,774		2,681
Finished goods		26,904		28,168
Total inventories at current cost		45,185		43,033
Less: Allowances to reduce current cost values to LIFO basis		(4,899)		(4,536)
Total inventories	$	40,286	$	38,497

Inventories determined using the LIFO cost method were $33,306,000 at June 30, 2005 and $31,096,000 at September 30, 2004, net of LIFO reserves. The remainder of our inventories were determined using the FIFO cost method.

3. Acquisition

On January 20, 2004, as part of our strategic objective to accelerate sales and profit growth in our pool business through development of a more comprehensive package of pool equipment and accessories, we acquired from Finchem USA, Inc. (Finnchem) substantially all of the assets of Huron Tech Systems, a Jacksonville, Florida manufacturer of automatic salt chlorine generators, used for swimming pool and spa water sanitation, and titanium heat exchangers, a component used in premium heat pumps. The purchase price after adjustments totaled $10,128,000 (consisting of $10,000,000 in cash and $128,000 in direct acquisition costs). The final allocation of the purchase price resulted in $9,127,000 of goodwill, $100,000 of identifiable intangible assets with estimated three- to five-year lives, $1,494,000 of current assets (primarily accounts receivable and inventory), $120,000 in property, plant and equipment and $713,000 in assumed liabilities. During the three months ended December 31, 2004, the allocation of the purchase price was adjusted to reflect additional information regarding the value of liabilities assumed and estimated contingent payments, which resulted in additional goodwill of $243,000. The goodwill was assigned to the Pool Products segment and is expected to be deductible for tax purposes. In connection with the acquisition, we entered into a component supply agreement for a period of five years with Finnchem. The results of operations of Huron Tech Systems are included in our consolidated results of operations beginning January 20, 2004.

4. Long-Term Debt

Long-term debt is comprised of the following:

	June 30, 2005	September 30, 2004
	(In thousands)	
Revolving credit facility	$ 56	$ 60
Mortgage notes payable	15,590	18,119
Promissory notes payable equipment financing agreement		6,443
Other	40	55
	15,686	24,677
Less: Current portion	(749)	(3,838)
Long-term debt	$ 14,937	$ 20,839

In June 2005, in connection with the sale of Heating Systems, we paid off the balance outstanding under the equipment financing agreement, which totaled $5,035,000, including accrued interest and prepayment costs of $55,000 and $16,000, respectively. In addition, we paid off the mortgage note payable of $1,925,000, including accrued interest, related to the Heating Systems manufacturing facility in Rochester, New Hampshire.

We utilized interest rate swap agreements as cash flow hedges to lock in the interest rate on borrowings and achieve a desired proportion of variable versus fixed-rate debt. At September 30, 2004, the aggregate notional amount of the swaps was $4,630,000, these interest rate swap agreements were due to expire on January 1, 2007. On a pre-tax basis, the changes in their fair values resulted in a gain of $25,000 and no gain or loss for the three months and nine months ended June 30, 2005, respectively, and gains of $119,000 and $193,000 for the three months and nine months ended June 30, 2004, respectively, which have been recognized in accumulated comprehensive income within stockholders equity. In June 2005, in connection with the repayment of the promissory notes under the equipment financing agreement, we paid $35,000 to terminate the two interest rate swap agreements.

Our revolving credit facility and our real estate loan agreement and related mortgage notes require us to be in compliance with specific financial and non-financial covenants and restrictions relating to indebtedness, liens, investments, dividends, fixed charge coverage, capital expenditures and the relationship of our total consolidated indebtedness to EBITDA (earnings before interest, income taxes, depreciation and amortization). We were in compliance with these covenants at June 30, 2005.

5. Stock Based Compensation

We account for stock-based employee compensation arrangements in accordance with the provisions of Accounting Principles Board (APB) No. 25, Accounting for Stock Issued to Employees, and comply with disclosure provisions of SFAS No. 123. If we had elected to recognize compensation cost for stock options based on their fair value at the grant dates, consistent with the method prescribed by SFAS No. 123, net income and net income per share, for the three months and nine months ended June 30, 2005 and 2004 would have been as follows:

	Three Months Ended June 30, 2005		Three Months Ended June 30, 2004		Nine Months Ended June 30, 2005		Nine Months Ended June 30, 2004
	(In thousands, except per share amounts)				(In thousands, except per share amounts)		
Net income, as reported	$	7,790	$	3,786	$	13,907	$	8,876
Stock-based compensation expense included in reported net income, net of tax		86		132		270		443
Total stock-based compensation expense determined under the fair value based method for all awards, net of tax		(378)		(374)		(1,138)		(996)
Pro forma net income	$	7,498	$	3,544	$	13,039	$	8,323
Basic net income per common share:								
As reported	$	0.65	$	0.32	$	1.16	$	0.74
Pro forma	$	0.62	$	0.30	$	1.08	$	0.70
Diluted net income per common share:								
As reported	$	0.61	$	0.30	$	1.10	$	0.71
Pro forma	$	0.59	$	0.28	$	1.03	$	0.66

For purposes of pro forma disclosure, the estimated fair value of the options is amortized ratably over the options vesting period.

Under SFAS No. 123, the fair value of each option grant was estimated on the date of grant using the Black-Scholes option valuation model. The following weighted average assumptions were used in estimating the fair value of option grants: an expected dividend yield of zero percent, an average expected life of the options of six years, an expected volatility of 40.2 percent and a risk-free interest rate of 3.7 percent. There were 5,000 options granted in the ni