MODINE MANUFACTURING CO
Form 10-Q
November 07, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

(Mark One)

þ QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2011

or

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 1-1373

MODINE MANUFACTURING COMPANY
(Exact name of registrant as specified in its charter)

WISCONSIN (State or other jurisdiction of incorporation or organization)	39-0482000 (I.R.S. Employer Identification No.)
1500 DeKoven Avenue, Racine, Wisconsin (Address of principal executive offices)	53403 (Zip Code)

Registrant's telephone number, including area code (262) 636-1200

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 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 þ No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

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 definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer o	Accelerated Filer þ
Non-accelerated Filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

The number of shares outstanding of the registrant's common stock, $0.625 par value, was 46,727,495 at October 28, 2011.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements.

MODINE MANUFACTURING COMPANY
CONSOLIDATED STATEMENTS OF OPERATIONS
For the three and six months ended September 30, 2011 and 2010
(In thousands, except per share amounts)
(Unaudited)

	Three months ended September 30		Six months ended September 30	
	2011	2010	2011	2010
Net sales	$397,290	$345,902	$815,153	$691,434
Cost of sales	335,271	290,133	683,703	576,689
Gross profit	62,019	55,769	131,450	114,745
Selling, general and administrative expenses	50,075	46,718	99,513	88,918
Income from operations	11,944	9,051	31,937	25,827
Interest expense	3,297	23,529	6,287	27,637
Other expense (income) – net	6,027	(5,610)	5,885	(2,012)
Earnings (loss) from continuing operations before income taxes	2,620	(8,868)	19,765	202
Provision for income taxes	1,995	4,822	6,024	8,866
Earnings (loss) from continuing operations	625	(13,690)	13,741	(8,664)
Earnings (loss) from discontinued operations (net of income taxes)	389	(2,900)	389	(2,932)
Loss on sale of discontinued operations (net of income taxes)	(16)	(70)	(16)	(76)
Net earnings (loss)	998	(16,660)	14,114	(11,672)
Less: Net earnings attributable to noncontrolling interest	38	-	29	-
Net earnings (loss) attributable to Modine	$960	$(16,660)	$14,085	$(11,672)
Earnings (loss) from continuing operations attributable to Modine common shareholders:				
Basic	$0.01	$(0.30)	$0.29	$(0.19)
Diluted	$0.01	$(0.30)	$0.29	$(0.19)
Net earnings (loss) attributable to Modine common shareholders:				
Basic	$0.02	$(0.36)	$0.30	$(0.25)
Diluted	$0.02	$(0.36)	$0.30	$(0.25)

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

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MODINE MANUFACTURING COMPANY
CONSOLIDATED BALANCE SHEETS
September 30, 2011 and March 31, 2011
(In thousands, except per share amounts)
(Unaudited)

	September 30, 2011	March 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$ 30,217	$ 32,930
Trade receivables, less allowance for doubtful accounts of $562 and $754	210,350	219,189
Inventories	135,214	122,629
Deferred income taxes and other current assets	58,114	52,877
Total current assets	433,895	427,625
Noncurrent assets:		
Property, plant and equipment – net	411,979	430,295
Investment in affiliates	3,655	3,863
Goodwill	29,545	31,572
Intangible assets – net	6,009	6,533
Other noncurrent assets	15,382	17,051
Total noncurrent assets	466,570	489,314
Total assets	$ 900,465	$ 916,939
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Short-term debt	$ 10,900	$ 8,825
Long-term debt – current portion	1,042	262
Accounts payable	167,324	177,549
Accrued compensation and employee benefits	51,063	63,163
Income taxes	7,578	3,739
Accrued expenses and other current liabilities	62,545	63,003
Total current liabilities	300,452	316,541
Noncurrent liabilities:		
Long-term debt	159,365	138,582
Deferred income taxes	9,719	9,988
Pensions	54,372	62,926
Postretirement benefits	6,084	5,967
Other noncurrent liabilities	16,178	19,983
Total noncurrent liabilities	245,718	237,446
Total liabilities	546,170	553,987
Commitments and contingencies (See Note 19)		
Shareholders' equity:		
Preferred stock, $0.025 par value, authorized 16,000 shares, issued - none	-	-
Common stock, $0.625 par value, authorized 80,000 shares, issued 47,310 and 47,105 shares	29,569	29,440
Additional paid-in capital	169,255	166,359
Retained earnings	217,771	203,686
Accumulated other comprehensive loss	(48,708)	(22,533)
Treasury stock at cost: 589 and 559 shares, respectively	(14,461)	(14,000)
Total Modine shareholders' equity	353,426	362,952

Noncontrolling interest		869		-
Total equity		354,295		362,952
Total liabilities and equity	$	900,465	$	916,939

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

MODINE MANUFACTURING COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the six months ended September 30, 2011 and 2010
(In thousands)
(Unaudited)

	Six months ended September 30 2011	2010
Cash flows from operating activities:		
Net earnings (loss)	$14,114	$(11,672)
Adjustments to reconcile net earnings (loss) with net cash provided by		
Depreciation and amortization	29,154	28,095
Other – net	6,876	7,115
Net changes in operating assets and liabilities,excluding dispositions	(46,988)	(39,402)
Net cash provided by (used for) operating activities	3,156	(15,864)
Cash flows from investing activities:		
Expenditures for property, plant and equipment	(32,532)	(20,199)
Proceeds from dispositions of assets	1,273	4,647
Settlement of derivative contracts	142	(183)
Other – net	379	3,746
Net cash used for investing activities	(30,738)	(11,989)
Cash flows from financing activities:		
Short-term debt – net	2,264	3,273
Borrowings of long-term debt	82,749	218,963
Repayments of long-term debt	(59,680)	(194,277)
Capital contribution by noncontrolling interest in joint venture	936	-
Book overdrafts	-	(407)
Other – net	(15)	15
Net cash provided by financing activities	26,254	27,567
Effect of exchange rate changes on cash	(1,385)	72
Net decrease in cash and cash equivalents	(2,713)	(214)
Cash and cash equivalents at beginning of period	32,930	43,657
Cash and cash equivalents at end of period	$30,217	$43,443

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

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MODINE MANUFACTURING COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except per share amounts)
(unaudited)

Note 1: General

The accompanying condensed consolidated financial statements were prepared in conformity with generally accepted accounting principles (GAAP) in the United States applied on a basis consistent with those principles used in the preparation of the annual consolidated financial statements by Modine Manufacturing Company (Modine or the Company) for the year ended March 31, 2011. The financial statements include all normal recurring adjustments that are, in the opinion of management, necessary for a fair statement of results for the interim periods. Results for the first six months of fiscal 2012 are not necessarily indicative of the results to be expected for the full year.

These financial statements should be read in conjunction with the consolidated financial statements and related notes in Modine's Annual Report on Form 10-K for the year ended March 31, 2011.

Note 2: Significant Accounting Policies and Change in Accounting Principles

Restricted cash: At September 30, 2011 and March 31, 2011, the Company had long-term restricted cash of $4,173 and $4,682, respectively, included in other noncurrent assets, consisting of $1,823 and $2,332, respectively, to secure long-term employee compensation arrangements for certain employees in Europe and $2,350 to collateralize insurance liabilities with an insurance carrier in North America.

Joint venture: During the first quarter of fiscal 2012, the Company completed the formation of its joint venture with OneGene, Inc. to form Modine OneGene Corporation in South Korea. The Company and OneGene, Inc. made initial capital contributions of 1,000,000 Korean won ($936 U.S. equivalent) each during the first quarter of fiscal 2012. Modine is considered the primary beneficiary of the joint venture in accordance with applicable consolidation guidance. Accordingly, the results of Modine OneGene Corporation are consolidated by the Company.

Revision of prior period financial statements: As described in Note 1 and Note 26 of the Notes to Consolidated Financial Statements in Modine’s Annual Report on Form 10-K for the year ended March 31, 2011, the quarterly results for fiscal 2011 have been revised as a result of errors identified during fiscal 2011 which were not considered material individually or in the aggregate to previously issued financial statements but were considered significant to the quarters in which they were identified. For the three months ended September 30, 2010, cost of goods sold increased $1,858, selling, general and administrative expenses increased $260, provision for income taxes decreased $190 and earnings from continuing operations decreased $1,928 as a result of the revisions. For the six months ended September 30, 2010, net sales increased $363, cost of goods sold increased $1,919, gross profit decreased $1,556, selling, general and administrative expenses increased $611, provision for income taxes increased $139 and earnings from continuing operations decreased $2,306 as a result of the revisions. For the three and six months ended September 30, 2010, diluted earnings per share from continuing operations and diluted net earnings per share decreased $0.04 and $0.05, respectively, as a result of these revisions.

Out of period adjustments: During the three months ended September 30, 2011, the Company identified two items that should have been recorded in the first quarter of fiscal 2012, but were instead corrected in the second quarter of fiscal 2012. Such errors overstated fiscal 2012 first quarter net income by approximately $438, and related to (1) an understatement of foreign currency transactions gains of $197, included in other expense (income) – net; and (2) an understatement of income tax expense of $635. The adjustments were not considered material to the financial statements of either the first quarter or second quarter of fiscal 2012.

Accounting standards changes and new accounting pronouncements: In October 2009, the Financial Accounting Standards Board (FASB) issued updated guidance on revenue arrangements with multiple deliverables, which addresses the unit of accounting for multiple-deliverable arrangements and revises the method by which consideration is allocated among the units of accounting. The overall consideration is allocated to each deliverable by establishing a selling price for individual deliverables based on a hierarchy of evidence, including vendor-specific objective evidence, other third party evidence of the selling price, or the reporting entity's best estimate of the selling price of individual deliverables in the arrangement. This guidance was effective for the Company on a prospective basis on April 1, 2011. The adoption of this guidance did not have a material impact on the consolidated financial statements.

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(In thousands, except per share amounts)
(unaudited)

In June 2011, the FASB issued an amendment to the accounting guidance for the presentation of comprehensive income. This amendment removes one of the three presentation options for presenting the components of other comprehensive income as part of the statement of changes in shareholders' equity and requires either a single continuous statement of net income and other comprehensive income or a two consecutive statement approach. This amendment shall be applied retrospectively and is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. The Company is currently evaluating the impact of this amendment.

In September 2011, the FASB issued an amendment to the accounting guidance for testing goodwill for impairment. The amendment provides an option for companies to first use a qualitative approach to test goodwill for impairment if certain conditions are met. If it is determined to be more likely than not that the fair value of the reporting unit is less than its carrying amount, entities must perform the quantitative analysis of the goodwill impairment test. The amendments are effective for goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The Company is assessing this new guidance and currently does not anticipate a material impact on the consolidated financial statements.

Note 3: Employee Benefit Plans

During the three months ended September 30, 2011 and 2010, the Company recorded compensation expense of $655 and $739, respectively, related to its defined contribution employee benefit plans. During the six months ended September 30, 2011 and 2010, the Company recorded compensation expense of $1,885 and $2,008, respectively, related to its defined contribution employee benefit plans.

During the three months ended September 30, 2011 and 2010, the Company elected to contribute $2,150 and $1,649, respectively, to its U.S. pension plans. During the six months ended September 30, 2011 and 2010, the Company elected to contribute $7,200 and $12,099, respectively, to its U.S. pension plans.

Costs for Modine's pension and postretirement benefit plans for the three and six months ended September 30, 2011 and 2010 include the following components:

	Three months ended September 30				Six months ended September 30			
	Pension		Postretirement		Pension		Postretirement	
	2011	2010	2011	2010	2011	2010	2011	2010
Service cost	$ 425	$ 341	$ 9	$ (3)	$ 851	$ 950	$ 21	$ 22
Interest cost	3,502	3,449	89	55	7,007	6,883	173	168
Expected return on plan assets	(3,848)	(3,944)	-	-	(7,696)	(7,612)	-	-
Amortization of:								
Unrecognized net loss (gain)	1,995	1,811	-	(78)	3,990	3,834	(12)	(56)
Unrecognized prior service cost (credit)	-	89	(416)	(298)	-	178	(831)	(890)
	-	15	-	-	-	15	-	-

Adjustment for settlement								
Curtailment gain	-	-	-	(348)	-	-	-	(2,075)
Net periodic benefit cost (income)	$ 2,074	$ 1,761	$ (318)	$ (672)	$ 4,152	$ 4,248	$ (649)	$ (2,831)

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MODINE MANUFACTURING COMPANY
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Note 4: Stock-Based Compensation

Stock-based compensation consists of stock options, restricted stock granted for retention and performance and discretionary unrestricted stock. Compensation cost is calculated based on the fair value of the instrument at the time of grant, and is recognized as expense over the vesting period of the stock-based instrument. Modine recognized stock-based compensation cost of $1,738 and $944 for the three months ended September 30, 2011 and 2010, respectively. Modine recognized stock-based compensation costs of $2,578 and $2,516 for the six months ended September 30, 2011 and 2010, respectively. The performance component of awards granted under the long-term incentive plan during the second quarter of fiscal 2012 is based on a target return on average capital employed (ROACE) and a target improvement in economic profit at the end of the three year performance period. The Company currently considers the attainment of these performance targets to be probable. ROACE is defined as net earnings, adding back after-tax interest expense and adjusted to exclude unusual, non-recurring or extraordinary non-cash charges and cash restructuring and repositioning charges in excess of $4,000; divided by the average total debt plus shareholders' equity. Economic profit is defined as ROACE minus a fixed weighted average cost of capital, multiplied by total debt plus shareholders' equity.

The following tables present, by type, the fair market value of stock-based compensation awards granted during the three and six months ended September 30, 2011 and 2010:

	Three months ended September 30,			
	2011		2010	
Type of award	Shares	Fair Value Per Award	Shares	Fair Value Per Award
Common stock options	112.9	$10.45	-	$-
Unrestricted common stock	27.9	$14.93	40.8	$8.91
Restricted common stock - retention	63.2	$14.93	-	$-
Restricted common stock - performance based	189.5	$14.93	-	$-

	Six months ended September 30,			
	2011		2010	
Type of award	Shares	Fair Value Per Award	Shares	Fair Value Per Award
Common stock options	112.9	$10.45	303.4	$5.96
Unrestricted common stock	27.9	$14.93	60.3	$8.43
Restricted common stock - retention	63.2	$14.93	97.2	$9.26
Restricted common stock - performance based	189.5	$14.93	291.6	$9.26

The accompanying table sets forth the assumptions used in determining the fair value for the options:

	Six months ended September 30,	
	2011	2010
Expected life of awards in years	6.3	6.3
Risk-free interest rate	1.93 %	2.36 %

Expected volatility of the Company's stock	79.56	%	77.99	%
Expected dividend yield on the Company's stock	0.00	%	0.00	%
Expected forfeiture rate	2.50	%	2.50	%

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As of September 30, 2011, the total remaining unrecognized compensation cost related to the non-vested stock-based compensation awards, which will be amortized over the weighted average remaining service periods, is as follows:

Type of award	Unrecognized Compenstion Costs	Weighted Average Remaining Service Period in Years
Common stock options	$ 1,674	2.1
Restricted common stock - retention	1,666	3.0
Restricted common stock - performance	3,990	2.1
Total	$ 7,330	2.4

Note 5: Other Income (Expense) – Net

Other income (expense) – net was comprised of the following:

	Three months ended September 30		Six months ended September 30	
	2011	2010	2011	2010
Equity in (loss) earnings of non-consolidated affiliates	$(13)	$26	$(415)	$225
Interest income	206	151	386	321
Foreign currency transactions	(6,216)	5,411	(5,866)	1,394
Other non-operating (expense) income - net	(4)	22	10	72
Total other (expense) income - net	$(6,027)	$5,610	$(5,885)	$2,012

Foreign currency transactions for the three and six months ended September 30, 2011 and 2010 were primarily comprised of foreign currency transaction (losses) gains on inter-company loans and other transactions denominated in a foreign currency.

Note 6: Income Taxes

For the three months ended September 30, 2011 and 2010, the Company’s effective income tax rate attributable to earnings (loss) from continuing operations before income taxes was 76.1 percent and 54.4 percent, respectively.

For the six months ended September 30, 2011 and 2010, the Company’s effective tax rate attributable to earnings (loss) from continuing operations before income taxes was 30.5 percent and 4,389.1 percent, respectively.

The most significant factors impacting changes in the effective tax rate for the three and six months ended September 30, 2011 as compared to prior periods were changes in the valuation allowance for certain foreign losses for which no benefit is recognized and the changing mix of foreign and domestic earnings. During the three months ended September 30, 2011, the Company continued to record a full valuation allowance against its net deferred tax assets located in the U.S. and certain foreign jurisdictions as it is more likely than not that these assets will not be realized based on historical performance. One of the Company's Chinese subsidiaries currently has a $687 valuation allowance against its net deferred tax assets as a result of its cumulative loss position; however, it is possible that the valuation allowance may be released later this fiscal year as the subsidiary becomes profitable.

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(In thousands, except per share amounts)
(unaudited)

Accounting policies for interim reporting require the Company to adjust its effective tax rate each quarter to be consistent with the estimated annual effective tax rate. Under this effective tax rate methodology, the Company applies an estimated annual income tax rate to its year-to-date ordinary earnings to derive its income tax provision each quarter. The tax impact of certain significant, unusual or infrequently occurring items must be recorded in the interim period in which they occur. For the six months ended September 30, 2011, the U.S. taxing jurisdiction had year-to-date pre-tax earnings and is also forecasting pre-tax earnings for the full fiscal year. As a result, the U.S. taxing jurisdiction is no longer considered on a discrete basis but is included in the overall annual effective tax rate methodology. The impact of the Company’s operations in Germany, Austria and certain other foreign locations are excluded from the overall effective tax rate methodology and recorded discretely based upon year-to-date results as these operations anticipate net operating losses for the year for which no tax benefit can be recognized. The income taxes for the Company’s other foreign operations continue to be estimated under the overall effective tax rate methodology.

During fiscal 2005, a German lower court ruling disallowed certain deductions for trade tax purposes. Based on this ruling, the Company established an uncertain tax position contingency for additional trade tax liability and interest. During the three months ended September 30, 2011, the German Supreme Court affirmed the lower court finding. As a result, the uncertain tax position established was reversed and amended tax returns for the fiscal years 2005 through 2010 are being filed resulting in an income tax payable for taxes and interest owed of $2,724. During the three and six months ended September 30, 201