

CAMBIUM LEARNING GROUP, INC.

Form 10-Q

May 11, 2012

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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: 001-34575

Cambium Learning Group, Inc.

(Exact name of registrant as specified in its charter)

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Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

27-0587428
(I.R.S. Employer
Identification No.)

17855 North Dallas Parkway,

Suite 400, Dallas, Texas
(Address of Principal Executive Offices)

75287
(Zip Code)

Registrant's telephone number, including area code: (214) 932-9500

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 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 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 definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

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

The number of shares of the registrant's common stock, \$0.001 par value per share, outstanding as of April 30, 2012 was 49,563,824.

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Cambium Learning Group, Inc. and Subsidiaries

Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)

(In thousands, except per share data)

(Unaudited)

	Three Months Ended	
	March 31,	March 31,
	2012	2011
Net revenues	\$ 27,855	\$ 30,695
Cost of revenues:		
Cost of revenues	11,166	10,967
Amortization expense	6,370	6,618
Total cost of revenues	17,536	17,585
Research and development expense	3,332	2,379
Sales and marketing expense	11,896	10,903
General and administrative expense	5,745	5,812
Shipping and handling costs	327	334
Depreciation and amortization expense	1,659	1,736
Embezzlement and related expense (recoveries)	(85)	(2,436)
Impairment of long-lived assets	2,791	
Total costs and expenses	43,201	36,313
Loss before interest, other income and income taxes	(15,346)	(5,618)
Net interest expense	(4,777)	(4,405)
Other income, net	36	363
Loss before income taxes	(20,087)	(9,660)
Income tax expense	(177)	(97)
Net loss	\$ (20,264)	\$ (9,757)
Other comprehensive income (loss):		
Amortization of net pension loss	9	
Comprehensive income (loss)	\$ (20,255)	\$ (9,757)
Net loss per common share:		
Basic net loss per common share	\$ (0.41)	\$ (0.22)
Diluted net loss per common share	\$ (0.41)	\$ (0.22)
Average number of common shares and equivalents outstanding:		
Basic	49,947	44,353
Diluted	49,947	44,353

The accompanying Notes to the Condensed Consolidated Financial Statements are an integral part of these statements.

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Cambium Learning Group, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(In thousands, except per share data)

	March 31, 2012 (unaudited)	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 41,768	\$ 63,191
Accounts receivable, net	10,649	13,485
Inventory	22,081	21,561
Deferred tax assets	2,800	2,829
Restricted assets, current	1,387	1,393
Assets held for sale	2,727	2,727
Other current assets	4,623	4,735
Total current assets	86,035	109,921
Property, equipment and software at cost	42,425	42,878
Accumulated depreciation and amortization	(14,531)	(12,968)
Property, equipment and software, net	27,894	29,910
Goodwill	114,297	114,297
Acquired curriculum and technology intangibles, net	24,653	26,996
Acquired publishing rights, net	24,544	26,861
Other intangible assets, net	17,246	18,111
Pre-publication costs, net	10,466	10,034
Restricted assets, less current portion	10,716	11,082
Other assets	22,142	22,468
Total assets	\$ 337,993	\$ 369,680

The accompanying Notes to the Condensed Consolidated Financial Statements are an integral part of these statements.

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Cambium Learning Group, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(In thousands, except per share data)

	March 31, 2012 (unaudited)	December 31, 2011
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Current portion of capital lease obligations	\$ 821	\$ 826
Accounts payable	4,304	3,024
Accrued expenses	15,887	21,203
Deferred revenue, current	32,216	38,984
Total current liabilities	53,228	64,037
Long-term liabilities:		
Long-term debt	174,206	174,165
Capital lease obligations, less current portion	11,903	12,294
Deferred revenue, less current portion	3,991	4,304
Contingent value rights	6,737	6,684
Other liabilities	17,813	18,126
Total long-term liabilities	214,650	215,573
Commitments and contingencies (See Note 13)		
Stockholders' equity:		
Preferred stock (\$.001 par value, 15,000 shares authorized, zero shares issued and outstanding at March 31, 2012 and December 31, 2011)		
Common stock (\$.001 par value, 150,000 shares authorized, 51,208 and 51,162 shares issued, and 49,564 and 49,518 shares outstanding at March 31, 2012 and December 31, 2011, respectively)	51	51
Capital surplus	281,540	281,240
Accumulated deficit	(204,923)	(184,659)
Treasury stock at cost (1,644 shares at March 31, 2012 and December 31, 2011)	(4,931)	(4,931)
Other comprehensive income (loss):		
Pension and postretirement plans	(1,623)	(1,632)
Net unrealized gain on securities	1	1
Accumulated other comprehensive income (loss)	(1,622)	(1,631)
Total stockholders' equity	70,115	90,070
Total liabilities and stockholders' equity	\$ 337,993	\$ 369,680

The accompanying Notes to the Condensed Consolidated Financial Statements are an integral part of these statements.

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Cambium Learning Group, Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Three Months Ended	
	March 31,	March 31,
	2012	2011
	(unaudited)	
Operating activities:		
Net loss	\$ (20,264)	\$ (9,757)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization expense	8,029	8,354
Gain from recovery of property held for sale		(2,649)
Amortization of note discount and deferred financing costs	435	203
Impairment of long-lived assets	2,791	
Change in fair value of contingent value rights obligation	53	308
Loss on disposal of assets	81	
Stock-based compensation and expense	225	290
Changes in operating assets and liabilities:		
Accounts receivable, net	2,836	17,505
Inventory	(520)	(4,450)
Other current assets	112	(867)
Other assets	(68)	189
Restricted assets	372	1,177
Accounts payable	1,280	(1,742)
Accrued expenses	(5,316)	(4,727)
Deferred revenue	(7,081)	(6,777)
Other long-term liabilities	(200)	(501)
Net cash used in operating activities	(17,235)	(3,444)
Investing activities:		
Expenditures for property, equipment, software and pre-publication costs	(3,792)	(3,354)
Net cash used in investing activities	(3,792)	(3,354)
Financing activities:		
Proceeds from debt		174,024
Repayment of debt		(152,130)
Deferred financing costs		(7,340)
Principal payments under capital lease obligations	(396)	(93)
Borrowings under revolving credit agreement		10,000
Payment of revolving credit facility		(10,000)
Net cash (used in) provided by financing activities	(396)	14,461
Increase (decrease) in cash and cash equivalents	(21,423)	7,663
Cash and cash equivalents, beginning of period	63,191	11,831
Cash and cash equivalents, end of period	\$ 41,768	\$ 19,494

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The accompanying Notes to the Condensed Consolidated Financial Statements are an integral part of these statements.

Table of Contents**Cambium Learning Group, Inc. and Subsidiaries****Notes to the Condensed Consolidated Financial Statements****(Unaudited)****Note 1 Basis of Presentation**

Presentation. The Condensed Consolidated Financial Statements include the accounts of Cambium Learning Group, Inc. and subsidiaries (the Company) and are unaudited. The condensed balance sheet as of December 31, 2011 has been derived from audited financial statements. All intercompany transactions are eliminated.

As permitted under the Securities and Exchange Commission (SEC) requirements for interim reporting, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been omitted. The Company believes that these financial statements include all necessary and recurring adjustments for the fair presentation of the interim period results. These financial statements should be read in conjunction with the Consolidated Financial Statements and related notes included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2011. Due to seasonality, the results of operations for the three months ended March 31, 2012 are not necessarily indicative of the results to be expected for the year ending December 31, 2012.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Subsequent actual results may differ from those estimates.

Nature of Operations. The Company operates as three reportable business segments with separate management teams and infrastructures: Voyager Learning, a comprehensive intervention business; Sopris Learning, a supplemental solutions education business; and Cambium Learning Technologies, a technology-based education business.

Note 2 Accounts Receivable

Accounts receivable are stated net of allowances for doubtful accounts and estimated sales returns. The allowance for doubtful accounts and estimated sales returns totaled \$0.7 million at March 31, 2012, compared to \$0.9 million at December 31, 2011. The allowance for doubtful accounts is based on a review of the outstanding balances and historical collection experience. The reserve for sales returns is based on historical rates of return as well as other factors that in the Company s judgment could reasonably be expected to cause sales returns to differ from historical experience.

Note 3 Stock-Based Compensation and Expense

The total amount of pre-tax expense for stock-based compensation recognized in the three months ended March 31, 2012 and 2011 was \$0.2 million and \$0.3 million, respectively. The stock-based compensation expense recorded was allocated as follows:

<i>(in thousands)</i>	Three Months Ended March 31,	
	2012	2011
Cost of revenues	\$ 12	\$ 15
Research and development expense	30	32
Sales and marketing expense	30	38
General and administrative expense	153	205
Total	\$ 225	\$ 290

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On February 8, 2012, the Company granted 195,000 options under the Cambium Learning Group, Inc. 2009 Equity Incentive Plan (the Plan) with a total grant date fair value, net of forecasted forfeitures, of \$0.1 million. These options have a per-share exercise price equal to \$4.50 and vest equally over a four year service period. The term of the options is ten years from the date of grant. The following assumptions were used in the Black-Scholes option-pricing model to estimate the fair value of these awards:

	Three Months Ended March 31,	
	2012	2011
Expected stock volatility	35.00%	35.00%
Risk-free interest rate	1.17%	2.50%
Expected years until exercise	6.25	6.25
Dividend yield	0.00%	0.00%

Due to a lack of exercise history or other means to reasonably estimate future exercise behavior, the Company used the simplified method as described in applicable accounting guidance for stock-based compensation to estimate the expected years until exercise on new awards.

During the quarter ended March 31, 2012, 105,258 of the options granted on January 27, 2010 and 12,239 of the options granted on February 1, 2011 were forfeited.

Restricted common stock awards of 46,295 shares were issued during the quarter ended March 31, 2012, in connection with the Company's Board of Directors compensation program. The restrictions on the common stock awards will lapse on the one-year anniversary of the grant date or upon a change in control of the Company. These awards were valued based on the Company's closing stock price on the date of grant, February 8, 2012.

During the quarter ended March 31, 2012, the related restrictions lapsed on restricted common stock awards of 36,084 shares.

Note 4 Net Loss per Common Share

Basic net loss per common share is computed by dividing net loss by the weighted-average number of common shares outstanding during the period. Diluted net loss per common share is computed by dividing net loss by the weighted-average number of common shares outstanding during the period, including the potential dilution that could occur if all of the Company's outstanding stock awards that are in-the-money were exercised, using the treasury stock method. A reconciliation of the weighted-average number of common shares and equivalents outstanding used in the calculation of basic and diluted net loss per common share is shown in the table below for the periods indicated:

<i>(in thousands)</i>	Three Months Ended March 31,	
	2012	2011
Basic	49,947	44,353
Dilutive effect of awards		
Diluted	49,947	44,353
Antidilutive securities:		
Options	4,145	3,946
Warrants	187	141
Restricted Stock	59	38
Subscription rights		6,419

Note 5 Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability (exit price), in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques are based on observable or unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs have created the following fair value hierarchy:

Level 1 Quoted prices for identical instruments in active markets.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which significant value drivers are observable.

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Level 3 Valuations derived from valuation techniques in which significant value drivers are unobservable.

Applicable guidance requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

As of March 31, 2012, financial instruments include \$41.8 million of cash and cash equivalents, restricted assets of \$12.1 million, collateral investments of \$2.0 million, \$174.2 million of senior secured notes, \$0.5 million of warrants, assets held for sale of \$2.7 million, and \$6.7 million in contingent value rights (CVRs). As of December 31, 2011, financial instruments include \$63.2 million of cash and cash equivalents, restricted assets of \$12.5 million, collateral investments of \$2.0 million, \$174.2 million of senior secured notes, \$0.5 million of warrants, assets held for sale of \$2.7 million, and \$6.7 million in CVRs. The fair market values of cash equivalents and restricted assets are equal to their carrying value, as these investments are recorded based on quoted market prices and/or other market data for the same or comparable instruments and transactions as of the end of the reporting period. The fair values of the properties held for sale were determined by an independent appraisal conducted by a licensed realtor based on the values of similar properties in the area. These properties were acquired by the Company as a result of its recovery efforts in connection with the employee embezzlement matter described in Note 16.

As of March 31, 2012, the fair value of the senior secured notes was \$169.5 million based on quoted market prices in active markets for these debt instruments when traded as assets.

Assets and liabilities measured at fair value on a recurring basis are as follows:

(in thousands)

Description	As of March 31, 2012	Fair Value at Reporting Date Using			Year-to-Date Total Gains (Losses)
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Restricted Assets:					
Money Market	\$ 12,103	\$ 12,103	\$	\$	\$
Collateral Investments:					
Money Market	902	902			
Certificate of Deposit	1,066	1,066			
Warrant	493		493		75
Assets held for sale	2,727		2,727		
CVRs	6,737			6,737	(53)

(in thousands)

Description	As of December 31, 2011	Fair Value at Reporting Date Using			Year-to-Date Total Gains (Losses)
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Restricted Assets:					
Money Market	\$ 12,475	\$ 12,475	\$	\$	\$
Collateral Investments:					
Money Market	902	902			
Certificate of Deposit	1,065	1,065			
Warrant	456		456		70
Assets held for sale	2,727		2,727		
CVRs	6,684			6,684	(1,308)

The warrant was valued using the Black-Scholes pricing model. Due to the low exercise price of the warrants, the model assumptions do not significantly impact the valuation.

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In accordance with applicable accounting guidance, goodwill and other indefinite-lived intangible assets are not amortized but are instead reviewed for impairment at least annually and if a triggering event is determined to have occurred in an interim period. The Company's annual impairment testing is performed as of December 1 of each year. During the quarter ended March 31, 2012, the Company did not identify any triggering events that would have required an additional impairment analysis.

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The fair value of the liability for the CVRs is determined using a probability weighted cash flow analysis which takes into consideration the likelihood, amount and timing of cash flows of each element of the pool of assets and liabilities included in the CVR. The determination of fair value of the CVRs involves significant assumptions and estimates, which are reviewed at each quarterly reporting date. As of March 31, 2012, a fair value of \$6.7 million has been recorded as a liability for the remaining CVR payments.

During the quarter ended March 31, 2012, a loss of \$0.1 million was recorded in general and administrative expense to reflect an increase in the estimated fair value of the CVR liability. The ultimate value of the remaining CVR payments is not known at this time; however, it could range from zero to a maximum possible value of approximately \$7.4 million. Future changes in the estimate of the fair value of the CVRs will impact results of operations and could be material.

The first and second CVR payment dates were in September 2010 and June 2011, with \$1.1 million and \$2.0 million, respectively, distributed to the escrow agent at those times for distribution to holders of the CVRs. The next scheduled distribution, if any, will be made no later than April 2013 and relates to a potential tax indemnity obligation. Additionally, as described in Note 13, any amounts due to CVR holders as a result of refunds received related to the Michigan tax payment will be distributed upon the final resolution of this agreed contingency.

A detail of the elements included in the CVR is as follows:

Fair Value Measurements Using Significant Unobservable Inputs (Level 3) CVRs (In thousands)			
	Estimated Fair Value as of December 31, 2011	Loss (Gain) for Changes in Estimated CVR Liability	Estimated Fair Value as of March 31, 2012
Components of CVR Liability:			
Tax refunds received before closing of the merger	\$ 1,583	\$	\$ 1,583
Other specified tax refunds	4,797		4,797
Tax indemnity obligation	1,717		1,717
Legal receivable	2,400		2,400
Michigan state tax liability	(252)	53	(199)
Other specified tax related liabilities	(53)		(53)
Costs incurred to collect tax refunds and by stockholders representative	(409)		(409)
Estimated fair value of CVR liability	9,783	53	9,836
Payments to holders of CVRs			3,099
Remaining estimated CVR liability			\$ 6,737

As of March 31, 2012, restricted assets in an escrow account for the benefit of the CVRs were \$3.0 million for a potential tax indemnity obligation, which, if such obligation is not triggered, will benefit the CVRs by \$1.9 million with the remainder reverting back to general cash of the Company.

Note 6 Other Current Assets

Other current assets at March 31, 2012 and December 31, 2011 consisted of the following:

<i>(in thousands)</i>	March 31, 2012	As of December 31, 2011

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Prepaid expenses	\$ 2,396	\$ 1,503
Deferred costs	2,193	2,714
Other current assets	34	518
Total	\$ 4,623	\$ 4,735

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Other assets at March 31, 2012 and December 31, 2011 consisted of the following:

<i>(in thousands)</i>	March 31, 2012	As of December 31, 2011
Tax receivables	\$ 11,156	\$ 11,039
Deferred financing costs	7,312	7,706
Collateral investments	1,967	1,967
Other	1,707	1,756
Total	\$ 22,142	\$ 22,468

Tax receivables include the \$11.2 million receivable from the state of Michigan as discussed in Note 13 to the Condensed Consolidated Financial Statements. The deferred financing costs represent costs incurred in connection with the issuance of the \$175 million aggregate principal amount of 9.75% senior secured notes as described in Note 14 to the Condensed Consolidated Financial Statements.

Note 8 Accrued Expenses

Accrued expenses at March 31, 2012 and December 31, 2011 consisted of the following:

<i>(in thousands)</i>	March 31, 2012	As of December 31, 2011
Salaries, bonuses and benefits	\$ 7,241	\$ 7,688
Accrued interest	2,215	6,503
Accrued royalties	1,257	1,689
Pension and post-retirement medical benefits	1,221	1,221
Deferred compensation	56	98
Other	3,897	4,004
Total	\$ 15,887	\$ 21,203

Accrued interest at March 31, 2012 primarily relates to our 9.75% senior secured notes. The notes require semi-annual interest payments in arrears on each February 15 and August 15 over the life of the notes.

Note 9 Other Liabilities

Other liabilities at March 31, 2012 and December 31, 2011 consisted of the following:

<i>(in thousands)</i>	March 31, 2012	As of December 31, 2011
Pension and post-retirement medical benefits, long-term portion	\$ 10,935	\$ 11,110
Long-term deferred tax liability	3,092	3,121
Long-term income tax payable	815	803
Long-term deferred compensation	492	544
Other	2,479	2,548

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Total	\$ 17,813	\$ 18,126
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