

CSP INC /MA/  
Form 10-Q  
August 14, 2015  
United States  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2015

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 0-10843

CSP Inc.  
(Exact name of Registrant as specified in its Charter)

Massachusetts  
(State of incorporation)

04-2441294  
(I.R.S. Employer Identification No.)

43 Manning Road  
Billerica, Massachusetts 01821-3901  
(978) 663-7598  
(Address and telephone number of principal executive offices)

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 the 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

Edgar Filing: CSP INC /MA/ - Form 10-Q

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

As of August 12, 2015, the registrant had 3,673,589 shares of common stock issued and outstanding.

1

---

INDEX

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	
<u>Consolidated Balance Sheets (unaudited) as of June 30, 2015 and September 30, 2014</u>	<u>3</u>
<u>Consolidated Statements of Operations (unaudited) for the three and nine months ended June 30, 2015 and 2014</u>	<u>4</u>
<u>Consolidated Statements of Comprehensive Income (loss) (unaudited) for the three and nine months ended June 30, 2015 and 2014</u>	<u>5</u>
<u>Consolidated Statement of Shareholders' Equity (unaudited) for the nine months ended June 30, 2015</u>	<u>6</u>
<u>Consolidated Statements of Cash Flows (unaudited) for the nine months ended June 30, 2015 and 2014</u>	<u>7</u>
<u>Notes to Consolidated Financial Statements (unaudited)</u>	<u>8</u>
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>17</u>
<u>Item 4. Controls and Procedures</u>	<u>26</u>
<u>PART II. OTHER INFORMATION</u>	
<u>Item 6. Exhibits</u>	<u>27</u>

## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

CSP INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

(Amounts in thousands, except par value)

	June 30, 2015 (Unaudited)	September 30, 2014
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$10,446	\$16,448
Accounts receivable, net of allowances of \$234 and \$241	17,367	12,532
Inventories, net	6,646	6,446
Refundable income taxes	658	418
Deferred income taxes	1,178	1,230
Other current assets	2,741	2,372
Total current assets	39,036	39,446
Property, equipment and improvements, net	1,367	1,472
Other assets:		
Intangibles, net	448	545
Deferred income taxes	1,819	1,892
Cash surrender value of life insurance	3,037	2,785
Other assets	275	167
Total other assets	5,579	5,389
Total assets	\$45,982	\$46,307
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$13,042	\$9,751
Deferred revenue	3,128	4,101
Pension and retirement plans	663	658
Income taxes payable	—	1
Total current liabilities	16,833	14,511
Pension and retirement plans	9,635	10,440
Other long term liabilities	—	69
Total liabilities	26,468	25,020
Commitments and contingencies		
Shareholders' equity:		
Common stock, \$.01 par value per share; authorized, 7,500 shares; issued and outstanding 3,674 and 3,619 shares, respectively	37	36
Additional paid-in capital	12,047	11,658
Retained earnings	15,442	17,517
Accumulated other comprehensive loss	(8,012)	(7,924)
Total shareholders' equity	19,514	21,287
Total liabilities and shareholders' equity	\$45,982	\$46,307

See accompanying notes to unaudited consolidated financial statements.

3

---

CSP INC. AND SUBSIDIARIES  
 UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

(Amounts in thousands, except for per share data)

	For the three months ended		For the nine months ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
Sales:				
Product	\$15,696	\$15,677	\$45,544	\$44,745
Services	6,591	6,959	16,050	20,126
Total sales	22,287	22,636	61,594	64,871
Cost of sales:				
Product	13,461	13,058	37,974	37,447
Services	3,560	3,474	10,356	11,705
Total cost of sales	17,021	16,532	48,330	49,152
Gross profit	5,266	6,104	13,264	15,719
Operating expenses:				
Engineering and development	626	945	2,305	2,372
Selling, general and administrative	3,945	4,192	11,824	12,169
Total operating expenses	4,571	5,137	14,129	14,541
Bargain purchase gain on acquisition, net of tax	—	—	—	462
Operating income (loss)	695	967	(865)	) 1,640
Other expense:				
Foreign exchange loss	(87)	) (67)	) (216)	) (120)
Other expense, net	(26)	) (37)	) (59)	) (58)
Total other expense	(113)	) (104)	) (275)	) (178)
Income (loss) before income taxes	582	863	(1,140)	) 1,462
Income tax expense (benefit)	333	(36)	) (277)	) 50
Net income (loss)	\$249	\$899	\$(863)	) \$1,412
Net income (loss) attributable to common stockholders	\$240	\$863	\$(863)	) \$1,361
Net income (loss) per share – basic	\$0.07	\$0.25	\$(0.25)	) \$0.40
Weighted average shares outstanding – basic	3,540	3,451	3,522	3,442
Net income (loss) per share – diluted	\$0.07	\$0.25	\$(0.25)	) \$0.39
Weighted average shares outstanding – diluted	3,633	3,499	3,522	3,488

See accompanying notes to unaudited consolidated financial statements.

## CSP INC. AND SUBSIDIARIES

## UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Amounts in thousands)

	For the three months ended		For the nine months ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
Net income (loss)	\$249	\$899	\$(863)	) \$1,412
Other comprehensive income (loss):				
Foreign currency translation gain (loss) adjustments	29	(92)	) (88)	) 62
Other comprehensive income (loss)	29	(92)	) (88)	) 62
Total comprehensive income (loss)	\$278	\$807	\$(951)	) \$1,474

See accompanying notes to unaudited consolidated financial statements.

## CSP INC. AND SUBSIDIARIES

## UNAUDITED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

For the nine Months Ended June 30, 2015:

(Amounts in thousands, except per share data)

	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated other comprehensive loss	Total Shareholders' Equity
Balance as of September 30, 2014	3,619	\$36	\$11,658	\$17,517	\$ (7,924 )	\$ 21,287
Net loss	—	—	—	(863 )	—	(863 )
Other comprehensive loss	—	—	—	—	(88 )	(88 )
Stock-based compensation	—	—	285	—	—	285
Restricted stock issuance	40	1	—	—	—	1
Issuance of shares under employee stock purchase plan	15	—	104	—	—	104
Cash dividends on common stock (\$0.33 per share)	—	—	—	(1,212 )	—	(1,212 )
Balance as of June 30, 2015	3,674	\$37	\$12,047	\$15,442	\$ (8,012 )	\$ 19,514

See accompanying notes to unaudited consolidated financial statements.



CSP INC. AND SUBSIDIARIES  
 UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)

	For the nine months ended	
	June 30, 2015	June 30, 2014
Cash flows from operating activities:		
Net income (loss)	\$(863	) \$1,412
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Bargain purchase gain	—	(462
Depreciation and amortization	385	364
Amortization of intangibles	97	92
Loss on sale of fixed assets, net	54	2
Foreign exchange loss	216	120
Non-cash changes in accounts receivable	(4	) (17
Non-cash changes in inventory	240	146
Stock-based compensation expense on stock options and restricted stock awards	285	260
Deferred income taxes	27	273
Increase in cash surrender value of life insurance	(59	) (114
Changes in operating assets and liabilities:		
Increase in accounts receivable	(5,439	) (2,110
Increase in inventories	(497	) (1,160
(Increase) decrease in refundable income taxes	(187	) 373
Increase in other current assets	(506	) (485
Increase in other assets	(119	) —
Increase in accounts payable and accrued expenses	3,691	425
Increase (decrease) in deferred revenue	(619	) 1,662
Decrease in pension and retirement plans liability	(58	) (168
Decrease in income taxes payable	(72	) (311
Increase in other long term liabilities	(69	) (338
Net cash used in operating activities	(3,497	) (36
Cash flows from investing activities:		
Life insurance premiums paid	(193	) (167
Proceeds from the sale of fixed assets	—	6
Cash paid to acquire business	—	(500
Purchases of property, equipment and improvements	(398	) (370
Net cash used in investing activities	(591	) (1,031
Cash flows from financing activities:		
Dividends paid	(1,212	) (1,148
Proceeds from issuance of shares under equity compensation plans	105	6
Net cash used in financing activities	(1,107	) (1,142
Effects of exchange rate on cash	(807	) 40
Net decrease in cash and cash equivalents	(6,002	) (2,169
Cash and cash equivalents, beginning of period	16,448	18,619
Cash and cash equivalents, end of period	\$10,446	\$16,450
Supplementary cash flow information:		
Cash paid for income taxes	\$72	\$96
Cash paid for interest	\$85	\$85

See accompanying notes to unaudited consolidated financial statements.



CSP INC. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
THREE AND NINE MONTHS ENDED JUNE 30, 2015 AND 2014

Organization and Business

CSP Inc. was founded in 1968 and is based in Billerica, Massachusetts. To meet the diverse requirements of its industrial, commercial and defense customers worldwide, CSP Inc. and its subsidiaries (collectively “we”, “us”, “our”, “CSPI” or the “Company”) develop and market IT integration solutions and high-performance cluster computer systems. The Company operates in two segments, its High Performance Products (“HPP”) segment (formerly the “High Performance Products and Solutions” segment) and its Technology Solutions (“TS”) segment (formerly the Information Technology Solutions segment).

1. Basis of Presentation

The accompanying consolidated financial statements have been prepared by the Company, without audit, and reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results of the interim periods presented. All adjustments were of a normal recurring nature. Certain information and footnote disclosures normally included in the annual consolidated financial statements, which are prepared in accordance with accounting principles generally accepted in the United States, have been omitted.

Accordingly, the Company believes that although the disclosures are adequate to make the information presented not misleading, the unaudited consolidated financial statements should be read in conjunction with the footnotes contained in the Company’s Annual Report on Form 10-K for the fiscal year ended September 30, 2014.

2. Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period, including estimates and assumptions related to reserves for bad debt, reserves for inventory obsolescence, the impairment assessment of intangible assets, the calculation of estimated selling price and post-delivery support obligations used for revenue recognition and the calculation of income tax liabilities. Actual results may differ from those estimates under different assumptions or conditions.

3. Earnings Per Share of Common Stock

Basic net income (loss) per common share is computed by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted net income (loss) per common share reflects the maximum dilution that would have resulted from the assumed exercise and share repurchase related to dilutive stock options and is computed by dividing net income (loss) by the assumed weighted average number of common shares outstanding.

We are required to present earnings per share, or EPS, utilizing the two class method because we had outstanding, non-vested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents, which are considered participating securities.



Basic and diluted earnings per share computations for the Company's reported net income (loss) attributable to common stockholders are as follows:

	For the three months ended		For the nine months ended	
	June 30, 2015	June 30, 2014	June 30, 2015	June 30, 2014
	(Amounts in thousands except per share data)			
Net income (loss)	\$249	\$899	\$(863	) \$1,412
Less: net income attributable to nonvested common stock	9	36	—	51
Net income (loss) attributable to common stockholders	\$240	\$863	\$(863	) \$1,361
Weighted average total shares outstanding – basic	3,674	3,593	3,522	3,572
Less: weighted average non-vested shares outstanding	134	142	—	130
Weighted average number of common shares outstanding – basic	3,540	3,451	3,522	3,442
Potential common shares from non-vested stock awards and the assumed exercise of stock options	93	48	—	46
Weighted average common shares outstanding – diluted	3,633	3,499	3,522	3,488
Net income (loss) per share – basic	\$0.07	\$0.25	\$(0.25	) \$0.40
Net income (loss) per share – diluted	\$0.07	\$0.25	\$(0.25	) \$0.39

All anti-dilutive securities, including certain stock options, are excluded from the diluted income (loss) per share computation. For the three months ended June, 2015 and 2014, 12,000 and 58,000 options, respectively, were excluded from the diluted income per share calculation because their inclusion would have been anti-dilutive as their exercise price exceeded fair value. For the nine months ended June, 2015 and 2014, 28,000 and 52,000 options, respectively, were excluded from the diluted income per share calculation because their inclusion would have been anti-dilutive as their exercise price exceeded fair value. Additionally, 130,000 non-vested restricted stock awards were excluded from the diluted income per share calculation as there was a net loss for the nine months ended June 30, 2015 and their inclusion would have been anti-dilutive.

Draft 5 Preliminary &amp; Tentative For Discussion Purposes Only

## 4. Inventories

Inventories consist of the following:

	June 30, 2015	September 30, 2014
	(Amounts in thousands)	
Raw materials	\$2,079	\$2,377
Work-in-process	812	229
Finished goods	3,755	3,840
Total	\$6,646	\$6,446

Finished goods includes inventory of approximately \$0.1 million and \$0.4 million as of June 30, 2015 and September 30, 2014, respectively, that has been shipped, but for which all revenue recognition criteria have not been met

Total inventory balances in the table above are shown net of reserves for obsolescence of approximately \$3.9 million and \$4.7 million as of June 30, 2015 and September 30, 2014.

## 5. Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss are as follows:

	June 30, 2015	September 30, 2014
	(Amounts in thousands)	
Cumulative effect of foreign currency translation	\$(2,583 )	\$(2,495 )
Cumulative unrealized loss on pension liability	(5,429 )	(5,429 )
Accumulated other comprehensive loss	\$(8,012 )	\$(7,924 )

## 6. Pension and Retirement Plans

The Company has defined benefit and defined contribution plans in the United Kingdom, Germany and the U.S. In the United Kingdom and Germany, the Company provides defined benefit pension plans and defined contribution plans for the majority of its employees. In the U.S., the Company provides benefits through supplemental retirement plans to certain current and former employees. The domestic supplemental retirement plans have life insurance policies which are not plan assets but were purchased by the Company as a vehicle to fund the costs of the plan. Domestically, the Company also provides for officer death benefits through post-retirement plans to certain officers. All of the Company's defined benefit plans are closed to newly hired employees and have been for the two years ended September 30, 2014 and 2013 and for the nine months ended June 30, 2015.

The Company funds its pension plans in amounts sufficient to meet the requirements set forth in applicable employee benefits laws and local tax laws. Liabilities for amounts in excess of these funding levels are accrued and reported in the consolidated balance sheets.

The Company's pension plan in the United Kingdom is the only plan with plan assets. The plan assets consist of an investment in a commingled fund which in turn comprises a diversified mix of assets including corporate equity securities, government securities and corporate debt securities.

The components of net periodic benefit costs related to the U.S. and international plans are as follows:

10

---

	For the Three Months Ended June 30, 2015			2014			
	Foreign	U.S.	Total	Foreign	U.S.	Total	
	(Amounts in thousands)						
Pension:							
Service cost	\$13	\$—	\$13	\$10	\$—	\$10	
Interest cost	157	13	170	196	17	213	
Expected return on plan assets	(105	) —	(105	) (120	) —	(120	)
Amortization of:							
Prior service gain	—	—	—	—	—	—	
Amortization of net gain	49	(1	) 48	24	(3	) 21	
Net periodic benefit cost	\$114	\$12	\$126	\$110	\$14	\$124	
Post Retirement:							
Service cost	\$—	\$9	\$9	\$—	\$3	\$3	
Interest cost	—	11	11	—	10	10	
Amortization of net gain	—	(13	) (13	) —	(35	) (35	)
Net periodic cost (benefit)	\$—	\$7	\$7	\$—	\$(22	) \$(22	)

	For the Nine Months Ended June 30, 2015			2014			
	Foreign	U.S.	Total	Foreign	U.S.	Total	
	(Amounts in thousands)						
Pension:							
Service cost	\$42	\$—	\$42	\$34	\$—	\$34	
Interest cost	476	39	515	579	51	630	
Expected return on plan assets	(317	) —	(317	) (352	) —	(352	)
Amortization of:							
Prior service gain	—	—	—	—	—	—	
Amortization of net gain	151	(2	) 149	70	(7	) 63	
Net periodic benefit cost	\$352	\$37	\$389	\$331	\$44	\$375	
Post Retirement:							
Service cost	\$—	\$26	\$26	\$—	\$8	\$8	
Interest cost	—	33	33	—	32	32	
Amortization of net gain	—	(38	) (38	) —	(107	) (107	)