

LANDEC CORP \CA\
Form 10-Q
April 05, 2018

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 Fiscal Quarter Ended February 25, 2018, or

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

For the Transition period for _____ to _____.

Commission file number: **0-27446**

LANDEC CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

94-3025618

(IRS Employer Identification Number)

5201 Great America Parkway, Suite 232

Santa Clara, California 95054

(Address of principal executive offices)

Registrant's telephone number, including area code:

(650) 306-1650

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock	The NASDAQ Global Select Stock Market

Securities registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Act 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 Website, 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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definition of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer

Non Accelerated Filer Smaller Reporting Company

Emerging Growth Company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act ____

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

As of April 2, 2018, there were 27,564,428 shares of Common Stock outstanding.

LANDEC CORPORATION

FORM 10-Q

For the Fiscal Quarter Ended February 25, 2018

INDEX

	Page
Facing sheet	
Index	i
Part I. <u>Financial Information</u>	
Item 1. <u>Financial Statements</u>	
a) <u>Consolidated Balance Sheets as of February 25, 2018 and May 28, 2017</u>	1
b) <u>Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended February 25, 2018 and February 26, 2017</u>	2
c) <u>Consolidated Statement of Changes in Stockholders' Equity for the Nine Months Ended February 25, 2018</u>	3
d) <u>Consolidated Statements of Cash Flows for the Nine Months Ended February 25, 2018 and February 26, 2017</u>	4
e) <u>Notes to Consolidated Financial Statements</u>	5
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	18
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	27
Item 4. <u>Controls and Procedures</u>	27
Part II. <u>Other Information</u>	28

Item 1.	<u>Legal Proceedings</u>	28
Item 1A.	<u>Risk Factors</u>	28
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	28
Item 3.	<u>Defaults Upon Senior Securities</u>	28
Item 4.	<u>Mine Safety Disclosures</u>	28
Item 5.	<u>Other Information</u>	28
Item 6.	<u>Exhibits</u>	29
	<u>Signatures</u>	30

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements****LANDEC CORPORATION****CONSOLIDATED BALANCE SHEETS****(In thousands except par value)**

	February 25, 2018 (unaudited)	May 28, 2017
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 7,650	\$ 5,409
Accounts receivable, less allowance for doubtful accounts	50,438	47,083
Inventories	28,749	25,290
Prepaid expenses and other current assets	7,614	3,498
Total Current Assets	94,451	81,280
Investment in non-public company, fair value	65,800	63,600
Property and equipment, net	143,362	133,220
Goodwill	54,779	54,779
Trademarks/tradenames, net	16,028	16,028
Customer relationships, net	6,052	6,783
Other assets	5,364	2,918
Total Assets	\$ 385,836	\$ 358,608
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 35,240	\$ 25,868
Accrued compensation	6,732	8,211
Other accrued liabilities	10,369	9,125
Deferred revenue	1,906	310
Line of credit	12,000	3,000
Current portion of long-term debt	4,940	4,940
Total Current Liabilities	71,187	51,454
Long-term debt, net	38,595	42,299
Capital lease obligation, less current portion	3,665	3,731
Deferred taxes, net	15,822	24,581
Other non-current liabilities	6,417	8,391
Total Liabilities	135,686	130,456

Stockholders' Equity:

Common stock, \$0.001 par value; 50,000 shares authorized; 27,555 and 27,499 shares issued and outstanding at February 25, 2018 and May 28, 2017, respectively	28	27
Additional paid-in capital	144,498	141,680
Retained earnings	103,191	84,470
Accumulated other comprehensive income	915	432
Total Stockholders' Equity	248,632	226,609
Non-controlling interest	1,518	1,543
Total Equity	250,150	228,152
Total Liabilities and Stockholders' Equity	\$ 385,836	\$ 358,608

See accompanying notes.

LANDEC CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(In thousands, except per share amounts)

	Three Months Ended		Nine Months Ended	
	February	February	February	February
	25,	26,	25,	26,
	2018	2017	2018	2017
Product sales	\$149,323	\$136,568	\$409,137	\$404,827
Cost of product sales	129,195	113,136	353,971	341,298
Gross profit	20,128	23,432	55,166	63,529
Operating expenses:				
Research and development	3,113	2,014	9,204	5,917
Selling, general and administrative	13,807	15,009	40,786	41,969
Legal settlement charge	—	2,080	—	2,580
Total operating costs and expenses	16,920	19,103	49,990	50,466
Operating income	3,208	4,329	5,176	13,063
Dividend income	413	413	1,238	1,238
Interest income	87	8	161	15
Interest expense	(531)	(400)	(1,415)	(1,432)
Loss on debt refinancing	—	—	—	(1,233)
Other income	—	700	2,200	700
Net income before taxes	3,177	5,050	7,360	12,351
Income tax benefit (expense)	12,909	(1,556)	11,451	(4,138)
Consolidated net income	16,086	3,494	18,811	8,213
Non-controlling interest benefit (expense)	2	6	(90)	(75)
Net income applicable to common stockholders	\$16,088	\$3,500	\$18,721	\$8,138
Basic net income per share	\$0.58	\$0.13	\$0.68	\$0.30
Diluted net income per share	\$0.58	\$0.13	\$0.67	\$0.29
Shares used in per share computation				
Basic	27,547	27,286	27,524	27,252
Diluted	27,918	27,682	27,884	27,608

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Other comprehensive income, net of tax:

Change in net unrealized gains on interest rate swap (net of tax effect of \$210, \$59, \$552, and \$251)	\$347	\$103	\$483	\$430
Other comprehensive income, net of tax	347	103	483	430
Total comprehensive income	\$16,435	\$3,603	\$19,204	\$8,568

See accompanying notes.

-2-

LANDEC CORPORATION

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(Unaudited)

(in thousands, except per share amounts)

	Common Stock		Additional Paid-in	Retained	Accumulated Other Comprehensive	Total Stockholders'	Non-controlling
	Shares	Amount	Capital	Earnings	Income	Equity	Interest
Balance at May 28, 2017	27,499	\$ 27	\$ 141,680	\$ 84,470	\$ 432	\$ 226,609	\$ 1,543
Issuance of common stock at \$5.63 to \$6.66 per share, net of taxes paid by Landec on behalf of employees	3	—	—	—	—	—	—
Issuance of common stock for vested restricted stock units ("RSUs")	53	1	—	—	—	1	—
Taxes paid by Company for employee stock plans	—	—	(394)	—	—	(394)	—
Stock-based compensation	—	—	3,212	—	—	3,212	—
Payments to non-controlling interest	—	—	—	—	—	—	(115)
Net income	—	—	—	18,721	—	18,721	90
Other comprehensive income, net of tax	—	—	—	—	483	483	—
Balance at February 25, 2018	27,555	\$ 28	\$ 144,498	\$ 103,191	\$ 915	\$ 248,632	\$ 1,518

See accompanying notes.

LANDEC CORPORATION**Consolidated StatementS of Cash Flows****(Unaudited)****(In thousands)**

	Nine Months Ended	
	February 25,	February 26,
	2018	2017
Cash flows from operating activities:		
Consolidated net income	\$18,811	\$8,213
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,076	7,827
Stock-based compensation expense	3,212	2,842
Deferred taxes	(9,055)	3,437
Loss on early debt extinguishment	—	1,233
Change in investment in non-public company, fair value	(2,200)	(700)
Net loss on disposal of property and equipment	93	264
Changes in current assets and current liabilities:		
Accounts receivable, net	(3,355)	488
Inventories	(3,459)	2,262
Prepaid expenses and other current assets	(3,876)	(137)
Deposit for workers' compensation collateral	—	(100)
Accounts payable	9,373	(6,140)
Accrued compensation	(1,548)	676
Other accrued liabilities	(449)	3,419
Deferred revenue	1,475	(403)
Net cash provided by operating activities	18,098	23,181
Cash flows from investing activities:		
Purchases of property and equipment	(18,533)	(9,488)
Issuance of note receivable	(2,099)	—
Proceeds from sales of fixed assets	88	74
Net cash used in investing activities	(20,544)	(9,414)
Cash flows from financing activities:		
Proceeds from sale of common stock	1	233
Taxes paid by Company for employee stock plans	(394)	(385)
Proceeds from long-term debt	—	50,000

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Payments on long-term debt	(3,805)	(55,966)
Proceeds from lines of credit	18,000	1,500
Payments on lines of credit	(9,000)	(5,000)
Payments for debt issuance costs	—	(902)
Payments for early debt extinguishment penalties	—	(233)
Payments to non-controlling interest	(115)	(166)
Other, net	—	(8)
Net cash provided by (used in) financing activities	4,687	(10,927)
Net increase in cash and cash equivalents	2,241	2,840
Cash and cash equivalents at beginning of period	5,409	9,894
Cash and cash equivalents at end of period	\$7,650	\$12,734

See accompanying notes.

LANDEC CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

I. Organization , Basis of Presentation, and Summary of Significant Accounting Policies

Organization

Landec Corporation and its subsidiaries (“Landec” or the “Company”) design, develop, manufacture, and sell differentiated products for food and biomaterials markets, and license technology applications to partners. The Company has *two* proprietary polymer technology platforms: 1) Intelimer® polymers, and 2) hyaluronan (“HA”) biopolymers. The Company sells specialty packaged branded Eat Smart® and GreenLine® and private label fresh-cut vegetables and whole produce to retailers, club stores, and foodservice operators, primarily in the United States, Canada, and Asia through its Apio, Inc. (“Apio”) subsidiary, and sells HA-based and non-HA biomaterials through its Lifecore Biomedical, Inc. (“Lifecore”) subsidiary. The Company’s HA biopolymers and non-HA materials are proprietary in that they are specially formulated for specific customers to meet strict regulatory requirements. Through its O Olive Oil and Vinegar (“O Olive”) division, which the Company acquired on *March 1, 2017*, the Company sells premier California specialty olive oils and wine vinegars under the O brand to natural food, conventional grocery and mass retail stores, primarily in the United States and Canada.

The Company’s technologies, along with its customer relationships and tradenames, are the foundation and key differentiating advantages upon which Landec has built its business.

Basis of Presentation

The accompanying unaudited consolidated financial statements of Landec have been prepared in accordance with United States generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal recurring accruals) have been made which are necessary to present fairly the financial position of the Company at *February 25, 2018* and the results of operations and cash flows for all periods presented. Although Landec believes that the disclosures in these financial statements are adequate to make the information presented *not* misleading, certain information normally included in financial statements and related footnotes prepared in accordance with GAAP have been condensed or omitted in accordance with the rules and regulations of the Securities and Exchange Commission. The accompanying financial data should be reviewed in conjunction with the audited

financial statements and accompanying notes included in Landec's Annual Report on Form 10-K for the fiscal year ended *May 28, 2017*.

The results of operations for the *nine* months ended *February 25, 2018* are *not* necessarily indicative of the results that *may* be expected for an entire fiscal year because there is some seasonality in Apio's food business, particularly, Apio's export business, and the order patterns of Lifecore's customers which *may* lead to significant fluctuations in Landec's quarterly results of operations.

Basis of Consolidation

The consolidated financial statements are presented on the accrual basis of accounting in accordance with GAAP and include the accounts of Landec Corporation and its subsidiaries, Apio and Lifecore. All intercompany transactions and balances have been eliminated.

Arrangements that are *not* controlled through voting or similar rights are reviewed under the guidance for variable interest entities ("VIEs"). A company is required to consolidate the assets, liabilities, and operations of a VIE if it is determined to be the primary beneficiary of the VIE.

An entity is a VIE and subject to consolidation, if by design: a) the total equity investment at risk is *not* sufficient to permit the entity to finance its activities without additional subordinated financial support provided by any party, including equity holders, or b) as a group the holders of the equity investment at risk lack any *one* of the following *three* characteristics: (i) the power, through voting rights or similar rights to direct the activities of an entity that most significantly impact the entity's economic performance, (ii) the obligation to absorb the expected losses of the entity, or (iii) the right to receive the expected residual returns of the entity. The Company reviewed the consolidation guidance and concluded that its partnership interest in Apio Cooling, LP and its equity investment in the non-public company are *not* VIEs.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make certain estimates and judgments that affect the amounts reported in the financial statements and accompanying notes. The accounting estimates that require management's most significant and subjective judgments include revenue recognition; loss contingencies; sales returns and allowances; inventories; self-insurance liabilities; recognition and measurement of current and deferred income tax assets and liabilities; the assessment of recoverability of long-lived assets including intangible assets; the valuation of investments; and the valuation and recognition of stock-based compensation and contingent liabilities.

These estimates involve the consideration of complex factors and require management to make judgments. The analysis of historical and future trends can require extended periods of time to resolve and are subject to change from period to period. The actual results *may* differ from management's estimates.

Cash and Cash Equivalents

The Company records all highly liquid securities with *three* months or less from date of purchase to maturity as cash equivalents. Cash equivalents consist mainly of money market funds. The market value of cash equivalents approximates their historical cost given their short-term nature.

Inventories

Inventories are stated at the lower of cost (*first-in, first-out* method) or net realizable value and consist of the following (in thousands):

	February 25, 2018	May 28, 2017
Raw materials	\$13,512	\$10,158
Work in progress	3,756	3,447
Finished goods	11,481	11,685
Total	\$28,749	\$25,290

If the cost of the inventories exceeds their net realizable value, provisions are recorded currently to reduce them to net realizable value. The Company also records a provision for slow moving and obsolete inventories based on the estimate of demand for its products.

Related Party Transactions

The Company sells products to and earns license fees from Windset Holdings 2010 Ltd. (“Windset”). During the *three* months ended *February 25, 2018* and *February 26, 2017*, the Company recognized revenues of *\$104,000* and *\$72,000*, respectively. During the *nine* months ended *February 25, 2018* and *February 26, 2017*, the Company recognized revenues of *\$299*