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ENVOY COMMUNICATIONS GROUP INC

Form 10-Q

March 09, 2001

Consolidated Balance Sheets

(In Canadian dollars)

(Unaudited - Prepared by Management)

| As at | December 31 2000 | September 30 2000 |
|---------------------------|---------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash | \$11,843,799 | \$7,105,418 |
| Accounts receivable | 41,638,478 | 34,234,974 |
| Prepaid expenses | 2,310,253 | 1,732,212 |
| | 55,792,530 | 43,072,604 |
| Restricted cash | 1,077,095 | 832,337 |
| Capital assets | 10,376,318 | 10,448,625 |
| Goodwill and other assets | 46,753,626 | 46,987,707 |
| Deferred income taxes | 771,024 | 966,715 |
| | \$114,770,593 | \$102,307,988 |

Liabilities and Shareholders' Equity

Current liabilities:

| | | |
|--|--------------|--------------|
| Accounts payable and accrued liabilities | \$35,513,548 | \$24,247,075 |
| Income taxes payable | 1,540,035 | 1,190,313 |
| Deferred revenue | 1,038,848 | 1,044,873 |
| Amounts collected in excess of pass-through costs incurred | 2,647,225 | 2,307,047 |
| Current portion of long-term debt | 3,146,116 | 2,848,430 |
| | 43,885,772 | 31,637,738 |
| Long-term debt | 6,848,351 | 7,983,449 |

Shareholders' equity:

| | | |
|------------------------------------|---------------|---------------|
| Share capital | 54,865,335 | 54,597,762 |
| Retained earnings | 9,487,615 | 8,403,367 |
| Cummulative translation adjustment | (316,480) | (314,328) |
| | 64,036,470 | 62,686,801 |
| | \$114,770,593 | \$102,307,988 |

Consolidated Statements of Operations and Retained Earnings

(In Canadian dollars)

(Unaudited - Prepared by Management)

| For the three months ended | December 31 2000 | December 31 1999 |
|----------------------------|---------------------|---------------------|
| Net revenue | \$21,776,358 | \$12,704,336 |

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Operating expenses:

| | | |
|--|-------------|-------------|
| Salaries and benefits | 12,210,069 | 7,804,946 |
| General and administrative | 4,044,752 | 2,373,245 |
| Occupancy costs | 1,087,311 | 457,934 |
| | 17,342,132 | 10,636,125 |
| | | |
| Earnings before interest expense, income taxes, depreciation and goodwill amortization | 4,434,226 | 2,068,211 |
| | | |
| Depreciation | 710,490 | 379,085 |
| Interest expense | 233,243 | 76,446 |
| Earnings before income taxes and goodwill amortization | 3,490,493 | 1,612,680 |
| | | |
| Income tax expense, excluding the undernoted | 1,575,378 | 703,181 |
| Impact of tax rate changes (Note 1) | 100,000 | - |
| | | |
| Earnings before goodwill amortization | 1,815,115 | 909,499 |
| | | |
| Goodwill amortization, net of income taxes of \$6,000 (1999-\$6,000) | 730,867 | 262,568 |
| | | |
| Net earnings | \$1,084,248 | \$646,931 |
| | | |
| Retained earnings, beginning of period | 8,403,367 | 5,492,940 |
| | | |
| Retained earnings, end of period | \$9,487,615 | \$6,139,871 |
| | | |
| Net earnings per share - basic | \$0.05 | \$0.04 |
| Net earnings per share - fully diluted | 0.05 | 0.04 |
| | | |
| Earnings per share before goodwill amortization - basic | 0.09 | 0.05 |
| Earnings per share before goodwill amortization - fully diluted | 0.08 | 0.05 |

Please see accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows
(In Canadian dollars)
(Unaudited-Prepared by Management)

| | December 31 2000 | December 31 1999 |
|---------------------------------------|---------------------|---------------------|
| For the three months ended | | |
| | | |
| Cash flows from operating activities: | | |
| Net earnings | \$1,084,248 | \$646,931 |

Items not involving cash:

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| | | |
|-----------------------|---------|----------|
| Deferred income taxes | 195,043 | (44,304) |
| Depreciation | 710,490 | 379,085 |
| Goodwill amortization | 736,867 | 268,568 |

Net changes in non-cash working capital balances:

| | | |
|--|-------------|-------------|
| Accounts receivable | (7,372,957) | (2,433,945) |
| Prepaid expenses | (575,959) | 103,856 |
| Accounts payable and accrued liabilities | 11,463,274 | (863,735) |
| Income taxes payable | 307,441 | (2,217,824) |
| Deferred revenue | (5,300) | - |
| Amounts collected in excess of pass-through costs incurred | 342,594 | 872,929 |
| Other | (73,019) | - |
| Net cash provided by (used in) operating activities | 6,812,722 | (3,288,439) |

Cash flows from financing activities:

| | | |
|---|-------------|-----------|
| Long-term debt | - | 400,000 |
| Long-term debt repayments | (1,459,996) | (441,766) |
| Issuance of common shares for cash | 267,573 | 269,500 |
| Reduction (Increase) in restricted cash | (245,758) | (225,014) |
| Other | 19,197 | - |
| Net cash provided by financing activities | (1,418,984) | 2,720 |

Cash flows from investing activities:

| | | |
|---|-----------|-------------|
| Acquisition of subsidiaries (net of cash acquired of nil; 1999 - nil) | - | (2,070,653) |
| Purchase of capital assets | (612,198) | (612,651) |
| Net cash used in investing activities | (612,198) | (2,683,304) |

| | | |
|--|----------|----------|
| Change in cash balance due to foreign exchange | (43,159) | (96,768) |
|--|----------|----------|

| | | |
|-----------------------------|-----------|-------------|
| (Decrease)/Increase in cash | 4,738,381 | (6,065,791) |
|-----------------------------|-----------|-------------|

| | | |
|---------------------------|-----------|------------|
| Cash, beginning of period | 7,105,418 | 15,300,454 |
|---------------------------|-----------|------------|

| | | |
|---------------------|--------------|-------------|
| Cash, end of period | \$11,843,799 | \$9,234,663 |
|---------------------|--------------|-------------|

Cash flow from operations per share:

| | | |
|---------------|--------|--------|
| Basic | \$0.13 | \$0.07 |
| Fully diluted | \$0.12 | \$0.07 |

Supplemental cash flow information:

| | | |
|--|-----------|-----------|
| Interest paid | \$40,419 | \$71,127 |
| Income taxes paid | 1,026,206 | 1,628,067 |
| Shares issued for non-cash consideration | 3,623,824 | 2,430,200 |

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Notes to Consolidated Financial Statements

1. Income taxes:

Effective October 1, 2000, the Company was required to adopt on a retroactive basis the new accounting standards of The Canadian Institute of Chartered Accountants ("CICA") for income taxes. Under this accounting standard, the Company is not required to restate its comparative figures for prior years.

Under these new standards, future tax assets and liabilities attributable to all temporary differences are measured using the future tax rates expected to be in effect when the items are recovered or settled. The effect of a change in tax rates must be recognized in income at the enactment date.

Previously, future tax assets and liabilities were recorded at the tax rate in effect in the period the temporary difference arose and were not adjusted for subsequent tax rate changes. The Company's temporary differences are principally in respect of deductible share issue costs which were recorded directly in capital stock rather than as a credit to income tax expense. There is no cumulative effect as of October 1, 2000 of this change in accounting policy. As a result of the December 2000 announcement by the government to introduce legislation to reduce income tax rates over the next four years, the Company was required to revalue its future tax assets as at December 31, 2000 to reflect the reduction in future expected tax rates. The impact of this was to increase the Company's tax provision for the three months ended December 31, 2000 by \$100,000. Under the CICA's new accounting standard the Company is required to record this item as an adjustment to income tax expense, notwithstanding the fact that such amounts were not previously reflected in income tax expense when recorded.

2. Segmented information:

The Company provides integrated marketing communication services to its clients. While the Company has subsidiaries in Canada, the United States, the United Kingdom and Continental Europe, it operates as a global business and has no distinct operating segments

The tables below set out the following information:

| | By Customer Location | By Geographic Area | |
|--|----------------------|--------------------|--------------|
| | Net Revenue | Capital Assets | Goodwill |
| December 31, 2000 | | | |
| Canada | \$6,186,066 | \$7,552,382 | \$21,970,618 |
| United States | 10,317,488 | 697,288 | 16,449,966 |
| United Kingdom and Continental Europe | 5,272,804 | 2,126,648 | 7,986,240 |
| | \$21,776,358 | \$10,376,318 | \$46,406,824 |
| December 31, 1999 | | | |
| Canada | \$3,845,186 | \$7,079,134 | \$10,245,724 |
| United States | 8,859,150 | 1,007,865 | 11,289,567 |
| United Kingdom and Continental Europe | - | - | - |
| | \$12,704,336 | \$8,086,999 | \$21,535,291 |

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The Company's external net revenue by type of service is as follows:

| December 31 | 2000 | 1999 |
|--------------|--------------|--------------|
| Net Revenue: | | |
| Marketing | \$7,668,623 | \$7,826,468 |
| Design | 9,389,802 | 4,538,385 |
| Technology | 4,717,933 | 339,483 |
| | \$21,776,358 | \$12,704,336 |