

GAIAM, INC
Form 10-Q
August 09, 2013
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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 AND EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2013

OR

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

Commission File Number 000-27517

GAIAM, INC.

(Exact name of registrant as specified in its charter)

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COLORADO
(State or other jurisdiction of
incorporation or organization)

84-1113527
(I.R.S. Employer
Identification No.)

833 WEST SOUTH BOULDER ROAD,
LOUISVILLE, COLORADO 80027
(Address of principal executive offices)

(303) 222-3600
(Registrant's telephone number, including area code)

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 and 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.:

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding at August 6, 2013
Class A Common Stock (\$.0001 par value)	17,346,287
Class B Common Stock (\$.0001 par value)	5,400,000

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This report may contain forward-looking statements that involve risks and uncertainties. The words anticipate, believe, plan, estimate, expect, strive, future, intend and similar expressions are intended to identify such forward-looking statements. Our actual results could differ materially from the results anticipated in these forward-looking statements as a result of certain factors set forth under Management's Discussion and Analysis of Financial Condition and Results of Operations, Quantitative and Qualitative Disclosures about Market Risk and elsewhere in this report. Risks and uncertainties that could cause actual results to differ include, without limitation, general economic conditions, competition, loss of key personnel, pricing, brand reputation, consumer trends, acquisitions, new initiatives undertaken by us, security and information systems, legal liability for website content, merchandise supply problems, failure of third parties to provide adequate service, our reliance on centralized customer service, overstocks and merchandise returns, our reliance on a centralized fulfillment center, increases in postage and shipping costs, E-commerce trends, future Internet related taxes, our founder's control of us, fluctuations in quarterly operating results, customer interest in our products, the effect of government regulation and other risks and uncertainties included in our filings with the Securities and Exchange Commission. We caution you that no forward-looking statement is a guarantee of future performance, and you should not place undue reliance on these forward-looking statements which reflect our view only as of the date of this report. We undertake no obligation to update any forward-looking information.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)
Unaudited Interim Condensed Consolidated Financial Statements

We have prepared our unaudited interim condensed consolidated financial statements included herein pursuant to the rules and regulations of the United States Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to these rules and regulations, although we believe that the disclosures made are adequate to make the information not misleading. In our opinion, the unaudited interim condensed financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary to present fairly, in all material respects, our consolidated financial position as of June 30, 2013, the interim results of operations for the three and six months ended June 30, 2013 and 2012, and cash flows for the six months ended June 30, 2013 and 2012. These interim statements have not been audited. The balance sheet as of December 31, 2012 was derived from our audited consolidated financial statements included in our annual report on Form 10-K. The interim condensed consolidated financial statements contained herein should be read in conjunction with our audited financial statements, including the notes thereto, for the year ended December 31, 2012.

Table of Contents**GAIAM, INC.****Condensed consolidated balance sheets**

(in thousands, except share and per share data)	June 30, 2013 (unaudited)	December 31, 2012
ASSETS		
Current assets:		
Cash	\$ 17,482	\$ 9,858
Accounts receivable, net	38,889	57,533
Inventory, less allowances	31,881	29,840
Deferred advertising costs	4,343	4,324
Deferred tax assets	8,002	9,129
Receivable from related party	2	64
Advances	15,816	13,197
Other current assets	3,329	2,463
Total current assets	119,744	126,408
Property and equipment, net	24,095	23,998
Media library, net	12,972	13,090
Deferred tax assets	11,530	14,692
Goodwill	10,011	9,405
Other intangibles, net	4,740	5,608
Other assets	741	661
Total assets	\$ 183,833	\$ 193,862
LIABILITIES AND EQUITY		
Current liabilities:		
Line of credit	\$ 11,972	\$ 16,231
Accounts payable	22,600	26,738
Participations payable	17,768	28,046
Accrued liabilities	4,226	3,975
Total current liabilities	56,566	74,990
Commitments and contingencies		
Equity:		
Gaiam, Inc. shareholders' equity:		
Class A common stock, \$.0001 par value, 150,000,000 shares authorized, 17,346,287 and 17,330,464 shares issued and outstanding at June 30, 2013 and December 31, 2012, respectively	2	2
Class B common stock, \$.0001 par value, 50,000,000 shares authorized, 5,400,000 issued and outstanding at June 30, 2013 and December 31, 2012	1	1
Additional paid-in capital	159,991	159,614
Accumulated other comprehensive income	30	118
Accumulated deficit	(36,089)	(43,661)
Total Gaiam, Inc. shareholders' equity	123,935	116,074
Noncontrolling interest	3,332	2,798
Total equity	127,267	118,872
Total liabilities and equity	\$ 183,833	\$ 193,862

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See accompanying Notes to the interim condensed consolidated financial statements.

Table of Contents**GAIAM, INC.****Condensed consolidated statements of operations**

(in thousands, except per share data)	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
	2013	2012	2013	2012
	(unaudited)		(unaudited)	
Net revenue	\$ 44,544	\$ 45,446	\$ 101,177	\$ 92,779
Cost of goods sold	20,909	17,435	45,337	37,662
Gross profit	23,635	28,011	55,840	55,117
Expenses:				
Selling and operating	24,294	26,896	52,523	51,057
Corporate, general and administration	3,227	3,081	7,052	5,654
Acquisition-related costs				1,667
Total expenses	27,521	29,977	59,575	58,378
Loss from operations	(3,886)	(1,966)	(3,735)	(3,261)
Interest and other expense, net	(52)	(123)	(281)	(67)
Gain on sale of investment	16,429		16,429	
Loss from equity method investment		(944)		(1,640)
Income (loss) before income taxes and noncontrolling interest	12,491	(3,033)	12,413	(4,968)
Income tax expense (benefit)	4,508	(924)	4,652	(1,561)
Net income (loss)	7,983	(2,109)	7,761	(3,407)
Net (income) loss attributable to noncontrolling interest	(135)	56	(189)	135
Net income (loss) attributable to Gaiam, Inc.	\$ 7,848	\$ (2,053)	\$ 7,572	\$ (3,272)
Net income (loss) per share attributable to Gaiam, Inc. common shareholders:				
Basic	\$ 0.35	\$ (0.09)	\$ 0.33	\$ (0.14)
Diluted	\$ 0.35	\$ (0.09)	\$ 0.33	\$ (0.14)
Weighted-average shares outstanding:				
Basic	22,741	22,702	22,736	22,700
Diluted	22,741	22,702	22,736	22,700

See accompanying Notes to the interim condensed consolidated financial statements.

Table of Contents**GAIAM, INC.****Condensed consolidated statements of comprehensive income (loss)**

(in thousands, except per share data)	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
	2013	2012	2013	2012
	(unaudited)		(unaudited)	
Net income (loss)	\$ 7,983	\$ (2,109)	\$ 7,761	\$ (3,407)
Other comprehensive loss, foreign currency translation, net of tax	(171)	(14)	(169)	(4)
Comprehensive income (loss)	7,812	(2,123)	7,592	(3,411)
Less: comprehensive income (loss) attributable to the noncontrolling interest	53	(63)	108	(137)
Comprehensive income (loss) attributable to Gaiam, Inc. shareholders	\$ 7,759	\$ (2,060)	\$ 7,484	\$ (3,274)

See accompanying Notes to the interim condensed consolidated financial statements.

Table of Contents**GAIAM, INC.****Condensed consolidated statements of cash flows**

(in thousands)	For the Six Months Ended June 30,	
	2013	2012
	(unaudited)	
Operating activities		
Net income (loss)	\$ 7,761	\$ (3,407)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation	1,219	1,142
Amortization	2,489	2,791
Share-based compensation expense	377	586
Deferred and stock option income tax expense (benefit)	4,415	(1,666)
Loss on translation of foreign currency	42	20
Gain on sale of investment	(16,429)	
Loss from equity method investment		1,640
Changes in operating assets and liabilities, net of effects from acquisitions:		
Accounts receivable, net	18,557	31,398
Inventory, net	(2,113)	(3,592)
Deferred advertising costs	(657)	(712)
Receivable from related party	62	8
Advances	(2,619)	(4,925)
Other current assets	(945)	(407)
Accounts payable	(4,146)	(2,842)
Participations payable	(10,278)	(3,664)
Accrued liabilities	255	992
Net cash provided by (used in) operating activities (a)	(2,010)	17,362
Investing activities		
Net proceeds from sale of investment	16,429	
Purchase of property, equipment and media rights	(1,956)	(2,324)
Purchase of businesses, net of acquired cash	(321)	(13,400)
Net cash provided by (used in) investing activities	14,152	(15,724)
Financing activities		
Net borrowings (payments) on revolving line of credit	(4,259)	14,000
Principal payments on debt (a)		(18,703)
Net cash used in financing activities	(4,259)	(4,703)
Effect of exchange rates on cash	(259)	(20)
Net change in cash	7,624	(3,085)
Cash at beginning of period	9,858	14,545
Cash at end of period	\$ 17,482	\$ 11,460
Supplemental cash flow information		
Income taxes paid	\$ 76	\$ 344
Interest paid	\$ 278	\$ 121

- (a) Net cash provided by operating activities for the six months ended June 30, 2012 includes approximately \$18.7 million of net cash provided by purchased Vivendi Entertainment (Vivendi) working capital, which was used to partially fund the acquisition of Vivendi. Excluding the net cash flows from the purchased Vivendi working capital, net cash from operating activities would have been a use of \$1.3 million for the six months ended June 30, 2012.

See accompanying Notes to the interim condensed consolidated financial statements

Table of Contents**Notes to interim condensed consolidated financial statements****1. Organization, Nature of Operations, and Principles of Consolidation**

References in this report to we, us, our, Gaiam or the Company refer to Gaiam, Inc. and its consolidated subsidiaries, unless we indicate otherwise. We are a lifestyle media company providing a broad selection of information, media, products and services to customers who value personal development, wellness, ecological lifestyles, responsible media and conscious community. We were incorporated under the laws of the State of Colorado on July 7, 1988.

We have prepared the accompanying unaudited interim condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States, or GAAP, and they include our accounts and those of our subsidiaries. Intercompany transactions and balances have been eliminated.

The unaudited condensed consolidated financial position, results of operations and cash flows for the interim periods disclosed in this report are not necessarily indicative of future financial results.

2. Significant Accounting Policies

No changes were made to our significant accounting policies during the three and six months ended June 30, 2013.

Goodwill

The following table sets forth the changes in goodwill for the period December 31, 2012 through June 30, 2013 by segment.

(in thousands)	Direct to Consumer Segment	Business Segment	Total
Balance at December 31, 2012	\$ 2,673	\$ 6,732	\$ 9,405
Acquisitions	606		606
Balance at June 30, 2013	\$ 3,279	\$ 6,732	\$ 10,011

Use of Estimates and Reclassifications

The preparation of financial statements in accordance with GAAP requires us to make estimates and assumptions that affect the amounts reported in the accompanying financial statements and disclosures. Although we base these estimates on our best knowledge of current events and actions that we may undertake in the future, actual results may be different from the estimates. We have made certain reclassifications to prior period amounts to conform to the current period presentations.

3. Related Party Transactions

Under Intercorporate Services and Industrial Building Lease Agreements, in the ordinary course of business, we bill and collect at least quarterly charges for services performed and facilities utilized by Real Goods Solar, Inc. (Real Goods Solar or RSOL).

On May 28, 2013, we sold in the public market 6,017,500 shares of our investment in Real Goods Solar Class A common stock for an average gross per share sale price of \$2.7552 and total net proceeds and gain of approximately \$16.4 million. At June 30, 2013, we owned approximately 13.4% of Real Goods Solar's Class A common stock and our Chairman had resigned from RSOL's board and, thus, we no longer had significant influence over Real Goods Solar. Therefore, we changed our accounting for our investment in RSOL from the equity to cost method. As a result of this accounting method change, we will no longer report our portion of RSOL's net earnings or losses each period.

At June 30, 2013, we had two subordinated loans receivable from Real Goods Solar with outstanding balances totaling \$2.6 million, which bear interest at an annual rate of 10%. On March 27, 2013, the maturity dates for these loans were extended, with \$1.0 million now due April 26, 2014 and \$1.6 million due April 30, 2014. On April 23, 2013, we entered into a conversion agreement with Real Goods Solar pursuant to which

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the principal amount of the \$1.7 million promissory note with Real Goods Solar dated March 27, 2013 was reduced by \$0.1 million in exchange for 62,111 shares of Real Goods Solar's Class A common stock. The conversion ratio was determined based on the closing market price of Real Goods Solar's Class A common stock on the date of the conversion agreement. The \$1.0 million loan includes certain customary language accelerating the maturity date upon the occurrence of certain events, such as RSOL's insolvency or bankruptcy. Also, if RSOL completes a sale of at least \$50,000 of its capital stock, then we have the option of converting all or any portion of the principal and interest owing on the loan into securities in such sale at the same purchase price as paid by other purchasers in such sale.

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During the three months ended June 30, 2013, we collected loan interest from Real Goods Solar of \$0.1 million, which is reported as Interest and other expense, net on our condensed consolidated statements of operations for the three and six months ended June 30, 2013.

4. Line of Credit

On July 31, 2012, each of our subsidiaries Gaiam Americas, Inc., SPRI Products, Inc., GT Direct, Inc., and Gaiam Vivendi Entertainment (collectively the Borrowers) entered into a Revolving Credit and Security Agreement (the PNC Credit Agreement) with PNC Bank, N.A. (PNC), as agent and lender. Borrowings are secured by a pledge of the Borrowers' assets. The PNC Credit Agreement provides for a revolving line of credit of up to \$35 million (\$26 million April 1st through June 30th of each calendar year), subject to borrowing base and related limitations. Subject to certain limitations, the principal amount of the revolving loan is due and payable on the earlier of July 30, 2015 or upon the termination of the PNC Credit Agreement. For additional information about this PNC Credit Agreement, see the Liquidity and Capital Resources section of this report.

As of June 30, 2013, the outstanding borrowings on the PNC Credit Agreement were approximately \$12.0 million at an average annual interest rate of approximately 3.35% and the amount reserved for outstanding letters of credit and other reserves was \$9.4 million. Net unamortized deferred fees and costs associated with this PNC Credit Agreement were \$0.3 million at June 30, 2013.

5. Equity

During the first half of 2013, we issued 15,823 shares of our Class A common stock under our 2009 Long-Term Incentive Plan to certain of our independent directors, in lieu of cash compensation, for services rendered in 2013. We recorded these shares at their estimated fair value based on the market's closing price of our stock on the date the shares were issued, which by policy is the last trading day of each quarter in which the services were rendered.

The following are reconciliations from December 31, 2012 to June 30, 2013 of the carrying amount of total equity, equity attributable to Gaiam, Inc., and equity attributable to the noncontrolling interest.

(in thousands)	Total	Gaiam, Inc. Shareholders					
		Comprehensive Income	Accumulated Deficit	Comprehensive Income	Class A and Class B Common Stock	Paid-in Capital	Noncontrolling Interest
Balance at December 31, 2012	\$ 118,872		\$ (43,661)	\$ 118	\$ 3	\$ 159,614	\$ 2,798
Issuance of Gaiam, Inc. common stock and share-based compensation	377					377	
Noncontrolling interest portion of subsidiary's business combinations	426						426
Comprehensive income:							
Net income	7,761	7,761	7,572				189
Foreign currency translation adjustment, net of taxes of \$73	(169)	(169)		(88)			(81)
Comprehensive income	7,592	\$ 7,592					
Balance at June 30, 2013	\$ 127,267		\$ (36,089)	\$ 30	\$ 3	\$ 159,991	\$ 3,332

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The tax effects allocated to our other comprehensive loss component, foreign currency translation, were as follows:

(in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Before-tax amount	\$ (245)	\$ (20)	\$ (242)	\$ (6)
Tax benefit	74	6	73	2
Net-of-tax amount	\$ (171)	\$ (14)	\$ (169)	\$ (4)

7. Share-Based Payments

During the first half of 2013, we granted 140,000 stock options under our 2009 Long-Term Incentive Plan. Total share-based compensation expense was \$0.2 million for each of the three months ended June 30, 2013 and 2012, and \$0.4 million and \$0.6 million for the six months ended June 30, 2013 and 2012, respectively, and are reported in corporate, general and administration expenses on our condensed consolidated statements of operations.

8. Net Income (Loss) Per Share Attributable To Gaiam, Inc. Common Shareholders

Basic net income (loss) per share attributable to Gaiam, Inc. common shareholders excludes any dilutive effects of options. We compute basic net income (loss) per share attributable to Gaiam, Inc. common shareholders using the weighted average number of shares of common stock outstanding during the period. We compute diluted net income (loss) per share attributable to Gaiam, Inc. common shareholders using the weighted average number of shares of common stock and common stock equivalents outstanding during the period. We excluded common stock equivalents of 1,544,000 and 1,398,000 for the three months ended June 30, 2013 and 2012, respectively, and 1,531,000 and 1,360,000 for the six months ended June 30, 2013 and 2012, respectively, from the computation of diluted net loss per share attributable to Gaiam, Inc. common shareholders because their effect was antidilutive.

The following table sets forth the computation of basic and diluted net income (loss) per share attributable to Gaiam, Inc. common shareholders:

(in thousands, except per share data)	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Numerator for basic and diluted net income (loss) per share attributable to Gaiam, Inc. common shareholders	\$ 7,848	\$ (2,053)	\$ 7,572	\$ (3,272)
Denominator:				
Weighted average shares for basic net income (loss) per share attributable to Gaiam, Inc. common shareholders	22,741	22,702	22,736	22,700
Effect of dilutive securities:				
Weighted average of common stock and stock options				
Denominators for diluted net income (loss) per share attributable to Gaiam, Inc. common shareholders	22,741	22,702	22,736	22,700
Net income (loss) per share attributable to Gaiam, Inc. common shareholders basic	\$ 0.35	\$ (0.09)	\$ 0.33	\$ (0.14)
Net income (loss) per share attributable to Gaiam, Inc. common shareholders diluted	\$ 0.35	\$ (0.09)	\$ 0.33	\$ (0.14)

9. Income Taxes

Income tax expense for the three and six months ended June 30, 2013 was increased primarily due to the repatriation of cash from one of our foreign subsidiaries and other permanent differences.

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We manage our company and aggregate our operational and financial information in accordance with two reportable segments. The direct to consumer segment contains direct response television marketing, catalog, Internet, retail store and subscription channels; and the business segment comprises retailer, media distribution, and corporate account channels.

Although we are able to track sales by channel, the management, allocation of resources, and analysis and reporting of expenses are presented on a combined basis, at the reportable segment level. Contribution margin is defined as net revenue less cost of goods sold and total operating expenses.

Financial information for our segments is as follows:

(in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net revenue:				
Direct to consumer	\$ 15,270	\$ 16,921	\$ 34,626	\$ 38,491
Business	29,274	28,525	66,551	54,288
Consolidated net revenue	44,544	45,446	101,177	92,779
Contribution loss:				
Direct to consumer	(4,873)	(4,357)	(9,724)	(6,199)
Business	987	2,391	5,989	2,938
Consolidated contribution loss	(3,886)	(1,966)	(3,735)	(3,261)