

Summer Infant, Inc.
Form 10-Q
November 04, 2015
Table of Contents

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 October 3, 2015

o 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 001-33346

Summer Infant, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction
Of Incorporation or Organization)

20-1994619
(IRS Employer Identification No.)

Edgar Filing: Summer Infant, Inc. - Form 10-Q

1275 Park East Drive
Woonsocket, RI 02895
(Address of principal executive offices) (Zip Code)

(401) 671-6550
(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 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
Non-accelerated filer
(Do not check if a smaller reporting company)

Accelerated filer
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 November 2, 2015, there were 18,338,674 shares outstanding of the registrant's Common Stock, \$0.0001 par value per share.

Table of Contents

Summer Infant, Inc.

Form 10-Q

Table of Contents

| | Page Number | |
|--------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------|
| <u>Part 1.</u> | <u>Financial Information</u> | |
| <u>Item 1.</u> | <u>Condensed Consolidated Financial Statements (unaudited)</u> | 1 |
| | <u>Condensed Consolidated Balance Sheets as of October 3, 2015 (unaudited) and January 3, 2015</u> | 1 |
| | <u>Condensed Consolidated Statements of Operations for the Three and Nine Months Ended October 3, 2015 and September 30, 2014 (unaudited)</u> | 2 |
| | <u>Condensed Consolidated Statements of Comprehensive Income (Loss) for the Three and Nine Months Ended October 3, 2015 and September 30, 2014 (unaudited)</u> | 3 |
| | <u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended October 3, 2015 and September 30, 2014 (unaudited)</u> | 4 |
| | <u>Notes to Condensed Consolidated Financial Statements</u> | 5 |
| <u>Item 2.</u> | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 11 |
| <u>Item 3.</u> | <u>Quantitative and Qualitative Disclosures About Market Risk</u> | 16 |
| <u>Item 4.</u> | <u>Controls and Procedures</u> | 16 |
| <u>Part II.</u> | <u>Other Information</u> | |
| <u>Item 1.</u> | <u>Legal Proceedings</u> | 17 |
| <u>Item 1A.</u> | <u>Risk Factors</u> | 17 |
| <u>Item 2.</u> | <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | 17 |
| <u>Item 3.</u> | <u>Defaults Upon Senior Securities</u> | 17 |
| <u>Item 4.</u> | <u>Mine Safety Disclosures</u> | 17 |
| <u>Item 5.</u> | <u>Other Information</u> | 17 |
| <u>Item 6.</u> | <u>Exhibits</u> | 17 |
| <u>Signatures</u> | | 18 |

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. Condensed Consolidated Financial Statements (unaudited)****Summer Infant, Inc. and Subsidiaries****Condensed Consolidated Balance Sheets**

Note that all amounts presented in the table below are in thousands of U.S. dollars, except share and par value amounts.

| | Unaudited October 3, 2015 | January 3, 2015 |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------|----------------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 1,104 | \$ 1,272 |
| Trade receivables, net of allowance for doubtful accounts | 36,057 | 38,794 |
| Inventory, net | 43,622 | 44,010 |
| Prepays and other current assets | 1,777 | 2,076 |
| Deferred tax assets | 1,194 | 1,194 |
| TOTAL CURRENT ASSETS | 83,754 | 87,346 |
| Property and equipment, net | 11,890 | 13,080 |
| Intangible assets, net | 20,326 | 20,679 |
| Other assets | 1,562 | 1,362 |
| TOTAL ASSETS | \$ 117,532 | \$ 122,467 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 31,818 | \$ 21,878 |
| Accrued expenses | 4,756 | 8,628 |
| Current portion of long term debt (including capital leases) | 2,089 | 1,641 |
| TOTAL CURRENT LIABILITIES | 38,663 | 32,147 |
| Long-term debt, less current portion | 51,436 | 57,097 |
| Other liabilities | 2,726 | 2,994 |
| Deferred tax liabilities | 2,418 | 2,378 |
| TOTAL LIABILITIES | 95,243 | 94,616 |
| STOCKHOLDERS' EQUITY | | |
| Preferred Stock, \$0.0001 par value, 1,000,000 authorized, none issued or outstanding at October 3, 2015 and January 3, 2015, respectively | | |
| Common Stock \$0.0001 par value, authorized, issued and outstanding of 49,000,000, 18,610,323, and 18,338,674 at October 3, 2015 and 49,000,000, 18,415,934, and 18,144,285 at January 3, 2015, respectively | 2 | 2 |

Edgar Filing: Summer Infant, Inc. - Form 10-Q

| | | |
|----------------------------------------------------------------------------------------------|------------|------------|
| Treasury Stock at cost (271,649 shares at October 3, 2015 and January 3, 2015, respectively) | (1,283) | (1,283) |
| Additional paid-in capital | 75,701 | 74,954 |
| Accumulated deficit | (49,958) | (44,412) |
| Accumulated other comprehensive loss | (2,173) | (1,410) |
| TOTAL STOCKHOLDERS EQUITY | 22,289 | 27,851 |
| TOTAL LIABILITIES AND STOCKHOLDERS EQUITY | \$ 117,532 | \$ 122,467 |

See notes to condensed consolidated financial statements

Table of Contents**Summer Infant, Inc. and Subsidiaries****Condensed Consolidated Statements of Operations**

Note that all amounts presented in the table below are in thousands of U.S. dollars, except share and per share amounts.

| | Unaudited | | Unaudited | |
|--------------------------------------|-----------------------------------|----------------------|----------------------------------|----------------------|
| | For the three months ended | | For the nine months ended | |
| | October 3, | September 30, | October 3, | September 30, |
| | 2015 | 2014 | 2015 | 2014 |
| Net sales | \$ 50,205 | \$ 51,020 | \$ 155,025 | \$ 154,390 |
| Cost of goods sold | 34,600 | 34,420 | 108,674 | 103,897 |
| Gross profit | 15,605 | 16,600 | 46,351 | 50,493 |
| General & administrative expenses | 12,953 | 10,107 | 35,235 | 29,503 |
| Selling expense | 4,119 | 4,456 | 13,295 | 13,742 |
| Depreciation and amortization | 1,275 | 1,369 | 3,927 | 4,132 |
| Operating (loss) income | (2,742) | 668 | (6,106) | 3,116 |
| Interest expense, net | 589 | 870 | 2,753 | 2,571 |
| (Loss) income before income taxes | (3,331) | (202) | (8,859) | 545 |
| (Benefit) provision for income taxes | (1,500) | (64) | (3,313) | 179 |
| NET (LOSS) INCOME | \$ (1,831) | \$ (138) | \$ (5,546) | \$ 366 |
| Net (loss) income per share: | | | | |
| BASIC | \$ (0.10) | \$ (0.01) | \$ (0.30) | \$ 0.02 |
| DILUTED | \$ (0.10) | \$ (0.01) | \$ (0.30) | \$ 0.02 |
| Weighted average shares outstanding: | | | | |
| BASIC | 18,309,381 | 18,086,441 | 18,239,490 | 18,029,659 |
| DILUTED | 18,309,381 | 18,086,441 | 18,239,490 | 18,196,470 |

See notes to condensed consolidated financial statements.

Table of Contents

Summer Infant, Inc. and Subsidiaries

Condensed Consolidated Statements of Comprehensive (Loss) Income

Note that all amounts presented in the table below are in thousands of U.S. dollars.

| | Unaudited For the three months ended | | Unaudited For the nine months ended | |
|-----------------------------------------------------|--------------------------------------------|-----------------------|-------------------------------------------|-----------------------|
| | October 3, 2015 | September 30, 2014 | October 3, 2015 | September 30, 2014 |
| Net (loss) income | \$ (1,831) | \$ (138) | \$ (5,546) | \$ 366 |
| Other comprehensive loss: | | | | |
| Changes in foreign currency translation adjustments | (371) | (431) | (763) | (144) |
| Comprehensive (loss) income | \$ (2,202) | \$ (569) | \$ (6,309) | \$ 222 |

See notes to condensed consolidated financial statements.

Table of Contents

Summer Infant, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows

Note that all amounts presented in the table below are in thousands of U.S. dollars.

| | Unaudited | |
|---------------------------------------------------------------------------------------------------|----------------------------------|----------------------|
| | For the nine months ended | |
| | October 3, | September 30, |
| | 2015 | 2014 |
| Cash flows from operating activities: | | |
| Net (loss) income | \$ (5,546) | \$ 366 |
| Adjustments to reconcile net income (loss) to net cash (used in) provided by operating activities | | |
| Depreciation and amortization | 3,897 | 4,132 |
| Stock-based compensation expense | 700 | 1,011 |
| Changes in assets and liabilities: | | |
| Decrease (increase) in trade receivables | 2,937 | (3,868) |
| Decrease (increase) in inventory | 630 | (10,527) |
| Decrease in prepaids and other assets | 139 | 160 |
| Increase (decrease) in accounts payable and accrued expenses | 5,720 | 3,614 |
| Net cash provided by (used in) operating activities | 8,477 | (5,112) |
| Cash flows from investing activities: | | |
| Acquisitions of intangible assets | (472) | (227) |
| Acquisitions of property and equipment | (1,875) | (1,976) |
| Net cash used in investing activities | (2,347) | (2,203) |
| Cash flows from financing activities: | | |
| Proceeds from exercise of stock options | 46 | 19 |
| Proceeds from new Term Loan Facility | 10,000 | |
| Proceeds from new FILO Facility | 5,000 | |
| Repayment of Prior Term Loan | (12,500) | (1,125) |
| Net (repayment) borrowings on revolving facilities | (7,712) | 7,861 |

Edgar Filing: Summer Infant, Inc. - Form 10-Q

| | | |
|--------------------------------------------------------------|----------|----------|
| Net cash (used in) provided by financing activities | (5,166) | 6,755 |
| Effect of exchange rate changes on cash and cash equivalents | (1,132) | 62 |
| Net decrease in cash and cash equivalents | (168) | (498) |
| Cash and cash equivalents, beginning of period | 1,272 | 1,573 |
| Cash and cash equivalents, end of period | \$ 1,104 | \$ 1,075 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for interest | \$ 1,818 | \$ 2,106 |
| Cash paid for income taxes | \$ 236 | \$ 23 |

See notes to condensed consolidated financial statements.

Table of Contents

SUMMER INFANT, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

The Company designs, markets and distributes branded juvenile health, safety and wellness products that are sold globally to large national retailers as well as independent retailers, primarily in North America. The Company currently markets its products in several product categories including monitoring, safety, nursery, baby gear, and feeding products. Most products are sold under our core brand names of Summer®, SwaddleMe®, Born Free®, and Kiddopotamus®.

Basis of Presentation and Principles of Consolidation

The accompanying interim, condensed consolidated financial statements of the Company are unaudited, but in the opinion of management, reflect all adjustments, consisting of normal recurring accruals, necessary for a fair presentation of the results for the interim periods. Accordingly, they do not include all information and notes required by generally accepted accounting principles in the United States of America (GAAP) for complete financial statements. The results of operations for interim periods are not necessarily indicative of results to be expected for the entire fiscal year or any other period. The balance sheet at January 3, 2015 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements. These interim condensed consolidated financial statements should be read in conjunction with the Company's consolidated financial statements and notes for the year ended January 3, 2015 included in its Annual Report on Form 10-K filed with the SEC on March 4, 2015.

It is the Company's policy to prepare its financial statements on the accrual basis of accounting in conformity with GAAP. The interim condensed consolidated financial statements include the accounts of its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in the consolidation.

All dollar amounts included in the Notes to Condensed Consolidated Financial Statements are in thousands of U.S. dollars, except share and per share amounts.

Revenue Recognition

The Company records revenue when all of the following occur: persuasive evidence of an arrangement exists, product delivery has occurred, the sales price to the customer is fixed or determinable, and collectability is reasonably assured. Sales are recorded net of provisions for returns and allowances, customer discounts, and other sales-related discounts. The Company bases its estimates for discounts, returns and allowances on negotiated customer terms and historical experience. Customers do not have the right to return products unless the products are defective. The Company records a reduction of sales for estimated future defective product deductions based on contractual terms and historical experience.

Sales incentives or other consideration given by the Company to customers that are considered adjustments to the selling price of the Company's products, such as markdowns, are reflected as reductions of revenue. Sales incentives and other consideration that represent costs incurred by the Company for assets or services received, such as the appearance of the Company's products in a customer's national circular ad, are reflected as selling expenses in the accompanying interim Condensed Consolidated Statements of Operations.

Inventory Valuation

Inventory is comprised mostly of finished goods and some component parts and is stated at the lower of cost using the first-in, first-out (FIFO) method, or market (net realizable value). The Company regularly reviews slow-moving and excess inventories, and writes down inventories to net realizable value if the ultimate expected net proceeds from the disposals of excess inventory are less than the carrying cost of the merchandise.

Income Taxes

Income taxes are computed using the asset and liability method of accounting. Under the asset and liability method, a deferred income tax asset or liability is recognized for estimated future tax effects attributable to temporary differences and carry-forwards. The

Table of Contents

measurement of deferred income tax assets is adjusted by a valuation allowance, if necessary, to recognize future tax benefits only to the extent, based on available evidence, that it is more likely than not that such benefits will be realized.

Tax positions must meet a more-likely-than-not recognition threshold at the effective date to be recognized upon adoption and in subsequent periods. As of October 3, 2015 and January 3, 2015, the Company did not have any material uncertain tax positions. No interest and penalties related to uncertain tax positions were accrued at October 3, 2015 and January 3, 2015.

Use of Estimates

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. These estimates are based on management's best knowledge of current events and actions the Company may undertake in the future. Accordingly, actual results could differ from those estimates.

Net Income (Loss) Per Share

Basic earnings (loss) per share for the Company are computed by dividing net income (loss) by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings (loss) per share includes the dilutive impact of outstanding stock options and unvested restricted shares.

Translation of Foreign Currencies

All assets and liabilities of the Company's foreign subsidiaries, each of whose functional currency is in its local currency, are translated into U.S. dollars at the exchange rate in effect at the end of the quarter and the income and expense accounts of these affiliates have been translated at average rates prevailing during each respective quarter. Resulting translation adjustments are made to a separate component of stockholders equity within accumulated other comprehensive income or loss.

Recently Issued Accounting Pronouncements

In May 2014, the FASB issued new accounting guidance related to revenue recognition. This guidance was originally proposed to be effective for reporting periods beginning after December 15, 2016, however in July 2015, the FASB approved the delay in this guidance until reporting periods beginning after December 15, 2017. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements.

Edgar Filing: Summer Infant, Inc. - Form 10-Q

In April 2015, the FASB issues ASU 2015-03, Interest-Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. This guidance requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability. This guidance is effective for fiscal years beginning after December 15, 2015. The Company has evaluated the impact this guidance will have on its consolidated financial statements and expects the impact to be immaterial.

In July 2015, the FASB issued ASU 2015-11, Simplifying the Measurement of Inventory. This guidance required inventory within the scope of ASU 2015-11 to be measured at the lower of cost and net realizable value. Net realizable value is defined as the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. This guidance is effective for fiscal years beginning after December 15, 2016. The Company is currently evaluating the impact this guidance will have on its consolidated financial statements.

2. DEBT

Credit Facilities

In April 2015, the Company and its wholly owned subsidiary, Summer Infant (USA), Inc., entered into an amended and restated loan and security agreement with Bank of America, N.A., as agent, providing for an asset-based credit facility (the Credit Facility). The Credit Facility replaced the Company's prior credit facility with Bank of America.

The Credit Facility consists of a \$60,000 asset-based revolving credit facility, with a \$10,000 letter of credit sub-line facility (the Revolving Facility), a \$5,000 first in last out (FILO) revolving credit facility (the FILO Facility) and a \$10,000 term loan facility (the Term Loan Facility). Pursuant to an accordion feature, the Credit Facility includes the ability to increase the Revolving Facility by an additional \$15,000 upon the Company's request and the agreement of the lenders participating in the increase. The total borrowing capacity under the Revolving Facility is based on a borrowing base, generally defined as 85% of the value of eligible accounts plus the lesser of (i) 70% of the value of eligible inventory or (ii) 85% of the net orderly liquidation value of eligible inventory, less reserves. The total borrowing capacity under the FILO Facility is based on a borrowing base, generally defined as a

Table of Contents

specified percentage of the value of eligible accounts that steps down over time, plus a specified percentage of the value of eligible inventory that steps down over time.

The scheduled maturity date of the loans under the Revolving Facility and the Term Loan Facility is April 21, 2020, and loans under the FILO Facility terminate April 21, 2018, subject in each case to customary early termination provisions. Any termination of the Revolving Facility would require termination of the Term Loan Facility and the FILO Facility.

All obligations under the Credit Facility are secured by substantially all of the Company's assets. In addition, Summer Infant Canada Limited and Summer Infant Europe Limited, subsidiaries of the Company, are guarantors under the Credit Facility. Proceeds from the loans were used to (i) repay the Company's outstanding term loan, (ii) pay fees and transaction expenses associated with the closing of the Credit Facility, (iii) pay obligations under the Credit Facility, and (iv) pay for lawful corporate purposes, including working capital.

Borrowings under the Revolving Facility will bear interest, at the Company's option, at a base rate or at LIBOR, plus applicable margins based on average quarterly availability and ranging between 1.75% and 2.25% on LIBOR borrowings and 0.25% and 0.75% on base rate borrowings. Loans under the FILO Facility and Term Loan Facility will bear interest, at the Company's option, at a base rate or at LIBOR, plus a margin of 4.00% on LIBOR borrowings and 2.50% on base rate borrowings.

Beginning on July 1, 2015, the Company is required to repay the Term Loan Facility in quarterly installments of \$500. Beginning with the fiscal year ending January 2, 2016, the Company is required to prepay the Term Loan Facility in an amount equal to 50% of the Company's excess cash flow, as such term is defined in the Credit Facility, at the end of each fiscal year.

Under the Credit Facility, the Company must comply with certain financial covenants, including that the Company (i) maintain a fixed charge coverage ratio of at least 1.0 to 1.0 for the twelve consecutive fiscal months most recently ended and (ii) beginning with the quarter ending July 4, 2015, maintain a certain leverage ratio at the end of each fiscal quarter. For purposes of the financial covenants, consolidated EBITDA is defined as net income before interest, taxes, depreciation and amortization, plus certain customary expenses, fees, non-cash charges and up to \$2,000 of specified inventory dispositions, and minus certain customary non-cash items increasing net income and other specified items.

The Credit Facility contains customary affirmative and negative covenants. Among other restrictions, the Company is restricted in its ability to incur additional debt, make acquisitions or investments, dispose of assets, or make distributions unless in each case certain conditions are satisfied. The Credit Facility also contains customary events of default, including the occurrence of a material adverse event and the occurrence of a change of control. In the event of a default, all of the Company's obligations under the Credit Facility may be declared immediately due and payable. For certain events of default relating to insolvency and receivership, all outstanding obligations immediately become due and payable.

As of October 3, 2015, the base rate on loans was 4.0% and the LIBOR rate was 2.5%. The amount outstanding on the Revolving Facility at October 3, 2015 was \$39,430. Total borrowing capacity under the Revolving Facility at October 3, 2015 was \$49,372 and borrowing availability was \$9,942. The amounts outstanding on the Term Loan Facility and FILO Facility at October 3, 2015 were \$9,000 and \$5,000, respectively.

Prior Credit Facility and Term Loan.

The Credit Facility replaced the Company's prior credit facility with Bank of America and the Company's prior term loan agreement with Salus Capital Partners, LLC. Prior to April 2015, the Company had a loan and security agreement with Bank of America N.A. that provided for an \$80,000, asset-based revolving credit facility, with a \$10,000 letter of credit sub-line facility.

The Credit Facility was evaluated, by lender, to determine the proper accounting treatment for the transaction. Accordingly, debt extinguishment accounting was used to account for the pay off of the prior term loan agreement with Salus Capital Partners, LLC and for the pay off of a member of the prior credit facility with Bank of America who did not continue in the Credit Facility resulting in the write off of \$549 in remaining unamortized deferred financing costs and \$135 in termination fees. Debt modification accounting was used for the remaining members of the prior credit facility resulting in their remaining unamortized deferred financing costs of \$601 and the new financing costs of \$1,054 to be capitalized and amortized over the life of the new debt beginning in the second quarter of 2015.

Table of Contents

Aggregate maturities of bank debt related to the Credit Facility are as follows:

| | | | |
|--------------|-------|----|--------|
| Year ending: | 2015 | \$ | 500 |
| | 2016 | | 3,250 |
| | 2017 | | 4,500 |
| | 2018 | | 3,250 |
| | 2019 | | 2,000 |
| | 2020 | | 39,930 |
| | Total | \$ | 53,430 |

Lease Amendment

On May 13, 2015, Summer Infant (USA), Inc. (Summer USA), a wholly-owned subsidiary of the Company, entered into an amendment (the Amendment) to its lease dated March 24, 2009 (the Lease) with Faith Realty II, LLC (the Landlord), a company which is owned by Jason Macari, former CEO and director of Summer Infant, Inc. and his spouse. Pursuant to the terms of the original Lease, the Landlord leased the property located at 1275 Park East Drive, Woonsocket, Rhode Island to Summer USA for an annual rent of \$390 for an initial seven-year term. Pursuant to the Amendment, (i) the initial term of the Lease was extended for two additional years, such that the initial term now ends on March 31, 2018, and the term of the Lease may be extended at Summer USA 's election for one additional term of three years (rather than five years) upon twelve months ' prior notice, (ii) the annual rent for the last two years of the newly amended initial term was set at \$429 and the annual rent for the extension period, if elected, was set at \$468 and (iii) the Landlord agreed to provide an aggregate improvement allowance of not more than \$78 for the newly amended initial term, to be applied against Summer USA 's monthly rent, and an additional improvement allowance of \$234 for the extension term, if elected, to be applied against Summer USA 's monthly rent during such extension term. The Amendment was reviewed and approved by the audit committee because it was a related party transaction.

3. INTANGIBLE ASSETS

Intangible assets consisted of the following:

| | October 3, 2015 | January 3, 2015 |
|--------------------------------|--------------------|--------------------|
| Brand names | \$ 14,812 | \$ 14,812 |
| Patents and licenses | 4,073 | 3,605 |
| Customer relationships | 6,946 | 6,946 |
| Other intangibles | 1,886 | 1,882 |
| | 27,717 | 27,245 |
| Less: Accumulated amortization | (7,391) | (6,566) |
| Intangible assets, net | \$ 20,326 | \$ 20,679 |

The amortization period for the majority of the intangible assets ranges from 5 to 20 years for those assets that have an estimated life; certain of the assets have indefinite lives (brand names). Total of intangibles not subject to amortization amounted to \$12,308 as of October 3, 2015 and January 3, 2015.

4. COMMITMENTS AND CONTINGENCIES

Litigation

The Company is a party to routine litigation and administrative complaints incidental to its business. The Company does not believe that the resolution of any or all of such routine litigation and administrative complaints is likely to have a material adverse effect on the Company's financial condition or results of operations, except as noted below.

On May 27, 2015, the Company filed a Complaint against Carol E. Bramson, Annamaria Dooley, Kenneth N. Price, Carson J. Darling, Dulcie M. Madden, and Bruce Work in the United States District Court for the District of Rhode Island (Civil Action No. 1:15-CV-00218-5-LDA). The Complaint alleges theft and misappropriation of the Company's confidential and proprietary trade secrets, intellectual property, and business, branding and marketing strategies. Ms. Bramson is a former member of the Company's Board of Directors and the Company's former Chief Executive Officer, Ms. Dooley is the Company's former Senior Vice President of Product Development, and Mr. Price is the former President of Global Sales & Marketing of the Company. Mr. Darling and Ms. Madden are principals of Rest Devices, Inc., a former consultant to the Company (the Rest Defendants). The Complaint alleges violation of trade secrets, misappropriation of confidential information, breaches of fiduciary duties by Mmes. Bramson and Dooley and Mr. Price, conversion, breaches of contract by Mmes. Bramson and Dooley and Mr. Price, tortious interference with employment agreements, consulting agreements, and prospective business relations, unjust enrichment and other related claims, and seeks injunctive relief, return of the Company's confidential and proprietary information, as well as other relief including compensatory damages.

Table of Contents

On June 23, 2015, the Rest Defendants filed a motion to dismiss the claims against them set forth in the Complaint, and the Company filed its opposition to the motion on July 3, 2015. On July 3, 2015, Mr. Price filed a motion to dismiss the claims against him set forth in the Complaint, and the Company filed its opposition to the motion on July 20, 2015. The Court has not yet ruled on Mr. Price's motion to dismiss. On July 3, 2015, Mmes. Bramson and Dooley filed an answer to the Complaint, and asserted counterclaims against the Company, including (i) a claim by Ms. Bramson for contractual indemnification and (ii) claims by Mmes. Bramson and Dooley for indemnification under the Company's bylaws, tortious interference with prospective business relations, unfair and deceptive trade practices and abuse of process. The Company filed a motion to dismiss certain counterclaims made by Mmes. Bramson and Dooley on July 27, 2015. Mmes. Bramson and Dooley filed an opposition to the Company's motion to dismiss their counterclaims on October 8, 2015, and the Company filed its reply on October 22, 2015. The Court has not yet ruled on the Company's motion to dismiss. In August 2015, the Court granted Ms. Bramson's motion for advancement of certain indemnification expenses.

On August 25, 2015, the Company and the Rest Defendants reached an agreement-in-principle with regard to a proposed settlement, and the Company subsequently withdrew its motion for a preliminary injunction. Following negotiation, as of November 1, 2015, the Company and the Rest Defendants entered into a confidential settlement agreement (the Settlement Agreement) pursuant to which the Company and the Rest Defendants mutually released claims against each other, and the Company has voluntarily dismissed all claims in the Complaint against the Rest Defendants.

The Settlement Agreement did not release any claims against Mmes. Bramson or Dooley or Mr. Price, and the Company intends to continue to vigorously pursue this matter with respect to the remaining defendants and to protect its confidential and proprietary information. The Company has incurred significant expenses related to this lawsuit to date and may continue to incur expenses related to this lawsuit. The Company is also reviewing its accounting treatment of \$315 in capitalized technology development costs incurred during its consulting agreement with Rest Devices, Inc. in light of the Settlement Agreement. The Company cannot predict the outcome of this lawsuit or for how long it will remain active.

5. SHARE BASED COMPENSATION

The Company is authorized to issue up to 3,000,000 shares for equity awards under the Company's 2006 Performance Equity Plan (2006 Plan) and 1,700,000 shares for equity awards under the Company's 2012 Incentive Compensation Plan (2012 Plan). The Company's stockholders approved an increase in the number of shares available under the 2012 Plan from 1,100,000 to 1,700,000 shares on August 4, 2015.

Under the 2006 Plan and 2012 Plan, awards may be granted to participants in the form of non-qualified stock options, incentive stock options, restricted stock, deferred stock, restricted stock units and other stock-based awards. Subject to the provisions of the plans, awards may be granted to employees, officers, directors, advisors and consultants who are deemed to have rendered or are able to render significant services to the Company or its subsidiaries and who are deemed to have contributed or to have the potential to contribute to the Company's success. The Company accounts for options under the fair value recognition standard. The application of this standard resulted in share-based compensation expense for the three months ended October 3, 2015 and September 30, 2014 of \$280 and \$468, respectively, and share-based compensation expense for the nine months ended October 3, 2015 and September 30, 2014 of \$700 and \$1,011, respectively. Share based compensation expense is included in selling, general and administrative expenses.

The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model that uses the assumptions noted in the table below. The Company uses the simplified method to estimate the expected term of the options, but used an estimate for grants of plain vanilla stock options based on a formula prescribed by the Securities and Exchange Commission. Forfeitures are estimated at the time of

Edgar Filing: Summer Infant, Inc. - Form 10-Q

grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Share-based compensation expense recognized in the consolidated financial statements in 2015 and 2014 is based on awards that are ultimately expected to vest.

As of October 3, 2015, there were 2,005,533 stock options outstanding and 234,268 unvested restricted shares outstanding.

During the nine months ended October 3, 2015, the Company granted 485,750 stock options and granted 216,135 shares of restricted stock. The following table summarizes the weighted average assumptions used for stock options granted during the periods ended October 3, 2015 and September 30, 2014.

Table of Contents

| | 2015 | 2014 |
|--------------------------|-------------|-------------|
| Expected life (in years) | 5.3 | 5.3 |
| Risk-free interest rate | 1.6% | 1.7% |
| Volatility | 67.4% | 67.0% |
| Dividend yield | 0.0% | 0.0% |
| Forfeiture rate | 16.5% | 13.3% |

As of October 3, 2015, there are 139,961 shares available to grant under the 2006 Plan and 806,000 shares available to grant under the 2012 Plan.

6. **WEIGHTED AVERAGE COMMON SHARES**

Basic and diluted earnings or loss per share (EPS) is based upon the weighted average number of common shares outstanding during the period. The Company does not include the anti-dilutive effect of common stock equivalents, including stock options, in computing net income (loss) per diluted common share. The computation of diluted common shares for the three months and nine months ended October 3, 2015 excluded 2,005,533 stock options and 234,268 shares of restricted stock outstanding.

7. **SUBSEQUENT EVENTS**

The Company has evaluated subsequent events through the filing date of this Quarterly Report and determined that no subsequent events occurred that would require recognition in the consolidated financial statements or disclosure in the notes thereto.

Table of Contents

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking information and statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). All forward-looking statements included in this document are based on information available to us on the date hereof. It is important to note that our actual results could differ materially from those projected in such forward-looking statements contained in this Quarterly Report on Form 10-Q. These forward-looking statements include statements concerning our expectations regarding our business strategy and future growth and profitability; our ability to deliver high quality, innovative products to the marketplace; our ability to maintain and build upon our existing customer and supplier relationships; our ability to build awareness of our core brands; our ability to manage expenses and reduce costs; and our ability to realize savings from our amended credit facility. These statements are based on current expectations that involve numerous risks and uncertainties. These risks and uncertainties include the concentration of our business with retail customers; the financial status of our customers and their ability to pay us in a timely manner; our ability to introduce new products or improve existing products that satisfy consumer preferences; our ability to develop new or improved products in a timely and cost-efficient manner; our ability to compete with larger and more financially stable companies in our markets; our ability to comply with financial and other covenants in our debt agreements; our dependence on key personnel; our reliance on foreign suppliers and potential disruption in foreign markets in which we operate; increases in the cost of raw materials used to manufacture our products; compliance with safety and testing regulations for our products; increases in legal expenses and costs associated with ongoing litigation; product liability claims arising from use of our products; unanticipated tax liabilities; an impairment of other intangible assets; and other risks as detailed in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended January 3, 2015 and subsequent filings with the Securities and Exchange Commission. All these matters are difficult or impossible to predict accurately, many of which may be beyond our control. Although we believe that the assumptions underlying our forward-looking statements are reasonable, any of the assumptions could be inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Quarterly Report on Form 10-Q will prove to be accurate.

The following discussion is intended to assist in the assessment of significant changes and trends related to the results of operations and financial condition of our Company and our consolidated subsidiaries. This Management's Discussion and Analysis should be read together with the unaudited interim condensed consolidated financial statements and related notes included elsewhere in this filing and with our consolidated financial statements for the year ended January 3, 2015 included in our Annual Report on Form 10-K for the year ended January 3, 2015.

Note that all dollar amounts in this section are in thousands of U.S. dollars, except share and per share data.

In 2014, our Board of Directors approved a change in our fiscal year, from a fiscal year ending on December 31 of each calendar year to a fiscal year ending on the Saturday closest to December 31 of each calendar year. This change was effective with the 2014 fiscal year. The following discussions compare the unaudited periods of the first, second, and third quarters of 2015 ended April 4, 2015 and July 4, 2015, and October 3, 2015, respectively, to our fiscal 2014 first, second, and third quarters ended March 31, 2014 and June 30, 2014, and September 30, 2014, respectively. As a result of the change in our fiscal year end, the quarterly periods of our newly adopted fiscal year do not entirely coincide with the historical quarterly periods that we had previously reported. We believe the comparative information provided for the three-month period and the nine-month period ended September 30, 2014 provides a meaningful comparison to the three-month period and the nine-month period ended October 3, 2015 and there are no factors, seasonal or otherwise, that materially impact the comparability of information or trends.

Overview

Edgar Filing: Summer Infant, Inc. - Form 10-Q

We are a premier infant and juvenile products company originally founded in 1985 and have publicly traded on the Nasdaq Stock Market since 2007 under the symbol SUMR. We create branded juvenile safety and infant care products (targeted for ages 0-3 years) that are intended to deliver a diverse range of parenting solutions to families. We focus on providing innovative products to meet the lifestyle and demands of families who seek more opportunities to connect with their children.

We operate in one principal industry segment across geographically diverse marketplaces, selling our products globally to large, national retailers as well as independent retailers, and on the internet through third-party websites and our own www.SummerInfant.com website. In North America, our customers include Babies R Us, Wal-Mart, Target, Amazon.com, Buy Buy Baby, Burlington Coat Factory, Kmart, Home Depot, and Lowe's. Our largest European-based customers are Mothercare, Toys R Us, Argos and Tesco. We also sell through international distributors, representatives, and to select international retail customers in geographic locations where we do not have a direct sales presence.

The juvenile products industry is estimated to be a \$20 billion market worldwide, and consumer focus is on quality, safety, innovation, and style. Due to the halo effect of baby products in retail stores, there is a strong retailer commitment to the juvenile

Table of Contents

category. We believe we are positioned to capitalize on positive market trends in the juvenile products industry, including a predicted increase in U.S. birth rates over the next several years.

During the third quarter of 2015, we continued to focus on our core product offerings, phasing out less profitable categories, liquidating related inventory, and improving our balance sheet and working capital positions. As we executed these initiatives, sales declined for the three months ended October 3, 2015 by 1.6% and increased 0.4% for the nine months ended October 3, 2015 and the liquidation of related inventory combined with the unfavorable effect of currency exchange rates (primarily on Canadian sales) led to gross margin declines of 6.0% and 8.2%, respectively, as compared to the same prior year periods. We do not expect that these efforts will continue to negatively impact our income statement in fourth quarter as they did in the second and third quarter.

Excluding \$11,681 and \$5,427 of sales related of non-core business in licensed, private label, and furniture sales for the first nine months of 2014 and 2015 as well \$2,466 of unfavorable foreign exchange impact on our international sales on a constant currency basis, our core branded sales increased by 6.6%. This increase in our core branded business, namely our Summer®, SwaddleMe®, and BornFree® branded products, was primarily attributable to increased sales of our 3D Lite Convenience Strollers, Pop n Play Portable Playards, gates and bath products. Constant currency basis is determined by applying a fixed exchange rate, calculated as the 12-month average in 2014, to the current local currency sales amounts, with the difference in reported sales being attributable to currency.

General and administrative expenses were negatively inflated during the first nine months of 2015 by legal costs associated with a complaint filed on May 27, 2015 as further described below under Legal Proceedings (the Complaint), added costs associated with the port slowdown in the first quarter, employee terminations, and investment in marketing and new product development. As a result, we ended the first nine months of 2015 with a net loss of \$0.30 per share.

As we continue to work to improve our balance sheet and improve working capital, we have reduced excess inventory, including selling inventory at below cost, which has negatively impacted our income statement and depressed margins in the second and third quarter. We also continue to focus on our core categories and phase out less profitable categories. We do not expect that the above efforts will continue to negatively impact our income statement in fourth quarter as they did in the second and third quarter. However, we do expect to continue to incur legal expenses in connection with the Complaint, albeit at a lower level than in the second and third quarters, which will increase our general and administrative expenses. We cannot predict the outcome of this lawsuit or for how long it will remain active. In July, we initiated cost reduction efforts to partially offset these losses.

Summary of Critical Accounting Policies and Estimates

There have been no significant changes in our critical accounting policies and estimates during the three months ended October 3, 2015 from our critical accounting policies and estimates disclosed under Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended January 3, 2015.

Results of Operations

| | For the three months ended (Unaudited) | | For the nine months ended (Unaudited) | |
|-----------------------------------------------------------|-------------------------------------------|-----------------------|------------------------------------------|-----------------------|
| | October 3, 2015 | September 30, 2014 | October 3, 2015 | September 30, 2014 |
| Net sales | \$ 50,205 | \$ 51,020 | \$ 155,025 | \$ 154,390 |
| Cost of goods sold | 34,600 | 34,420 | 108,674 | 103,897 |
| Gross profit | 15,605 | 16,600 | 46,351 | 50,493 |
| General & administrative expense | 12,953 | 10,107 | 35,235 | 29,503 |
| Selling expense | 4,119 | 4,456 | 13,295 | 13,742 |
| Depreciation and amortization | 1,275 | 1,369 | 3,927 | 4,132 |
| Operating (loss) income | (2,742) | 668 | (6,106) | 3,116 |
| Interest expense, net | 589 | 870 | 2,753 | 2,571 |
| (Loss) income before (benefit) provision for income taxes | (3,331) | (202) | (8,859) | 545 |
| (Benefit) provision for income taxes | (1,500) | (64) | (3,313) | 179 |
| Net (loss) income | \$ (1,831) | \$ (138) | \$ (5,546) | \$ 366 |

Three Months ended October 3, 2015 compared with Three Months ended September 30, 2014

Net sales declined 1.6% from \$51,020 for the three months ended September 30, 2014 to \$50,205 for the three months ended October 3, 2015, primarily as a result of our exiting non-core business in licensed, private label, and furniture categories as well as the unfavorable effect of a strengthening U.S. dollar. Excluding \$2,733 and \$1,530 of sales related to non-core business in licensed, private label, and furniture sales in fiscal 2014 and 2015, respectively, as well as \$838 unfavorable foreign exchange effect on a constant currency basis, our core branded sales increased by 2.5% in the third quarter of 2015. This increase in our core branded business, namely our Summer®,

Table of Contents

SwaddleMe®, and BornFree® branded products, was primarily attributable to increased sales of our 3D Lite Convenience Strollers, gates, and bath products.

Cost of goods sold included the cost of the finished product from suppliers, duties on certain imported items, freight-in from suppliers, and miscellaneous charges. The components of cost of goods sold remained relatively the same for the quarter ended October 3, 2015 as compared to the quarter ended September 30, 2014.

Gross profit decreased 6.0% from \$16,600 for the quarter ended September 30, 2014 to \$15,605 for the quarter ended October 3, 2015. Gross margin decreased from 32.5% for the quarter ended September 30, 2014 to 31.1% for the quarter ended October 3, 2015. The decline in gross margin dollars and as a percent of sales was primarily due to \$103 in losses on the sale of inventory below cost relating to our bank-approved inventory reduction plan, \$215 of inventory charges taken as we completed our exit of the furniture category, \$280 in temporary additional costs due to inventory mix changes in our west coast distribution center, and a \$536 unfavorable foreign exchange effect on a constant currency basis, primarily due to the decline in the value of the Canadian dollar. Excluding the impact of the above charges, gross margin as a percent of net sales for the third quarter of 2015 would have been 33.8%.

General and administrative expenses increased 28.2% from \$10,107 for the quarter ended September 30, 2014 to \$12,953 for the quarter ended October 3, 2015. General and administrative expenses also increased as a percent of sales from 19.8% for the quarter ended September 30, 2014 to 25.8% for the quarter ended October 3, 2015. The increase in general and administrative expense dollars and as a percent of net sales was primarily attributable to \$3,720 of legal costs incurred in connection with the Complaint, as further described below under Legal Proceedings. Excluding these legal fees, general and administrative expenses would have been \$9,233 for the 2015 quarter, down 8.6% from prior year quarter and 18.4% as a percent of sales.

Selling expenses decreased 7.6% from \$4,456 for the quarter ended September 30, 2014 to \$4,119 for the quarter ended October 3, 2015. Selling expenses also decreased as a percent of sales from 8.7% for the quarter ended September 30, 2014 to 8.2% for the quarter ended October 3, 2015. This decrease in dollars and as a percent of sales for the quarter ended October 3, 2015 was primarily attributable to lower sales during the quarter as well as cost controls implemented over retailer programs such as cooperative advertising and lower royalty costs under licensing agreements as part of discontinuing certain licensing arrangements.

Depreciation and amortization decreased 6.9% from \$1,369 in the quarter ended September 30, 2014 to \$1,275 for the quarter ended October 3, 2015. The decrease in depreciation is attributable to a reduction in capital investment partially offset by higher amortization on new finite-lived intangible capitalized assets.

Interest expense decreased 32.3% from \$870 in the quarter ended September 30, 2014 to \$589 for the quarter ended October 3, 2015. The Company refinanced its credit facilities in April of this year which has resulted in lower interest rates on our credit facilities.

For the quarter ended September 30, 2014, we recorded a \$64 tax benefit for income taxes on \$202 of pretax loss, reflecting an estimated 31.7% tax rate for the quarter. For the quarter ended October 3, 2015, we recorded a \$1,500 tax benefit on \$3,331 of pretax loss for the quarter, reflecting an estimated 45.0% tax rate for the quarter. The increase in the rate for 2015 is primarily attributable to the increase in pretax loss for the quarter.

Nine Months ended October 3, 2015 compared with Nine Months ended September 30, 2014

Net sales increased 0.4% from \$154,390 for the nine months ended September 30, 2014 to \$155,025 for the nine months ended October 3, 2015, as net sales were impacted by our focus on our core branded business and exiting non-core business in licensing, private label, and furniture categories, as well as the unfavorable effect of a strengthening U.S. dollar. Excluding \$11,681 and \$5,427 of sales related to non-core business in licensed, private label, and furniture sales in fiscal 2014 and 2015, respectively, as well as \$2,466 unfavorable foreign exchange effect on a constant currency basis, our core branded sales increased by 6.6% in the 2015 period. This increase in our core branded business, namely our Summer®, SwaddleMe®, and BornFree® branded products, was primarily attributable to increased sales of our 3D Lite Convenience Strollers, Pop n Play Portable Playards, gates and bath products.

Cost of goods sold included the cost of the finished product from suppliers, duties on certain imported items, freight-in from suppliers, and miscellaneous charges. The components of cost of goods sold remained relatively the same for the nine months ended October 3, 2015 as compared to the quarter ended September 30, 2014.

Gross profit decreased 8.2% from \$50,493 for the nine months ended September 30, 2014 to \$46,351 for the nine months ended October 3, 2015. Gross margin decreased from 32.7% for the nine months ended September 30, 2014 to 29.9% for the nine months ended October 3, 2015. The decline in gross margin dollars and as a percent of sales was primarily due to \$1,877 in losses on the sale of inventory below cost relating primarily to our bank-approved inventory reduction plan, \$949 inventory charges taken as we completed our exit of the furniture category, \$312 in temporary additional costs due to inventory mix changes in our west coast distribution center, and a \$1,535 unfavorable foreign exchange effect on a constant currency basis, primarily due to the decline in the value of the Canadian dollar. Excluding the impact of the above charges, gross margin as a percent of net sales for the nine months of 2015 would have been 33.6%.

General and administrative expenses increased 19.4% from \$29,503 for the nine months ended September 30, 2014 to \$35,235 for the nine months ended October 3, 2015. General and administrative expense increased as a percent of sales from 19.1% for the nine months ended September 30, 2014 to 22.7% for the nine months ended October 3, 2015. The increase in general and

Table of Contents

administrative expense dollars and as a percent of net sales is primarily attributable to \$5,329 in legal costs incurred in connection with the Complaint, as further described below under Legal Proceedings, an employee termination that was settled in the second quarter of 2015, as well as additional costs incurred in the first quarter of 2015 to manage operations during the recent west coast port slowdown and ongoing investments in marketing and new product development.

Selling expenses decreased 3.3% from \$13,742 for the nine months ended September 30, 2014 to \$13,295 for the nine months ended October 3, 2015. Selling expenses also decreased as a percent of sales from 8.9% for the nine months ended September 30, 2014 to 8.6% for the nine months ended October 3, 2015. This decrease in dollars and as a percent of sales for the nine months ended October 3, 2015 was primarily attributable to continuing cost controls implemented over retailer programs such as cooperative advertising and lower royalty costs under licensing agreements as part of discontinuing certain licensing arrangements.

Depreciation and amortization decreased 5.0% from \$4,132 in the nine months ended September 30, 2014 to \$3,927 for the nine months ended October 3, 2015. The decrease in depreciation is attributable to a reduction in capital investment partially offset by higher amortization on new finite-lived intangible assets capitalized.

Interest expense increased 7.1% from \$2,571 in the nine months ended September 30, 2014 to \$2,753 for the nine months ended October 3, 2015. The Company refinanced its credit facilities in April of this year which resulted in lower interest rates on our new credit facilities. However, the refinancing resulted in a non cash write off of \$685 of past unamortized financing fees and termination fees.

For the nine months ended September 30, 2014, we recorded a \$179 tax provision for income taxes on \$545 of pretax income for the period resulting in an estimated tax rate of 32.8% for the period. For the nine months ended October 3, 2015, we recorded a \$3,313 tax benefit on \$8,859 of pretax loss for the period resulting in an estimated tax rate of 37.4% for the period. The increase in the rate for 2015 is primarily attributable to the increase in pretax loss for the period.

Liquidity and Capital Resources

We fund our operations and working capital needs through cash generated from operations and borrowings under our credit facilities.

In our typical operational cash flow cycle, inventory is purchased in US dollars to meet expected demand plus a safety stock. Because the majority of our suppliers are based in Asia, inventory takes from three to four weeks to arrive from Asia to the various distribution points we maintain in the United States, Canada and the United Kingdom. Payment terms for these vendors are approximately 60-90 days from the date the product ships from Asia, therefore we are generally paying for the product a short time after it is physically received in the United States. In turn, sales to customers generally have payment terms of 30 to 60 days, resulting in an accounts receivable and increasing the amount of cash required to fund working capital. To bridge the gap between paying our suppliers and receiving payment from our customers for goods sold, we rely on our credit facilities.

Edgar Filing: Summer Infant, Inc. - Form 10-Q

The majority of our capital expenditures are for tools and molds related to new product introductions. We receive indications from retailers generally around the middle of each year as to what products the retailer will be taking into its product line for the upcoming year. Based on these indications, we will then acquire the tools and molds required to build and produce the products. In most cases, the payments for the tools are spread out over a three to four month period.

For the nine months ending October 3, 2015, net cash provided by operating activities totaled \$8,477. For the nine months ended September 30, 2014, net cash used by operating activities totaled \$5,112. The increase in net cash generated from operating activities for the nine months ended October 3, 2015 as compared to the same period in the prior year is primarily attributable to a reduction in inventory of \$5,058.

For the nine months ended October 3, 2015, net cash used in investing activities was approximately \$2,347. For the nine months ending September 30, 2014, net cash used in investing activities was \$2,203. The use of cash in both periods was primarily for tooling and technology related to new product introductions.

For the nine months ended October 3, 2015, net cash used in financing activities was approximately \$5,166, reflecting the use of proceeds from operating activities as well as \$10,000 from our new Term Loan Facility, and \$5,000 from our new FILO Loan Facility to repay \$12,500 of our prior Term Loan and \$7,712 of our revolving credit facilities. For the nine months ended September 30, 2014, net cash provided by financing activities was \$6,755. These funds were used to pay for the added inventory during the nine months ended September 30, 2014.

Based primarily on the above factors, net cash decreased for the nine months ended October 3, 2015 by \$168, resulting in a cash balance of approximately \$1,104 at October 3, 2015.

Table of Contents

Capital Resources

In addition to operating cash flow, we also rely on our asset-based revolving credit facility with Bank of America, N.A. to meet our financing requirements, which are subject to changes in our inventory and account receivable levels, and which we amended and restated in April 2015. We regularly evaluate market conditions, our liquidity profile, and various financing alternatives for opportunities to enhance our capital structure. Based on past performance and current expectations, we believe that our anticipated cash flow from operations and availability under our existing credit facility are sufficient to fund our working capital, capital expenditures and debt service requirements for at least the next 12 months.

However, if we are unable to meet our current financial forecast or to manage our legal and other general and administrative costs and expenses and cannot raise additional funds or adjust our operations accordingly, we may not remain in compliance with the financial covenants required under our credit facility. Unforeseen circumstances, such as softness in the retail industry or deterioration in the business of a significant customer, could create a situation where we cannot access all of our available lines of credit due to not having sufficient assets or fixed charge coverage ratio as required under our credit facility. There is no assurance that we will meet all of our financial or other covenants in the future, or that our lenders will grant waivers if there are covenant violations. In addition, should we need to raise additional funds through additional debt or equity financings, any sale of additional debt or equity securities may cause dilution to existing stockholders. If sufficient funds are not available or are not available on acceptable terms, our ability to address any unexpected changes in our operations could be limited. Furthermore, there can be no assurance that we will be able to raise such funds if and when they are required. Failure to obtain future funding when needed or on acceptable terms could materially adversely affect our results of operations.

Credit Facilities

The following is a summary of our credit facility currently in place. Additional information about the credit facility and our prior credit facility may be found in Note 2 to our Condensed Consolidated Financial Statements included in this report.

In April 2015, we and our wholly owned subsidiary, Summer Infant (USA), Inc., entered into an amended and restated loan and security agreement with Bank of America, N.A., as agent, providing for an asset-based credit facility (the *Credit Facility*). The *Credit Facility* replaced our prior credit facility with Bank of America. The *Credit Facility* consists of a \$60,000 asset-based revolving credit facility, with a \$10,000 letter of credit sub-line facility (the *Revolving Facility*), a \$5,000 first in last out (FILO) revolving credit facility (the *FILO Facility*) and a \$10,000 term loan facility (the *Term Loan Facility*). The total borrowing capacity under the *Revolving Facility* is based on a borrowing base, generally defined as 85% of the value of eligible accounts plus the lesser of (i) 70% of the value of eligible inventory or (ii) 85% of the net orderly liquidation value of eligible inventory, less reserves. The total borrowing capacity under the *FILO Facility* is based on a borrowing base, generally defined as a specified percentage of the value of eligible accounts that steps down over time, plus a specified percentage of the value of eligible inventory that steps down over time.

The scheduled maturity date of the loans under the *Revolving Facility* and the *Term Loan Facility* is April 21, 2020, and loans under the *FILO Facility* terminate April 21, 2018, subject in each case to customary early termination provisions. Any termination of the *Revolving Facility* would require termination of the *Term Loan Facility* and the *FILO Facility*. All obligations under the *Credit Facility* are secured by substantially all of the Company's assets. In addition, Summer Infant Canada Limited and Summer Infant Europe Limited, subsidiaries of the Company, are guarantors under the *Credit Facility*. Borrowings under the *Revolving Facility* will bear interest, at our option, at a base rate or at LIBOR, plus applicable margins based on average quarterly availability and ranging between 1.75% and 2.25% on LIBOR borrowings and 0.25% and 0.75% on base rate borrowings. Loans under the *FILO Facility* and *Term Loan Facility* will bear interest, at our option, at a base rate or at LIBOR, plus

Edgar Filing: Summer Infant, Inc. - Form 10-Q

a margin of 4.00% on LIBOR borrowings and 2.50% on base rate borrowings.

Under the Credit Facility, we must comply with certain financial covenants, including that we (i) maintain a fixed charge coverage ratio of at least 1.0 to 1.0 for the twelve consecutive fiscal months most recently ended and (ii) beginning with the quarter ending July 4, 2015, maintain a certain leverage ratio for each fiscal quarter. For purposes of the financial covenants, consolidated EBITDA is defined as net income before interest, taxes, depreciation and amortization, plus certain customary expenses, fees, non-cash charges and up to \$2,000 of specified inventory dispositions, and minus certain customary non-cash items increasing net income and other specified items.

The amount outstanding on the Revolving Facility at October 3, 2015 was \$39,430. Total borrowing capacity under the Revolving Facility at October 3, 2015 was \$49,372 and borrowing availability was \$9,942. The amounts outstanding on the Term Loan Facility and FILO Facility at October 3, 2015 were \$9,000 and \$5,000, respectively.

We were in compliance with the financial covenants under the Credit Facility as of October 3, 2015.

Table of Contents

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

As a smaller reporting company, as defined by Rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are not required to provide the information requested by this Item.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As required by Rule 13a-15(b) under the Securities Exchange Act of 1934, as of the end of the period covered by this Quarterly Report, we carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of our disclosure controls and procedures, as of October 3, 2015. Our Chief Executive Officer and our Chief Financial Officer have concluded, based on this evaluation, that our controls and procedures were effective as of October 3, 2015.

Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting that occurred during the period covered by this Quarterly Report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

The information set forth in Note 4, Commitments and Contingencies, under Part I, Item 1 of this Quarterly Report on Form 10-Q is incorporated herein by reference.

ITEM 1A. Risk Factors

There have been no material changes from the risk factors previously disclosed in Part I, Item 1A, Risk Factors, of our Annual Report on Form 10-K for the fiscal year ended January 3, 2015 and in our Quarterly Report on Form 10-Q for the first quarter ended July 4, 2015.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information.

None.

ITEM 6. Exhibits

The exhibits listed in the Exhibit Index immediately preceding the exhibits are filed as part of this Quarterly Report on Form 10-Q.

Table of Contents

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Summer Infant, Inc.

Date: November 4, 2015

By: /s/ Robert Stebenne
Robert Stebenne
Principal Executive Officer

Date: November 4, 2015

By: /s/ William E. Mote, Jr.
William E. Mote, Jr.
Chief Financial Officer
(Principal Financial and Accounting Officer)

Table of Contents

EXHIBIT INDEX

| Exhibit No. | Description |
|--------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 10.1 | 2012 Incentive Compensation Plan, as amended (incorporated by reference to Exhibit 10.1 to the Registrant's current report on Form 8-K filed on August 5, 2015) |
| 31.1 | Certification of Chief Executive Officer |
| 31.2 | Certification of Chief Financial Officer |
| 32.1 | Section 1350 Certification of Chief Executive Officer |
| 32.2 | Section 1350 Certification of Chief Financial Officer |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Labels Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |