MAGNETEK INC
Form 10-Q
November 13, 2006

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: October 1, 2006

OR

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

For the transition period from

Commission file number 1-10233

MAGNETEK, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE	**95-3917584**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

N49 W13650 Campbell Drive

Menomonee Falls, Wisconsin 53051

(Address of principal executive offices)

(262) 783-3500

(Registrant s telephone number, including area code)

8966 Mason Ave.

Chatsworth, California 91311

(Former name, former address and former fiscal year,
if changed since last report)

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 x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer x	Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

The number of shares outstanding of Registrant s Common Stock, as of October 31, 2006, was 29,312,152 shares.

2007 MAGNETEK FORM 10-Q

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Amounts in thousands, except per share data, unaudited)

	Three Months Ended (13 Weeks) October 1, 2006	**(13 Weeks) October 2, 2005**
Net sales	$ 22,514	$ 20,083
Cost of sales	15,403	13,640
Gross profit	7,111	6,443
Operating expenses:		
Research and development	1,019	962
Selling, general and administrative	6,658	5,987
Loss from operations	(566)	(506)
Non operating expense (income):		
Interest expense	1,076	409
Interest income	(288)	(26)
Loss from continuing operations before provision for income taxes	(1,354)	(889)
Provision for income taxes	276	334
Loss from continuing operations	(1,630)	(1,223)
Income (loss) from discontinued operations, net of tax	(1,564)	169
Net loss	$ (3,194)	$ (1,054)
Earnings (loss) per common share		
Basic and diluted:		
Loss from continuing operations	$ (0.06)	$ (0.05)
Income (loss) from discontinued operations	(0.05)	0.01
Net loss	$ (0.11)	$ (0.04)
Weighted average shares outstanding:		
Basic	28,966	28,868
Diluted	28,966	29,118

See accompanying notes

MAGNETEK, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Amounts in thousands)

	October 1, 2006 (Unaudited)	**July 2, 2006**
ASSETS		
Current assets:		
Cash	$ 496	$ 96
Restricted cash	22,602	22,602
Accounts receivable, net	14,195	13,056
Inventories	10,884	9,836
Prepaid expenses and other current assets	1,207	646
Assets held for sale	139,355	145,282
Total current assets	188,739	191,518
Property, plant and equipment	18,077	18,039
Less-accumulated depreciation	14,397	14,066
Net property, plant and equipment	3,680	3,973
Goodwill	28,150	28,150
Other assets	8,237	8,822
Total Assets	$ 228,806	$ 232,463
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 8,424	$ 6,996
Accrued liabilities	6,893	7,992
Accrued arbitration award	22,602	22,602
Liabilities held for sale	73,999	76,907
Current portion of long-term debt	28,336	27,412
Total current liabilities	140,254	141,909
Long-term debt, net of current portion	40	43
Pension benefit obligations, net	46,264	45,494
Deferred income taxes	2,334	2,109
Commitments and contingencies		
Stockholders equity		
Common stock	287	287
Paid in capital in excess of par value	129,689	129,473
Accumulated deficit	(10,025)	(6,831)
Accumulated other comprehensive loss	(80,037)	(80,021)
Total stockholders equity	39,914	42,908
Total Liabilities and Stockholders Equity	$ 228,806	$ 232,463

See accompanying notes

MAGNETEK, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOW

(Amounts in thousands, unaudited)

	Three Months Ended (13 Weeks) October 1, 2006	(13 Weeks) October 2, 2005
Cash flows from continuing operating activities:		
Loss from continuing operations	$ (1,630)	$ (1,223)
Adjustments to reconcile loss from continuing operations to net cash used in operating activities:		
Depreciation and amortization	542	652
Stock based compensation expense	126	82
Changes in operating assets and liabilities	(1,035)	(191)
Total adjustments	(367)	543
Net cash used in continuing operating activities	(1,997)	(680)
Cash flows from discontinued operations:		
Income (loss) from discontinued operations	(1,564)	169
Adjustments to reconcile (income) loss from discontinued operations to net cash provided by discontinued operations:		
Depreciation and amortization		1,634
Changes in operating assets and liabilities	3,813	889
Capital expenditures	(794)	(1,060)
Net cash provided by discontinued operations	1,455	1,632
Net cash provided by (used in) operating activities	(542)	952
Cash flows from investing activities:		
Capital expenditures	(43)	(103)
Net cash used in investing activities	(43)	(103)
Cash flow from financing activities:		
Proceeds from issuance of common stock	90	91
Borrowings (repayments) under line-of-credit agreements	924	(153)
Principal payments under capital lease obligations	(3)	(3)
Increase in deferred financing costs	(26)	(1,315)
Net cash provided by (used in) financing activities	985	(1,380)
Net increase (decrease) in cash	400	(531)
Cash at the beginning of the period	96	595
Cash at the end of the period	$ 496	$ 64

See accompanying notes

MAGNETEK, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

OCTOBER 1, 2006

(Amounts in thousands unless otherwise noted, except per share data, unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Magnetek, Inc. and its subsidiaries (the Company). All significant intercompany accounts and transactions have been eliminated.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial reporting and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the financial statements and footnotes thereto included in the Company s Form 10-K for the year ended July 2, 2006 filed with the Securities and Exchange Commission. In the Company s opinion, these unaudited statements contain all adjustments, consisting of normal recurring adjustments, necessary to present fairly the financial position of the Company as of October 1, 2006, and the results of its operations and its cash flows for the three months then ended. Results for the three-months ended October 1, 2006 are not necessarily indicative of results that may be experienced for the full fiscal year.

The Company uses a fifty-two, fifty-three week fiscal year ending on the Sunday nearest to June 30. Fiscal quarters are the thirteen or fourteen week periods ending on the Sunday nearest September 30, December 31, March 31 and June 30. The three-month periods ended October 1, 2006 and October 2, 2005 each contained thirteen weeks.

Use of Estimates - The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Significant areas requiring management estimates include the following key financial areas:

Accounts Receivable

Accounts receivable represent receivables from customers in the ordinary course of business. The Company is subject to losses from uncollectible receivables in excess of its allowances. The Company maintains allowances for doubtful accounts for estimated losses from customers inability to make required payments. In order to estimate the appropriate level of this allowance, the Company analyzes historical bad debts, customer concentrations, current customer creditworthiness, current economic trends and changes in customer payment patterns. If the financial conditions of the Company s customers were to deteriorate and to impair their ability to make payments, additional allowances may be required in future periods. The Company s management believes that all appropriate allowances have been provided.

Inventories

The Company s inventories are stated at the lower of cost or market. Cost is determined by the first-in, first-out (FIFO) method, including material, labor and factory overhead. Inventory on hand may exceed future demand either because the product is obsolete, or the amount on hand is more than can be used to meet future needs. The Company identifies potentially obsolete and excess inventory by evaluating overall inventory levels. In assessing the ultimate realization of inventories, the Company is required to make judgments as to future demand requirements and compare those with the current or committed inventory levels. If future demand requirements are less favorable than those projected by management, additional inventory write-downs may be required.

Reserves for Litigation and Environmental Issues

The Company periodically records the estimated impacts of various conditions, situations or circumstances involving uncertain outcomes. The accounting for such events is prescribed under Statement of Financial Accounting Standard (SFAS) No. 5, *Accounting for Contingencies*. SFAS

No. 5 defines a contingency as an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss to an enterprise that will ultimately be resolved when one or more future events occur or fail to occur.

SFAS No. 5 does not permit the accrual of gain contingencies under any circumstances. For loss contingencies, the loss must be accrued if (1) information is available that indicates it is probable that the loss has been incurred, given the likelihood of uncertain events; and (2) that the amount of the loss can be reasonably estimated.

The accrual of a contingency involves considerable judgment on the part of management. The Company uses its internal expertise, and outside experts, as necessary, to help estimate the probability that a loss has been incurred and the amount or range of the loss.

Income Taxes

The Company uses the liability method to account for income taxes. The preparation of consolidated financial statements involves estimating the Company s current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in the condensed consolidated balance sheets. An assessment of the recoverability of the deferred tax assets is made, and a valuation allowance is established based upon this assessment.

Pension Benefits

The valuation of the Company s pension plan requires the use of assumptions and estimates to develop actuarial valuations of expenses, assets and liabilities. These assumptions include discount rates, investment returns and mortality rates. Changes in assumptions and future investments returns could potentially have a material impact on the Company s expenses and related funding requirements.

Revenue Recognition The Company s policy is to recognize revenue when the earnings process is complete. The criteria used in making this determination are persuasive evidence that an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collectibility is reasonably assured. Sales are recorded net of returns and allowances, which are estimated using historical data at the time of sale.

Revenue is recognized upon shipment, except in those few cases where terms of shipment are FOB destination, or where product is shipped to customers with consignment stock agreements, wherein revenue is recognized when the customer receives the product, or removes the product from consignment stock. With the foregoing exceptions, terms of shipment are FOB shipping point, and payment is not contingent upon resale or any other matter other than passage of time. Amounts billed to customers for shipping costs are reflected in net sales; shipping costs are reflected in cost of sales.

Sales to distributors are recorded with appropriate reserves for future returns in accordance with SFAS No. 48, *Revenue Recognition When Right of Return Exists*, and generally do not include future installation obligations or acceptance requirements.

Stock-Based Compensation The Company accounts for all stock-based compensation in accordance with SFAS No. 123 (R), *Share-Based Payment*, which requires all share-based payments to employees, including grants of employee stock options, to be recognized in the Company s financial statements based upon their fair values. The Company adopted SFAS No. 123R in July, 2005 (fiscal year 2006) and selected the modified prospective method of adoption in which compensation cost is recognized beginning with the effective date. In accordance with the modified prospective method of adoption, the Company s results of operations for periods prior to adoption were not restated.

Property, Plant and Equipment Additions and improvement are capitalized at cost, whereas expenditures for maintenance and repair are charged to expense as incurred. Depreciation is provided over the estimated useful lives of the respective assets principally on the straight-line method (machinery and equipment normally five to ten years, buildings and improvements normally ten to forty years).

Goodwill In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, the Company reviews the carrying value of Goodwill at least annually, and more frequently if indicators of potential impairment arise, using discounted future cash flow analysis as prescribed in SFAS No. 142.

Deferred Financing Costs Costs incurred to obtain financing are deferred and included in other assets in the condensed consolidated balance sheets. Deferred financing costs are amortized over the term of the financing facility and these expenses are included in interest expense in the accompanying condensed consolidated statements of operations.

Warranties   The Company offers warranties for certain products that it manufactures, with the warranty term generally ranging from one to two years. Warranty reserves are established for costs expected to be incurred after the sale and delivery of products under warranty, based mainly on known product failures and historical experience. Actual repair costs incurred for products under warranty are charged against the established reserve balance as incurred.

Earnings per Share   In accordance with SFAS No. 128, *Earnings per Share*, basic earnings per share are computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share incorporate the incremental shares issuable upon the assumed exercise of stock options as if all exercises had occurred at the beginning of the fiscal period.

Recent Accounting Pronouncements   In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections.* SFAS No. 154 replaces APB No. 20, *Accounting Changes*, and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements*, and establishes retrospective application as the required method for reporting a change in accounting principle. SFAS No. 154 provides guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. The reporting of a correction of an error by restating previously issued financial statements is also addressed. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of this pronouncement on July 3, 2006, did not have a material effect on the Company s financial position, results of operations or liquidity.

On July 13, 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 creates a single model to address uncertainty in tax positions, clarifying the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 applies to all tax positions related to income taxes subject to SFAS No. 109, *Accounting for Income Taxes*.

FIN 48 utilizes a two-step approach for evaluating tax positions. Recognition (step one) occurs when an enterprise concludes that a tax position, based solely on its technical merits, is more-likely-than-not to be sustained upon examination. Measurement (step two) is only addressed if step one has been satisfied. Those tax positions failing to qualify for initial recognition are recognized in the first subsequent interim period they meet the more-likely-than-not standard, or are resolved through negotiation or litigation with the taxing authority, or upon expiration of the statute of limitations.

FIN 48 is effective for fiscal years beginning after December 15, 2006. Differences between the amounts recognized in the statements of financial position prior to the adoption of FIN 48 and the amounts reported after adoption would be accounted for as a cumulative-effect adjustment recorded to the beginning balance of retained earnings. The adoption of this pronouncement is not expected to have a material effect on the Company s financial position, results of operations, or liquidity.

Derivative Financial Instruments   The Company periodically uses derivative financial instruments to reduce financial market risks. These instruments are used to hedge foreign currency and interest rate market exposures. The Company does not use derivative financial instruments for speculative or trading purposes. The accounting policies for these instruments are based on the Company s designation of such instruments as hedging transactions. The criteria the Company uses for designating an instrument as a hedge include the instrument s effectiveness in risk reduction and the matching of the derivative to the underlying transaction. The resulting gains or losses are accounted for as part of the transactions being hedged, except that losses not expected to be recovered upon the completion of the hedge transaction are expensed. The Company s continuing operations had no derivative financial instruments at October 1, 2006 and July 2, 2006.

Foreign Currency Translation - The Company s foreign entities accounts are measured using local currency as the functional currency. Assets and liabilities are translated at the exchange rate in effect at year-end. Revenues and expenses are translated at the rates of exchange prevailing during the year. Unrealized translation gains and losses arising from differences in exchange rates from period to period are included as a component of accumulated other comprehensive loss in stockholders equity.

Reclassifications   Certain prior year balances were reclassified to conform to the current year presentation.

2. **Discontinued Operations**

The Company s power electronics business and telecom power business, as well as certain expenses incurred related to businesses the Company no longer owns, are classified as discontinued operations. The results of discontinued operations are as follows:

	Three Months Ended October 1, 2006	October 2, 2005
Net sales	$ 46,930	$ 40,537
Income (loss) from discontinued operations before interest and income taxes	$ (965)	$ 1,124
Interest expense, net	274	339
Provision for income taxes		