UNIVERSAL FOREST PRODUCTS INC
Form 10-Q
August 01, 2018
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10 Q

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

For the quarterly period ended June 30, 2018

OR

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

Commission File Number 0 22684

UNIVERSAL FOREST PRODUCTS, INC.

(Exact name of registrant as specified in its charter)

Michigan	38 1465835
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
2801 East Beltline NE, Grand Rapids, Michigan	49525
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code (616) 364 6161

NONE

(Former name or former address, if changed since last report.)

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

Large Accelerated Filer   Accelerated Filer   Non-Accelerated Filer   Smaller reporting company
Emerging Growth Company

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

Indicate by checkmark whether the registrant is a shell company (as defined by 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 as of June 30, 2018
Common stock, $1 par value	61,632,401

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UNIVERSAL FOREST PRODUCTS, INC.

CONSOLIDATED CONDENSED BALANCE SHEETS

(Unaudited)

(in thousands, except share data)

	June 30, 2018	December 30, 2017	July 1, 2017
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	$ 27,501	$ 28,339	$ 24,625
Restricted cash	16,758	477	905
Investments	14,493	11,269	10,401
Accounts receivable, net	489,145	327,751	398,529
Inventories:			
Raw materials	272,765	234,354	218,356
Finished goods	259,109	225,954	220,079
Total inventories	531,874	460,308	438,435
Refundable income taxes	2,396	7,228	—
Other current assets	30,464	28,115	21,970
TOTAL CURRENT ASSETS	1,112,631	863,487	894,865
DEFERRED INCOME TAXES	2,235	1,865	1,981
RESTRICTED INVESTMENTS	10,950	8,359	7,911
OTHER ASSETS	7,081	7,368	7,842
GOODWILL	219,595	212,644	213,597
INDEFINITE-LIVED INTANGIBLE ASSETS	7,384	7,415	2,340
OTHER INTANGIBLE ASSETS, NET	36,045	34,910	37,547
PROPERTY, PLANT AND EQUIPMENT:			
Property, plant and equipment	791,348	763,101	735,474
Less accumulated depreciation and amortization	(450,650)	(434,472)	(419,518)
PROPERTY, PLANT AND EQUIPMENT, NET	340,698	328,629	315,956
TOTAL ASSETS	1,736,619	1,464,677	1,482,039
LIABILITIES AND SHAREHOLDERS’ EQUITY			
CURRENT LIABILITIES:			
Cash overdraft	$ 33,608	$ 25,851	$ 22,769
Accounts payable	197,408	140,106	160,250
Accrued liabilities:			
Compensation and benefits	88,771	97,556	77,187
Income taxes	—	—	960
Other	50,038	38,404	48,063
Current portion of long-term debt	542	1,329	2,378
TOTAL CURRENT LIABILITIES	370,367	303,246	311,607
LONG-TERM DEBT	276,274	144,674	204,752
DEFERRED INCOME TAXES	13,856	14,079	20,360
OTHER LIABILITIES	28,399	28,655	28,959

TOTAL LIABILITIES	688,896	490,654	565,678
SHAREHOLDERS' EQUITY:			
Controlling interest shareholders' equity:			
Preferred stock, no par value; shares authorized 1,000,000; issued and outstanding, none	$ —	$ —	$ —
Common stock, $1 par value; shares authorized 80,000,000; issued and outstanding, 61,632,401, 61,191,888 and 61,265,325	61,632	61,192	61,266
Additional paid-in capital	174,749	161,928	158,248
Retained earnings	800,237	736,212	684,808
Accumulated other comprehensive income	(4,077)	144	(2,590)
Total controlling interest shareholders' equity	1,032,541	959,476	901,732
Noncontrolling interest	15,182	14,547	14,629
TOTAL SHAREHOLDERS' EQUITY	1,047,723	974,023	916,361
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 1,736,619	$ 1,464,677	$ 1,482,039

See notes to consolidated condensed financial statements.

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UNIVERSAL FOREST PRODUCTS, INC.

CONSOLIDATED CONDENSED STATEMENTS OF EARNINGS

AND COMPREHENSIVE INCOME

(Unaudited)

(in thousands, except per share data)

	Three Months Ended		Six Months Ended	
	June 30, 2018	July 1, 2017	June 30, 2018	July 1, 2017
NET SALES	$ 1,294,440	$ 1,072,375	$ 2,288,297	$ 1,918,505
COST OF GOODS SOLD	1,128,751	924,135	1,991,719	1,649,526
GROSS PROFIT	165,689	148,240	296,578	268,979
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	104,595	94,605	197,800	181,587
NET LOSS (GAIN) ON DISPOSITION OF ASSETS AND IMPAIRMENT OF ASSETS	477	(264)	(6,057)	(328)
EARNINGS FROM OPERATIONS	60,617	53,899	104,835	87,720
INTEREST EXPENSE	2,248	1,840	4,025	3,343
INTEREST AND INVESTMENT INCOME	(181)	(329)	(898)	(411)
EQUITY IN EARNINGS OF INVESTEE	—	(21)	—	(26)
	2,067	1,490	3,127	2,906
EARNINGS BEFORE INCOME TAXES	58,550	52,409	101,708	84,814
INCOME TAXES	13,420	17,835	22,994	28,605
NET EARNINGS	45,130	34,574	78,714	56,209
LESS NET EARNINGS ATTRIBUTABLE TO NONCONTROLLING INTEREST	(1,086)	(932)	(1,836)	(1,505)
NET EARNINGS ATTRIBUTABLE TO CONTROLLING INTEREST	$ 44,044	$ 33,642	$ 76,878	$ 54,704
EARNINGS PER SHARE - BASIC	$ 0.71	$ 0.55	$ 1.24	$ 0.89
EARNINGS PER SHARE - DILUTED	$ 0.71	$ 0.55	$ 1.24	$ 0.89
OTHER COMPREHENSIVE INCOME:				
NET EARNINGS	45,130	34,574	78,714	56,209
OTHER COMPREHENSIVE GAIN (LOSS)	(3,905)	1,387	(4,344)	4,422
COMPREHENSIVE INCOME	41,225	35,961	74,370	60,631
LESS COMPREHENSIVE INCOME ATTRIBUTABLE TO NONCONTROLLING INTEREST	(119)	(1,460)	(1,713)	(2,887)
COMPREHENSIVE INCOME ATTRIBUTABLE TO CONTROLLING INTEREST	$ 41,106	$ 34,501	$ 72,657	$ 57,744

See notes to consolidated condensed financial statements.

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UNIVERSAL FOREST PRODUCTS, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Unaudited)

(in thousands, except share and per share data)

	Controlling Interest Shareholders' Equity					
	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Earnings	Noncontrolling Interest	Total
Balance at December 31, 2016	$ 61,026	$ 144,649	$ 649,135	$ (5,630)	$ 11,286	$ 860,466
Net earnings			54,704		1,505	56,209
Foreign currency translation adjustment				2,817	1,382	4,199
Unrealized gain (loss) on investment & foreign currency				223		223
Distributions to noncontrolling interest					(1,953)	(1,953)
Additional purchases of noncontrolling interest					2,409	2,409
Cash dividends - $0.150 per share			(9,208)			(9,208)
Issuance of 12,699 shares under employee stock plans	13	319				332
Issuance of 426,435 shares under stock grant programs	426	6,784				7,210
Issuance of 132,624 shares under deferred compensation plans	133	(133)				—
Repurchase of 332,640 shares	(332)	221	(9,823)			(9,934)
Tax benefits from non-qualified stock options exercised		—				—
Expense associated with share-based compensation arrangements		1,282				1,282
Accrued expense under deferred compensation plans		5,126				5,126
Balance at July 1, 2017	$ 61,266	$ 158,248	$ 684,808	$ (2,590)	$ 14,629	$ 916,361
Balance at December 30, 2017	61,192	161,928	736,212	144	14,547	974,023
Net earnings			76,878		1,836	78,714
Foreign currency translation adjustment				(3,669)	(123)	(3,792)
Unrealized gain (loss) on investment & foreign currency				(552)		(552)
Distributions to noncontrolling interest					(1,078)	(1,078)
Cash dividends - $0.180 per share			(11,090)			(11,090)
Issuance of 16,917 shares under employee stock plans	17	483				500
Issuance of 346,777 shares under stock grant programs	347	4,990				5,337
	132	(132)				—

Issuance of 132,603 shares under deferred compensation plans						
Repurchase of 55,784 shares	(56)		(1,763)			(1,819)
Expense associated with share-based compensation arrangements		1,817				1,817
Accrued expense under deferred compensation plans		5,663				5,663
Balance at June 30, 2018	$ 61,632	$ 174,749	$ 800,237	$ (4,077)	$ 15,182	$ 1,047,723

See notes to consolidated condensed financial statements.

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UNIVERSAL FOREST PRODUCTS, INC.

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)	Six Months Ended	
	June 30, 2018	July 1, 2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	$ 78,714	$ 56,209
Adjustments to reconcile net earnings to net cash from operating activities:		
Depreciation	26,144	23,248
Amortization of intangibles	2,702	2,377
Expense associated with share-based and grant compensation arrangements	1,924	1,381
Deferred income taxes (credits)	(565)	355
Equity in earnings of investee	—	(26)
Net gain on disposition of assets	(6,057)	(328)
Changes in:		
Accounts receivable	(155,666)	(101,239)
Inventories	(61,828)	(26,979)
Accounts payable and cash overdraft	62,665	38,146
Accrued liabilities and other	15,895	22,067
NET CASH USED IN OPERATING ACTIVITIES	(36,072)	15,211
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(54,313)	(34,549)
Proceeds from sale of property, plant and equipment	36,724	1,039
Acquisitions, net of cash received	(37,960)	(59,658)
Purchases of investments	(9,348)	(15,118)
Proceeds from sale of investments	3,180	7,247
Other	(1,352)	1,152
NET CASH FROM (USED IN) INVESTING ACTIVITIES	(63,069)	(99,887)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings under revolving credit facilities	488,853	444,601
Repayments under revolving credit facilities	(431,657)	(349,311)
Borrowings of debt	1,639	—
Repayment of debt	(5,437)	—
Issuance of long-term debt	75,000	—
Proceeds from issuance of common stock	500	331
Dividends paid to shareholders	(11,090)	(9,207)
Distributions to noncontrolling interest	(1,078)	(1,953)
Repurchase of common stock	(1,819)	(9,934)
Other	(71)	(6)
NET CASH FROM FINANCING ACTIVITIES	114,840	74,521
Effect of exchange rate changes on cash	(256)	1,196
NET CHANGE IN CASH AND CASH EQUIVALENTS	15,443	(8,959)

CASH, CASH EQUIVALENTS, AND RESTRICTED CASH, BEGINNING OF YEAR	28,816	34,489
CASH, CASH EQUIVALENTS, AND RESTRICTED CASH, END OF PERIOD	$ 44,259	$ 25,530
RECONCILIATION OF CASH AND CASH EQUIVALENTS AND RESTRICTED CASH:		
Cash and cash equivalents, beginning of period	$ 28,339	$ 34,091
Restricted cash, beginning of period	477	398
Cash, cash equivalents, and restricted cash, beginning of period	$ 28,816	$ 34,489
Cash and cash equivalents, end of period	$ 27,501	$ 24,625
Restricted cash, end of period	16,758	905
Cash, cash equivalents, and restricted cash, end of period	$ 44,259	$ 25,530
SUPPLEMENTAL INFORMATION:		
Interest paid	$ 3,889	$ 3,049
Income taxes paid	18,745	15,895
NON-CASH FINANCING ACTIVITIES:		
Common stock issued under deferred compensation plans	4,779	4,231

See notes to consolidated condensed financial statements.

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UNIVERSAL FOREST PRODUCTS, INC.

NOTES TO UNAUDITED

CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

A. BASIS OF PRESENTATION

The accompanying unaudited interim consolidated condensed financial statements (the “Financial Statements”) include our accounts and those of our wholly-owned and majority-owned subsidiaries and partnerships, and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, the Financial Statements do not include all of the information and footnotes normally included in the annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States. All intercompany transactions and balances have been eliminated.

In our opinion, the Financial Statements contain all material adjustments necessary to present fairly our consolidated financial position, results of operations and cash flows for the interim periods presented. All such adjustments are of a normal recurring nature. These Financial Statements should be read in conjunction with the annual consolidated financial statements, and footnotes thereto, included in our Annual Report to Shareholders on Form 10 K for the fiscal year ended December 30, 2017.

Seasonality has a significant impact on our working capital from March to August which historically results in negative or modest cash flows from operations in our first and second quarters. Conversely, we experience a substantial decrease in working capital from September to February which typically results in significant cash flow from operations in our third and fourth quarters. For comparative purposes, we have included the July 1, 2017 balances in the accompanying unaudited consolidated condensed balance sheets.

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B. FAIR VALUE

We apply the provisions of ASC 820, Fair Value Measurements and Disclosures, to assets and liabilities measured at fair value. Assets measured at fair value are as follows:

	June 30, 2018				July 1, 2017		
(in thousands)	Quoted Prices in Active Markets (Level 1)	Prices with Other Observable Inputs (Level 2)	Prices with Unobservable Inputs (Level 3)	Total	Quoted Prices in Active Markets (Level 1)	Prices with Other Observable Inputs (Level 2)	Total
Money market funds	$ 56	$ 1,513	$ —	$ 1,569	$ 64	$ 891	$ 955
Fixed income funds	2,879	7,968	—	10,847	1,495	6,451	7,946
Equity securities	7,892	—	—	7,892	9,822	—	9,822
Hedge funds	—	—	1,689	1,689			
Mutual funds:							
Domestic stock funds	413	—	—	413	330	—	330
International stock funds	3,951	—	—	3,951	84	—	84
Target funds	249	—	—	249	254	—	254
Bond funds	725	—	—	725	206	—	206
Total mutual funds	5,338	—	—	5,338	874	—	874
Total	$ 16,165	$ 9,481	$ 1,689	$ 27,335	$ 12,255	$ 7,342	$ 19,597
Assets at fair value	$ 16,165	$ 9,481	$ 1,689	$ 27,335	$ 12,255	$ 7,342	$ 19,597

We maintain money market, mutual funds, bonds, and/or stocks in our non-qualified deferred compensation plan and our wholly owned licensed captive insurance company. These funds are valued at prices quoted in an active exchange market and are included in "Cash and Cash Equivalents", "Investments", "Restricted Cash", and "Restricted Investments". We have elected not to apply the fair value option under ASC 825, Financial Instruments, to any of our financial instruments except for those expressly required by U.S. GAAP.

During the second quarter of 2018, we purchased a private real estate income trust which will be valued as a Level 3 asset. We did not maintain any Level 3 assets or liabilities at July 1, 2017.

In 2017, our wholly-owned captive, Ardellis Insurance Ltd. ("Ardellis") transferred $4.1 million in fixed income securities from its Investment Account and purchased an additional $3.8 million in fixed income securities which are held in a newly formed collateral trust account in line with regulatory requirements in the State of Michigan to allow Ardellis to act as an admitted carrier in the State. These funds are intended to safeguard the insureds of the Michigan Branch of Ardellis. The funds are classified as "Restricted Investments".

In accordance with our investment policy, our wholly-owned captive, Ardellis Insurance Ltd. (“Ardellis”), maintains an investment portfolio, totaling $24.8 million as of June 30, 2018, consisting of domestic and international stocks, hedge funds, and fixed income bonds.

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Ardellis' available for sale investment portfolio, including funds held with the State of Michigan, consists of the following (in thousands):

	June 30,2018		
	Cost	Unrealized Gain/(Loss)	Fair Value
Fixed Income	$ 11,068	$ (221)	$ 10,847
Equity	7,013	879	7,892
Mutual Funds	4,508	(123)	4,385
Hedge Funds	1,679	10	1,689
Total	$ 24,268	$ 545	$ 24,813

Our fixed income investments consist of a blend of US Government and Agency bonds and investment grade corporate bonds with varying maturities. Our equity investments consist of small, mid, and large cap growth and value funds, as well as international equity. Our hedge funds consist of the private real estate income trust which is valued as a Level 3 asset. The net pre-tax effected unrealized gain was $0.5 million. Carrying amounts above are recorded in the investments and restricted investments line items within the balance sheet as of June 30, 2018. During the first six months of 2018, Ardellis' investments reported a net realized gain of $514 thousand, which was recorded in interest income on the statement of earnings.

C. REVENUE RECOGNITION

On May 28, 2014, the FASB issued ASU No. 2014-09 (Accounting Standard Codification 606), Revenue from Contracts with Customers. Topic 606 supersedes the revenue recognition requirements in Accounting Standards Codification Topic 605, Revenue Recognition, and requires the recognition of revenue when promised goods or services are transferred to customers in an amount that reflects the considerations to which the entity expects to be entitled to in exchange for those goods or services. The ASU requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments. The Company has adopted the requirements of the new standard as of January 1, 2018, and utilized the modified retrospective method of transition which was applied to all contracts.

The Company completed the new revenue recognition standard assessment and determined that there was no material impact to our consolidated financial statements, aside from additional required disclosures, thus no needed adjustment to the opening retained earnings for the annual reporting period.

Within the three markets (retail, industrial, and construction) that the Company operates, there are a variety of written and oral contracts that are utilized to generate revenue from the sale of wood, wood composite and other products. The transaction price is stated at the purchase order level, which includes shipping and/or freight costs and any applicable governmental authority taxes. The majority of our contracts have a single performance obligation concentrated around the delivery of goods to the carrier, Free On Board (FOB) shipping point. Therefore, revenue is recognized when this performance obligation is satisfied. Generally, title and control passes at the time of shipment. In certain circumstances, the customer takes title when the shipment arrives at the destination. However, our shipping process is typically completed the same day.

Certain customer products that we provide require installation by the Company or a 3rd party. Installation revenue is recognized upon completion, which is typically 2-3 days after receipt. If it is determined to utilize a 3rd party for installation, the party will act as an agent to the Company until completion of the installation. Installation revenue represents an immaterial share of the Company's total sales.

UNIVERSAL FOREST PRODUCTS, INC.

The Company utilizes rebates, credits, discounts and/or cash-based incentives with certain customers which are accounted for as variable consideration. We estimate these amounts based on the expected amount to be provided to customers and reduce revenues recognized. We believe that there will not be significant changes to our estimates of variable consideration. The allocation of these costs are applied at the invoice level and recognized in conjunction with revenue. Additionally, the volume returns and refunds are estimated on a historical and expected basis which is a reduction of revenue recognized.

Earnings on construction contracts are reflected in operations using over time accounting, under either cost to cost or units of delivery methods, depending on the nature of the business at individual operations, which is in accordance with ASC 606 as revenue is recognized when certain performance obligations are performed. Under over time accounting using the cost to cost method, revenues and related earnings on construction contracts are measured by the relationships of actual costs incurred related to the total estimated costs. Under over time accounting using the units of delivery method, revenues and related earnings on construction contracts are measured by the relationships of actual units produced related to the total number of units. Revisions in earnings estimates on the construction contracts are recorded in the accounting period in which the basis for such revisions becomes known. Projected losses on individual contracts are charged to operations in their entirety when such losses become apparent.

Our construction contracts are generally entered into with a fixed price and completion of the projects can range from 6 to 18 months in duration. Therefore, our operating results are impacted by, among many other things, labor rates and commodity costs. During the year, we update our estimated costs to complete our projects using current labor and commodity costs and recognize losses to the extent that they exist.

The following table presents our gross revenues disaggregated by revenue source:

	Three Months Ended			Six Months Ended		
(in thousands)	June 30,	July 1,		June 30,	July 1,	
Market Classification	2018	2017	% Change	2018	2017	% Change
FOB Shipping Point Revenue	$ 1,281,557	$ 1,058,777	21.04%	$ 2,263,248	$ 1,885,652	20.02%
Construction Contract Revenue	38,811	33,418	16.14%	68,787	65,400	5.18%
Total Sales	1,320,368	1,092,195	20.89%	2,332,035	1,951,052	19.53%

In the first six months of 2018, the North and West segments comprise the construction contract revenue above, $47.3 million and $21.5 million, respectively. Construction contract revenue is primarily made up of site-built and framing customers.

The following table presents the balances of over time accounting accounts which are included in “Other current assets” and “Accrued liabilities: Other”, respectively (in thousands):

	June 30, 2018	December 30, 2017	July 1, 2017

Cost and Earnings in Excess of Billings	$ 5,501	$ 5,005	$ 3,521
Billings in Excess of Cost and Earnings	4,616	4,435	3,725

UNIVERSAL FOREST PRODUCTS, INC.

D. EARNINGS PER SHARE

The computation of earnings per share ("EPS") is as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2018	July 1, 2017	June 30, 2018	July 1, 2017
Numerator:				
Net earnings attributable to controlling interest	$ 44,044	$ 33,642	$ 76,878	$ 54,704
Adjustment for earnings allocated to non-vested restricted common stock	(1,018)	(663)	(1,728)	(994)
Net earnings for calculating EPS	$ 43,026	$ 32,979	$ 75,150	$ 53,710
Denominator:				
Weighted average shares outstanding	61,895	61,632	61,770	61,482
Adjustment for non-vested restricted common stock	(1,431)	(1,215)	(1,389)	(1,119)
Shares for calculating basic EPS	60,464	60,417	60,381	60,363
Effect of dilutive restricted common stock	85	93	80	111
Shares for calculating diluted EPS	60,549	60,510	60,461	60,474
Net earnings per share:				
Basic	$ 0.71	$ 0.55	$ 1.24	$ 0.89
Diluted	$ 0.71	$ 0.55	$ 1.24	$ 0.89

No options were excluded from the computation of diluted EPS for the quarters ended June 30, 2018, or July 1, 2017.

On October 17, 2017, our Board of Directors declared a three-for-one stock split effected in the form of a stock dividend. The record date of the stock split was on October 31, 2017, and the eventual stock distribution to shareholders occurred on November 14, 2017. As a result of the stock split, all historical per share data and number of shares outstanding presented in future financial statements are retroactively adjusted.

E. COMMITMENTS, CONTINGENCIES, AND GUARANTEES

We are self-insured for environmental impairment liability, including certain liabilities which are insured through a wholly owned subsidiary, Ardellis Insurance Ltd., a licensed captive insurance company.

We own and operate a number of facilities throughout the United States that chemically treat lumber products. In connection with the ownership and operation of these and other real properties, and the disposal or treatment of hazardous or toxic substances, we may, under various federal, state, and local environmental laws, ordinances, and regulations, be potentially liable for removal and remediation costs, as well as other potential costs, damages, and expenses. Environmental reserves, calculated with no discount rate, have been established to cover remediation activities at wood preservation facilities in Stockertown, PA; Elizabeth City, NC; and Auburndale, FL. In addition, a reserve was established for our facility in Thornton, CA to remove certain lead containing materials which existed on the property at the time of purchase.

On a consolidated basis, we have reserved approximately $2.5 million and $3.6 million on June 30, 2018, and July 1, 2017, respectively, representing the estimated costs to complete future remediation efforts. These amounts have not been reduced by an insurance receivable.

Many of our wood treating operations utilize “Subpart W” drip pads, defined as hazardous waste management units by the Environmental Protection Agency. The rules regulating drip pads require that a pad be “closed” at the point that it is no longer intended to be used for wood treating operations or to manage hazardous waste. Closure involves identification and disposal of contaminants which are required to be removed from the facility. The cost of closure is dependent upon a number of factors including, but not limited to, identification and removal of contaminants, cleanup standards that vary from state to state, and the time period over which the cleanup would be completed. Based on our present knowledge of existing circumstances, it is considered probable that these costs will approximate $0.2 million. As a result, this amount is recorded in other long-term liabilities on June 30, 2018.

In February 2014, one of our operations was served with a federal grand jury subpoena from the Southern District of New York. The subpoena was issued in connection with an investigation being conducted by the US Attorney's Office for the Southern District of New York. The subpoena requested documents relating to a developer and construction projects for which our operation had provided materials and labor. Following receipt of the subpoena, the Audit Committee of the Company's Board of Directors retained outside counsel to conduct an internal investigation and respond to the subpoena. The Company cooperated in all respects with the US Attorney's Office, complied with this subpoena and voluntarily provided additional information. As a result of the internal investigation, in 2014, two Company employees were terminated for violating the Company's Code of Business Conduct and Ethics. In May 2015, those ex-employees were indicted by the grand jury. In April 2016, one of the two former employees pled guilty to four of the charges included in the indictment. In May 2016, the other former employee was found guilty by a jury on four of the charges included in the indictment. The Company has not been named as a target and continues to cooperate with the US Attorney's Office in this matter. Based upon prior communications with the US Attorney's Office, we do not believe that the resolution of this matter will have a material adverse impact on our financial condition or the results of our operations.

In addition, on June 30, 2018, we were parties either as plaintiff or defendant to a number of lawsuits and claims arising through the normal course of our business. In the opinion of management, our consolidated financial statements will not be materially affected by the outcome of these contingencies and claims.

On June 30, 2018, we had outstanding purchase commitments on commenced capital projects of approximately $23.4 million.

We provide a variety of warranties for products we manufacture. Historically, warranty claims have not been material. We distribute products manufactured by other companies, some of which are no longer in business. While we do not warrant these products, we have received claims as a distributor of these products when the manufacturer no longer exists or has the ability to pay. Historically, these costs have not had a material effect on our consolidated financial statements.

As part of our operations, we supply building materials and labor to site-built construction projects or we jointly bid on contracts with framing companies for such projects. In some instances, we are required to post payment and performance bonds to insure the project owner that the products and installation services are completed in accordance with our contractual obligations. We have agreed to indemnify the surety for claims made against the bonds. As of June 30, 2018, we had approximately $15.8 million outstanding payment and performance bonds for open projects. We had approximately $1.7 million in payment and performance bonds outstanding for completed projects which are still under warranty.

On June 30, 2018, we had outstanding letters of credit totaling $30.4 million, primarily related to certain insurance contracts and industrial development revenue bonds described further below.

In lieu of cash deposits, we provide irrevocable letters of credit in favor of our insurers to guarantee our performance under certain insurance contracts. We currently have irrevocable letters of credit outstanding totaling approximately $20.6 million for these types of insurance arrangements. We have reserves recorded on our balance sheet, in accrued liabilities, that reflect our expected future liabilities under these insurance arrangements.

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We are required to provide irrevocable letters of credit in favor of the bond trustees for all industrial development revenue bonds that have been issued. These letters of credit guarantee principal and interest payments to the bondholders. We currently have irrevocable letters of credit outstanding totaling approximately $9.8 million related to our outstanding industrial development revenue bonds. These letters of credit have varying terms but may be renewed at the option of the issuing banks.

Certain wholly owned domestic subsidiaries have guaranteed the indebtedness of Universal Forest Products, Inc. in certain debt agreements, including the Series 2012 Senior Notes and our revolving credit facility. The maximum exposure of these guarantees is limited to the indebtedness outstanding under these debt arrangements and this exposure will expire concurrent with the expiration of the debt agreements.

We did not enter into any new guarantee arrangements during the second quarter of 2018 which would require us to recognize a liability on our balance sheet.

F. BUSINESS COMBINATIONS

We completed the following acquisitions in six months ended 2018 and 2017 which were accounted for using the purchase method in thousands unless otherwise noted:

Company Name	Acquisition Date	Purchase Price	Intangible Assets	Net Tangible Assets	Operating Segment
	June 1, 2018	$23,893 cash paid for 100% asset purchase	$ 7,123	$ 16,770	South
North American Container Corporation ("NACC")	A manufacturer of structural packaging products, including steel, corrugated and hardwood packaging. NACC had annual sales of approximately $71 million. The acquisition of NACC allowed us to expand our presence in this region, expand our product offering, and serve customers more cost effectively.				
	April 9, 2018	$3,890 cash paid for 100% asset purchase	$ 2,235	$ 1,655	West
Fontana Wood Products ("Fontana")	A manufacturer and distributor lumber and trusses in the Southern California region. Fontana had annual sales of approximately $12 million. The acquisition of Fontana allows us to expand our manufactured housing business and creates operating leverage by consolidating with another regional operation.				
	April 3, 2018	$1,404 cash paid for 100% asset purchase	$ 1,344	$ 60	All Other
Expert Packaging ("Expert")	A manufacturer and distributor of total packaging solutions in timber, crates, pallets, and skids. Expert had annual sales of approximately $3.6 million. The acquisition of Expert allows us to make progress on our goal of becoming a				

	global provider of packaging solutions.				
	January 23, 2018	$2,942 cash paid for 100% asset purchase	$ 850	$ 2,092	West
Spinner Wood Products, LLC ("Spinner")	A manufacturer and distributor of agricultural bin and various industrial packaging. Spinner had annual sales of approximately $8 million. The acquisition of Spinner allows us to expand our industrial packaging product offering and creates operating leverage by consolidating with other regional operations.				

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Company Name	Acquisition Date	Purchase Price	Intangible Assets	Net Tangible Assets	Operating Segment
	January 15, 2018	$5,845 cash paid for 100% asset purchase	$ 50	$ 5,795	North
Great Northern Lumber, LLC	A manufacturer of industrial products as well as serving the concrete forming market in the Chicago area. Great Northern Lumber had annual sales of approximately $25 million. The acquisition of Great Northern Lumber enables us to expand our concrete forming product offering and regional coverage.				
	October 16, 2017	$931 cash paid for 100% asset purchase	$ 909	$ 22	All Other
Silverwater Box	A manufacturer and distributor of total packaging solutions in timber, plastic, steel, fiberglass, and cardboard. Silverwater Box had annual sales of approximately $2.8 million. The acquisition of Silverwater Box allows us to make progress on our goal of becoming a global provider of packaging solutions.				
	May 26, 2017	$5,042 cash paid for 100% asset purchase	$ 4,880	$ 162	South
Go Boy Pallets, LLC ("Go Boy")	A manufacturer and distributor of industrial pallets and packaging in Georgia and North Carolina. Go Boy had annual sales of approximately $8 million. The acquisition of Go Boy enabled us to expand our industrial packaging product offering and lumber sourcing in this region.				
	March 6, 2017	$31,818 cash paid for 100% asset purchase	$ 7,653	$ 24,165	South
Robbins Manufacturing Co. ("Robbins")	A manufacturer of treated wood products with facilities in Florida, Georgia, and North Carolina. Robbins had annual sales of approximately $86 million. The acquisition of Robbins allowed us to expand our presence in this region and serve customers more cost effectively.				
	March 6, 2017	$22,789 cash paid for 100% asset purchase	$ 14,341	$ 8,448	North
Quality Hardwood Sales, LLC ("Quality")	A manufacturer and supplier of hardwood products, including components of cabinets used in homes and recreational vehicles. Quality had annual sales of approximately $30 million. The acquisition of Quality enabled us to expand our product offering to include hardwood-based products.				

The intangible assets for each acquisition were finalized and allocated to their respective identifiable intangible asset and goodwill accounts during 2018, excluding the NACC aquisition. In aggregate, acquisitions completed since the end of June 2017 contributed approximately $14.2 million in revenue and $0.7 million in operating profit during the second quarter of 2018.

G. SEGMENT REPORTING

ASC 280, Segment Reporting ("ASC 280"), defines operating segments as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance.

The Company operates manufacturing, treating and distribution facilities throughout North America, but primarily in the United States. The Company manages the operations of its individual locations primarily through a geographic reporting structure under which each location is included in a region and regions are included in our North, South, West, and International divisions. The exceptions to this geographic reporting and management structure are (a) the Company's Alternative Materials Division, which offers a portfolio of non-wood products

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and distributes those products nation-wide (b) the Company's distribution unit (referred to as UFPD) which distributes a variety of products to the manufactured housing industry nation-wide and is accounted for as a reporting unit within the North segment, and (c) the idX division, which designs, produces, and installs customized in-store environments, for customers world-wide.

With respect to the facilities in the north, south, and west segments, these facilities generally supply the three markets the Company serves nationally - Retail, Industrial, and Construction. Also, substantially all of our facilities support customers in the immediate geographical region surrounding the facility.

Our Alternative Materials, International and idX division have been included in the "All Other" column of the table below. The "Corporate" column includes unallocated administrative costs and certain incentive compensation expense.

	Three Months Ended June 30, 2018					
	North	South	West	All Other	Corporate	Total
Net sales to outside customers	$ 390,821	$ 291,320	$ 456,825	$ 155,474	$ —	$ 1,294,440
Intersegment net sales	18,558	20,675	14,464	61,957	—	115,654
Segment operating profit	19,822	14,902	29,698	4,319	(8,124)	60,617

	Three Months Ended July 1, 2017					
	North	South	West	All Other	Corporate	Total
Net sales to outside customers	$ 319,554	$ 221,583	$ 390,868	$ 140,370	$ —	$ 1,072,375
Intersegment net sales	16,790	19,378	22,249	49,197	—	107,614
Segment operating profit	16,246	10,229	24,704	5,798	(3,078)	53,899

	Six Months Ended June 30, 2018					
	North	South	West	All Other	Corporate	Total
Net sales to outside customers	$ 661,007	$ 533,340	$ 819,293	$ 274,657	$ —	$ 2,288,297
Intersegment net sales	30,583	39,323	30,063	124,677	—	224,646
Segment operating profit (loss)	28,517	34,447	50,780	1,219	(10,128)	104,835

	Six Months Ended July 1, 2017					
	North	South	West	All Other	Corporate	Total
Net sales to outside customers	$ 547,475	$ 410,326	$ 710,030	$ 250,674	$ —	$ 1,918,505
Intersegment net sales	32,962	36,656	44,082	68,127	—	181,827
Segment operating profit	26,224	20,918	43,008	6,404		