

MESA LABORATORIES INC /CO  
Form 10-Q  
November 04, 2015

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**United States**

**Securities and Exchange Commission**

**Washington, D.C. 20549**

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**FORM 10-Q**

**(Mark one)**

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

**For the quarterly period ended September 30, 2015**

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

**For the transition period from \_\_\_ to \_\_\_**

**Commission File No: 0-11740**

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**MESA LABORATORIES, INC.**

(Exact name of registrant as specified in its charter)

**Colorado**  
(State or other jurisdiction of  
incorporation or organization)

**84-0872291**  
(I.R.S. Employer  
Identification number)

**12100 West Sixth Avenue**

**Lakewood, Colorado** **80228**  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(303) 987-8000**

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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company  
(Do not check if a smaller reporting company)

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

Yes No

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

There were 3,603,713 shares of the Issuer's common stock, no par value, outstanding as of October 31, 2015.



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Signatures

Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)  
 Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)  
 Certification of Chief Executive Officer Pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350  
 Certification of Chief Financial Officer Pursuant to Rule 13a-14(b) and 18 U.S.C. Section 1350

**Part I. Financial Information****Item 1. Financial Statements****Mesa Laboratories, Inc.****Condensed Consolidated Balance Sheets**

(In thousands, except share amounts)

	<b>September 30, 2015</b>	<b>March 31, 2015</b>
	<b>(Unaudited)</b>	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 5,460	\$2,034
Accounts receivable, net	12,687	12,145
Inventories, net	13,363	12,420
Prepaid expenses and other	1,943	1,334
Deferred income taxes	1,541	1,689
Total current assets	34,994	29,622
Property, plant and equipment, net	14,713	9,598
Intangibles, net	40,794	33,231
Goodwill	65,392	44,869
Total assets	\$ 155,893	\$ 117,320
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 3,038	\$2,503
Accrued salaries and payroll taxes	4,021	4,105
Unearned revenues	3,041	1,314
Current portion of contingent consideration	4,892	1,220
Other accrued expenses	5,629	1,307
Income taxes payable	233	1,208
Current portion of long-term debt	3,000	3,000
Total current liabilities	23,854	14,657
Deferred income taxes	4,861	5,122
Long-term debt	43,750	23,250

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Contingent consideration	4,480	812
Total liabilities	76,945	43,841
Commitments and Contingencies (Note 7)		
Stockholders' equity:		
Common stock, no par value; authorized 25,000,000 shares; issued and outstanding, 3,602,331 and 3,561,540 shares, respectively	19,675	17,751
Retained earnings	58,876	55,962
Accumulated other comprehensive income (loss)	397	(234 )
Total stockholders' equity	78,948	73,479
Total liabilities and stockholders' equity	\$ 155,893	\$ 117,320

See accompanying notes to condensed consolidated financial statements.

**Mesa Laboratories, Inc.****Condensed Consolidated Statements of Income**

(Unaudited)

(In thousands except per share data)

	<b>Three Months Ended September 30,</b>		<b>Six Months Ended September 30,</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Revenues	\$21,776	\$18,540	\$39,934	\$34,940
Cost of revenues	8,709	7,417	15,726	14,112
Gross profit	13,067	11,123	24,208	20,828
Operating expenses				
Selling	2,288	1,342	4,087	3,405
General and administrative	6,782	4,005	11,519	7,841
Research and development	991	876	1,954	1,627
Total operating expenses	10,061	6,223	17,560	12,873
Operating income	3,006	4,900	6,648	7,955
Other expense, net	213	157	329	319
Earnings before income taxes	2,793	4,743	6,319	7,636
Income taxes	1,041	1,683	2,261	2,695
Net income	\$1,752	\$3,060	\$4,058	\$4,941
Net income per share:				
Basic	\$0.49	\$0.87	\$1.13	\$1.41
Diluted	0.47	0.84	1.09	1.35
Weighted average common shares outstanding:				
Basic	3,598	3,508	3,587	3,504
Diluted	3,742	3,640	3,715	3,648

See accompanying notes to condensed consolidated financial statements.





**Mesa Laboratories, Inc.****Condensed Consolidated Statements of Comprehensive Income**

(Unaudited)

(In thousands)

	<b>Three Months Ended September 30, 2015 2014</b>		<b>Six Months Ended September 30, 2015 2014</b>	
Net Income	\$1,752	\$3,060	\$4,058	\$4,941
Other comprehensive income, net of tax:				
Foreign currency translation	603	--	631	--
Total comprehensive income	\$2,355	\$3,060	\$4,689	\$4,941

See accompanying notes to condensed consolidated financial statements.

**Mesa Laboratories, Inc.****Condensed Consolidated Statements of Cash Flows**

(Unaudited)

(In thousands)

	<b>Six Months Ended</b>	
	<b>September 30,</b>	
	<b>2015</b>	<b>2014</b>
Cash flows from operating activities:		
Net income	\$4,058	\$4,941
Depreciation and amortization	3,439	2,721
Stock-based compensation	657	516
Loss on disposition of assets	--	16
Deferred income taxes	(113 )	--
Foreign currency adjustments	647	--
Change in assets and liabilities, net of effects of acquisitions		
Accounts receivable, net	668	(1,952 )
Inventories, net	(548 )	(1,515 )
Prepaid expenses and other	(609 )	(682 )
Accounts payable	65	632
Accrued liabilities and taxes payable	2,785	(307 )
Unearned revenues	114	(626 )
Contingent consideration	(2,201 )	--
Net cash provided by operating activities	8,962	3,744
Cash flows from investing activities:		
Acquisitions	(20,687)	(13,817)
Purchases of property, plant and equipment	(5,035 )	(908 )
Net cash used in investing activities	(25,722)	(14,725)
Cash flows from financing activities:		
Proceeds from the issuance of debt	22,500	18,000
Payments on debt	(2,000 )	(8,750 )
Dividends	(1,144 )	(1,052 )
Proceeds from the exercise of stock options	846	865
Net cash provided by financing activities	20,202	9,063
Effect of exchange rate changes on cash and cash equivalents	(16 )	--
Net increase (decrease) in cash and cash equivalents	3,426	(1,918 )
Cash and cash equivalents at beginning of period	2,034	5,575

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Cash and cash equivalents at end of period	\$5,460	\$3,657
Cash paid for:		
Income taxes	\$2,862	\$1,492
Interest	315	210
Supplemental non-cash activity:		
Repayment of employee loans for stock options	\$--	\$24
Contingent consideration as part of an acquisition	9,541	--

See accompanying notes to condensed consolidated financial statements.

**Mesa Laboratories, Inc.**

**Notes to Condensed Consolidated Financial Statements**

**Note 1 -Description of Business and Summary of Significant Accounting Policies**

*Description of Business*

Mesa Laboratories, Inc. was incorporated under the laws of the State of Colorado on March 26, 1982. The terms “we,” “us,” “our,” the “Company” or “Mesa” are used in this report to refer collectively to the parent company and the subsidiaries through which our various businesses are actually conducted. We pursue a strategy of focusing primarily on quality control products and services, which are sold into niche markets that are driven by regulatory requirements. We prefer markets that have limited competition where we can establish a commanding presence and achieve high gross margins. We are organized into four divisions across eight physical locations. Our Instruments Division designs, manufactures and markets quality control instruments and disposable products utilized in connection with the healthcare, pharmaceutical, food and beverage, medical device, industrial hygiene, environmental air sampling and semiconductor industries. Our Biological Indicators Division manufactures and markets biological indicators and distributes chemical indicators used to assess the effectiveness of sterilization processes, including steam, hydrogen peroxide, ethylene oxide and radiation, in the hospital, dental, medical device and pharmaceutical industries. Our Continuous Monitoring Division designs, develops and markets systems which are used to monitor various environmental parameters such as temperature, humidity and differential pressure to ensure that critical storage and processing conditions are maintained in hospitals, pharmaceutical and medical device manufacturers, blood banks, pharmacies and a number of other laboratory and industrial environments. Our Cold Chain Division provides parameter monitoring of products in a cold chain, consulting services such as compliance monitoring, packaging development and validation or mapping of transport and storage containers, and thermal packaging products such as coolers, boxes, insulation materials and phase-change products to control temperature during transport.

*Basis of Presentation*

The accompanying condensed consolidated balance sheet as of March 31, 2015, has been derived from audited consolidated financial statements. The accompanying unaudited interim condensed consolidated financial statements have been prepared on the same basis as our annual audited consolidated financial statements and in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial statements. In the opinion of management, such unaudited information includes all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation of this interim information. Operating results and cash flows for interim periods are not necessarily indicative of results that can be expected for the entire year. The information included in this report should be read in conjunction with our audited consolidated financial statements and notes thereto included in our

Annual Report on Form 10-K for the year ended March 31, 2015.

The summary of our significant accounting policies is incorporated by reference to our Annual Report on Form 10-K for the year ended March 31, 2015.

***Recently Issued Accounting Pronouncements***

In May 2014, the Financial Accounting Standards Board (“FASB”) and International Accounting Standards Board (“IASB”) issued a jointly converged standard on the recognition of revenue from contracts with customers. The issued guidance converges the criteria for reporting revenues, as well as requiring disclosures sufficient to describe the nature, amount, timing and uncertainty of revenues and cash flows arising from these contracts. Companies can transition to the standard either retrospectively or as a cumulative effective adjustment as of the date of adoption. The new standard is effective for our fiscal year (and interim periods within that year) ending March 31, 2019. We are evaluating the impact of this standard on our condensed consolidated financial statements and disclosures.

## Note 2 – Acquisitions and Dispositions

### *Acquisitions*

For the six months ended September 30, 2015, our acquisitions of businesses (net of cash acquired) totaled \$30,228,000, which consisted of the following:

#### **Infitrak**

On July 6, 2015, we completed a business combination (the “Infitrak Acquisition”) whereby we acquired all of the common stock of 2396081 Ontario Inc. and its wholly owned operating subsidiary, Infitrak Inc. (collectively “Infitrak”), a company whose business provides consulting, packaging and measuring solutions for cold chain applications. The stock purchase agreement (the “Infitrak Agreement”) includes provisions for both contingent consideration based upon the two year growth in gross profit (as defined in the Earn-Out Agreement) of our cold chain business subsequent to the acquisition and for a holdback payment (subject to a post-closing adjustment), payable at the one year anniversary of the closing date.

Under the terms of the Infitrak Agreement, we are required to pay contingent consideration if the gross profit (as defined in the Earn-Out Agreement) for our cold chain business for the two years subsequent to the acquisition meets certain levels. The potential consideration payable ranges from \$0 to \$15,000,000 CDN (approximately \$11,500,000) and is based upon a sliding scale of growth in gross profit (as defined in the Earn-Out Agreement) for year one and year two of 30 to 70 percent and 15 to 75 percent, respectively. Based upon both historical and projected growth rates, we recorded \$9,541,000 of contingent consideration payable which represents our best estimate of the amount that will ultimately be paid. After the finalization of our purchase accounting, any changes to the contingent consideration ultimately paid will result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results of our cold chain business and we will adjust the contingent liability on a go forward basis, based on then current information. The contingent consideration is payable in two annual installments beginning in the second quarter of our year ending March 31, 2017.

We expect to achieve savings and generate growth as we integrate the Infitrak operations and sales and marketing functions. These factors, among others, contributed to a purchase price in excess of the estimated fair value of the net identifiable assets acquired and, as a result, we recorded goodwill in connection with this transaction. The goodwill is not expected to be deductible for tax purposes and it was assigned to our Cold Chain segment.

The Infitrak Acquisition constituted the acquisition of a business and was recognized at fair value. Due to the recent nature of the transaction, the purchase price allocation was based upon a preliminary estimated fair value of the assets and liabilities acquired as we are in the process of finalizing our valuation of the assets acquired and liabilities assumed. We determined the preliminary estimated fair values using discounted cash flow analyses and estimates made by management. The following reflects our preliminary allocation of the consideration, subject to customary purchase price adjustments in accordance with the Infitrak Agreement (in thousands):

Cash consideration	\$8,748
Holdback payment liability	637
Contingent consideration liability	9,541
Aggregate consideration	\$18,926
Accounts receivable, net	\$925
Inventories, net	310
Property, plant and equipment, net	530
Intangibles, net	5,869
Goodwill	12,529
Accounts payable	(470 )
Accrued liabilities	(767 )
Total purchase price allocation	\$18,926

The accompanying condensed consolidated statements of income include the results of the Infitrak Acquisition from the acquisition date of July 6, 2015. The pro forma effects of the acquisition on the results of operations as if the acquisition had been completed on April 1, 2015 and 2014, are as follows (in thousands, except per share data):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>September 30, 2015</b>	<b>2014</b>	<b>September 30, 2015</b>	<b>2014</b>
Revenues	\$21,858	\$19,302	\$41,774	\$36,465
Net income	1,765	3,150	4,360	5,122
Net Income per common share:				
Basic	\$0.49	\$0.90	\$1.22	\$1.46
Diluted	0.47	0.87	1.17	1.40

**North Bay**

On August 6, 2015, we completed a business combination (the “North Bay Acquisition”) whereby we acquired substantially all of the assets (other than certain fixed assets) and certain liabilities of the dental sterilizer testing business of North Bay Bioscience, LLC (“North Bay”). The asset purchase agreement (the “North Bay Agreement”) includes a provision for a holdback payment (subject to a post-closing adjustment), payable at the one year anniversary of the closing date.

We expect to achieve savings and generate growth as we integrate the North Bay operations and sales and marketing functions. These factors, among others, contributed to a purchase price in excess of the estimated fair value of the net identifiable assets acquired and, as a result, we recorded goodwill in connection with this transaction. The goodwill is expected to be deductible for tax purposes and it was assigned to our Biological Indicators segment.

The North Bay Acquisition constituted the acquisition of a business and was recognized at fair value. Due to the recent nature of the transaction, the purchase price allocation was based upon a preliminary estimated fair value of the assets and liabilities acquired as we are in the process of finalizing our valuation of the assets acquired and liabilities assumed. We determined the preliminary estimated fair values using discounted cash flow analyses and estimates made by management. The following reflects our preliminary allocation of the consideration, subject to customary purchase price adjustments in accordance with the North Bay Agreement (in thousands):

Cash consideration	\$10,322
Holdback payment liability	1,000
Aggregate consideration	\$11,322
Cash	\$20
Accounts receivable, net	285
Inventories, net	85
Property, plant and equipment, net	229
Intangibles, net	4,454
Goodwill	7,962
Accrued liabilities	(100 )
Unearned revenues	(1,613 )
Total purchase price allocation	\$11,322

The accompanying condensed consolidated statements of income include the results of the North Bay Acquisition from the acquisition date of August 6, 2015. The pro forma effects of the acquisition on the results of operations as if the acquisition had been completed on April 1, 2015 and 2014, are as follows (in thousands, except per share data):



	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Revenues	\$22,124	\$19,620	\$41,328	\$37,100
Net income	1,826	3,210	4,352	5,241
Net Income per common share:				
Basic	\$0.51	\$0.91	\$1.21	\$1.50
Diluted	0.49	0.88	1.17	1.44

**Note 3 - Inventories**

Inventories consist of the following (in thousands):

	<b>September 30, 2015</b>	<b>March 31, 2015</b>
Raw materials	\$ 11,641	\$10,366
Work-in-process	124	530
Finished goods	2,022	1,913
Less: reserve	(424 )	(389 )
	\$ 13,363	\$12,420

**Note 4 - Long-Term Debt**

Long-term debt consists of the following (in thousands):

	<b>September 30, 2015</b>	<b>March 31, 2015</b>
Line of credit (1.94% at September 30, 2015)	\$ 27,500	\$ 13,500
Term loan (1.94% at September 30, 2015)	19,250	12,750
Less: current portion	(3,000 )	(3,000 )
Long-term portion	\$ 43,750	\$ 23,250

In February 2012, we entered into a three year agreement (the “Credit Facility”) for a \$20,000,000 revolving line of credit (“Line of Credit”) and up to \$1,000,000 of letters of credit. Funds from the Credit Facility were used for general working capital and corporate needs, retiring existing debt, or to support acquisitions and capital expenditures.

In April 2014, the Credit Facility was amended to include a \$15,000,000 term loan (the “Initial Term Loan”) and to extend the maturity date of the Credit Facility to June 30, 2017.

On July 1, 2015, we further amended our Credit Facility to extend the maturity date to June 30, 2020, increase the Line of Credit to \$50,000,000 and establish a new \$20,000,000 term loan (the “Term Loan”). The majority of the proceeds from the Term Loan were used to pay down the remaining \$12,000,000 balance of the Initial Term Loan. The remaining \$8,000,000 was combined with a \$1,000,000 draw under the Line of Credit to fund the Infitrak Acquisition (see Note 2).

Under the Line of Credit, indebtedness bears interest at either: (1) LIBOR, as defined, plus an applicable margin ranging from 1.5% to 2.25%; or (2) the bank’s commercial bank floating rate (“CBFR”), which is the bank’s prime rate adjusted down by 0.5%. We elect the interest rate with each borrowing under the line of credit. In addition, there is an unused line fee of 0.25%. Letter of credit fees are based on the applicable LIBOR rate.

The Term Loan bears interest at LIBOR, as defined, plus an applicable margin ranging from 1.5% to 2.25% and requires 20 quarterly principal payments (the first due date was July 15, 2015) in the amount of \$750,000 with the remaining balance of principal and accrued interest due on June 30, 2020.

The Credit Facility is secured by all of our assets and requires us to maintain a ratio of funded debt to our trailing four quarters of EBIDTA, as defined, of 3.25 to 1.0 through March 31, 2016 and 3.0 to 1.0 thereafter, and a minimum fixed charge coverage ratio of 1.35 to 1.0. We were in compliance with the required covenants at September 30, 2015.

As of September 30, 2015, future contractual maturities of debt as are as follows (in thousands):

<b>Year Ending March 31,</b>	
2016	\$1,500
2017	3,000
2018	3,000
2019	3,000
2020	3,000
Thereafter	33,250
	\$46,750

In October 2015, we made a \$750,000 required principle payment on the Term Loan and we borrowed \$2,000,000 under the Line of Credit to fund a litigation settlement payment (see Note 7).

**Note 5 - Stock-Based Compensation**

Amounts recognized in the condensed consolidated financial statements related to stock-based compensation are as follows (in thousands, except per share data):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Total cost of stock-based compensation charged against income before income taxes	\$ 330	\$ 237	\$ 657	\$ 516
Amount of income tax benefit recognized in earnings	123	84	235	182
Amount charged against net income	\$ 207	\$ 153	\$ 422	\$ 334
Impact on net income per common share:				
Basic	\$0.06	\$0.04	\$0.12	\$0.10
Diluted	0.06	0.04	\$0.11	0.09

Stock-based compensation expense is included in cost of revenues, selling, and general and administrative expense in the accompanying condensed consolidated statements of income.

The fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model (“Black-Scholes”). We use historical data to estimate the expected price volatility, the expected stock option life and expected forfeiture rate. The risk-free interest rate is based on the United States Treasury yield curve in effect at the time of grant for the estimated life of the stock option. The dividend yield is calculated based upon the dividend payments made during the prior four quarters as a percent of the average stock price for that period.

The following is a summary of stock option activity for the six months ended September 30, 2015:

<b>Number of Shares</b>	<b>Weighted- Average Exercise Price per Share</b>	<b>Weighted- Average Remaining Contractual</b>	<b>Aggregate Intrinsic Value (000s)</b>
---------------------------------	---	--	---

			<b>Term</b>	
Outstanding at March 31, 2015	437,248	\$ 55.81	4.9	\$ 9,445
Stock options granted	180,050	72.18	7.3	
Stock options forfeited	(11,989 )	77.29	7.6	
Stock options expired	--	--		
Stock options exercised	(49,822 )	38.56		
Outstanding at September 30, 2015	555,487	62.20	5.5	27,330
Exercisable at September 30, 2015	189,816	40.93	3.7	13,376

The total intrinsic value of stock options exercised was \$2,759,463 and \$1,516,000 for the six months ended September 30, 2015 and 2014, respectively.

A summary of the status of our unvested stock option shares as of September 30, 2015 is as follows:

	<b>Number of Shares</b>	<b>Weighted- Average Grant-Date Fair Value</b>
Unvested at March 31, 2015	274,038	\$ 18.42
Stock options granted	180,050	18.5
Stock options forfeited	(11,989 )	19.63
Stock options vested	(76,428 )	14.56
Unvested at September 30, 2015	365,671	19.23

As of September 30, 2015, there was \$5,214,386 of total unrecognized compensation expense related to unvested stock options. As of September 30, 2015, we have 917,610 shares available for future stock option grants.

**Note 6 - Net Income Per Share**

Basic net income per share is computed by dividing net income by the weighted-average number of common shares outstanding during the reporting period. Diluted net income per share is computed similarly to basic net income per share, except that it includes the potential dilution that could occur if dilutive securities were exercised.

The following table presents a reconciliation of the denominators used in the computation of net income per share - basic and diluted (in thousands, except per share data):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>September 30, 2015</b>	<b>2014</b>	<b>September 30, 2015</b>	<b>2014</b>
Net income available for shareholders	\$1,752	\$3,060	\$4,058	\$4,941
Weighted average outstanding shares of common stock	3,598	3,508	3,587	3,504
Dilutive effect of stock options	144	132	128	144
Common stock and equivalents	3,742	3,640	3,715	3,648
Net income per share:				
Basic	\$0.49	\$0.87	\$1.13	\$1.41
Diluted	0.47	0.84	1.09	1.35

For both the three and six months ended September 30, 2015, \$136,000 and \$135,000 outstanding stock options, respectively, were excluded from the calculation of diluted net income per share because the exercise prices of the stock options were greater than or equal to the average price of the common shares and, therefore, their inclusion would have been anti-dilutive.

For both the three and six months ended September 30, 2014, 156,000 and zero outstanding stock options, respectively, were excluded from the calculation of diluted net income per share because the exercise prices of the stock options were greater than or equal to the average price of the common shares and, therefore, their inclusion would have been anti-dilutive.

**Note 7- Commitments and Contingencies**

Under the terms of the Amega Agreement, we were required to pay contingent consideration (the “Amega Earn-Out”) if the cumulative revenues for our Continuous Monitoring Division for the three years subsequent to the acquisition met certain levels. The potential consideration payable ranged from \$0 to \$10,000,000 and was based upon a sliding scale of three-year cumulative revenues between \$31,625,000 and \$43,500,000. Based upon both historical and projected growth rates, we recorded \$500,000 of contingent consideration payable which represented our best estimate of the amount that would ultimately be paid. Any changes to the contingent consideration ultimately paid would have resulted in additional income or expense in our condensed consolidated statements of income. The contingent consideration was payable in the third quarter of our year ending March 31, 2017.

In November 2014, Amega and its owner Anthony Amato (“Amato”) filed a complaint (*Anthony Amato and Amega Scientific Corporation v. Mesa Laboratories, Inc., Civil Action No. 1:14-cv-03228*) in the United States District Court for the district of Colorado asserting, among other items, that our termination of Amato as an employee impacted his ability to maximize the potential consideration payable under the Amega Earn-Out and to exercise stock options that failed to vest. The plaintiff was seeking an immediate maximum payout of \$10,000,000 under the Amega Earn-Out, the immediate acceleration of the 10,000 stock options granted Amato upon his initial employment along with other consequential damages in excess of \$500,000, lost future earnings and punitive damages. In addition, Amato alleged that we improperly withheld \$704,065.86 from the holdback consideration under the Amega Agreement. In January 2015 we filed a motion to dismiss the complaint with prejudice.

In October 2015, we entered into a settlement agreement (the “Amato Settlement”) whereby we paid Amato \$3,165,000. In exchange, Amato agreed to dismiss the complaint, release Mesa of any and all claims by Amega and Amato, and relieve us of any future payment obligation under the Amega Earn-Out. Insurance covered \$415,000 of the settlement payment while we had \$1,041,000 accrued on our condensed consolidated balance sheet remaining from the original hold back and contingent consideration payable. The remaining \$1,709,000 was recorded as general and administrative expense in the accompanying condensed consolidated statements of income for the three and six months ended September 30, 2015.

Under the terms of the PCD Agreement, we are required to pay contingent consideration if the cumulative revenues for our process challenge device business for the three years subsequent to the acquisition meet certain levels. The potential consideration payable ranges from \$0 to \$1,500,000 and is based upon a sliding scale of three-year cumulative revenues between \$9,900,000 and \$12,600,000. Based upon both historical and projected growth rates, we recorded \$300,000 of contingent consideration payable which represented our best estimate of the amount that will ultimately be paid. The contingent consideration is payable in our quarter ending December 31, 2015 (based upon the current run rate projected over the entire three-year contingent consideration period) and is subject to modification at the end of the earn-out period based upon the actual revenues earned over the contingent consideration period. Any changes to the contingent consideration ultimately paid will result in additional income or expense in our condensed consolidated statements of income. We will continue to monitor the results of our process challenge device business and we will adjust the contingent liability on a go forward basis, based on then current information.

A company is required to collect and remit state sales tax from certain of its customers if that company is determined to have “nexus” in a particular state. The determination of nexus varies state by state and often requires knowledge of each jurisdiction’s tax case law. During the year ended March 31, 2013, we determined that there are states in which we most likely had established nexus during prior periods without properly collecting and remitting sales tax. We recorded an estimate of \$100,000 associated with one specific state but we were unable to estimate our remaining exposure at that time. During the year ended March 31, 2014, we completed our analysis associated with the remaining states and we recorded an estimate of \$1,408,000, which was included in other accrued expenses on the consolidated balance sheets and in general and administrative expense on the consolidated statements of income for the year ended March 31, 2014. That estimate was based upon facts and circumstances known at such time and our ultimate liability was subject to change as further analysis is completed and state sales tax returns are filed.

During the year ended March 31, 2015 we successfully completed and filed several state sales tax returns which concluded our obligation for historical sales taxes in those states. In addition we continued to work through the process in the remaining states. As a result of this work, we determined that our exposure had increased above and beyond our original accrual and as a result, we recorded an additional accrual of \$460,000 during the year ended March 31, 2015. During the six months ended September 30, 2015 we successfully completed and filed additional state sales tax returns which concluded our obligation for historical sales taxes in those remaining states.

## Note 8 – Comprehensive Income

The following table summarizes the changes in each component of accumulated other comprehensive income (“AOCI”), net of tax (in thousands):

<b>Foreign Currency Translation</b>	<b>AOCI</b>
---	-------------



Balance at June 30, 2015	\$ (206	) \$(206 )
Quarter ended September 30, 2015:		
Unrealized gain arising during the period	603	603
Balance at September 30, 2015	\$ 397	\$397

	<b>Foreign</b>	
	<b>Currency</b>	
	<b>Translation</b>	<b>AOCI</b>
Balance at June 30, 2014	\$ --	\$ --
Quarter ended September 30, 2014:		
Unrealized gain arising during the period	--	--
Balance at September 30, 2014	\$ --	\$ --

	<b>Foreign</b>	
	<b>Currency</b>	
	<b>Translation</b>	<b>AOCI</b>
Balance at March 31, 2015	\$ (234	) \$(234 )
Six months ended September 30, 2015:		
Unrealized gain arising during the period	631	631
Balance at September 30, 2015	\$ 397	\$397

	<b>Foreign Currency Translation</b>	<b>AOCI</b>
Balance at March 31, 2014	\$ --	\$ --
Six months ended September 30, 2014:		
Unrealized gain arising during the period	--	--
Balance at September 30, 2014	\$ --	\$ --

**Note 9 - Segment Information**

We have four reporting segments: Biological Indicators, Instruments, Continuous Monitoring and Cold Chain. The following tables set forth our segment information (in thousands):

**Three Months Ended September 30, 2015**

	<b>Biological Indicators</b>		<b>Instruments</b>	<b>Continuous Monitoring</b>	<b>Cold Chain</b>	<b>Total</b>
Revenues	\$8,482	\$ 9,228		\$ 2,226	\$1,840	\$21,776
Gross profit	\$5,539	\$ 5,705		\$ 955	\$868	\$13,067
Selling expenses	507	1,210		508	63	2,288
	\$5,032	\$ 4,495		\$ 447	\$805	10,779
Reconciling items <sup>(1)</sup>						(7,986)
Earnings before income taxes						\$2,793

**Three Months Ended September 30, 2014**

	<b>Biological Indicators</b>		<b>Instruments</b>	<b>Continuous Monitoring</b>	<b>Cold Chain</b>	<b>Total</b>
Revenues	\$6,441	\$ 9,065		\$ 3,034	\$ --	\$18,540
Gross profit	\$4,051	\$ 5,455		\$ 1,617	\$ --	\$11,123
Selling expenses	368	829		145	--	1,342
	\$3,683	\$ 4,626		\$ 1,472	\$ --	9,781
Reconciling items <sup>(1)</sup>						(5,038)
Earnings before income taxes						\$4,743

**Six Months Ended September 30, 2015**

	<b>Biological Indicators</b>		<b>Instruments</b>	<b>Continuous Monitoring</b>	<b>Cold Chain</b>	<b>Total</b>
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Revenues	\$15,718	\$ 17,559	\$ 4,817	\$1,840	\$39,934
Gross profit	\$10,288	\$ 11,060	\$ 1,992	\$868	\$24,208
Selling expenses	867	2,191	966	63	4,087
	\$9,421	\$ 8,869	\$ 1,026	\$805	20,121
Reconciling items <sup>(1)</sup>					(13,802)
Earnings before income taxes					\$6,319

**Six Months Ended September 30, 2014**

	<b>Biological Indicators</b>	<b>Instruments</b>	<b>Continuous Monitoring</b>	<b>Cold Chain</b>	<b>Total</b>
Revenues	\$12,858	\$ 16,750	\$ 5,332	\$ --	\$34,940
Gross profit	\$7,835	\$ 10,382	\$ 2,611	\$ --	\$20,828
Selling expenses	772	1,821	812	--	3,405
	\$7,063	\$ 8,561	\$ 1,799	\$ --	17,423
Reconciling items <sup>(1)</sup>					(9,787)
Earnings before income taxes					\$7,636

<sup>(1)</sup> Reconciling items include general and administrative, research and development, and other expenses.

	<b>September 30, 2015</b>	<b>March 31, 2015</b>
Total assets		
Biological Indicators	\$ 51,641	\$36,304
Instruments	44,952	44,401
Continuous Monitoring	30,339	31,558
Cold Chain	20,017	--
Corporate and administrative	8,944	5,057
	\$ 155,893	\$ 117,320

All long-lived assets are located in the United States except for \$4,359,000 and \$18,690,000 which are associated with our French and Canadian subsidiaries, respectively.

Revenues from external customers are attributed to individual countries based upon locations to which the product is shipped or exported, as follows (in thousands):

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>September 30, 2015</b>	<b>2014</b>	<b>September 30, 2015</b>	<b>2014</b>
Net revenues from unaffiliated customers:				
United States	\$12,529	\$9,698	\$24,723	\$18,189
Foreign	9,247	8,842	15,211	16,751

\$21,776 \$18,540 \$39,934 \$34,940

No foreign country exceeds 10% of total revenues other than Canada, which represents 10.6% of revenues for the three months ended September 30, 2015.

#### **Note 10 – Income Taxes**

For interim income tax reporting, we estimate our annual effective tax rate and apply this effective tax rate to our year to date pre-tax income. Each quarter, the estimate of the annual effective tax rate is updated, and if the estimated effective tax rate changes, a cumulative adjustment is made. There is a potential for volatility of the effective tax rate due to several factors, including changes in the mix of the pre-tax income and the jurisdictions to which it relates, changes in tax laws and foreign tax holidays, settlement with taxing authorities and foreign currency fluctuations.

Our effective income tax rate was 37.3 and 35.5 percent for the three months ended September 30, 2015 and 2014, respectively and 35.8 and 35.3 percent for the six months ended September 30, 2015 and 2014, respectively. The effective tax rate for the three and six months ended September 30, 2015 differed from the statutory federal rate of 35 percent primarily as a result of the impact of state income taxes and certain discrete period items. We anticipate that our effective tax rate for the year ending March 31, 2016 will approximate 35 to 37 percent.

**Note 11 - Subsequent Event**

In October 2015, our Board of Directors declared a quarterly cash dividend of \$0.16 per share of common stock, payable on December 15, 2015, to shareholders of record at the close of business on November 30, 2015.

## **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

### **Forward Looking Statements**

*This report contains information that may constitute "forward-looking statements." Generally, the words "believe," "expect," "project," "anticipate," "estimate," "intend," "will" and similar expressions identify forward-looking statements, which generally are not historical in nature. However, the absence of these words or similar expressions does not mean that a statement is not forward-looking. All statements that address operating performance, events or developments that we expect or anticipate will occur in the future — including statements relating to revenue growth and statements expressing general views about future operating results — are forward-looking statements. Management believes that these forward-looking statements are reasonable as and when made. However, caution should be taken not to place undue reliance on any such forward-looking statements because such statements speak only as of the date when made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. In addition, forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or projections. These risks and uncertainties include, but are not limited to those described in Part II, "Item 1A. Risk Factors" and elsewhere in this report and in our Annual Report on Form 10-K for the year ended March 31, 2015, and those described from time to time in our subsequent reports filed with the Securities and Exchange Commission.*

### **General Discussion**

We pursue a strategy of focusing primarily on quality control products and services, which are sold into niche markets that are driven by regulatory requirements. We prefer markets that have limited competition where we can establish a commanding presence and achieve high gross margins. We are organized into four divisions across eight physical locations. Our Instruments Division designs, manufactures and markets quality control instruments and disposable products utilized in connection with the healthcare, pharmaceutical, food and beverage, medical device, industrial hygiene, environmental air sampling and semiconductor industries. Our Biological Indicators Division manufactures and markets biological indicators and distributes chemical indicators used to assess the effectiveness of sterilization processes, including steam, hydrogen peroxide, ethylene oxide and radiation, in the hospital, dental, medical device and pharmaceutical industries. Our Continuous Monitoring Division designs, develops and markets systems which are used to monitor various environmental parameters such as temperature, humidity and differential pressure to ensure that critical storage and processing conditions are maintained in hospitals, pharmaceutical and medical device manufacturers, blood banks, pharmacies and a number of other laboratory and industrial environments. Our Cold Chain Division provides parameter monitoring of products in a cold chain, consulting services such as compliance monitoring, packaging development and validation or mapping of transport and storage containers, and thermal packaging products such as coolers, boxes, insulation materials and phase-change products to control temperature during transport.

Our revenues come from two main sources – product sales and services. Product sales are dependent on several factors, including general economic conditions, both domestic and international, customer capital spending trends, competition, introduction of new products and acquisitions. Biological indicator and cold chain packaging products are disposable and are used on a routine basis for quality control, thus product sales are less sensitive to general economic conditions. Instrument products, cold chain services and continuous monitoring systems have a longer life, and their purchase by our customers is somewhat discretionary, so sales are more sensitive to general economic conditions. Service demand is driven by our customers' quality control and regulatory environments, some of which require periodic repair and recalibration or certification of our instrument products and continuous monitoring systems. We typically evaluate costs and pricing annually. Our policy is to price our products and systems competitively and, where possible, we try to pass along cost increases in order to maintain our margins.

Gross profit is affected by our product mix, manufacturing efficiencies and price competition. Historically, as we have integrated our acquisitions and taken advantage of manufacturing efficiencies, our gross margins for some of the products have improved. There are, however, differences in gross margins between different product lines, and ultimately the mix of sales will continue to impact our overall gross margin.

Selling expense is driven primarily by labor costs, including salaries and commissions. Accordingly, it may vary with sales levels. Labor costs and amortization of intangible assets drive the substantial majority of general and administrative expense. Research and development expense is predominantly comprised of labor costs and third party consultants.



Year Ending March 31, 2016 Acquisitions

During the year ending March 31, 2016, we completed the following eight acquisitions (the “2016 Acquisitions”):

In October 2015, we completed six business combinations (the “October 2015 European BI Distributor Acquisitions”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of BIOLOGIK S.R.L., VWR International PBI S.R.L., Cruinn Diagnostics Ltd., Mecolab AG, Miclev Medical Products AB and Tiselab S.L.’s business segment associated with the distribution of our biological indicator products.

In August 2015, we completed a business combination (the “North Bay Acquisition”) whereby we acquired substantially all of the assets (other than certain fixed assets) and certain liabilities of the dental sterilizer testing business of North Bay Bioscience, LLC (“North Bay”).

In July 2015, we completed a business combination (the “Infitrak Acquisition”) whereby we acquired all of the common stock of 2396081 Ontario Inc. and its wholly owned operating subsidiary, Infitrak Inc. (collectively “Infitrak”), a company whose business provides consulting, packaging and measuring solutions for cold chain applications.

Year Ended March 31, 2015 Acquisitions

During the year ended March 31, 2015, we completed the following six acquisitions (the “2015 Acquisitions”):

In March 2015, we completed a business combination (the “Früh Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of Dr. Früh Control GmbH’s (“Fruh”) business segment associated with the distribution of our biological indicator products.

In February 2015, we completed a business combination (the “Cherwell Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of Cherwell Laboratories Limited’s (“Cherwell”), business segment associated with the distribution of our biological indicator products.

In October 2014, we completed a business combination (the “ATI Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of ATI Atlas Limited (“ATI”), a distributor of our biological indicator products.

In October 2014, we completed a business combination (the “PCD Acquisition”) with PCD-Process Challenge Devices, LLC (“PCD”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of PCD’s business segment associated with the sale of process challenge devices (“PCD’s”), which are used for quality control purposes in the field of ethylene oxide sterilization of medical devices.

In April 2014, we completed a business combination (the “BGI Acquisition”) whereby we acquired substantially all of the assets (other than cash and accounts receivable) and certain liabilities of BGI, Incorporated and BGI Instruments, Inc., (collectively “BGI”), businesses focused on the sale of equipment used primarily for particulate air sampling.

In April 2014, we completed a business combination (the “Amilabo Acquisition”) whereby we acquired all of the common stock of Amilabo SAS (“Amilabo”), a distributor of our biological indicator products.

## **General Trends and Outlook**

Our strategic objectives include growth both organically and through further acquisitions. During the year ended March 31, 2015, we continued to build our infrastructure to prepare for future growth, including the addition of key personnel to our operations, sales and marketing, research and development, and finance teams. We also invested in upgrading our information systems and intend to continue doing so.

The markets for our biological indicators and cold chain packaging products remain strong, as the disposable nature of these products makes them less sensitive to general economic conditions. The worldwide market for biological indicators is growing as more countries focus on verifying the effectiveness of sterilization processes.

In general, our instruments products, cold chain services and our continuous monitoring systems are impacted more by general economic conditions than our biological indicator and cold chain packaging products. As a result, uncertainty about global economic conditions may cause businesses to postpone spending in response to tighter credit, unemployment, negative financial news and/or declines in income or asset values. Worldwide and regional economic conditions could also reduce the demand for our products and services, as our customers reduce or delay capital equipment and other types of purchases. However demand for our instruments products, cold chain services and continuous monitoring systems remains strong and we strive to continue to grow revenues going forward.



We are working on several research and development projects that, if completed, may result in new products for both existing customers and new markets. We are hopeful that all of our divisions will have new products available for sale in the coming year.

## Results of Operations

The following table sets forth, for the periods indicated, condensed consolidated statements of income data. The table and the discussion below should be read in conjunction with the accompanying condensed consolidated financial statements and the notes thereto appearing elsewhere in this report (in thousands, except percent data):

	Three Months Ended September 30,			Percent		
	2015	2014	Change	Change		
Revenues	\$21,776	\$18,540	\$3,236	17	%	
Cost of revenues	8,709	7,417	1,292	17	%	
Gross profit	\$13,067	\$11,123	\$1,944	17	%	
Gross profit margin	60	%	60	%	--	%
Operating expenses						
Selling	\$2,288	\$1,342	\$946	70	%	
General and administrative	6,782	4,005	2,777	69	%	
Research and development	991	876	115	13	%	
	\$10,061	\$6,223	\$3,838	62	%	
Operating income	\$3,006	\$4,900	\$(1,894)	(39)	%	
Net income	1,752	3,060	(1,308)	(43)	%	
Net profit margin	8	%	17	%	(9)	%

	Six Months Ended September 30,			Percent		
	2015	2014	Change	Change		
Revenues	\$39,934	\$34,940	\$4,994	14	%	
Cost of revenues	15,726	14,112	1,614	11	%	
Gross profit	\$24,208	\$20,828	\$3,380	16	%	
Gross profit margin	61	%	60	%	1	%
Operating expenses						
Selling	\$4,087	\$3,405	\$682	20	%	
General and administrative	11,519	7,841	3,678	47	%	
Research and development	1,954	1,627	327	20	%	

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	\$17,560	\$12,873	\$4,687	36	%	
Operating income	\$6,648	\$7,955	\$(1,307)	(16	)%	
Net income	4,058	4,941	(883 )	(18	)%	
Net profit margin	10	%	14	%	(4	)%

**Revenues**

The following table summarizes our revenues by source (in thousands, except percent data):

	<b>Three Months Ended September 30,</b>			<b>Percent</b>	
	<b>2015</b>	<b>2014</b>	<b>Change</b>	<b>Change</b>	
Biological Indicators	\$8,482	\$6,441	\$2,041	32	%
Instruments	9,228	9,065	163	2	%
Continuous Monitoring	2,226	3,034	(808 )	(27	)%
Cold Chain	1,840	--	1,840	100	%
Total	\$21,776	\$18,540	\$3,236	17	