

Edgar Filing: FORWARD AIR CORP - Form 10-Q

FORWARD AIR CORP  
Form 10-Q  
October 26, 2016  
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 September 30, 2016  
Commission File No. 000-22490

FORWARD AIR CORPORATION  
(Exact name of registrant as specified in its charter)

Tennessee	62-1120025
(State or other jurisdiction of incorporation)	(I.R.S. Employer Identification No.)
430 Airport Road	
Greeneville, Tennessee	37745
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (423) 636-7000

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 "

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 x 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 definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer o Non-accelerated filer o Smaller reporting company o

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

Yes ☐ No ☒

The number of shares outstanding of the registrant's common stock, \$0.01 par value, as of October 20, 2016 was 30,523,021.

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## Part I. Financial Information

## Item 1. Financial Statements (Unaudited).

## Forward Air Corporation

## Condensed Consolidated Balance Sheets

(Dollars in thousands, except share and per share amounts)

(Unaudited)

	September 30, 2016	December 31, 2015
Assets		
Current assets:		
Cash	\$ 11,312	\$ 33,312
Accounts receivable, less allowance of \$1,924 in 2016 and \$2,405 in 2015	115,327	109,165
Other current assets	17,321	30,980
Total current assets	143,960	173,457
Property and equipment	369,582	343,147
Less accumulated depreciation and amortization	172,348	155,859
Total property and equipment, net	197,234	187,288
Goodwill and other acquired intangibles:		
Goodwill	184,675	205,609
Other acquired intangibles, net of accumulated amortization of \$58,943 in 2016 and \$51,212 in 2015	109,041	127,800
Total net goodwill and other acquired intangibles	293,716	333,409
Other assets	6,603	5,778
Total assets	\$ 641,513	\$ 699,932
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	\$ 18,415	\$ 23,334
Accrued expenses	30,843	29,823
Current portion of debt and capital lease obligations	41,866	55,887
Total current liabilities	91,124	109,044
Long-term debt and capital lease obligations, less current portion	814	28,617
Other long-term liabilities	14,726	12,340
Deferred income taxes	39,007	39,876
Shareholders' equity:		
Preferred stock	—	—
Common stock, \$0.01 par value: Authorized shares - 50,000,000, Issued and outstanding shares - 30,283,518 in 2016 and 30,543,864 in 2015	303	305
Additional paid-in capital	174,450	160,855
Retained earnings	321,089	348,895
Total shareholders' equity	495,842	510,055
Total liabilities and shareholders' equity	\$ 641,513	\$ 699,932

The accompanying notes are an integral part of the financial statements.



Forward Air Corporation  
Condensed Consolidated Statements of Comprehensive Income  
(In thousands, except per share data)  
(Unaudited)

	Three months ended		Nine months ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Operating revenue	\$249,552	\$ 247,093	\$717,737	\$ 702,705
Operating expenses:				
Purchased transportation	105,039	104,434	300,783	301,253
Salaries, wages and employee benefits	60,161	59,025	175,857	174,815
Operating leases	16,215	17,072	44,684	51,105
Depreciation and amortization	9,399	9,399	28,409	27,601
Insurance and claims	7,170	5,161	19,213	16,531
Fuel expense	3,416	3,826	9,375	12,034
Other operating expenses	23,452	23,575	65,218	66,608
Impairment of goodwill, intangibles and other assets	—	—	42,442	—
Total operating expenses	224,852	222,492	685,981	649,947
Income from operations	24,700	24,601	31,756	52,758
Other income (expense):				
Interest expense	(216)	(554)	(1,230)	(1,489)
Other, net	(4)	10	(149)	(127)
Total other income (expense)	(220)	(544)	(1,379)	(1,616)
Income before income taxes	24,480	24,057	30,377	51,142
Income tax expense	12,549	8,370	15,413	18,795
Net income and comprehensive income	\$11,931	\$ 15,687	\$14,964	\$ 32,347
Net income per share:				
Basic	\$0.39	\$ 0.51	\$0.49	\$ 1.04
Diluted	\$0.39	\$ 0.50	\$0.49	\$ 1.03
Dividends per share:	\$0.12	\$ 0.12	\$0.36	\$ 0.36

The accompanying notes are an integral part of the financial statements.

Forward Air Corporation  
Condensed Consolidated Statements of Cash Flows  
(In thousands)  
(Unaudited)

	Nine months ended September 30, 2016		September 30, 2015	
Operating activities:				
Net income	\$14,964		\$ 32,347	
Adjustments to reconcile net income to net cash provided by operating activities				
Depreciation and amortization	28,409		27,601	
Impairment of goodwill, intangible and other assets	42,442		—	
Share-based compensation	6,204		5,562	
Loss (gain) on disposal of property and equipment	201		(3	)
Provision for loss on receivables	268		463	
Provision for revenue adjustments	1,570		3,391	
Deferred income tax	661		5,546	
Excess tax benefit for stock options exercised	(137	)	(2,365	)
Changes in operating assets and liabilities				
Accounts receivable	(8,000	)	866	
Other current assets	13,083		(1,531	)
Accounts payable and accrued expenses	(5,057	)	(14,562	)
Net cash provided by operating activities	94,608		57,315	
Investing activities:				
Proceeds from disposal of property and equipment	1,795		1,200	
Purchases of property and equipment	(28,725	)	(18,541	)
Acquisition of business, net of cash acquired	(11,800	)	(61,878	)
Other	(673	)	(598	)
Net cash used in investing activities	(39,403	)	(79,817	)
Financing activities:				
Proceeds from term loan	—		125,000	
Payments of debt and capital lease obligations	(41,825	)	(87,367	)
Proceeds from exercise of stock options	7,041		11,351	
Payments of cash dividends	(10,987	)	(11,133	)
Repurchase of common stock (repurchase program)	(29,986	)	(9,996	)
Common stock issued under employee stock purchase plan	215		228	
Excess tax benefit for stock options exercised	137		2,365	
Cash settlement of share-based awards for minimum tax withholdings	(1,800	)	(1,931	)
Net cash (used in) provided by financing activities	(77,205	)	28,517	
Net (decrease) increase in cash	(22,000	)	6,015	
Cash at beginning of period	33,312		41,429	
Cash at end of period	\$11,312		\$ 47,444	

The accompanying notes are an integral part of the financial statements.





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Forward Air Corporation

Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

1. Basis of Presentation

Forward Air Corporation's ("the Company", "We", "Our") services can be classified into four principal reportable segments: Expedited LTL, Expedited Truckload Services ("TLX"), Intermodal and Pool Distribution (See note 11).

In our Expedited LTL segment, we provide time-definite transportation services to the North American deferred air freight market. Our Expedited LTL service operates a comprehensive national network for the time-definite surface transportation of expedited ground freight. The Expedited LTL service offers customers local pick-up and delivery and scheduled surface transportation of cargo as a cost effective, reliable alternative to air transportation. Expedited LTL's other services include shipment consolidation and deconsolidation, warehousing, customs brokerage, and other handling. The Expedited LTL segment primarily provides its transportation services through a network of terminals located at or near airports in the United States and Canada.

In our TLX segment, we provide expedited truckload brokerage, dedicated fleet services and maximum security and temperature-controlled logistics services. We are able to expedite this service by utilizing a dedicated fleet of team owner operators, some team company drivers as well as third party transportation providers. The TLX segment provides full truckload service in the United States and Canada.

In our Intermodal segment, we provide container and intermodal drayage services primarily within the Midwest region of the United States. Drayage is essentially the first and last mile of the movement of an intermodal container. We are providing this service both to and from ports and rail heads. Our Intermodal segment also provides dedicated contract and Container Freight Station ("CFS") warehouse and handling services. Today Intermodal operates primarily in the Midwest but through acquisition as well as green-field start-ups we anticipate moving into other geographies within the United States.

In our Pool Distribution segment, we provide pool distribution services throughout the Mid-Atlantic, Southeast, Midwest and Southwest continental United States. Pool distribution involves managing high-frequency handling and distribution of time-sensitive product to numerous destinations in specific geographic regions. Our primary customers for this service are regional and nationwide distributors and retailers, such as mall, strip mall and outlet based retail chains.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles for interim financial information 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 notes required by United States generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The Company's operating results are subject to seasonal trends when measured on a quarterly basis; therefore operating results for the three and nine months ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. For further information, refer to the consolidated financial statements and notes thereto included in the Forward Air Corporation Annual Report on Form 10-K for the year ended December 31, 2015.

The accompanying unaudited condensed consolidated financial statements of the Company include Forward Air Corporation and its subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

## 2. Recent Accounting Pronouncements

In March 2016, the Financial Accounting Standards Board (FASB) issued guidance that changes the accounting for certain aspects of share-based payments to employees. The guidance requires the recognition of the income tax effects of awards in the income statement when the awards vest or are settled, thus eliminating additional paid in capital (APIC) pools. The guidance also allows for the employer to repurchase more of an employee's shares for tax withholding purposes without triggering liability accounting. In addition, the guidance allows for a policy election to account for forfeitures as they occur rather than on an estimated basis. The guidance is effective in 2017 with early adoption permitted. We plan to adopt this guidance in January 2017 and while the elimination of APIC pools will result in increased volatility of our effective tax rate, the overall impact is expected to be minimal.

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Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

In February 2016, the FASB, issued ASU 2016-02, Leases, which introduces the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous guidance. The guidance will be effective for annual reporting periods beginning after December 15, 2018 and interim periods within those fiscal years with early adoption permitted. We are evaluating the impact of the future adoption of this standard on our consolidated financial statements.

In November 2015, the FASB issued Accounting Standard Update No. 2015-17, "Balance Sheet Classification of Deferred Taxes", an update to ASC 740, Income Taxes ("Update"). Current GAAP requires an entity to separate deferred income tax liabilities and assets into current and noncurrent amounts in a classified statement of financial position. To simplify the presentation of deferred income taxes, the amendments in this Update require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in this Update. For public business entities, the amendments in this Update are effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within those annual periods. The FASB also decided to permit earlier application by all entities as of the beginning of any interim or annual reporting period. The FASB further provides that this Update may be applied to all deferred tax liabilities and assets retrospectively to all periods presented. We adopted the Update retrospectively for the year ended December 31, 2015.

In May 2014, the FASB issued guidance on revenue from contracts with customers that will supersede most current revenue recognition guidance, including industry-specific guidance. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The guidance provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include capitalization of certain contract costs, consideration of time value of money in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. The guidance also requires enhanced disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The guidance is effective for the interim and annual periods beginning on or after December 15, 2017. The guidance permits the use of either a retrospective or cumulative effect transition method. We have not yet selected a transition method and are currently evaluating the impact of the amended guidance on our consolidated financial position, results of operations and related disclosures.

### 3. Acquisitions and Goodwill

#### Acquisition of Towne

On March 9, 2015, the Company acquired CLP Towne Inc. ("Towne") pursuant to the Agreement and Plan of Merger (the "Merger Agreement") resulting in Towne becoming an indirect, wholly-owned subsidiary of the Company. For the acquisition of Towne, the Company paid \$61,878 in net cash and assumed \$59,544 in debt and capital leases. With the exception of assumed capital leases, the assumed debt was immediately paid in full after funding of the acquisition. Of the total aggregate cash consideration paid, \$16,500 was placed into an escrow account, with \$2,000 of such amount being available to settle any shortfall in Towne's net working capital and with \$14,500 of such amount being available for a period of time to settle certain possible claims against Towne's common stockholders for indemnification. To the

extent the escrow fund is insufficient, certain equity holders have agreed to indemnify Forward Air, subject to certain limitations set forth in the Merger Agreement, as a result of inaccuracies in or breaches of certain of Towne's representations, warranties, covenants and agreements and other matters. Forward Air financed the Merger Agreement with a \$125,000 2 year term loan available under the senior credit facility discussed in note 5.

Towne is a full-service trucking provider offering time-sensitive less-than-truckload shipping, full truckload service, an extensive cartage network, container freight stations and dedicated trucking. Towne's airport-to-airport network provides scheduled deliveries to 61 service points. A fleet of approximately 525 independent contractor tractors provides the line-haul between those service points. The acquisition of Towne provides the Expedited LTL and TLX segments with opportunities to expand their service points and service offerings, such as pick up and delivery services. Additional benefits of the acquisition include increased linehaul network shipping density and a significant increase to our owner operator fleet, both of which are key to the profitability of the Company.

The assets, liabilities, and operating results of Towne have been included in the Company's consolidated financial statements from the date of acquisition and have been assigned to the Expedited LTL and TLX reportable segments. As the operations of Towne

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Forward Air Corporation

Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

were fully integrated into the Company's existing networks and operations, the Company is not able to provide the revenue and operating results from Towne included in our consolidated revenue and results since the date of acquisition.

Effective with the acquisition of Towne, the Company immediately entered into a restructuring plan to remove duplicate costs, primarily in the form of, but not limited to salaries, wages and benefits and facility leases. As a result of these plans, during the nine months ended September 30, 2015 the Company recognized expense and recorded liabilities of \$2,588 and \$11,290 for severance obligations and remaining net payments on vacated, duplicate facilities, respectively. The expenses associated with the severance obligations and vacated, duplicate facilities were recognized in the salaries, wages and benefits and operating lease line items, respectively. During the nine months ended September 30, 2015, the Company also incurred expense of \$9,059 for various other integration and transaction related costs which are largely included in other operating expenses.

In conjunction with the Towne acquisition, the Company vacated certain duplicate facilities under long-term non-cancelable leases and recorded contract termination costs. As of September 30, 2016, the Company's reserve for remaining payments on vacated facilities was \$4,775. During the three and nine months ended September 30, 2016, we paid \$700 and \$3,862 respectively in recurring payments on these non-cancelable leases.

Acquisition of Triumph and Ace

As part of the Company's strategy to expand its Intermodal operations, in August 2016, we acquired certain assets of Triumph Transport, Inc. and Triumph Repair Service, Inc. (together referred to as "Triumph") for \$10,100 and a potential earnout of \$1,250. The assets, liabilities, and operating results of Triumph have been included in the Company's consolidated financial statements from the date of acquisition and have been assigned to the Intermodal reportable segment.

In January 2016, the Company also acquired certain assets of Ace Cargo, LLC ("Ace") for \$1,700. The assets, liabilities, and operating results of Ace have been included in the Company's consolidated financial statements from the date of acquisition and have been assigned to the Intermodal reportable segment.

Allocations of Purchase Prices

The following table presents the allocations of the Towne, Triumph and Ace purchase prices to the assets acquired and liabilities assumed based on their estimated fair values and resulting residual goodwill (in thousands):

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Forward Air Corporation

Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

	Triumph & Ace 2016	Towne March 9, 2015
Tangible assets:		
Accounts receivable	\$—	\$24,068
Prepaid expenses and other current assets	—	2,916
Property and equipment	1,294	2,095
Other assets	—	614
Total tangible assets	1,294	29,693
Intangible assets:		
Non-compete agreements	139	—
Customer relationships	5,335	66,000
Goodwill	6,282	59,666
Total intangible assets	11,756	125,666
Total assets acquired	13,050	155,359
Liabilities assumed:		
Current liabilities	—	28,920
Other liabilities	1,250	3,886
Debt and capital lease obligations	—	59,544
Deferred income taxes	—	1,131
Total liabilities assumed	1,250	93,481
Net assets acquired	\$11,800	\$61,878

The acquired definite-live intangible assets have the following useful lives:

	Useful Lives	
	Triumph & Ace	Towne
Customer relationships	15 years	20 years
Non-compete agreements	5 years	-

The fair value of the non-compete agreements and customer relationships assets were estimated using an income approach (level 3). Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To estimate fair value, the Company used cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. Cash flows were assumed to extend through the remaining economic useful life of each class of intangible asset.

## Pro forma

The following unaudited pro forma information presents a summary of the Company's consolidated results of operations as if the Towne acquisition occurred as of January 1, 2015 (in thousands, except per share data).

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Forward Air Corporation

Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

	Nine months ended	
	September 30, 2016	September 30, 2015
Operating revenue	\$717,737	\$ 736,932
Income from operations	31,756	50,451
Net income	14,964	29,868
Net income per share		
Basic	\$0.49	\$ 0.97
Diluted	\$0.49	\$ 0.96

The unaudited pro forma consolidated results for the nine month periods are based on the historical financial information of Towne. The unaudited pro forma consolidated results incorporate historical financial information since January 1, 2015. The historical financial information has been adjusted to give effect to pro forma adjustments that are: (i) directly attributable to the acquisition, (ii) factually supportable and (iii) expected to have a continuing impact on the combined results. The unaudited pro forma consolidated results are not necessarily indicative of what the Company's consolidated results of operations actually would have been had it completed these acquisitions on January 1, 2015.

Goodwill

The Company conducted its annual impairment assessments and tests of goodwill for each reporting unit as of June 30, 2016. The first step of the goodwill impairment test is the Company's assessment of qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than the reporting unit's carrying amount, including goodwill. When performing the qualitative assessment, the Company considers the impact of factors including, but not limited to, macroeconomic and industry conditions, overall financial performance of each reporting unit, litigation and new legislation. If based on the qualitative assessments, the Company believes it more likely than not that the fair value of a reporting unit is less than the reporting unit's carrying amount, or periodically as deemed appropriate by management, the Company will prepare an estimation of the respective reporting unit's fair value utilizing a quantitative approach. If a quantitative fair value estimation is required, the Company estimates the fair value of the applicable reportable units, using a combination of discounted projected cash flows and market valuations for comparable companies as of the valuation date. The Company's inputs into the fair value estimates for goodwill are classified within level 3 of the fair value hierarchy as defined in the FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles ("the FASB Codification"). If this estimation of fair value indicates that impairment potentially exists, the Company will then measure the amount of the impairment, if any. Goodwill impairment exists when the estimated implied fair value of goodwill is less than its carrying value. Changes in strategy or market conditions could significantly impact these fair value estimates and require adjustments to recorded asset balances.

Our 2016 assessments and calculations for LTL, Intermodal and Pool Distribution indicated that, as of June 30, 2016, the fair value of each reporting unit exceeded their carrying value. However, due to the financial performance of the Total Quality, Inc. ("TQI") reporting unit falling notably short of previous projections, declining revenue from significant customers and strategic initiatives not having the required impact on financial results, the Company reduced TQI's projected cash flows and as a result the estimate of TQI's fair value no longer exceeded the respective carrying value. As a result of these assessments, the Company concluded that an impairment loss was probable and could be reasonably estimated for the TQI reporting unit, which is included in the TLX reportable segment. Consequently, the Company recorded a goodwill impairment charge of \$25,686 for the TQI reporting unit during the

three months ended June 30, 2016.

The following is a summary of the changes in goodwill for the nine months ended September 30, 2016. Approximately \$100,156 of goodwill, not including the goodwill acquired with the Towne acquisition, is deductible for tax purposes.

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Forward Air Corporation

Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

	Expedited LTL		Expedited Truckload		Pool Distribution		Intermodal		Total
	Accumulated		Accumulated		Accumulated		Accumulated		Net
	Goodwill	Impairment	Goodwill	Impairment	Goodwill	Impairment	Goodwill	Impairment	
Beginning balance, December 31, 2015	\$99,123	\$—	—	\$—	\$12,359	\$ (6,953)	\$55,916	\$—	—\$205,609
Triumph and Ace Acquisition	—	—	—	—	—	—	6,282	—	6,282
TQI impairment	—	—	—	(25,686)	—	—	—	—	(25,686)
Adjustment to Towne acquisition	(1,530)	—	—	—	—	—	—	—	(1,530)
Ending balance, September 30, 2016	\$97,593	\$—	—	\$ (25,686)	\$12,359	\$ (6,953)	\$62,198	\$—	—\$184,675

Additionally, the Company reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Impairment is recognized on assets classified as held and used when the sum of undiscounted estimated cash flows expected to result from the use of the asset is less than the carrying value. If such measurement indicates a possible impairment, the estimated fair value of the asset is compared to its net book value to measure the impairment charge, if any. In conjunction with the TQI goodwill impairment assessment the Company determined there were indicators that TQI's customer relationship and non-compete intangible assets were impaired as the undiscounted cash flows associated with the applicable assets no longer exceeded the related assets' net book values. The Company then estimated the current market values of the customer relationship and non-compete assets using an income approach (level 3). Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To estimate fair value, the Company used cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. As a result of these estimates the Company recorded an impairment charge of \$16,501 related to TQI customer relationships.

The Company is still in the process of finalizing certain valuations related to the goodwill and customer relationship impairment analyses. Adjustments, if any, to its estimates as a result of completing its valuation analysis will be recorded during the three months ended December 31, 2016.

In addition, during the three months ended June 30, 2016, the Company also discontinued use of an owned maintenance facility and began efforts to sell the property. In conjunction with these actions, the Company incurred a \$255 impairment charge that was estimated using current offers received to sell the property less estimated cost to sell the facility.

#### 4. Share-Based Payments

The Company's general practice has been to make a single annual grant of share-based compensation to key employees and to make other employee grants only in connection with new employment or promotions. Forms of share-based compensation granted to employees by the Company include stock options, non-vested shares of common stock ("non-vested share"), and performance shares. The Company also typically makes a single annual grant of non-vested

shares to non-employee directors in conjunction with the annual election of non-employee directors to the Board of Directors. Share-based compensation is based on the grant date fair value of the instrument and is recognized, net of estimated forfeitures, ratably over the requisite service period, or vesting period. The Company estimates forfeitures based upon historical experience. All share-based compensation expense is recognized in salaries, wages and employee benefits.

#### Employee Activity - Stock Options

Stock option grants to employees generally expire seven years from the grant date and typically vest ratably over a three-year period. The Company used the Black-Scholes option-pricing model to estimate the grant-date fair value of options granted. The weighted-average fair value of options granted and assumptions used to estimate their fair value during the three and nine months ended September 30, 2016 and 2015 were as follows:

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Forward Air Corporation

Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

	Three months ended			
	September 30, 2016		September 30, 2015	
Expected dividend yield	—	%	1.2	%
Expected stock price volatility	—	%	29.8	%
Weighted average risk-free interest rate	—	%	1.4	%
Expected life of options (years)	—		4.5	
Weighted average grant date fair value	\$ —		\$ 12	

	Nine months ended			
	September 30, 2016		September 30, 2015	
Expected dividend yield	1.0	%	1.0	%
Expected stock price volatility	29.0	%	33.7	%
Weighted average risk-free interest rate	1.3	%	1.6	%
Expected life of options (years)	6.0		6.0	
Weighted average grant date	\$ 12		\$ 16	

fair value

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Forward Air Corporation

Notes to Condensed Consolidated Financial Statements

(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

The following tables summarize the Company's employee stock option activity and related information:

	Three months ended September 30, 2016			
	Options	Weighted-Average Exercise Price	Aggregate Intrinsic Value	Weighted-Average Remaining Contractual Term
	(000)		(000)	
Outstanding at June 30, 2016	855	\$ 34		
Granted	—	—		
Exercised	(263)	23		
Forfeited	—	—		
Outstanding at September 30, 2016	592	\$ 40	\$ 3,355	4.0
Exercisable at September 30, 2016	364	\$ 36	\$ 3,351	2.8

	Three months ended September 30, 2016		Three months ended September 30, 2015	
Share-based compensation for options	\$377	\$ 352		
Tax benefit for option compensation	\$140	\$ 137		
Unrecognized compensation cost for options, net of estimated forfeitures	\$2,036	\$ 1,977		
Weighted average period over which unrecognized compensation will be recognized (years)	1.9			

	Nine months ended September 30, 2016			
	Options	Weighted-Average Exercise Price	Aggregate Intrinsic Value	Weighted-Average Remaining Contractual Term
	(000)		(000)	
Outstanding at December 31, 2015	786	\$ 32		
Granted	122	44		
Exercised	(311)	23		
Forfeited	(5)	38		
Outstanding at September 30, 2016	592	\$ 40	\$ 3,355	4.0
Exercisable at September 30, 2016	364	\$ 36	\$ 3,351	2.8

	Nine months ended September 30, 2016		Nine months ended September 30, 2015	
Share-based compensation for options	\$1,101	\$ 1,029		
Tax benefit for option compensation	\$407	\$ 403		
Unrecognized compensation cost for options, net of estimated forfeitures	\$2,036	\$ 1,977		

Weighted average period over which unrecognized compensation will be recognized (years) 1.9

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Forward Air Corporation

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(In thousands, except share and per share data)

(Unaudited)

September 30, 2016

## Employee Activity - Non-vested Shares

Non-vested share grants to employees vest ratably over a three-year period. The non-vested shares' fair values were estimated using closing market prices on the day of grant. The following tables summarize the Company's employee non-vested share activity and related information:

	Three months ended September 30, 2016		
	Weighted-Average Grant Non-vested Shares Date		
	Grant Date	Fair Value	
	(000)	(000)	
Outstanding and non-vested at June 30, 2016	228	\$ 45	
Granted	—	—	
Vested	(1 )	47	
Forfeited	(3 )	45	
Outstanding and non-vested at September 30, 2016	224	\$ 45	\$ 10,173

	Three months ended September 30, 2016		Three months ended September 30, 2015	
Share-based compensation for non-vested shares	\$1,176	\$ 1,031		
Tax benefit for non-vested share compensation	\$434	\$ 403		
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	\$7,147	\$ 6,148		
Weighted average period over which unrecognized compensation will be recognized (years)	2.0			

	Nine months ended September 30, 2016		
	Weighted-Average Grant Non-vested Shares Date		
	Grant Date	Fair Value	
	(000)	(000)	
Outstanding and non-vested at December 31, 2015	191	\$ 46	
Granted	134	44	
Vested	(94 )	44	
Forfeited	(7 )	46	
Outstanding and non-vested at September 30, 2016	224	\$ 45	\$ 10,173

Nine months ended

	September 30, 2016	September 30, 2015
Share-based compensation for non-vested shares	\$3,434	\$ 3,042
Tax benefit for non-vested share compensation	\$1,270	\$ 1,190
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	\$7,147	\$ 6,148
Weighted average period over which unrecognized compensation will be recognized (years)	2.0	



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## Employee Activity - Performance Shares

The Company annually grants performance shares to key employees. Under the terms of the performance share agreements, on the third anniversary of the grant date, the Company will issue to the employees a calculated number of common stock shares based on the three year performance of the Company's total shareholder return as compared to the total shareholder return of a selected peer group. No shares may be issued if the Company's total shareholder return outperforms 30% or less of the peer group, but the number of shares issued may be doubled if the Company's total shareholder return performs better than 90% of the peer group. The fair value of the performance shares was estimated using a Monte Carlo simulation. The weighted average assumptions used in the Monte Carlo estimate were as follows:

	Nine months ended			
	September 30, 2016		September 30, 2015	
Expected stock price	22.3	%	23.5	%
volatility				
Weighted average				
risk-free interest rate	0.8	%	1.0	%

The following tables summarize the Company's employee performance share activity, assuming median share awards, and related information:

	Three months ended September 30, 2016		
	Weighted-Aggregate Performance Grant Average Date		
	Grant Shares Date		
	Fair Value		
	(000)		
Outstanding and non-vested at June 30, 2016	80	\$ 55	
Granted	—	—	
Additional shares awarded based on performance	—	—	
Vested	—	—	
Outstanding and non-vested at September 30, 2016	80	\$ 55	\$ 4,373

	Three months ended	
	September 30, 2016	September 30, 2015
Share-based compensation for performance shares	\$367	\$ 337
Tax benefit for performance share compensation	\$136	\$ 132

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Unrecognized compensation cost for performance shares, net of estimated forfeitures	\$2,076\$ 2,062
Weighted average period over which unrecognized compensation will be recognized (years)	1.8

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September 30, 2016

	Nine months ended September 30, 2016		
	Weighted-	Aggregate	
Performance	Average	Grant	
Shares	Grant	Date	Fair Value
	Date		
(000)	Fair Value	(000)	
Outstanding and non-vested at December 31, 2015	77	\$ 52	
Granted	29	49	
Additional shares awarded based on performance	7	40	
Vested	(33)	40	
Outstanding and non-vested at September 30, 2016	80	\$ 55	\$ 4,373

	Nine months ended September 30, 2016		
	2016	2015	
Share-based compensation for performance shares	\$1,080	\$ 972	
Tax benefit for performance share compensation	\$400	\$ 380	
Unrecognized compensation cost for performance shares, net of estimated forfeitures	\$2,076	\$ 2,062	
Weighted average period over which unrecognized compensation will be recognized (years)	1.8		

## Employee Activity - Employee Stock Purchase Plan

Under the 2005 Employee Stock Purchase Plan (the "ESPP"), which has been approved by shareholders, the Company is authorized to issue up to a remaining 387,395 shares of common stock to employees of the Company. These shares may be issued at a price equal to 90% of the lesser of the market value on the first day or the last day of each six-month purchase period. Common stock purchases are paid for through periodic payroll deductions and/or up to two large lump sum contributions. For the nine months ended September 30, 2016, participants under the plan purchased 5,592 shares at an average price of \$38.50 per share. For the nine months ended September 30, 2015, participants under the plan purchased 5,087 shares at an average price of \$44.74 per share. The weighted-average fair value of each purchase right under the ESPP granted for the nine months ended September 30, 2016, which is equal to the discount from the market value of the common stock at the end of each six month purchase period, was \$6.03 per share. The weighted-average fair value of each purchase right under the ESPP granted for the nine months ended September 30, 2015, which is equal to the discount from the market value of the common stock at the end of each six month purchase period, was \$7.52 per share. Share-based compensation expense of \$34 and \$37 was recognized during the nine months ended September 30, 2016 and 2015, respectively.

## Non-employee Director Activity - Non-vested Shares

Grants of non-vested shares to non-employee directors vest ratably over the elected term to the Board of Directors, or approximately one year. The following tables summarize the Company's non-employee non-vested share activity and related information:



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September 30, 2016

	Three months ended September 30, 2016	
	Weighted-Average Non-vested Shares (000)	Grant Date Fair Value (000)
Outstanding and non-vested at June 30, 2016	16	\$ 44
Granted	—	—
Vested	—	—
Outstanding and non-vested at September 30, 2016	16	\$ 44 \$ 688

	Three months ended September 30, 2016	
Share-based compensation for non-vested shares	\$ 173	\$ 166
Tax benefit for non-vested share compensation	\$ 64	\$ 65
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	\$ 419	\$ 424
Weighted average period over which unrecognized compensation will be recognized (years)	0.6	

	Nine months ended September 30, 2016	
	Weighted-Average Non-vested Shares (000)	Grant Date Fair Value (000)
Outstanding and non-vested at December 31, 2015	15	\$ 51
Granted	16	44
Vested	(15)	51
Outstanding and non-vested at September 30, 2016	16	\$ 44 \$ 688

	Nine months ended September 30, 2016	
Share-based compensation for non-vested shares	\$ 555	\$ 482
Tax benefit for non-vested share compensation	\$ 198	\$ 189
Unrecognized compensation cost for non-vested shares, net of estimated forfeitures	\$ 419	\$ 424
Weighted average period over which unrecognized compensation will be recognized (years)	0.6	

## 5. Senior Credit Facility

On February 4, 2015, the Company entered into a five-year senior, unsecured credit facility (the “Facility”) with a maximum aggregate principal amount of \$275,000, including a revolving credit facility of \$150,000 and a term loan facility of \$125,000. The revolving credit facility has a sublimit of \$25,000 for letters of credit and a sublimit of \$15,000 for swing line loans. The revolving credit facility is scheduled to expire in February 2020 and may be used to refinance existing indebtedness of the Company and for working capital, capital expenditures and other general corporate purposes. Unless the Company elects otherwise under the credit agreement, interest on borrowings under the Facility are based on the highest of (a) the federal funds rate plus 0.5%, (b)

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the administrative agent's prime rate and (c) the LIBOR Rate plus 1.0%, in each case plus a margin that can range from 0.1% to 0.6% with respect to the term loan facility and from 0.3% to 0.8% with respect to the revolving credit facility depending on the Company's ratio of consolidated funded indebtedness to earnings as set forth in the credit agreement. The Facility contains financial covenants and other covenants that, among other things, restrict the ability of the Company, without the approval of the lenders, to engage in certain mergers, consolidations, asset sales, investments, transactions or to incur liens or indebtedness, as set forth in the credit agreement. As of September 30, 2016, the Company had no borrowings outstanding under the revolving credit facility. At September 30, 2016, the Company had utilized \$9,414 of availability for outstanding letters of credit and had \$140,586 of available borrowing capacity outstanding under the revolving credit facility.

In conjunction with the acquisition of Towne (see note 3), the Company borrowed \$125,000 on the available term loan. The term loan is payable in quarterly installments of 11.1% of the original principal amount of the term loan plus accrued and unpaid interest, and matures in March 2017. The interest rate on the term loan was 1.8% at September 30, 2016. The remaining balance on the term loan was \$41,675 as of September 30, 2016 and is a current liability. The balance on the term loan was \$83,338 and the interest rate was 1.5% as of December 31, 2015.

## 6. Net Income Per Share

The following table sets forth the computation of basic and diluted net income per share:

	Three months ended September 30, 2016		September 30, 2015		Nine months ended September 30, 2016		September 30, 2015	
Numerator:								
Net income and comprehensive income	\$11,931		\$ 15,687		\$14,964		\$ 32,347	
Income allocated to participating securities	(93	)	(104	)	(114	)	(215	)
Numerator for basic and diluted income per share - net income	\$11,838		\$ 15,583		\$14,850		\$ 32,132	
Denominator (in thousands):								
Denominator for basic income per share - weighted-average shares	30,191		30,715		30,316		30,750	
Effect of dilutive stock options (in thousands)	117		250		151		300	
Effect of dilutive performance shares (in thousands)	30		33		29		34	
Denominator for diluted income per share - adjusted weighted-average shares	30,338		30,998		30,496		31,084	
Basic net income per share	\$0.39		\$ 0.51		\$0.49		\$ 1.04	
Diluted net income per share	\$0.39		\$ 0.50		\$0.49		\$ 1.03	

The number of instruments that could potentially dilute net income per basic share in the future, but that were not included in the computation of net income per diluted share because to do so would have been anti-dilutive for the periods presented, are as follows:

	September 30, 2016	September 30, 2015
Anti-dilutive stock options (in thousands)	309	176
Anti-dilutive performance shares (in thousands)	—	23
Anti-dilutive non-vested shares and deferred stock units (in thousands)	—	—

Total anti-dilutive shares (in thousands)	309	199
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7. Income Taxes

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, various states and Canada. With a few exceptions, the Company is no longer subject to U.S. federal, state and local, or Canadian examinations by tax authorities for years before 2010.

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For the three and nine months ended September 30, 2016 and 2015, the effective income tax rates varied from the statutory federal income tax rate of 35.0%, primarily as a result of the effect of state income taxes, net of the federal benefit, and permanent differences between book and tax net income. The combined federal and state effective tax rate for the nine months ended September 30, 2016 was 50.7% compared to a rate of 36.8% for the same period in 2015. The increase in the 2016 effective tax rate was attributable to the TQI goodwill write off (Note 3) that is not deductible for tax purposes.

8. Financial Instruments

Fair Value of Financial Instruments

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

Accounts receivable and accounts payable: The carrying amounts reported in the balance sheet for accounts receivable and accounts payable approximate their fair value based on their short-term nature.

The Company's revolving credit facility and term loan bear variable interest rates plus additional basis points based upon covenants related to total indebtedness to earnings. As the term loan bears a variable interest rate, the carrying value approximates fair value. Using interest rate quotes and discounted cash flows, the Company estimated the fair value of its outstanding capital lease obligations as follows:

	September 30,	
	2016	
	Carrying	Fair
	Value	Value
Capital leases	\$1,103	\$1,220

The Company's fair value estimates for the above financial instruments are classified within level 3 of the fair value hierarchy.

9. Shareholders' Equity

During each quarter of 2015 and the first, second and third quarters of 2016, the Company's Board of Directors declared a cash dividend of \$0.12 per share of common stock. The Company expects to continue to pay regular quarterly cash dividends, though each subsequent quarterly dividend is subject to review and approval by the Board of Directors.

On February 7, 2014, our Board of Directors approved a stock repurchase authorization for up to two million shares of our common stock. During the three months ended September 30, 2016, we repurchased 222,388 shares for \$9,996, or an average of \$44.95 per share. During the nine months ended September 30, 2016, we repurchased 676,773 shares for \$29,986, or an average of \$44.31 per share. During the three and nine months ended September 30, 2015, we

repurchased 204,590 for \$9,996, or \$48.86 per share.

On July 21, 2016, our Board of Directors canceled the Company's remaining 2014 share repurchase authorization and approved a stock repurchase authorization for up to three million shares of the Company's common stock. All shares remain for repurchase, as shares repurchased in the three months ended September 30, 2016 were made under the 2014 plan.

#### 10. Commitments and Contingencies

From time to time, the Company is party to ordinary, routine litigation incidental to and arising in the normal course of business. The Company does not believe that any of these pending actions, individually or in the aggregate, will have a material adverse effect on its business, financial condition or results of operations.

The primary claims in the Company's business relate to workers' compensation, property damage, vehicle liability and medical benefits. Most of the Company's insurance coverage provides for self-insurance levels with primary and excess coverage which management believes is sufficient to adequately protect the Company from catastrophic claims. In the opinion of management, adequate provision has been made for all incurred claims up to the self-insured limits, including provision for estimated claims incurred but not reported.

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The Company estimates its self-insurance loss exposure by evaluating the merits and circumstances surrounding individual known claims and by performing hindsight and actuarial analysis to determine an estimate of probable losses on claims incurred but not reported. Such losses should be realized immediately as the events underlying the claims have already occurred as of the balance sheet dates.

Because of the uncertainty of the ultimate resolution of outstanding claims, as well as uncertainty regarding claims incurred but not reported, it is possible that management's provision for these losses could change materially in the near term. However, no estimate can currently be made of the range of additional loss that is at least reasonably possible.

## 11. Segment Reporting

The Company operates in four reportable segments based on information available to and used by the chief operating decision maker. Expedited LTL provides time-definite transportation and logistics services to the deferred air freight market. The TLX segment provides expedited truckload brokerage, dedicated fleet services and maximum security and temperature-controlled logistics services. Our Intermodal segment provides container and intermodal drayage services. Pool Distribution provides pool distribution services primarily to regional and national distributors and retailers.

During the first quarter of 2016, the Company changed its reportable segments to separate its truckload and intermodal businesses from our Expedited LTL service and to aggregate reporting for truckload services into a single segment. The Company previously reported three segments: Forward Air, Forward Air Solutions and Total Quality, Inc. Consequently, the Company now reports four segments: Expedited LTL, Expedited Truckload Services ("TLX"), Intermodal and Pool Distribution. All prior year segment amounts have been restated to reflect this new reporting structure.

Except for certain insurance activity, the accounting policies of the segments are the same as those described in the summary of significant accounting policies disclosed in Note 1 to the Consolidated Financial Statements included in the Company's 2015 Annual Report on Form 10-K. For workers compensation and vehicle claims each segment is charged an insurance premium and is also charged a deductible that corresponds with the our corporate deductibles disclosed in Note 1 to the Consolidated Financial Statements included in the Company's 2015 Annual Report on Form 10-K. However, any losses beyond our deductibles and any loss development factors applied to our outstanding claims as a result of actuary analysis are not passed to the segments, but kept at the corporate level.

Segment data includes intersegment revenues. Assets and costs of the corporate headquarters are allocated to the segments based on usage. The Company evaluates the performance of its segments based on income from operations. The Company's business is conducted in the U.S. and Canada.

The following tables summarize segment information about results from operations and assets used by the chief operating decision maker of the Company in making decisions regarding allocation of assets and resources as of and for the three and nine months ended September 30, 2016 and 2015.



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(Unaudited)

September 30, 2016

	Three months ended September 30, 2016					
	Expedited LTL	Expedited Truckload	Pool Distribution	Intermodal	Eliminations & other	Consolidated
External revenues	\$143,753	\$ 41,927	\$ 36,305	\$ 27,567	\$ —	\$ 249,552
Intersegment revenues	584	283	132	12	(1,011 )	—
Depreciation and amortization	5,470	1,470	1,472	987	—	9,399
Share-based compensation expense	1,792	98	84	119	—	2,093
Interest expense	385	—	—	12	(181 )	216
Income (loss) from operations	21,014	2,038	66	3,041	(1,459 )	24,700
Total assets	634,028	52,465	46,327	128,048	(219,355 )	641,513
Capital expenditures	11,915	36	722	11	—	12,684

	Three months ended September 30, 2015					
	Expedited LTL	Expedited Truckload	Pool Distribution	Intermodal	Eliminations & other	Consolidated
External revenues	\$148,647	\$ 38,088	\$ 31,949	\$ 28,568	\$ (159 )	\$ 247,093
Intersegment revenues	565	440	184	322	(1,511 )	—
Depreciation and amortization	5,403	1,590	1,451	939	16	9,399
Share-based compensation expense	1,514	219	69	84	—	1,886
Interest expense	535	—	—	19	—	554
Income (loss) from operations	21,594	3,170	555	3,536	(4,254 )	24,601
Total assets	652,946	89,659	45,017	118,035	(206,992 )	698,665
Capital expenditures	3,484	1,879	1,108	108	—	6,579

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Forward Air Corporation

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September 30, 2016

	Nine months ended September 30, 2016					
	Expedited LTL	Expedited Truckload	Pool Distribution	Intermodal	Eliminations & other	Consolidated
External revenues	\$421,194	\$119,574	\$100,726	\$76,243	\$—	\$717,737
Intersegment revenues	2,216	696	427	148	(3,487)	—
Depreciation and amortization	16,278	4,944	4,434	2,753	—	28,409
Share-based compensation expense	5,353	260	251	340	—	6,204
Interest expense	1,345	—	—	66	(181)	1,230
Income (loss) from operations	63,026	(36,679)	(191)	8,170	(2,570)	31,756
Total assets	634,028	52,465	46,327	128,048	(219,355)	641,513
Capital expenditures	24,487	1,821	2,275	142	—	28,725

	Nine months ended September 30, 2015					
	Expedited LTL	Expedited Truckload	Pool Distribution	Intermodal	Eliminations & other	Consolidated
External revenues	\$425,992	\$110,935	\$86,460	\$78,705	\$613	\$702,705
Intersegment revenues	1,285	1,460	580	707	(4,032)	—
Depreciation and amortization	15,707	4,514	4,492	2,854	34	27,601
Share-based compensation expense	4,511	637	220	194	—	5,562
Interest expense	1,058	—	—	65	366	1,489
Income (loss) from operations	57,275	10,521	758	8,843	(24,639)	52,758
Total assets	652,946	89,659	45,017	118,035	(206,992)	698,665
Capital expenditures	8,834	5,968	3,344	395	—	18,541

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

#### Overview and Executive Summary

Our services are classified into four principal reportable segments: Expedited LTL, Expedited Truckload Services ("TLX"), Intermodal and Pool Distribution.

Through the Expedited LTL segment, we provide time-definite transportation services to the North American deferred air freight market. Our Expedited LTL service operates a comprehensive national network for the time-definite surface transportation of expedited ground freight. The Expedited LTL service offers customers local pick-up and delivery and scheduled surface transportation of cargo as a cost effective, reliable alternative to air transportation. Expedited LTL's other services include shipment consolidation and deconsolidation, warehousing, customs brokerage, and other handling. The Expedited LTL segment primarily provides its transportation services through a network of terminals located at or near airports in the United States and Canada.

Through our TLX segment we provide expedited truckload brokerage, dedicated fleet services and maximum security and temperature-controlled logistics services. We are able to expedite this service by utilizing a dedicated fleet of team owner operators, some team company drivers as well as third party transportation providers. The TLX segment provides full truckload service in the United States and Canada.

Our Intermodal segment provides container and intermodal drayage services primarily within the Midwest region of the United States. Drayage is essentially the first and last mile of the movement of an intermodal container. We are providing this service both to and from ports and rail heads. Our Intermodal segment also provides dedicated contract and Container Freight Station ("CFS") warehouse and handling services. Today Intermodal operates primarily in the Midwest but through acquisition as well as green-field start-ups we anticipate moving into other geographies within the United States.

We provide pool distribution services throughout the Mid-Atlantic, Southeast, Midwest and Southwest continental United States. Pool distribution involves managing high-frequency handling and distribution of time-sensitive product to numerous destinations in specific geographic regions. Our primary customers for this service are regional and nationwide distributors and retailers, such as mall, strip mall and outlet based retail chains.

Our operations, particularly our network of hubs and terminals, represent substantial fixed costs. Consequently, our ability to increase our earnings depends in significant part on our ability to increase the amount of freight and the revenue per pound for the freight shipped through our networks and to grow other lines of businesses, such as Truckload, Intermodal and Pool Distribution, which will allow us to maintain revenue growth in challenging shipping environments.

#### Trends and Developments

##### Acquisition of Towne

On March 9, 2015, we completed the acquisition of CLP Towne Inc. ("Towne"). Towne is a full-service trucking provider offering time-sensitive less-than-truckload shipping, full truckload service, an extensive cartage network, container freight stations and dedicated trucking. For the acquisition of Towne, we paid \$61.9 million in net cash and assumed \$59.5 million in debt and capital leases. The transaction was funded with proceeds from a \$125 million two year term loan. The assets, liabilities, and operating results of Towne have been included in the Expedited LTL reportable segment.

#### Acquisition of Triumph and Ace

As part of the Company's strategy to expand its Intermodal operations, in August , we acquired certain assets of Triumph Transport, Inc. and Triumph Repair Service, Inc. (together referred to as "Triumph") for \$10.1 million and a potential earnout of \$1.3 million. The assets, liabilities, and operating results of Triumph have been included in the Company's consolidated financial statements from the date of acquisition and have been assigned to the Intermodal reportable segment.

In January 2016, we acquired certain assets of Ace Cargo, LLC ("Ace") for \$1.7 million. The assets, liabilities, and operating results of Ace have been included in the Company's consolidated financial statements from the date of acquisition and have been assigned to the Intermodal reportable segment.



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Change in Reportable Segments

During the first quarter of 2016, we changed our reportable segments to separate our truckload and intermodal businesses from our Expedited LTL service and to aggregate our reporting for truckload services into a single segment. We previously reported three segments: Forward Air, Forward Air Solutions and Total Quality, Inc. Consequently, we now report four segments: Expedited LTL, Expedited Truckload Services (“TLX”), Intermodal and Pool Distribution. All prior year segment amounts have been restated to reflect this new reporting structure.

Goodwill

In conjunction with our policy to annually test goodwill for impairment as of June 30 we determined there were indicators of potential impairment of the goodwill and other long lived assets assigned to the TQI acquisition. This determination was based on TQI's financial performance falling notably short of previous projections, declining revenue from significant customers and strategic initiatives not having the required impact on financial results. As a result of these factors we reduced TQI's projected cash flows and consequently the estimate of TQI's fair value no longer exceeded the respective carrying value. Based on the results of the impairment test, we concluded that an impairment loss was probable and could be reasonably estimated. Therefore, during the second quarter of 2016, we recorded impairment charges for goodwill, intangibles and other assets of \$42.4 million related to the TQI reporting unit.

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## Results from Operations

The following table sets forth our consolidated historical financial data for the three months ended September 30, 2016 and 2015 (in millions):

	Three months ended September 30			
	2016	2015	Change	Percent Change
Operating revenue:				
Expedited LTL	\$144.3	\$149.2	\$ (4.9 )	(3.3 )%
Expedited Truckload	42.2	38.5	3.7	9.6
Pool Distribution	36.4	32.1	4.3	13.4
Intermodal	27.6	28.9	(1.3 )	(4.5 )
Eliminations and other operations	(1.0 )	(1.6 )	0.6	(37.5)
Operating revenue	249.5	247.1	2.4	1.0
Operating expenses:				
Purchased transportation	105.0	104.4	0.6	0.6
Salaries, wages, and employee benefits	60.2	59.1	1.1	1.9
Operating leases	16.2	17.0	(0.8 )	(4.7 )
Depreciation and amortization	9.4	9.4	—	—
Insurance and claims	7.2	5.2	2.0	38.5
Fuel expense	3.4	3.8	(0.4 )	(10.5)
Other operating expenses	23.4	23.6	(0.2 )	(0.8 )
Total operating expenses	224.8	222.5	2.3	1.0
Income from operations:				
Expedited LTL	21.0	21.6	(0.6 )	(2.8 )
Expedited Truckload	2.0	3.2	(1.2 )	(37.5)
Pool Distribution	0.1	0.5	(0.4 )	(80.0)
Intermodal	3.0	3.5	(0.5 )	(14.3)
Other operations	(1.4 )	(4.2 )	2.8	(66.7)
Income from operations	24.7	24.6	0.1	0.4
Other expense:				
Interest expense	(0.2 )	(0.5 )	0.3	(60.0)
Total other expense	(0.2 )	(0.5 )	0.3	(60.0)
Income before income taxes	24.5	24.1	0.4	1.7
Income taxes	12.6	8.4	4.2	50.0
Net income	\$11.9	\$15.7	\$ (3.8 )	(24.2)%

During the three months ended September 30, 2016, we experienced a 1.0% increase in our consolidated revenues compared to the three months ended September 30, 2015. Operating income increased \$0.1 million, or 0.4%, from 2015 to \$24.7 million for the three months ended September 30, 2016.

## Segment Operations

Expedited LTL's revenue decreased \$4.9 million, or 3.3%, while operating income decreased \$0.6 million, or 2.8% for the three months ended September 30, 2016, compared to the same period in 2015. The decrease of Expedited LTL's revenue was the result of lower airport-to-airport volumes due to a sluggish economic environment and reduced net fuel surcharge revenue as a result of the decline in fuel prices since the third quarter of 2015. The revenue decrease was partially offset by improved pricing, the implementation of the February 2016 change to our dim-factor standard and further operating efficiencies leading to a slight increase in operating income as a percentage of revenue.

TLX's revenue increased \$3.7 million, or 9.6%, but operating income decreased \$1.2 million, or 37.5%, for the three months ended September 30, 2016, compared to the same period in 2015. The increase in revenue was due to an increase in overall miles and

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new business wins. The decrease of TLX's operating income was the result of the decline of higher-margin pharmaceutical business and TLX revenue per mile declining at a faster pace than cost per mile.

Pool Distribution revenue increased \$4.3 million, or 13.4%, while operating results decreased \$0.4 million for the three months ended September 30, 2016, compared to the same period in 2015. The revenue increase was due to new business, rate increases and increased volumes. The decline in Pool Distribution operating income was primarily the result of higher lease costs as Pool Distribution opened new facilities and relocated others to support business wins since the third quarter of 2015.

Intermodal revenue decreased \$1.3 million, or 4.5%, and operating income decreased \$0.5 million, or 14.3%, for the three months ended September 30, 2016, compared to the same period in 2015. The decreases in operating revenue and income were primarily attributable to suppressed market conditions, the negative impact of decreased fuel surcharges and decreased chassis rental and rail storage revenues, partially offset by the Ace and Triumph acquisitions.

Fuel Surcharge

Our net fuel surcharge revenue is the result of our fuel surcharge rates, which are set weekly using the national average for diesel price per gallon, and volume transiting our network. During the three months ended September 30, 2016, total net fuel surcharge revenue decreased 19.9% as compared to the same period in 2015, mostly due to decreased fuel prices and decreased volumes in the Expedited LTL and Intermodal segments.

Interest Expense

Interest expense was \$0.2 million for the three months ended September 30, 2016 compared to \$0.5 million for the same period of 2015. The decrease in interest expense was attributable to principal payments made on the term loan used to finance the Towne acquisition in March 2015.

Income Taxes

The combined federal and state effective tax rate for the third quarter of 2016 was 51.3% compared to a rate of 34.8% for the same period in 2015. The higher effective tax rate for the third quarter of 2016 is the result of the impairment of goodwill in the second quarter of 2016 that is non-deductible for tax purposes. Also, 2015 benefited from the amending of prior year federal and state income tax returns to take advantage of qualified production property deductions.

Net Income

As a result of the foregoing factors, net income decreased by \$3.8 million, or 24.2%, to \$11.9 million for the third quarter of 2016 compared to \$15.7 million for the same period in 2015.

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Expedited LTL - Three Months Ended September 30, 2016 compared to Three Months Ended September 30, 2015

The following table sets forth our historical financial data of the Expedited LTL segment for the three months ended September 30, 2016 and 2015 (in millions):

Expedited LTL Segment Information

(In millions)

(Unaudited)

	Three months ended		September 30, 2015		Percent	
	September 30, 2016	Percent of Revenue	September 30, 2015	Percent of Revenue	Change	Percent Change
Operating revenue	\$144.3	100.0 %	\$ 149.2	100.0 %	\$ (4.9 )	(3.3 )%
Operating expenses:						
Purchased transportation	56.3	39.0	61.7	41.4	(5.4 )	(8.8 )
Salaries, wages and employee benefits	33.8	23.4	35.7	23.9	(1.9 )	(5.3 )
Operating leases	9.0	6.2	8.4	5.6	0.6	7.1
Depreciation and amortization	5.5	3.8	5.4	3.6	0.1	1.9
Insurance and claims	3.9	2.7	2.6	1.7	1.3	50.0
Fuel expense	0.8	0.6	1.0	0.7	(0.2 )	(20.0)
Other operating expenses	14.0	9.7	12.8	8.6	1.2	9.4
Total operating expenses	123.3	85.4	127.6	85.5	(4.3 )	(3.4 )
Income from operations	\$21.0	14.6 %	\$ 21.6	14.5 %	\$ (0.6	