FOX FACTORY HOLDING CORP
Form 10-Q
August 05, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2015

OR

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

Commission File Number: 001-36040

Fox Factory Holding Corp.
(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	26-1647258 (I.R.S. Employer Identification No.)
915 Disc Drive Scotts Valley, CA	95066
(Address of Principal Executive Offices)	(Zip Code)

(831) 274-6500
(Registrant’s Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý 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 ý 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. (Check one):

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

As of July 30, 2015, there were 36,951,699 shares of the Registrant’s common stock outstanding.

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
FOX FACTORY HOLDING CORP.
Condensed Consolidated Balance Sheets
(in thousands, except per share data)

	As of June 30, 2015 (Unaudited)	As of December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$6,188	$4,212
Accounts receivable (net of allowances of $379 and $348 at June 30, 2015 and December 31, 2014, respectively)	51,676	39,221
Inventory	78,808	59,191
Prepaids and other current assets	10,304	6,257
Deferred tax assets	7,344	4,298
Total current assets	154,320	113,179
Property, plant and equipment, net	22,436	19,759
Goodwill	59,181	58,745
Intangibles, net	61,425	65,184
Other assets	1,231	1,570
Total assets	$298,593	$258,437
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$44,267	$30,371
Accrued expenses	20,055	12,128
Liability reserve for uncertain tax positions	9,287	7,785
Current portion of long-term debt	2,837	2,837
Current portion of contingent consideration	7,150	7,704
Total current liabilities	83,596	60,825
Line of credit	20,000	—
Long-term debt, less current portion	45,744	47,163
Deferred rent	726	681
Deferred tax liabilities	7,152	7,414
Contingent consideration, less current portion	6,300	13,548
Total liabilities	163,518	129,631
Commitments and contingencies (Note 7)		
Stockholders' equity		
Preferred stock, $0.001 par value—10,000 authorized and no shares issued or outstanding as of June 30, 2015 and December 31, 2014	—	—
Common stock, $0.001 par value—90,000 authorized; 37,258 shares issued and 36,952 outstanding as of June 30, 2015; 37,117 shares issued and 37,078 outstanding as of December 31, 2014	37	37
Additional paid-in capital	95,804	97,006
Accumulated other comprehensive loss	(468)	(406)
Retained earnings	39,702	32,169
Total stockholders' equity	135,075	128,806
Total liabilities and stockholders' equity	$298,593	$258,437

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FOX FACTORY HOLDING CORP.
Condensed Consolidated Statements of Income
(in thousands, except per share data)
(Unaudited)

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Sales	$97,171	$86,374	$164,959	$142,482
Cost of sales	67,303	59,421	116,308	98,512
Gross profit	29,868	26,953	48,651	43,970
Operating expenses:				
Sales and marketing	6,140	5,118	11,437	8,962
Research and development	4,158	3,625	7,560	6,760
General and administrative	4,855	4,678	9,496	8,608
Amortization of purchased intangibles	1,839	1,674	3,679	3,035
Fair value adjustment of contingent consideration and acquisition related compensation	2,339	122	4,403	122
Total operating expenses	19,331	15,217	36,575	27,487
Income from operations	10,537	11,736	12,076	16,483
Other expense, net:				
Interest expense	414	321	744	431
Other expense (income), net	2	(125)	(13)	(157)
Other expense, net	416	196	731	274
Income before income taxes	10,121	11,540	11,345	16,209
Provision (benefit) for income taxes	3,358	(41)	3,812	1,687
Net income	$6,763	$11,581	$7,533	$14,522
Earnings per share:				
Basic	$0.18	$0.32	$0.20	$0.40
Diluted	$0.18	$0.31	$0.20	$0.38
Weighted average shares used to compute earnings per share:				
Basic	36,921	36,648	36,986	36,534
Diluted	37,827	37,812	37,883	37,734

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FOX FACTORY HOLDING CORP.
Condensed Consolidated Statements of Comprehensive Income
(in thousands)
(Unaudited)

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Net income	$6,763	$11,581	$7,533	$14,522
Other comprehensive (loss) income:				
Foreign currency translation adjustments, net of tax effects	4	3	(62)	9
Other comprehensive (loss) income	4	3	(62)	9
Comprehensive income	$6,767	$11,584	$7,471	$14,531

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FOX FACTORY HOLDING CORP.
Condensed Consolidated Statements of Cash Flows
(in thousands)
(Unaudited)

	For the six months ended June 30, 2015	2014
OPERATING ACTIVITIES:		
Net income	$7,533	$14,522
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,789	4,535
Cost of goods on acquired inventory step up	1,084	348
Provision for doubtful accounts	25	22
Stock-based compensation	2,412	1,922
Excess tax benefit from exercise of stock options	(471)	(1,662)
(Gain) loss on disposal of property and equipment	(46)	3
Deferred taxes	(3,028)	(1,865)
Amortization of loan fees	99	87
Change in fair value of contingent consideration	52	—
Changes in operating assets and liabilities:		
Accounts receivable	(12,380)	(4,044)
Inventory	(20,593)	(12,185)
Income taxes payable	4,621	1,000
Prepaids and other assets	(3,851)	(2,592)
Accounts payable	13,852	5,987
Accrued expenses	5,186	(1,895)
Deferred rent	45	(130)
Net cash provided by operating activities	329	4,053
INVESTING ACTIVITIES:		
Acquisition of businesses	(765)	(40,770)
Purchases of property and equipment	(4,593)	(2,244)
Acquisition of other assets	—	(1,401)
Proceeds from sale of property and equipment	82	—
Net cash used in investing activities	(5,276)	(44,415)
FINANCING ACTIVITIES:		
Proceeds from line of credit	34,000	13,000
Payments on line of credit	(14,000)	(21,000)
Payment of contingent consideration liability	(7,854)	—
Proceeds from issuance of debt, net of origination fees of $278	—	49,722
Repurchase of common stock	(3,993)	—
Repayment of debt	(1,419)	(4,625)
Proceeds (repurchases) from stock compensation, net	(92)	1,750
Excess tax benefit from exercise of stock options	471	1,662
Net cash provided by financing activities	7,113	40,509

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EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(190)	26
CHANGE IN CASH AND CASH EQUIVALENTS	1,976	173
CASH AND CASH EQUIVALENTS—Beginning of period	4,212	1,683
CASH AND CASH EQUIVALENTS—End of period	$6,188	$1,856
SUPPLEMENTAL CASH FLOW INFORMATION:		
Cash paid during the period for:		
Income taxes	$4,565	$2,506
Interest	$641	$342
Non-cash investing and financing activities:		
Contingent consideration - acquisition of Sport Truck USA, Inc.	$—	$19,035

The accompanying notes are an integral part of these condensed consolidated financial statements.

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FOX FACTORY HOLDING CORP.
Notes to Condensed Consolidated Financial Statements
(in thousands, except per share amounts)
(Unaudited)

1. Description of the Business, Basis of Presentation and Summary of Significant Accounting Policies
Fox Factory Holding Corp. (the "Company") designs and manufactures performance ride dynamics products primarily for bicycles, side-by-side vehicles, on-road and off-road vehicles and trucks, all-terrain vehicles, snowmobiles, specialty vehicles and applications, and motorcycles. The Company acts both as a tier one supplier to leading action sports original equipment manufacturers and provides aftermarket products to retailers and distributors.
Throughout this Form 10-Q, unless stated otherwise or as the context otherwise requires, the "Company," "FOX," "Fox Factory," "we," "us," "our," and "ours" refer to Fox Factory Holding Corp. and its wholly owned operating subsidiaries on a consolidated basis.
Basis of Presentation - The accompanying condensed consolidated financial statements are unaudited. These unaudited interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and applicable rules and regulations of the Securities and Exchange Commission (“SEC”) regarding interim financial reporting. Certain information and footnote disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Accordingly, these interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2014 included in the Company’s Annual Report on Form 10-K as filed with the SEC. In management’s opinion, the unaudited interim consolidated financial statements reflect all adjustments, which are of a normal and recurring nature, that are necessary for a fair presentation of financial results for the interim periods presented. Operating results for the three and six months ended June 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015.
Initial Public Offering- On August 13, 2013, the Company completed the initial public offering (“IPO”) of its common stock pursuant to a registration statement on Form S-1. In the IPO, the Company sold 2,857 shares of common stock and the selling stockholders sold a total of 7,000 shares of common stock (including the shares sold pursuant to the exercise of the option granted to the underwriters) at an initial public offering price to the public of $15.00 per share. The Company received net proceeds from the IPO of approximately $36,122 from its sale of 2,857 shares of common stock after deducting underwriting discounts, commissions and offering expenses. The Company did not receive any proceeds from the sale of shares by the selling stockholders. The Company used the net proceeds it received to pay down related party debt. In July 2014, certain selling stockholders completed a secondary offering of the Company's common stock.
Principles of Consolidation- These condensed consolidated financial statements include the Company and its wholly owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

Summary of Significant Accounting Policies - Self-Insurance. Beginning in January 2015, the Company is partially self-insured for its U.S. employee health and welfare benefits. The Company’s liability for self-insurance is based on claims filed and an estimate of claims incurred but not yet reported. The Company considers a number of factors, including historical claims information, when determining the amount of the accrual. Costs related to the administration of the plan and related claims are expensed as incurred. The Company has third-party insurance coverage to limit exposure for individually significant claims. The estimate for claims incurred as of June 30, 2015 is $573 and is recorded within accrued expenses on the condensed consolidated balance sheets. There have been no other changes to our significant accounting policies described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014 that have had a material impact on our condensed consolidated financial statements and related notes.

Use of Estimates- The preparation of the Company’s condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. These estimates are based on information available as of the date of the financial statements; therefore, actual results could differ from management’s estimates.

(in thousands, except per share amounts)

Certain Significant Risks and Uncertainties- The Company is subject to those risks common in manufacturing-driven markets, including, but not limited to, competitive forces, dependence on key personnel, customer demand for its products, the successful protection of its proprietary technologies, compliance with government regulations, and the possibility of not being able to obtain additional financing when needed.
Recent Accounting Pronouncements- In May 2014, the Financial Accounting Standards Board ("FASB") and International Accounting Standards Board issued their converged standard on revenue recognition, Accounting Standards Update No. 2014-09, “Revenue from Contracts with Customers". This standard outlines a single comprehensive model for companies to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that revenue is recognized when a customer obtains control of a good or service. A customer obtains control when it has the ability to direct the use of and obtain the benefits from the good or service. Transfer of control is not the same as transfer of risks and rewards, as it is considered in current guidance. We will apply the new guidance to determine whether revenue should be recognized over time or at a point in time. This standard will be effective for the first interim period within annual reporting periods beginning after December 15, 2016, with no early adoption permitted, and the Company can choose to apply this standard retrospectively for each prior reporting period presented or retrospectively with the cumulative effect of initially applying the standard recognized at the date of the initial application in retained earnings. In July 2015, the FASB affirmed a proposal to defer the effective date of ASU 2014-09. ASU 2014-09 will be effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, but entities will be permitted to early adopt the standard as of the original effective date. The Company has not yet developed an expectation of the impact that adoption will have on its consolidated financial statements.

Reclassifications- We have reclassified certain prior period amounts within our condensed consolidated balance sheet for the year ended December 31, 2014, the condensed consolidated statements of income for the three and six months ended June 30, 2014, and the condensed consolidated statement of cash flows for the six months ended June 30, 2014 to conform to our current year presentation.

2. Inventory
Inventory consisted of the following:

	As of June 30, 2015	As of December 31, 2014
Raw materials	$56,104	$39,655
Work-in-process	2,612	1,568
Finished goods	20,092	17,968
Total inventory	$78,808	$59,191

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FOX FACTORY HOLDING CORP.
Notes to Condensed Consolidated Financial Statements - continued
(in thousands, except per share amounts)
(unaudited)

3. Property, Plant and Equipment, net
Property, plant and equipment consisted of the following:

	As of June 30, 2015	As of December 31, 2014
Machinery and manufacturing equipment	$20,879	$17,739
Information systems, office equipment and furniture	6,184	5,297
Transportation equipment	2,072	2,041
Building and land	3,469	3,469
Leasehold improvements	6,490	5,971
Total	39,094	34,517
Less: accumulated depreciation and amortization	(16,658)	(14,758)
Property, plant and equipment, net	$22,436	$19,759

4. Intangibles, net
Intangible assets, excluding goodwill, are comprised of the following:

	Gross carrying amount	Accumulated amortization	Net carrying amount	Weighted average life (years)
June 30, 2015:				
Customer relationships	$36,511	$(10,646)	$25,865	13
Core technology	33,700	(30,534)	3,166	8
Patents	835	(467)	368	5
Total	71,046	(41,647)	29,399	
Trademarks and brands, not subject to amortization			32,026	
Total			$61,425	
December 31, 2014:				
Customer relationships	$36,555	$(9,144)	$27,411	13
Core technology	33,700	(28,438)	5,262	8
Patents	835	(394)	441	5
Total	71,090	(37,976)	33,114	
Trademarks and brands, not subject to amortization			32,070	
Total			$65,184	

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Amortization of intangibles	$1,839	$1,674	$3,679	$3,035

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FOX FACTORY HOLDING CORP.
Notes to Condensed Consolidated Financial Statements - continued
(in thousands, except per share amounts)
(unaudited)

Future amortization expense for finite-lived intangibles as of June 30, 2015 is as follows:

For the years ending December 31,	Amortization Expense
2015 (remaining six months)	$3,680
2016	2,747
2017	2,685
2018	2,686
2019	2,613
Thereafter	14,988
Total expected future amortization	$29,399

Goodwill activity consisted of the following:

Balance as of December 31, 2014	$58,745
Acquisitions	567
Currency translation and other adjustments	(131)
Balance as of June 30, 2015	$59,181

5. Accrued Expenses

Accrued expenses consisted of the following:

	As of June 30, 2015	As of December 31, 2014
Payroll and related expenses	$10,096	$5,626
Warranty	4,324	4,215
Income tax payable	4,087	1,405
Other accrued expenses	1,548	882
Total	$20,055	$12,128

Activity related to warranties is as follows:

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Beginning warranty liability	$4,170	$3,778	$4,215	$3,857
Charge to cost of sales	697	978	1,103	1,717
Fair value of warranty assumed in acquisition	—	—	—	192
Costs incurred	(543)	(876)	(994)	(1,886)
Ending warranty liability	$4,324	$3,880	$4,324	$3,880

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Notes to Condensed Consolidated Financial Statements - continued
(in thousands, except per share amounts)
(unaudited)

6. Debt

Amended and Restated 2013 Credit Facility

In August 2013, the Company entered into a credit facility with Sun Trust Bank and other named lenders (the "2013 Credit Facility"). The 2013 Credit Facility provided a revolving line of credit. On March 31, 2014, the Company amended and restated the 2013 Credit Facility (the “Amended and Restated 2013 Credit Facility”). The Amended and Restated 2013 Credit Facility provided a maturing secured term loan in the principal amount of $50,000, (the "Term Loan"), subject to quarterly amortization payments, and extended the term of the 2013 Credit Facility through March 31, 2019. The proceeds of the Term Loan were used, in part, to fund the acquisition of Sport Truck USA, Inc. ("Sport Truck") and to pay down the revolving line of credit provided under the 2013 Credit Facility. On December 12, 2014, the Company entered into the First Amendment to the Amended and Restated 2013 Credit Facility (the "First Amendment"). The First Amendment increased the Term Loan principal amount by $30,000 to a total of $56,750, subject to quarterly amortization payments, and extended the maturity of the Amended and Restated 2013 Credit Facility through December 12, 2019. The additional proceeds of the Term Loan made available through the First Amendment were used to partially fund the acquisition of Race Face Performance Products, Inc. and Easton Cycling (together "Race Face/Easton"). On May 29, 2015 the Company entered into a Second Amendment to the Amended and Restated 2013 Credit Facility solely to revise the definition of "Continuing Director" contained therein.

The Amended and Restated 2013 Credit Facility provides for interest at either a rate based on the London Interbank Offered Rate, or LIBOR, plus a margin ranging from 1.50% to 2.50%, or based on the prime rate offered by SunTrust Bank plus a margin ranging from 0.50% to 1.50%. At June 30, 2015, the one month LIBOR and prime rates were 0.19% and 3.25%, respectively. The Amended and Restated 2013 Credit Facility is secured by substantially all of the Company’s assets, restricts the Company's ability to make certain payments and engage in certain transactions, and also requires that the Company satisfy customary financial ratios. The Company was in compliance with the covenants as of June 30, 2015.

The following table summarizes the line of credit under the Amended and Restated 2013 Credit Facility:

	As of June 30, 2015
Amount outstanding	$20,000
Available borrowing capacity	$40,000
Maximum borrowing capacity	$60,000
Interest rate at June 30, 2015	2.35 %
Maturity date	December 12, 2019

As of June 30, 2015, future principal payments for long-term debt, including the current portion, are summarized as follows:

Fiscal Year	
2015 (remaining six months)	$1,419
2016	2,837
2017	4,256
2018	4,256
2019	35,813
Total	48,581
Less: current portion	(2,837)
Long-term debt less current portion	$45,744

(in thousands, except per share amounts)

7. Commitments and Contingencies

Operating Leases—The Company has operating lease agreements for administrative, research and development, manufacturing and sales and marketing facilities and equipment that expire at various dates. The Company recognizes rent expense on a straight-line basis over the lease term and records the difference between cash rent payments and the recognition of rent expense as a deferred rent liability.

Indemnification Agreements—In the ordinary course of business, the Company may provide indemnifications of varying scope and terms to customers, vendors, lessors, business partners, and other parties with respect to certain matters, including, but not limited to, losses arising out of breach of such agreements, services to be provided by the Company or intellectual property infringement claims made by third parties. In addition, the Company has entered into indemnification agreements with directors and certain officers and employees that will require the Company, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors, officers or employees. While the outcome of these matters cannot be predicted with certainty, the Company does not believe that the outcome of any claims under indemnification arrangements will have a material effect on the Company's results of operations, financial position or liquidity.

Other Commitments—In connection with the acquisition of businesses, the Company has agreed to pay up to $36,945 in additional consideration and acquisition related compensation through 2017, contingent upon the achievement of certain financial performance goals and in some cases continued employment through 2016. A portion of the obligation is denominated in Canadian dollars. See Note 9 - Fair Value Measurements and Note 13 - Acquisitions. No other material contractual obligation has changed since the Company's Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the SEC on March 2, 2015.

8. Stockholders' Equity

Share Repurchase Program

On November 3, 2014, the Company's Board of Directors authorized the repurchase of up to an aggregate of $40,000 in shares of our common stock under our stock repurchase program. Shares of common stock repurchased under this program are deemed issued but not outstanding. During the six months ended June 30, 2015, the Company repurchased 268 shares for a total of $3,993. At June 30, 2015, $35,436 remains available for repurchase under this plan. The repurchase program will expire on December 31, 2015 unless extended by the Board of Directors.

Equity Incentive Plans

During the six months ended June 30, 2015 and 2014, 53 and 421 shares of common stock, respectively, were issued due to the exercise of stock options, resulting in proceeds to the Company of approximately $170 and $1,750, respectively. There were no stock options granted or forfeited during the six months ended June 30, 2015. There were no options granted and there were 19 options forfeited during the six months ended June 30, 2014.

The following table summarizes the allocation of stock-based compensation in the accompanying consolidated statements of income:

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Cost of sales	20	12	31	20
Sales and marketing	126	81	208	116
Research and development	49	30	72	42
General and administrative	1,165	978	2,101	1,744

Total	$1,360	$1,101	$2,412	$1,922

FOX FACTORY HOLDING CORP.
Notes to Condensed Consolidated Financial Statements - continued
(in thousands, except per share amounts)
(unaudited)

The following table summarizes the activity for the Company's unvested restricted stock units ("RSU") for the six months ended June 30, 2015.

	Unvested RSUs	
	Number of shares outstanding	Weighted-average grant date fair value
Unvested at December 31, 2014	780	17.30
Granted	227	16.68
Forfeited	(1)	17.12
Vested	(105)	17.16
Unvested at June 30, 2015	901	$ 17.16

As of June 30, 2015, the Company had approximately $13,073 of unrecognized stock-based compensation expense related to RSUs, which will be recognized over the remaining weighted-average vesting period of approximately 2.82 years. Additionally, as of June 30, 2015, the Company had approximately $513 of unrecognized stock-based compensation expense related to stock options, which will be recognized over the remaining weighted-average vesting period of approximately 1.93 years.

9. Fair Value Measurements

The FASB's Accounting Standards Codification 820, "Fair Value Measurements and Disclosures" requires the valuation of assets and liabilities required or permitted to be either recorded or disclosed at fair value based on hierarchy of available inputs as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2: Quoted prices for similar assets and liabilities in active markets, quoted prices for identical assets and liabilities in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability; and

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e. supported by little or no market activity).

As of June 30, 2015, the carrying amount of the principal under the Company’s Amended and Restated 2013 Credit Facility approximates fair value because it has a variable interest rate that reflects market changes in interest rates and changes in the Company’s net leverage ratio. As of June 30, 2015, the Company used Level 2 inputs to determine the fair value of its Amended and Restated 2013 Credit Facility.

The Company measured its contingent consideration liability arising from the acquisition of Sport Truck using Level 3 unobservable inputs (see Note 13 - Acquisitions). The fair value of the contingent consideration liability associated with the achievement of adjusted EBITDA targets is estimated at each balance sheet date by applying a Black-Scholes model to the Company's most recent financial projection. The unobservable inputs to the valuation model that have the most significant effect on the estimated fair value of the Company's contingent consideration liability are the projected financial results, the probabilities that actual results will exceed the projection and the volatility surrounding the expected results. The Company estimated the probabilities of actual results exceeding the projection during various years of the earn-out at values ranging from 70% to 75% as of June 30, 2015, compared to an overall estimate of 75% for all annual periods at the acquisition date. Additionally, volatility was measured at 35% as of June 30, 2015, compared to 41% at the acquisition date. The change in fair value is recorded as a component of fair value adjustment of contingent consideration and acquisition related compensation in the accompanying condensed consolidated statements of income for the three and six months ended June 30, 2015.

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FOX FACTORY HOLDING CORP.
Notes to Condensed Consolidated Financial Statements - continued
(in thousands, except per share amounts)
(unaudited)

The following table provides a reconciliation of the beginning and ending balances for the Company's contingent consideration liability measured at fair value using Level 3 inputs:

	Contingent consideration liability (level 3 measurement)
Balance at December 31, 2014	$21,252
Change in fair value	52
Payment of contingent liability	(7,854)
Balance at June 30, 2015	$13,450

10. Income Taxes

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Provision for income taxes	$3,358	$(41)	$3,812	$1,687
Effective tax rates	33.2 %	(0.4)%	33.6 %	10.4 %

For the three and six months ended June 30, 2015, the difference between the Company's effective tax rate and the 35% federal statutory rate resulted primarily from the benefit from domestic production activity deduction and tax credits, partially offset by state taxes.

For the three and six months ended June 30, 2014, the difference between the Company's effective tax rate and the 35% federal statutory rate resulted primarily from a second quarter discrete tax benefit of $3,848, or $0.10 per basic and fully diluted share for the three months ended June 30, 2014 and $0.11 and $0.10 per basic and fully diluted share, respectively, for the six months ended June 30, 2014, related to the reapportionment of income amongst the jurisdictions where the Company does business. The Company periodically evaluates opportunities to enhance tax efficiencies and to minimize tax liabilities through operating, legal and administrative strategies. The reapportionment benefit relates to tax years 2009 through 2013 and resulted from the Company's examination of evolving laws, existing court cases, and its business practices. The tax benefit includes the impact of a reduction in the rate used to measure the Company's net deferred tax liability and unrecognized tax benefit. The benefit was accounted for as a change in estimate. The effective tax rate for the three and six months ended June 30, 2014 was also benefited by the domestic production activity deduction, partially offset by 2014 state taxes.

As of June 30, 2015, the Company had $9,287 of unrecognized tax benefits, of which approximately $8,397, if recognized, would favorably impact the effective tax rate. The Company regularly engages in discussions and negotiations with tax authorities regarding tax matters in various jurisdictions. The Company believes it is reasonably possible that certain federal, foreign, and state tax matters may be concluded in the next 12 months. Specific positions that may be resolved include issues involving the deductibility of amortization and depreciation deductions which were incurred as a result of the acquisition of the Company in 2008. The Company estimates that it is reasonably possible that the unrecognized tax benefits at June 30, 2015 could be reduced by approximately $1,323 in the next twelve months.

The Company's federal tax returns for 2011 forward are subject to examination by tax authorities. The Company’s 2011 and 2012 state tax returns are currently under examination by the California Franchise Tax Board, and 2009 and 2013 forward California tax returns are subject to future examination.

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FOX FACTORY HOLDING CORP.
Notes to Condensed Consolidated Financial Statements - continued
(in thousands, except per share amounts)
(unaudited)

11. Earnings Per Share

Basic earnings per share ("EPS") amounts are computed by dividing net income for the period by the weighted average number of common shares outstanding during the period. Diluted EPS amounts are computed by dividing net income for the period by the weighted average number of shares of common stock and potentially dilutive common stock outstanding during the period. Potentially dilutive common shares include shares issuable upon the exercise of outstanding stock options and vesting of restricted stock units, which are reflected in diluted earnings per share by application of the treasury stock method.

The following table presents the calculation of basic and diluted earnings per share:

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Net income	$6,763	$11,581	$7,533	$14,522
Weighted average shares used to compute basic earnings per share	36,921	36,648	36,986	36,534
Dilutive effect of employee stock plans	906	1,164	897	1,200
Weighted average shares used to compute diluted earnings per share	37,827	37,812	37,883	37,734
Earnings per share:				
Basic	$0.18	$0.32	$0.20	$0.40
Diluted	$0.18	$0.31	$0.20	$0.38

The Company did not exclude any potentially dilutive shares from the calculation of diluted earnings per share for the three and six months ended June 30, 2015 and 2014, as none of these shares would have been antidilutive.

12. Segments

The Company has determined that it has a single operating and reportable segment. The Company considers operating segments to be components of the Company in which separate financial information is available that is evaluated regularly by the Company's chief operating decision maker in deciding how to allocate resources and in assessing performance. The chief operating decision maker for the Company is the Chief Executive Officer. The Chief Executive Officer reviews financial information presented on a consolidated basis for purposes of allocating resources and evaluating financial performance.

The following table summarizes total sales generated by geographic location of the customer:

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
United States	$40,562	$39,143	$73,355	$63,176
Asia	36,390	28,099	48,735	39,430
Europe	14,461	15,036	29,526	31,230
Rest of the world	5,758	4,096	13,343	8,646
Total sales	$97,171	$86,374	$164,959	$142,482

(in thousands, except per share amounts)

The Company’s long-lived assets by geographic location are as follows:

	As of June 30, 2015	As of December 31, 2014
United States	$19,745	$16,579
International	2,691	3,180
Total long-lived assets	$22,436	$19,759

The following table summarizes total sales by product category:

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Bikes	$61,557	$49,653	$97,179	$83,339
Power vehicles	35,614	36,721	67,780	59,143
Total sales	$97,171	$86,374	$164,959	$142,482

13. Acquisitions

Sport Truck, USA, Inc.

On March 31, 2014, the Company acquired certain assets and assumed certain liabilities of Sport Truck. The transaction was accounted for as a business combination. The Company paid cash of $40,770, plus the effective settlement of trade receivables in the amount of $473. In addition, certain members of Sport Truck’s executive management team agreed to refund up to $1,432 of the proceeds from the sale, on a graduated basis, if they terminate employment prior to March 31, 2017. As a result, such payments have been excluded from the acquisition consideration, and will be recognized as compensation expense over the expected three year service period. In the three and six months ended June 30, 2015, the Company recognized $122 and $240 of acquisition related compensation expense, respectively, related to the arrangement, which is recorded as a component of fair value adjustment of contingent consideration and acquisition related compensation in the accompanying condensed consolidated statements of income. As of June 30, 2015, prepaid compensation of $476 and $351 is included in prepaids and other current assets and other assets, respectively, in the accompanying condensed consolidated balance sheet.

The Company agreed to total contingent consideration of up to $29,295 upon achievement of adjusted earnings before interest, taxes, depreciation and amortization ("EBITDA") targets of the acquired business through 2016, subject to adjustments defined in the asset purchase agreement. Performance compared to the targets is measured annually over a three year period, and payment of the contingent consideration will be made upon final determination of the adjusted EBITDA for each year. The estimated acquisition date fair value of the contingent consideration was $19,035, based on a Black-Scholes model, and is included in the computation of total consideration. As of June 30, 2015, $7,854 of contingent consideration has been paid under this arrangement. See Note 9 - Fair Value Measurements.

FOX FACTORY HOLDING CORP.
Notes to Condensed Consolidated Financial Statements - continued
(in thousands, except per share amounts)
(unaudited)

The Company’s allocation of the purchase price to the net tangible and intangible assets acquired and liabilities assumed is as follows:

Fair market values	
Tangible assets acquired and liabilities assumed	$13,046
Intangible assets	35,270
Goodwill	11,962
Total	$60,278

The values assigned to the identifiable intangible assets were determined by discounting the estimated future cash flows associated with these assets to their present value. The goodwill of $11,962 reflects the strategic fit of Sport Truck with the Company’s operations. Sport Truck is well-aligned with the Company’s mission of improving vehicle performance, delivering best in-class service, and entering into strategic and adjacent markets. The Company will amortize the acquired customer relationships asset over its expected useful life of 15 years. Trademarks, brand names and goodwill are expected to have an indefinite life, and will be subject to impairment testing. The goodwill is expected to be deductible for income tax purposes.

The Company incurred $222 and $1,247 of transaction costs in conjunction with the Sport Truck acquisition for the three and six months ended June 30, 2014, and $0 and $34 for the three and six months ended 2015, respectively which is included in general and administrative expense in the accompanying condensed consolidated statements of income.

Race Face Performance and Easton Cycling Businesses

On December 12, 2014, the Company acquired certain assets and assumed certain liabilities of Race Face/Easton, which was engaged in the design, manufacture, and global distribution of performance mountain and road bike wheels and other performance cycling components including cranks, bars, stems, and seat posts. In connection with the acquisition, the Company paid approximately $30,168. The acquisition was financed with debt and includes a potential earn-out opportunity of up to a maximum of CAD $19,500, or approximately $15,795 US dollars at the exchange rate in effect at June 30, 2015, contingent upon continued employment and the achievement of certain performance-based financial targets through October 2016. In the three and six months ended June 30, 2015, the Company recognized $2,221 and $4,111, respectively, of acquisition related compensation related to the earn-out opportunity, which is recorded as a component of fair value adjustment of contingent consideration and acquisition related compensation in the accompanying condensed consolidated statements of income. The Company incurred $135 and $540 of acquisition related costs in conjunction with the Race Face/Easton acquisition for the three and six months ended June 30, 2015, respectively, which is included in general and administrative expense in the accompanying condensed consolidated statements of income.

The allocation of the purchase price to the assets acquired and liabilities assumed is preliminary, subject to the completion of the Company's validation of working capital and completion of its intangible valuation procedures, with the assistance of specialists. Goodwill acquired is expected to be deductible for income tax purposes.

14. Related Party Agreement

In September 2014, the Company entered into an agreement with Compass Group Diversified Holdings, LLC ("Compass") to assist with compliance requirements pursuant to the Sarbanes-Oxley Act of 2002, as amended. Compass purchased a controlling interest in the Company in January, 2008, and beneficially owned approximately 40.9% of our outstanding common stock at June 30, 2015. Fees for services provided under this arrangement are estimated to be approximately $100 annually. The agreement will terminate on March 31, 2016 unless terminated earlier by either party.

Fox Factory, Inc. has a triple-net building lease for its manufacturing and office facilities in Watsonville, California. The building is owned by Robert Fox, a founder and minority stockholder of the Company. The term of the lease ends June 30, 2018, with monthly rental payments, which are adjusted annually for a cost-of-living increase based upon the consumer price index. Payments made under this lease were $301 and $602 for the three and six months ended June 30, 2015, respectively, and $293 and $586 for the three and six months ended June 30, 2014, respectively.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our unaudited condensed consolidated financial statements and related notes thereto included elsewhere in this Quarterly Report on Form 10-Q and with our audited consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the Securities and Exchange Commission ("SEC") on March 2, 2015 and our other reports and registration statements that we file with the SEC from time to time. In addition to historical condensed consolidated financial information, the following discussion contains forward-looking statements that reflect our plans, estimates, and beliefs. Our actual results could differ materially from those discussed below. Factors that could cause or contribute to these differences include those discussed below and elsewhere in this Quarterly Report on Form 10-Q, particularly in the "Risk Factors" section included in Part II, Item 1A.

Unless the context otherwise requires, the terms "FOX," the "Company," "we," "us," and "our" in this Quarterly Report on Form 10-Q refer to Fox Factory Holding Corp. and its wholly owned operating subsidiaries, on a consolidated basis.

Cautionary Note Regarding Forward-Looking Statements

This quarterly report includes forward-looking statements, which are subject to the "safe harbor" created by section 27A of the Securities Act of 1933, as amended, and section 21E of the Securities Exchange Act of 1934, as amended. We may make forward-looking statements in our SEC filings, press releases, news articles, earnings presentations and when we are speaking on behalf of the Company. Forward-looking statements generally relate to future events or our future financial or operating performance which involve substantial risks and uncertainties. In some cases, you can identify forward-looking statements because they contain words such as "may," "might," "will," "would," "should," "expect," "anticipate," "could," "intend," "target," "project," "contemplate," "believe," "estimate," "predict," "likely," "potential" or "co
negative of these words or other similar terms or expressions that concern our expectations, strategy, plans or intentions. Forward-looking statements contained in this Quarterly Report on Form 10-Q are subject to numerous risks and uncertainties, including but not limited to risks related to:

- our ability to develop new and innovative products in our current end-markets;
- our ability to leverage our technologies and brand to expand into new categories and end-markets;
- our ability to increase our aftermarket penetration;
- our ability to accelerate international growth;
- our ability to improve operating and supply chain efficiencies;
- our future financial performance, including our sales, cost of sales, gross profit or gross margins, operating expenses, ability to generate positive cash flow and ability to maintain our profitability;
- our ability to maintain our premium brand image and high-performance products;
- our ability to maintain relationships with the professional athletes and race teams we sponsor;
- our transition of the majority of our mountain bike manufacturing operations to Taiwan and our expectations related to such transition;
- our ability to selectively add additional dealers and distributors in certain geographic markets;
- the growth of the markets in which we compete, our expectations regarding consumer preferences and our ability to respond to changes in consumer preferences;
- changes in demand for high-end suspension and ride dynamics products;
- our ability to successfully identify, evaluate and manage potential acquisitions and to benefit from such acquisitions; and
- future economic or market conditions.

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You should not rely upon forward-looking statements as predictions of future events. We have based the forward-looking statements contained in this Quarterly Report on Form 10-Q primarily on our current expectations and projections about future events and trends that we believe may affect our business, financial condition, results of operations, and prospects and the outcomes of any of the events described in any forward-looking statements are subject to risks, uncertainties, and other factors. In addition to the risks, uncertainties and other factors discussed above and elsewhere in this Quarterly Report on Form 10-Q, the risks, uncertainties and other factors expressed or implied discussed in Item 1A, "Risk Factors" of Part I of our 2014 Annual Report on Form 10-K filed with the SEC on March 2, 2015 could cause or contribute to actual results differing materially from those set forth in any forward-looking statement. Moreover, we operate in a very competitive and challenging environment. New risks and uncertainties emerge from time to time, and it is not possible for us to predict all risks and uncertainties that could have an impact on the forward-looking statements contained in this Quarterly Report on Form 10-Q. We cannot assure you that the results, events, and circumstances reflected in the forward-looking statements will be achieved or occur. Actual results, events, or circumstances could differ materially from those contemplated by, set forth in, or underlying any forward-looking statements. For all of these forward-looking statements we claim the protection of the safe harbor for forward-looking statements in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended.

The forward-looking statements made in this Quarterly Report on Form 10-Q relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward-looking statements made in this Quarterly Report on Form 10-Q to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q or to reflect new information or the occurrence of unanticipated events, except as required by law. We may not actually achieve the plans, intentions, or expectations disclosed in our forward-looking statements and you should not place undue reliance on our forward-looking statements. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments we may make.

Critical Accounting Policies and Estimates

Self-Insurance. Beginning in January 2015, the Company is partially self-insured for its U.S. employee health and welfare benefits. The Company’s liability for self-insurance is based on claims filed and an estimate of claims incurred but not yet reported. The Company considers a number of factors, including historical claims information, when determining the accrual. Costs related to the administration of the plan and related claims are expensed as incurred. The Company has third-party insurance coverage to limit exposure for individually significant claims. There have been no other material changes to our critical accounting policies and estimates as compared to the critical accounting policies and estimates included in our Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the SEC on March 2, 2015.

Recent Accounting Pronouncements

See Note 1 to the accompanying notes to unaudited condensed consolidated financial statements included in this Quarterly Report on Form 10-Q.

Seasonality

Our business is seasonal. In each of the last three fiscal years, our quarterly sales have been the lowest in the first quarter and the highest during our third quarter of the year. We believe this seasonality is due to the delivery of new products, including our suspension products related to the new mountain bike season, during the late spring and summer each year.

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Results of Operations

The table below summarizes our results of operations:

	For the three months ended June 30,		For the six months ended June 30,	
(in thousands)	2015	2014	2015	2014
Sales	$97,171	$86,374	$164,959	$142,482
Cost of sales	67,303	59,421	116,308	98,512
Gross profit	29,868	26,953	48,651	43,970
Operating expenses:				
Sales and marketing	6,140	5,118	11,437	8,962
Research and development	4,158	3,625	7,560	6,760
General and administrative	4,855	4,678	9,496	8,608
Amortization of purchased intangibles	1,839	1,674	3,679	3,035
Fair value adjustment of contingent consideration and acquisition related compensation	2,339	122	4,403	122
Total operating expenses	19,331	15,217	36,575	27,487
Income from operations	10,537	11,736	12,076	16,483
Other expense, net:				
Interest expense	414	321	744	431
Other expense (income), net	2	(125)	(13)	(157)
Other expense, net	416	196	731	274
Income before income taxes	10,121	11,540	11,345	16,209
Provision (benefit) for income taxes	3,358	(41)	3,812	1,687
Net income	$6,763	$11,581	$7,533	$14,522

The following table sets forth selected statement of income data as a percentage of sales for the periods indicated:

	For the three months ended June 30,		For the six months ended June 30,	
	2015	2014	2015	2014
Sales	100.0 %	100.0 %	100.0 %	100.0 %
Cost of sales	69.3	68.8	70.5	69.1
Gross profit	30.7	31.2	29.5	30.9
Operating expenses:				