CELADON GROUP INC
Form 10-Q
November 12, 2013

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

# FORM 10-Q

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

For the quarterly period ended September 30, 2013

or

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

Commission file number: 001-34533

CELADON GROUP, INC.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware<br>(State or other jurisdiction of incorporation or organization) | 13-3361050<br>(IRS Employer Identification No.) |
| 9503 East 33rd Street<br>One Celadon Drive<br>Indianapolis, IN<br>(Address of principal executive offices) | 46235-4207<br>(Zip Code) |

(Registrant's telephone number, including area code): (317) 972-7000

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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer [ ]    Accelerated filer [X]    Non-accelerated filer [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12-b2 of the Exchange Act).
Yes [ ] No [X]

As of November 8, 2013 (the latest practicable date), 23,843,953 shares of the registrant's common stock, par value $0.033 per share, were outstanding.

CELADON GROUP, INC.

Index to

September 30, 2013 Form 10-Q

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PART I. FINANCIAL INFORMATION

Item I. Financial Statements

CELADON GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Dollars and shares in thousands except per share amounts)
(Unaudited)

| | Three months ended September 30, 2013 | 2012 |
|---|---|---|
| REVENUE: | | |
| Freight revenue | $141,956 | $122,108 |
| Fuel surcharge revenue | 33,146 | 31,189 |
| Total revenue | 175,102 | 153,297 |
| | | |
| OPERATING EXPENSES: | | |
| Salaries, wages, and employee benefits | 46,654 | 40,401 |
| Fuel | 36,843 | 37,452 |
| Purchased transportation | 41,744 | 28,337 |
| Revenue equipment rentals | 1,652 | 1,998 |
| Operations and maintenance | 11,274 | 8,066 |
| Insurance and claims | 4,140 | 3,501 |
| Depreciation and amortization | 14,928 | 12,675 |
| Communications and utilities | 1,364 | 1,292 |
| Operating taxes and licenses | 2,832 | 2,588 |
| General and other operating | 2,139 | 1,848 |
| Total operating expenses | 163,570 | 138,158 |
| | | |
| Operating Income | 11,532 | 15,139 |
| | | |
| Interest expense | 1,224 | 1,490 |
| Other (income) expense | (241 ) | 38 |
| Income before income taxes | 10,549 | 13,611 |
| Income tax expense | 3,983 | 5,349 |
| Net income | $6,566 | $8,262 |
| | | |
| Income per common share: | | |
| Diluted | $0.28 | $0.36 |
| Basic | $0.29 | $0.37 |
| | | |
| Diluted weighted average shares outstanding | 23,662 | 23,185 |
| Basic weighted average shares outstanding | 22,930 | 22,383 |

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

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CELADON GROUP, INC.
CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(in thousands)
(Unaudited)

| | Three months ended September 30, 2013 | 2012 |
|---|---|---|
| Net income | $6,566 | $8,262 |
| Other comprehensive income (loss): | | |
| Unrealized gain (loss) on fuel derivative instruments, net of tax | 2 | 587 |
| Unrealized gain (loss) on currency derivative instruments, net of tax | 165 | 124 |
| Foreign currency translation adjustments, net of tax | 447 | 1,509 |
| Total other comprehensive income (loss) | 614 | 2,220 |
| Comprehensive income | $7,180 | $10,482 |

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

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CELADON GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
September 30, 2013 and June 30, 2013
(Dollars in thousands except par value and share amounts)

| ASSETS | (unaudited) September 30, 2013 | June 30, 2013 |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents | $3,610 | $1,315 |
| Trade receivables, net of allowance for doubtful accounts of $869 and $919 at September 30, 2013 and June 30, 2013, respectively | 81,518 | 77,623 |
| Prepaid expenses and other current assets | 33,058 | 13,434 |
| Tires in service | 1,015 | 1,245 |
| Equipment held for resale | 7,746 | 9,923 |
| Income tax receivable | 3,056 | 9,506 |
| Deferred income taxes | 4,236 | 4,342 |
| Total current assets | 134,239 | 117,388 |
| Property and equipment | 621,155 | 612,236 |
| Less accumulated depreciation and amortization | 119,542 | 115,366 |
| Net property and equipment | 501,613 | 496,870 |
| Tires in service | 1,527 | 1,785 |
| Goodwill | 20,415 | 17,730 |
| Investment in unconsolidated companies | 4,346 | 4,604 |
| Other assets | 3,201 | 2,785 |
| Total assets | $665,341 | $641,162 |
| | | |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| | | |
| Current liabilities: | | |
| Accounts payable | $5,785 | $10,401 |
| Accrued salaries and benefits | 10,416 | 11,197 |
| Accrued insurance and claims | 10,262 | 10,092 |
| Accrued fuel expense | 8,414 | 7,461 |
| Other accrued expenses | 21,988 | 20,070 |
| Current maturities of capital lease obligations | 30,631 | 25,669 |
| Total current liabilities | 87,496 | 84,890 |
| Capital lease obligations, net of current maturities | 179,186 | 190,625 |
| Long term debt | 104,591 | 78,137 |
| Deferred income taxes | 59,808 | 61,821 |
| Stockholders' equity: | | |
| Common stock, $0.033 par value, authorized 40,000 shares; issued and outstanding 23,882 and 23,887 shares at September 30, 2013 and June 30, 2013, respectively | 788 | 788 |
| Treasury stock at cost; 595 and 696 shares at September 30, 2013 and June 30, 2013, respectively | (4,104) | (4,811) |
| Additional paid-in capital | 104,890 | 103,749 |

| | | |
|---|---|---|
| Retained earnings | 137,333 | 131,224 |
| Accumulated other comprehensive loss | (4,647) | (5,261) |
| Total stockholders' equity | 234,260 | 225,689 |
| Total liabilities and stockholders' equity | $665,341 | $641,162 |

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

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CELADON GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

| | Three months ended September 30, 2013 | 2012 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $6,566 | $8,262 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 16,083 | 14,642 |
| Gain on sale of equipment | (1,157) | (1,911) |
| Stock based compensation | 545 | 537 |
| Deferred income taxes | (2,395) | 2,341 |
| Provision for doubtful accounts | --- | 3 |
| Changes in assets and liabilities: | | |
| Trade receivables | 295 | (590) |
| Income taxes | 5,690 | (127) |
| Tires in service | 490 | (174) |
| Prepaid expenses and other current assets | (5,411) | (4,989) |
| Other assets | (261) | 927 |
| Accounts payable and accrued expenses | (4,561) | 935 |
| Net cash provided by operating activities | 15,884 | 19,856 |
| | | |
| Cash flows from investing activities: | | |
| Purchase of property and equipment | (19,758) | (63,084) |
| Proceeds on sale of property and equipment | 8,833 | 28,504 |
| Purchase of businesses | (9,284) | (24,094) |
| Net cash used in investing activities | (20,209) | (58,674) |
| | | |
| Cash flows from financing activities: | | |
| Proceeds from borrowings on long-term debt | 81,510 | 107,480 |
| Payments on bank borrowing on long-term debt | (69,882) | (78,890) |
| Principal payments under capital lease obligations | (6,476) | (20,007) |
| Dividends paid | (457) | (448) |
| Proceeds from issuance of common stock | 1,304 | 39 |
| Net cash provided by financing activities | 5,999 | 8,174 |
| Effect of exchange rates on cash and cash equivalents | 621 | 351 |
| Increase (Decrease) in cash and cash equivalents | 2,295 | (30,293) |
| Cash and cash equivalents at beginning of period | 1,315 | 33,646 |
| Cash and cash equivalents at end of period | $3,610 | $3,353 |
| Supplemental disclosure of cash flow information: | | |
| Interest paid | $1,224 | $1,490 |
| Income taxes paid | $94 | $3,035 |
| Lease obligation incurred in the purchase of equipment | $--- | $24,280 |

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

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1. Basis of Presentation

References in this Report on Form 10-Q to "we," "us," "our," "Celadon," the "Company," or similar terms refer to Celadon Group, Inc. and its consolidated subsidiaries. All inter-company balances and transactions have been eliminated in consolidation.

The accompanying condensed consolidated unaudited financial statements of Celadon Group, Inc. and its subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America and Regulation S-X, instructions to Form 10-Q, and other relevant rules and regulations of the Securities and Exchange Commission (the "SEC"), as applicable to the preparation and presentation of interim financial information. Certain information and footnote disclosures have been omitted or condensed pursuant to such rules and regulations. We believe all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Results of operations in interim periods are not necessarily indicative of results for a full year. These unaudited condensed consolidated financial statements and notes thereto should be read in conjunction with our consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended June 30, 2013.

The preparation of the financial statements in conformity with United States generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes.  Actual results could differ from those estimates.

2. Earnings Per Share (in thousands, except per share data)

A reconciliation of the basic and diluted earnings per share is as follows:

| | Three months ended September 30, | |
|---|---|---|
| | 2013 | 2012 |
| Weighted average common shares outstanding – basic | 22,930 | 22,383 |
| Dilutive effect of stock options and unvested restricted stock units | 732 | 802 |
| Weighted average common shares outstanding – diluted | 23,662 | 23,185 |
| | | |
| Net income | $ 6,566 | $ 8,262 |
| Earnings per common share | | |
| Basic | $ 0.29 | $ 0.37 |
| Diluted | $ 0.28 | $ 0.36 |

Certain shares of common stock were excluded from the computation of diluted earnings per share because the options exercise prices were greater than the average market price of the common shares, and therefore, the effect would be anti-dilutive. A summary of those options follows:

| Three months ended September 30, | |
|---|---|
| 2013 | 2012 |

| | | |
|---|---|---|
| Number of anti-dilutive shares | --- | 90 |

3. Stock Based Compensation

The following table summarizes the components of our stock based compensation program expense (in thousands):

| | For three months ended September 30, 2013 | 2012 |
|---|---|---|
| Stock compensation expense for options, net of forfeitures | $ 74 | $ 106 |
| Stock compensation expense for restricted stock, net of forfeitures | 471 | 475 |
| Stock compensation income for stock appreciation rights, including forfeitures | --- | (44 ) |
| Total stock compensation expense (income) | $ 545 | $ 537 |

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As of September 30, 2013, we have approximately $0.2 million of unrecognized compensation cost related to unvested options granted under the Company's 2006 Omnibus Incentive Plan, as amended (the "2006 Plan"). This cost is expected to be recognized over a weighted-average period of 0.6 year and a total period of 1.5 years.

A summary of the award activity of the Company's stock option plans as of September 30, 2012, and changes during the three-month period then ended is presented below:

| Options | Option Totals | Weighted-Average Exercise Price per Share | |
|---|---|---|---|
| Outstanding at July 1, 2013 | 1,148,790 | $ | 10.76 |
| Granted | --- | | --- |
| Exercised | 100,037 | $ | 12.81 |
| Forfeited or expired | 1,750 | $ | 12.79 |
| Outstanding at September 30, 2013 | 1,047,003 | $ | 9.62 |
| Exercisable at September 30, 2013 | 989,003 | $ | 9.73 |

As of September 30, 2013, we also have approximately $4.0 million of unrecognized compensation expense related to restricted stock awards, which is anticipated to be recognized over a weighted-average period of 2.4 years and a total period of 3.3 years. A summary of the restricted stock award activity under the 2006 Plan as of September 30, 2013, and changes during the three-month period then ended is presented below:

| | Number of Restricted Stock Awards | Weighted-Average Grant Date Fair Value | |
|---|---|---|---|
| Unvested at July 1, 2013 | 355,963 | $ | 15.75 |
| Granted | --- | | --- |
| Vested and Issued | --- | | --- |
| Forfeited | 4,525 | $ | 12.40 |
| Outstanding at September 30, 2013 | 351,438 | $ | 15.79 |

The fair value of each restricted stock award is based on the closing market price on the date of grant.

The Company had no outstanding stock appreciation rights as of September 30, 2013 and 143,156 outstanding stock appreciation rights as of September 30, 2012. These stock appreciation rights were granted at a fair value market price of $8.64 based on the closing market price on the date of the grant. All stock rights vested and were paid out in the December 2012 quarter.

4. Segment Information (in thousands)

We have two reportable segments comprised of an asset-based segment and an asset-light-based segment. Our asset-based segment includes our asset-based dry van carrier and rail services, which are geographically diversified but have similar economic and other relevant characteristics, as they all provide truckload carrier services of general commodities to a similar class of customers. Our asset-light-based segment consists of our warehousing, brokerage, and less-than-truckload ("LTL") operations, which we have determined qualifies as a reportable segment under ASC 280-10, Segment Reporting.

| | Operating Revenues Three Months Ended September 30, | |
|---|---|---|
| | 2013 | 2012 |
| Asset-Based | $ 162,621 | $ 142,435 |
| Asset-light-Based | 12,481 | 10,862 |
| Total | $ 175,102 | $ 153,297 |

| | Operating Income Three Months Ended September 30, | |
|---|---|---|
| | 2013 | 2012 |
| Asset-Based | $ 10,376 | $ 14,309 |
| Asset-light-Based | 1,155 | 830 |
| Total | $ 11,532 | $ 15,139 |

Information as to the Company's operating revenue by geographic area is summarized below. The Company allocates operating revenue based on the country of origin of the tractor hauling the freight:

| | Operating Revenue Three Months Ended September 30, | |
|---|---|---|
| | 2013 | 2012 |
| United States | $ 146,205 | $ 134,131 |
| Canada | 21,087 | 10,903 |
| Mexico | 7,810 | 8,263 |
| Consolidated | $ 175,102 | $ 153,297 |

5. Income Taxes

Our effective income tax rate was 37.8% for the three-month period ended September 30, 2013, compared with 39.3% for the three-month period ended September 30, 2012. In determining our quarterly provision for income taxes, we use an estimated annual effective tax rate, which is based on our expected annual income, statutory tax rates, nontaxable and nondeductible items of income and expense, and the ultimate outcome of tax audits. Income tax expense varies from the amount computed by applying the statutory federal tax rate to income before income taxes primarily due to state income taxes, net of federal income tax effect, adjusted for permanent differences, the most significant of which is the effect of the per diem pay structure for drivers. Drivers may elect to receive non-taxable per diem pay in lieu of a portion of their taxable wages. This per diem program increases our drivers’ net pay per mile, after taxes, while decreasing gross pay, before taxes. As a result, salaries, wages and employee benefits are slightly lower, and our effective income tax rate is higher than the statutory rate. Generally, as pre-tax income increases, the impact of the driver per diem program on our effective tax rate decreases because aggregate per diem pay becomes smaller in relation to pre-tax income. Due to the partially nondeductible effect of per diem pay, our tax rate will fluctuate in future periods based on fluctuations in earnings and in the number of drivers who elect to receive this pay structure.

The Company follows ASC Topic 740-10-25 in accounting for uncertainty in income taxes ("Topic 740"). Topic 740 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We account for any uncertainty in income taxes by determining whether it is more likely than not that a tax position taken or expected to be taken in a tax return will be sustained upon examination by the appropriate taxing authority based on the technical merits of the position. In that regard, we have analyzed filing positions in our federal and applicable state tax returns as well as in all open tax years. The only periods subject to examination for our federal returns are the 2009 through 2011 tax years. We believe that our income tax filing positions and deductions will be sustained on audit and do not anticipate any adjustments that will result in a material change to our consolidated financial position, results of operations and cash flows. As of September 30, 2013, the Company recorded a $0.5 million liability for unrecognized tax benefits, a portion of which represents penalties and interest.

6. Commitments and Contingencies

The Company has outstanding commitments to purchase approximately $18.6 million of revenue equipment at September 30, 2013.

Standby letters of credit, not reflected in the accompanying consolidated financial statements, aggregated approximately $0.8 million at September 30, 2013.

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7. Lease Obligations and Long-Term Debt

The Company leases certain revenue and service equipment under long-term lease agreements, payable in monthly installments.

Equipment obtained under a capital lease is reflected on the Company's balance sheet as owned and the related leases mature at various dates through 2020.

Assets held under operating leases are not recorded on the Company's balance sheet. The Company leases revenue and service equipment under non-cancellable operating leases expiring at various dates through April 2019.

Long-Term Debt

The Company had outstanding borrowings, excluding capital leases, of $104.6 million at September 30, 2013 compared with $28.6 million at September 30, 2012 and $78.1 million at June 30, 2013.

Future minimum lease payments relating to capital leases and operating leases as of September 30, 2013 (in thousands):

| | Capital Leases | Operating Leases |
|---|---|---|
| 2014 | $ 34,130 | $ 4,941 |
| 2015 | 74,343 | 20,301 |
| 2016 | 12,877 | 2,555 |
| 2017 | 12,860 | 2,540 |
| 2018 | 27,691 | 2,540 |
| Thereafter | 59,919 | 14,360 |
| Total minimum lease payments | 221,820 | $ 47,237 |
| Less amounts representing interest | 12,003 | |
| Present value of minimum lease payments | 209,817 | |
| Less current maturities | 30,631 | |
| Non-current portion | $ 179,186 | |

8. Fair Value Measurements

ASC 820-10 Fair Value Measurements and Disclosure for non-recurring fair value measurements of non-financial assets and liabilities. This standard defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This standard establishes a three-level hierarchy for fair value measurements based upon the significant inputs used to determine fair value. Observable inputs are those which are obtained from marked participants external to the Company, while unobservable inputs are generally developed internally, utilizing management’s estimates assumptions, and specific knowledge of the nature of the assets or liabilities and related markets. The three levels are defined as follows:

Level 1 – Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date. An active market is defined as a market in which transactions for the assets or liabilities occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active (markets with few transactions), inputs other than quoted prices that are observable for the asset or liability (i.e., interest rates, yield curves, etc.), and inputs that are derived principally from or corroborated by observable market data correlation or other means (market corroborated inputs).

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Level 3 – Unobservable inputs, only used to the extent that observable inputs are not available, reflect the Company's assumptions about the pricing of an asset or liability.

In accordance with the fair value hierarchy described above, the following table shows the fair value of the Company's financial assets and liabilities (in thousands) that are required to be measured at fair value as of September 30, 2013, and June 30, 2013.

| | | | Level 1 | | Level 2 | | Level 3 | |
|---|---|---|---|---|---|---|---|---|
| | Balance at September 30, 2013 | Balance at June 30, 2013 | Balance at September 30, 2013 | Balance at June 30, 2013 | Balance at September 30, 2013 | Balance at June 30, 2013 | Balance at September 30, 2013 | Balance at June 30, 2013 |
| Foreign currency derivatives | $ 95 | $ (70 ) | $ --- | $ --- | $ 95 | $ (70 ) | $ --- | $ --- |
| Fuel derivatives | 47 | 45 | --- | --- | 47 | 45 | --- | --- |

Our other financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, long-term debt, and capital lease obligations. At September 30, 2013 the fair value of these instruments were approximated by their carrying values.

9. Dividend

On July 28, 2013, the Company declared a cash dividend of $0.02 per share of common stock. The dividend was payable to shareholders of record on October 4, 2013, and was paid on October 18, 2013. Future payment of cash dividends, and the amount of any such dividends, will depend on our financial condition, results of operations, cash requirements, tax treatment, and certain corporate law requirements, as well as other factors deemed relevant by our Board of Directors.

10. Fuel Derivatives

In the Company’s day to day business activities we are exposed to certain market risks, including the effects of changes in fuel prices. The Company continually reviews new ways to reduce the potentially adverse effects that the volatility of fuel markets may have on operating results. In an effort to reduce the variability of the ultimate cash flows associated with fluctuations in diesel fuel prices, the Company has begun to enter into futures contracts. These instruments will be heating oil futures contracts as the related index, New York Mercantile Exchange ("NYMEX"), generally exhibits high correlation with the changes in the dollars of the forecasted purchase of diesel fuel. The Company does not engage in speculative transactions, nor does it hold or issue financial instruments for trading purposes.

We have entered into futures contracts, which pertain to 378,000 total gallons, 126,000 gallons per month for October 2013 through December 2013, approximately 4.0% of our monthly projected fuel requirements. Under these contracts, we pay a fixed rate per gallon of heating oil and receive the monthly average price of New York heating oil per the NYMEX. The Company has done retrospective and prospective regression analyses that showed the changes in the prices of diesel fuel and heating oil were deemed to be highly effective based on the relevant authoritative guidance. Accordingly, we have designated the respective hedges as cash flow hedges.

We perform both a prospective and retrospective assessment of the effectiveness of our hedge contracts at inception and quarterly. If our analysis shows that the derivatives are not highly effective as hedges, we will discontinue hedge accounting for the period and prospectively recognize changes in the fair value of the derivative being recognized through earnings. As a result of our effectiveness assessment at inception and at September 30, 2013, we believe our hedge contracts have been and will continue to be highly effective in offsetting changes in cash flows attributable to the hedged risk.

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We recognize all derivative instruments at fair value on our condensed consolidated balance sheets in other assets or other accrued expenses. The Company's derivative instruments are designated as cash flow hedges, thus the effective portion of the gain or loss on the derivative is reported as a component of accumulated other comprehensive income and will be reclassified into earnings in the same period during which the hedged transactions affect earnings. The effective portion of the derivative represents the change in fair value of the hedge that offsets the change in fair value of the hedged item. To the extent the change in the fair value of the hedge does not perfectly offset the change in the fair value of the hedged item, the ineffective portion of the hedge is immediately recognized in other income or expense on our consolidated condensed statements of income. The ineffective portion of the hedge for the quarter was immaterial and therefore not recognized through earnings.

Based on the amounts in accumulated other comprehensive income as of September 30, 2013, and the expected timing of the purchases of the diesel hedged, we expect to reclassify $0.1 million of gain on derivative instruments from accumulated other comprehensive income to the statement of income, as an offset to fuel expense, due to the actual diesel fuel purchases. The amounts actually realized will depend on the fair values as of the date of settlement.

Outstanding financial derivative instruments expose us to credit loss in the event of nonperformance by the companies with which we have these agreements. Our credit exposure related to these financial instruments is represented by the fair value of contracts reported as assets. To evaluate credit risk, we review each counterparty's audited financial statements and credit ratings and obtain references. Any credit valuation adjustments deemed necessary would be reflected in the fair value of the instrument. As of September 30, 2013, we have not made any adjustments.

11. Acquisitions and Equipment Held for Resale

On August 26, 2013, we acquired certain assets and assumed certain liabilities of Houg, LLC (“Houg”) in Denver, CO. We acquired trade receivables of $2.3 million, property and equipment of $2.7 million, intangible assets of $1.0 million, other assets of $0.3 million offset by $4.4 million in debt and $1.9 million of various liabilities. The property and equipment includes tractors and trailers that we intend to operate in the short term. We used borrowings under our existing line of credit to fund the purchase price. The purposes of the acquisition were to offer employment opportunities to Houg drivers and continue dry-van and temperature controlled services for the Houg customers.

On August 26, 2013, we acquired certain assets and assumed certain liabilities of Land Span Motor Equipment, Inc. (“Land Span”) in Lakeland, FL for $5.4 million. We acquired property and equipment of $11.4 million, other assets of $0.1 million offset by $6.1 million in debt. The property and equipment includes tractors and trailers that we intend to operate in the short term. We used borrowings under our existing line of credit to fund the purchase price. The purposes of the acquisition were to offer employment opportunities to Land Span drivers and continue dry-van services for the Land Span customers.

On September 13, 2013, we acquired the stock of TCI Logistics, Inc. (“TCI”) in Kernersville, NC for $2.9 million. TCI had trade receivables of $1.8 million, property and equipment of $4.0 million, intangible assets of $1.6 million, cash and other assets of $0.6 million offset by debt of $4.0 million and $1.1 million of various liabilities. The property and equipment owned by TCI includes tractors and trailers that we intend to continue to utilize. We used borrowings under our existing line of credit to fund the purchase price. The purposes of the acquisition were to continue employment of TCI drivers and continue dry-van services for the TCI customers.

On September 16, 2013, we acquired certain assets and assumed certain liabilities of Hoss Cartage & Distribution Systems, Inc. (“Hoss”) in Ayr, Ontario, Canada for $1.0 million. We acquired property and equipment of $1.2 million, offset by $0.2 million in debt. The property and equipment includes tractors and trailers that we intend to operate in the short term. We used borrowings under our existing line of credit to fund the purchase price. The purposes of the acquisition were to offer employment opportunities to Hoss drivers and continue dry-van services for the Hoss customers.

12. Recent Accounting Pronouncements

In February 2013, the FASB issued ASU No. 2013-02, "Comprehensive Income (ASC Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income" ("ASU 2013-02"), which amends current comprehensive income guidance. The Company will be required to present significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required that provide additional detail about those amounts. The amendment is effective prospectively for public entities in fiscal years, and interim periods within those years, beginning after December 15, 2012. The amendments do not change the existing requirements for reporting net income or other comprehensive income in financial statements and the adoption of this guidance has not had a material impact on our consolidated financial statements.

13. Goodwill and Other Intangible Assets

The acquired intangible assets relate to customer relations acquired through acquisition in fiscal 2013. There have been no additions to intangible assets in fiscal 2014. The Company did not have any amortizable intangible assets prior to fiscal 2013.

| | September 30, 2013 | | |
|---|---|---|---|
| | Gross carrying amount | Amortization period | Accumulated amortization |
| Amortizing intangible assets: | | | |
| Customer list | $ 650 | 4 years | $ 116 |

The additions to goodwill relate to the Houg and TCI acquisitions of $1.1 million and $1.6 million respectively. The Houg related goodwill is tax deductible.

| | Goodwill | | |
|---|---|---|---|
| | June 30, 2013 | Current year additions | September 30, 2013 |
| Asset based | $ 16,362 | $ 2,685 | $ 19,047 |
| Asset light | $ 1,368 | --- | $ 1,368 |
| Total Goodwill | $ 17,730 | $ 2,685 | $ 20,415 |

14. Reclassifications and Adjustments

Certain items in the prior year's consolidated financial statements have been reclassified to conform to the current presentation.

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

Disclosure Regarding Forward Looking Statements

Except for certain historical information contained herein, this report contains certain statements that may be considered "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and Section 27A of the Securities Act of 1933, as amended, and such statements are subject to the safe harbor created by those sections and the Private Securities Litigation Reform Act of 1995, as amended. All statements, other than statements of historical fact, are statements that could be deemed forward-looking statements, including without limitation: any projections of revenues, earnings, cash flows, capital expenditures, or other financial items; any statement of plans, strategies, and objectives of management for future operations; any statements concerning proposed acquisition plans, new services, or developments; any statements regarding future economic conditions or performance; and any statements of belief and any statement of assumptions underlying any of the foregoing. Words such as "believe," "may," "could," "will," "expects," "hopes," "estimates," "projects," "intends," "anticipates," and "likely," and variations of these words, or similar expressions, terms, or phrases, are intended to identify such forward-looking statements. Forward-looking statements are inherently subject to risks, assumptions, and uncertainties, some of which cannot be predicted or quantified, which could cause future events and actual results to differ materially from those set forth in, contemplated by, or underlying the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the section entitled "Item 1A. Risk Factors," set forth in our Form 10-K for the year ended June 30, 2013, along with any supplements in Part II below.

All such forward-looking statements speak only as of the date of this Form 10-Q.  You are cautioned not to place undue reliance on such forward-looking statements.  The Company expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in the Company's expectations with regard thereto or any change in the events, conditions, or circumstances on which any such statement is based.

References to the "Company," "we," "us," "our," and words of similar import refer to Celadon Group, Inc. and its consolidated subsidiaries.

Business Overview

We are one of North America's twenty largest truckload carriers as measured by revenue. We generated $613.6 million in operating revenue during our fiscal year ended June 30, 2013. We provide asset-based dry van truckload carrier and rail services and asset-light based services including brokerage services, LTL, and warehousing services. Through our asset-based and asset-light-based services, we are able to transport or arrange for transportation throughout the United States, Canada, and Mexico.

We generated approximately 43% of our revenue in fiscal 2013 from international movements, and we believe our annual border crossings make us one of the largest providers of international truckload movements in North America. We believe that our strategically located terminals and experience with the language, culture, and border crossing requirements of each North American country provide a competitive advantage in the international trucking marketplace.

We believe our international operations, particularly those involving Mexico, offer an attractive business niche. The additional complexity of and need to establish cross-border business partners and to develop strong organization and adequate infrastructure in Mexico affords some barriers to competition that are not present in traditional U.S. truckload services.

Recent Results of Operations

Our results of operations for the quarter ended September 30, 2013, compared to the same period in 2012 are:

- Freight revenue increased 16.3% to $142.0 million from $122.1 million;
- Net income decreased 20.5% to $6.6 million from $8.3 million; and
- Net income per diluted share decreased 22.2% to $0.28 from $0.36.

In the quarter ended September 30, 2013, average revenue per loaded mile increased 2.2% from the September 2012 quarter. Average revenue per seated tractor per week increased 0.5%, which was primarily attributable to average miles per seated tractor increasing 0.2% from the quarter ended September 30, 2012.

Our average seated line haul tractors increased to 3,024 tractors in the quarter ended September 30, 2013, compared to 2,736 tractors for the same period a year ago. The net change of 288 units is comprised of a 277-unit increase in independent contractor tractors and an 11-unit increase in company tractors. The number of tractors operated by independent contractors increased 68.7% from a year ago, and now represents 22.5% of our total fleet.

Revenue and Expenses

We primarily generate revenue by transporting freight for our customers. Generally, we are paid a predetermined rate per mile or per load for our services. We enhance our revenue by charging for tractor and trailer detention, loading and unloading activities, brokerage operations, and other specialized services, as well as through the collection of fuel surcharges to mitigate the impact of the cost of fuel. The main factors that affect our revenue are the revenue per mile we receive from our customers, the percentage of miles for which we are compensated, and the number of miles we generate with our equipment. These factors relate to, among other things, the general level of economic activity in the United States, inventory levels, specific customer demand, the level of capacity in the trucking industry, and driver availability.

The main factors that impact our profitability in terms of expenses are the variable costs of transporting freight for our customers. These costs include fuel expense, driver-related expenses, such as wages, benefits, training and recruitment, and independent contractor and third party carrier costs, which are recorded on the "Purchased Transportation" line of our consolidated statements of income. Expenses that have both fixed and variable components include maintenance, insurance, and claims. These expenses generally vary with the miles we travel, but also have a controllable component based on safety, fleet age, efficiency, and other factors. Our main fixed costs are the acquisition and depreciation of long-term assets, such as revenue equipment and the compensation of non-driver personnel. We believe effectively controlling our expenses and managing our net cost of revenue equipment acquisitions and dispositions, including any related gains or losses, are important elements of assuring our profitability. We evaluate our profitability using operating ratio, excluding the impact of fuel surcharge revenue (operating expenses, net of fuel surcharge, expressed as a percentage of revenue, before fuel surcharge), and income before income taxes, which eliminates shifting operating lease expenses "above the line" from interest expense on owned or capital leased equipment.

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Results of Operations

The following table sets forth the percentage relationship of expense items to freight revenue for the periods indicated:

| | For the three months ended September 30, | | | |
|---|---|---|---|---|
| | 2013 | | 2012 | |
| Operating Revenue | 100.0 | % | 100.0 | % |
| | | | | |
| Operating expenses: | | | | |
| Salaries, wages, and employee benefits | 26.7 | % | 26.3 | % |
| Fuel | 21.0 | % | 24.4 | % |
| Purchased transportation | 23.8 | % | 18.5 | % |
| Revenue equipment rentals | 1.0 | % | 1.3 | % |
| Operations and maintenance | 6.4 | % | 5.3 | % |
| Insurance and claims | 2.4 | % | 2.3 | % |
| Depreciation and amortization | 8.5 | % | 8.3 | % |
| Communications and utilities | 0.8 | % | 0.8 | % |
| Operating taxes and licenses | 1.6 | % | 1.7 | % |
| General and other operating | 1.2 | % | 1.2 | % |
| Total operating expenses | 93.4 | % | 90.1 | % |
| | | | | |
| Operating income | 6.6 | % | 9.9 | % |
| | | | | |
| Other expense: | | | | |
| Interest expense | 0.7 | % | 1.0 | % |
| Other income, net | (0.1 | )% | 0.0 | % |
| | | | | |
| Income before income taxes | 6.0 | % | 8.9 | % |
| Provision for income taxes | 2.3 | % | 3.5 | % |
| | | | | |
| Net income | 3.7 | % | 5.4 | % |
| | | | | |
| Freight revenue(1) | 100.0 | % | 100.0 | % |
| | | | | |
| Operating expenses: | | | | |
| Salaries, wages, and employee benefits | 32.9 | % | 33.1 | % |
| Fuel(1) | 2.6 | % | 5.1 | % |
| Purchased transportation | 29.4 | % | | |