EPLUS INC
Form 10-Q
February 08, 2018

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

FORM 10-Q

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

For the quarterly period ended December 31, 2017

OR

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

For the transition period from____ to ____ .

Commission file number: 1-34167

ePlus inc.

(Exact name of registrant as specified in its charter)

Delaware	54-1817218
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

13595 Dulles Technology Drive, Herndon, VA 20171-3413
(Address, including zip code, of principal executive offices)

Registrant's telephone number, including area code: (703) 984-8400

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes No

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	(do not check if smaller reporting company)	Smaller reporting company
		Emerging growth company

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes No

The number of shares of common stock outstanding as of January 31, 2018 was 13,948,590.

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CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains certain statements that are, or may be deemed to be, “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, or “Exchange Act,” and are made in reliance upon the protections provided by such acts for forward-looking statements. Such statements are not based on historical fact, but are based upon numerous assumptions about future conditions that may not occur. Forward-looking statements are generally identifiable by use of forward-looking words such as “may,” “should,” “would,” “intend,” “estimate,” “will,” “potential,” “poss “could,” “believe,” “expect,” “intend,” “plan,” “anticipate,” “project,” and similar expressions. Readers are cautioned not to pla undue reliance on any forward-looking statements made by us or on our behalf. Forward-looking statements are made based upon information that is currently available or management’s current expectations and beliefs concerning future developments and their potential effects upon us, speak only as of the date hereof, and are subject to certain risks and uncertainties. We do not undertake any obligation to publicly update or correct any forward-looking statements to reflect events or circumstances that subsequently occur, or of which we hereafter become aware. Actual events, transactions and results may materially differ from the anticipated events, transactions or results described in such statements. Our ability to consummate such transactions and achieve such events or results is subject to certain risks and uncertainties. Such risks and uncertainties include, but are not limited to, the matters set forth below:

- national and international political instability fostering uncertainty and volatility in the global economy including exposure to fluctuation in foreign currency rates, and downward pressure on prices;
- significant adverse changes in, reductions in, or loss of our largest volume customer or one or more of our large volume customers, or vendors;
- exposure to changes in, interpretations of, or enforcement trends in legislation and regulatory matters;
- the creditworthiness of our customers and our ability to reserve adequately for credit losses;
- reduction of vendor incentives provided to us;
- we offer a comprehensive set of solutions — integrating information technology (IT) product sales, third-party software assurance and maintenance, our advanced professional and managed services, our proprietary software, and financing, and encounter the following challenges, risks, difficulties and uncertainties:
  - managing a diverse product set of solutions in highly competitive markets with a number of key vendors;
  - increasing the total number of customers utilizing integrated solutions by up-selling within our customer base and gaining new customers;
  - adapting to meet changes in markets and competitive developments;
  - maintaining and increasing advanced professional services by retaining highly skilled, competent, personnel and vendor certifications;
  - increasing the total number of customers who utilize our managed services and professional services and continuing to enhance our managed services offerings to remain competitive in the marketplace;
  - performing professional and managed services competently;
  - maintaining our proprietary software and updating our technology infrastructure to remain competitive in the marketplace; and
  - reliance on third parties to perform some of our service obligations to our customers;
- changes in the IT industry and/or rapid changes in product offerings, including the proliferation of the cloud, infrastructure as a service and software as a service;
- our dependency on continued innovations in hardware, software, and services offerings by our vendors and our ability to partner with them;
- future growth rates in our core businesses;
- failure to comply with public sector contracts or applicable laws;
- changes to or loss of members of our senior management team and/or failure to successfully implement succession plans;
- our dependence on key personnel to maintain certain customer relationships, and our ability to hire, train, and retain sufficient qualified personnel;

- our ability to implement comprehensive plans for the integration of sales forces, cost containment, asset rationalization, systems integration and other key strategies;
- a possible decrease in the capital spending budgets of our customers or a decrease in purchases from us;
- our contracts may not be adequate to protect us, and we are subject to audit in which we may not pass, and our professional and liability insurance policies coverage may be insufficient to cover a claim;
- disruptions or a security breach in our IT systems and data and audio communication networks;

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- our ability to secure our customers' electronic and other confidential information, and remain secure during a cyber-security attack;
- our ability to raise capital, maintain or increase as needed our lines of credit with vendors or floor planning facility, or obtain debt for our financing transactions or the effect of those changes on our common stock or its holders;
- our ability to realize our investment in leased equipment;
- our ability to successfully perform due diligence and integrate acquired businesses;
- the possibility of goodwill impairment charges in the future;
- our ability to protect our intellectual property rights and successfully defend any challenges to the validity of our patents or allegations that we are infringing upon any third party patents, and the costs associated with those actions, and, when appropriate, license required technology; and
- significant changes in accounting standards including changes to the financial reporting of leases which could impact the demand for our leasing services, or misclassification of products and services we sell resulting in the misapplication of revenue recognition policies or inaccurate costs and completion dates for our services which could affect our estimates.

We cannot be certain that our business strategy will be successful or that we will successfully address these and other challenges, risks and uncertainties. For a further list and description of various risks, relevant factors and uncertainties that could cause future results or events to differ materially from those expressed or implied in our forward-looking statements, see Item 1A, "Risk Factors" and Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections contained elsewhere in this report, as well as other reports that we file with the Securities and Exchange Commission ("SEC").

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ePlus inc. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

	As of December 31, 2017	As of March 31, 2017
	(in thousands, except per share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 76,105	$ 109,760
Accounts receivable—trade, net	285,820	266,029
Accounts receivable—other, net	30,690	24,987
Inventories	51,295	93,557
Financing receivables—net, current	74,598	51,656
Deferred costs	24,740	7,971
Other current assets	25,970	43,364
Total current assets	569,218	597,324
Financing receivables and operating leases—net	72,575	71,883
Deferred tax assets—net	1,268	-
Property, equipment and other assets	17,632	11,956
Goodwill	76,546	48,397
Other intangible assets—net	27,414	12,160
TOTAL ASSETS	$ 764,653	$ 741,720
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Current liabilities:		
Accounts payable	$ 125,850	$ 113,518
Accounts payable—floor plan	107,761	132,612
Salaries and commissions payable	20,568	18,878
Deferred revenue	50,739	65,312
Recourse notes payable—current	-	908
Non-recourse notes payable—current	27,649	26,085
Other current liabilities	26,116	19,179
Total current liabilities	358,683	376,492
Non-recourse notes payable—long term	3,840	10,431
Deferred tax liability—net	-	1,799
Other liabilities	18,518	7,080
TOTAL LIABILITIES	381,041	395,802

COMMITMENTS AND CONTINGENCIES (Note 8)

STOCKHOLDERS' EQUITY		
Preferred stock, $.01 per share par value; 2,000 shares authorized; none outstanding	-	-
Common stock, $.01 per share par value; 25,000 shares authorized;14,046 outstanding at December 31, 2017 and 14,161 outstanding at March 31, 2017	142	142
Additional paid-in capital	128,392	123,536
Treasury stock, at cost	(14,165)	-
Retained earnings	269,048	222,823
Accumulated other comprehensive income—foreign currency translation adjustment	195	(583)
Total Stockholders' Equity	383,612	345,918
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 764,653	$ 741,720

See Notes to Unaudited Condensed Consolidated Financial Statements.

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ePlus inc. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2017	2016	2017	2016
	(in thousands, except per share data)			
Net sales	$342,569	$326,657	$1,080,571	$996,622
Cost of sales	265,881	252,871	838,719	773,239
Gross profit	76,688	73,786	241,852	223,383
Selling, general, and administrative expenses	57,134	50,160	168,138	149,821
Depreciation and amortization	2,894	1,910	7,086	5,408
Interest and financing costs	270	409	903	1,158
Operating expenses	60,298	52,479	176,127	156,387
Operating income	16,390	21,307	65,725	66,996
Other income (expense)	(131)	-	(1)	380
Earnings before tax	16,259	21,307	65,724	67,376
Provision for income taxes	678	8,687	19,499	27,310
Net earnings	$15,581	$12,620	$46,225	$40,066
Net earnings per common share—basic	$1.12	$0.92	$3.34	$2.88
Net earnings per common share—diluted	$1.11	$0.91	$3.30	$2.86
Weighted average common shares outstanding—basic	13,851	13,791	13,845	13,891
Weighted average common shares outstanding—diluted	13,990	13,920	14,022	14,026

See Notes to Unaudited Condensed Consolidated Financial Statements.

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ePlus inc. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2017	2016	2017	2016
	(amounts in thousands)			
NET EARNINGS	$ 15,581	$ 12,620	$ 46,225	$ 40,066
OTHER COMPREHENSIVE INCOME, NET OF TAX:				
Foreign currency translation adjustments	75	(145)	778	(240)
Other comprehensive income (loss)	75	(145)	778	(240)
TOTAL COMPREHENSIVE INCOME	$ 15,656	$ 12,475	$ 47,003	$ 39,826

See Notes to Unaudited Condensed Consolidated Financial Statements.

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ePlus inc. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended December 31,	
	2017	2016
	(in thousands)	
Cash Flows From Operating Activities:		
Net earnings	$ 46,225	$ 40,066
Adjustments to reconcile net earnings to net cash (used in) provided by operating activities:		
Depreciation and amortization	11,324	8,758
Reserve for credit losses, inventory obsolescence and sales returns	286	926
Share-based compensation expense	4,856	4,520
Deferred taxes	(3,058)	-
Payments from lessees directly to lenders—operating leases	(1,325)	(1,831)
Gain on disposal of property, equipment and operating lease equipment	(7,555)	(3,742)
Gain on sale of financing receivables	(4,625)	(3,968)
Other	1	316
Changes in:		
Accounts receivable—trade	(8,295)	(57,732)
Accounts receivable—other	(1,976)	(4,232)
Inventories	43,332	(77,422)
Financing receivables—net	(13,045)	17,797
Deferred costs, other intangible assets and other assets	(26,188)	1,838
Accounts payable	18,406	53,208
Salaries and commissions payable, deferred revenue and other liabilities	(9,539)	51,200
Net cash provided by operating activities	$ 48,824	$ 29,702
Cash Flows From Investing Activities:		
Proceeds from sale of property, equipment and operating lease equipment	9,967	6,380
Purchases of property, equipment, software, and operating lease equipment	(6,298)	(7,300)
Purchases of assets to be leased or financed	(5,716)	(5,897)
Issuance of financing receivables	(138,160)	(114,671)
Repayments of financing receivables	59,029	44,091
Proceeds from sale of financing receivables	64,103	39,857
Cash used in acquisitions, net of cash acquired	(37,718)	(9,500)
Net cash used in investing activities	$ (54,793)	$ (47,040)

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UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - continued

	Nine Months Ended December 31, 2017	2016
	(in thousands)	
Cash Flows From Financing Activities:		
Borrowings of non-recourse and recourse notes payable	$ 39,365	$ 34,020
Repayments of non-recourse and recourse notes payable	(27,269)	(5,412)
Repurchase of common stock	(13,399)	(30,493)
Payment of contingent consideration	-	(718)
Repayments of financing of acquisitions	(1,604)	-
Net borrowings (repayments) on floor plan facility	(24,851)	(5,602)
Net cash used in financing activities	(27,758)	(8,205)
Effect of exchange rate changes on cash	72	454
Net Decrease in Cash and Cash Equivalents	(33,655)	(25,089)
Cash and Cash Equivalents, Beginning of Period	109,760	94,766
Cash and Cash Equivalents, End of Period	$ 76,105	$ 69,677
Supplemental Disclosures of Cash Flow Information:		
Cash paid for interest	$ 421	$ 38
Cash paid for income taxes	$ 29,987	$ 23,381
Schedule of Non-Cash Investing and Financing Activities:		
Proceeds from sale of property, equipment, and operating lease equipment	$ 3,463	$ 429
Purchases of property, equipment, software, and operating lease equipment	$ (751)	$ (2,442)
Purchase of assets to be leased or financed	$ (7,225)	$ (12,700)
Issuance of financing receivables	$ (74,907)	$ (110,120)
Repayment of financing receivables	$ 9,572	$ 16,454
Proceeds from sale of financing receivables	$ 83,954	$ 104,430
Financing of acquisitions	$ (12,050)	$ -
Borrowing of non-recourse and recourse notes payable	$ 8,904	$ 33,651
Repayments of non-recourse and recourse notes payable	$ (14,465)	$ (20,438)
Vesting of share-based compensation	$ 12,010	$ 7,982
Repurchase of common stock included in accounts payable	$ (766)	$ -

See Notes to Unaudited Condensed Consolidated Financial Statements.

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ePlus inc. AND SUBSIDIARIES

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Common Stock		Additional Paid-In	Treasury	Retained	Accumulated Other Comprehensive	
	Shares	Par Value	Capital	Stock	Earnings	Income	Total
Balance, April 1, 2017	14,161	$ 142	$ 123,536	$-	$222,823	$ (583)	$345,918
Issuance of restricted stock awards	68	-	-	-	-	-	-
Share-based compensation	-	-	4,856	-	-	-	4,856
Repurchase of common stock	(183)	-	-	(14,165)	-	-	(14,165)
Net earnings	-	-	-	-	46,225	-	46,225
Foreign currency translation adjustment	-	-	-	-	-	778	778
Balance, December 31, 2017	14,046	$ 142	$ 128,392	$(14,165)	$269,048	$ 195	$383,612

See Notes to Unaudited Condensed Consolidated Financial Statements.

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ePlus inc. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

DESCRIPTION OF BUSINESS — Our company was founded in 1990 and is a Delaware corporation. ePlus inc. is sometimes referred to in this Quarterly Report on Form 10-Q as "we," "our," "us," "ourselves," or "ePlus." ePlus inc. is a holding company that through its subsidiaries provides information technology solutions which enable organizations to optimize their IT environment and supply chain processes. We also provide consulting, professional and managed services and complete lifecycle management services including flexible financing solutions. We focus on middle market and large enterprises in North America and the United Kingdom.

BASIS OF PRESENTATION — The unaudited condensed consolidated financial statements include the accounts of ePlus inc. and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation. The accounts of businesses acquired are included in the unaudited condensed consolidated financial statements from the dates of acquisition.

INTERIM FINANCIAL STATEMENTS — The unaudited condensed consolidated financial statements for the three and nine months ended December 31, 2017 and 2016 were prepared by us, without audit, and include all normal and recurring adjustments that, in the opinion of management, are necessary for a fair presentation of our financial position, results of operations, changes in comprehensive income and cash flows for such periods. Operating results for the three and nine months ended December 31, 2017 and 2016 are not necessarily indicative of results that may be expected for any other interim period or for the full fiscal year ending March 31, 2018 or any other future period. These unaudited condensed consolidated financial statements do not include all disclosures required by the accounting principles generally accepted in the United States (“U.S. GAAP”) for annual financial statements. Our audited consolidated financial statements are contained in our annual report on Form 10-K for the year ended March 31, 2017 (“2017 Annual Report”), which should be read in conjunction with these interim condensed consolidated financial statements.

USE OF ESTIMATES — The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Estimates are used when accounting for items and matters including, but not limited to, revenue recognition, residual values, vendor consideration, lease classification, goodwill and intangible assets, reserves for credit losses, inventory obsolescence, and the recognition and measurement of income tax assets and other provisions and contingencies. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from these estimates.

The notes to the consolidated financial statements contained in the 2017 Annual Report include additional discussion of the significant accounting policies and estimates used in the preparation of our consolidated financial statements. There have been no material changes to our significant accounting policies and estimates during the nine months ended December 31, 2017.

STOCK SPLIT — On March 31, 2017, we completed a two-for-one stock split in the form of a stock dividend. References made to outstanding shares or per share amounts in the accompanying financial statements and disclosures have been retroactively adjusted for this stock split. The number of authorized shares reflected on the consolidated balance sheets was not affected by the stock split.

CONCENTRATIONS OF RISK — A substantial portion of our sales of product and services are from sales of Cisco Systems, Hewlett Packard Enterprise (“HPE”) and HP, Inc. (collectively “Hewlett Packard companies”), and NetApp products, which represented approximately 39%, 5% and 7%, and 45%, 7%, and 5%, respectively, for the three and nine months ended December 31, 2017. Sales of Cisco Systems, Hewlett Packard companies, and NetApp represented approximately 45%, 6% and 6%, and 49%, 6% and 5%, respectively, for the three and nine months ended December 31, 2016. Any changes in our vendors’ ability to provide products or incentive programs could have a material adverse effect on our business, results of operations and financial condition.

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2. RECENT ACCOUNTING PRONOUNCEMENTS

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED — In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which, along with amendments issued in 2015 and 2016, will replace most existing revenue recognition guidance under GAAP and eliminate industry specific guidance. The core principle of the new guidance is that an entity should recognize revenue for the transfer of goods and services equal to an amount it expects to be entitled to receive for those goods and services. In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, to defer the effective date of ASU 2014-09 by one year. Including the one-year deferral, these updates become effective for us in our quarter ending June 30, 2018. The new guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (modified retrospective method).

We have established a cross-functional implementation team and utilized a bottom-up approach to analyze the impact of the standard on our arrangements by reviewing the current accounting policies and practices to identify potential differences that would result from applying the requirements of the new standard to our revenue contracts. Based on our analysis to date, we have reached the following tentative conclusions regarding the new standard and how we expect it to affect our consolidated financial statements and related disclosures:

- We will adopt the guidance in our quarter ending June 30, 2018. We currently prefer to adopt the standard using the full retrospective method; however, our ability to do so is dependent on many factors, including the completion of our analysis of information necessary to recast prior period financial statements. Based on these and other factors, we may decide to use the modified retrospective method.
- Substantially all of our revenue within our technology segment is contractual and is within the scope of ASU No. 2014-09, as amended. The majority of our revenues within our financing segment are scoped out of this update.
- The majority of our revenues within our technology segment are derived from sales of third-party products, third-party software, third-party services, such as maintenance and software assurance, and sales of ePlus professional and managed services.
  - We recognize revenue on sales of third party product and third-party software on a gross basis upon delivery and we are still assessing whether we are acting as a principal or an agent in these transactions under the update.
  - We recognize sales of third party maintenance and software assurance on a net basis at the date of sale and sales of ePlus professional and managed services on a gross basis as the services are performed. We do not anticipate a material impact to our revenue recognition for these transactions under the update.
- We expect that our disclosures in our notes to our consolidated financial statements related to revenue recognition will be significantly expanded under the new standard.

Our analysis and evaluation of the new standard will continue through its effective date in our quarter ending June 30, 2018. A substantial amount of work remains to be completed due to the complexity of the new standard, the application of judgment and the requirement for the use of estimates in applying the new standard, as well as the volume of our customer portfolio and the related terms and conditions of our contracts that must be reviewed.

In November 2016, the FASB issued ASU 2016-02, Leases, which will supersede the current U.S. GAAP on this topic. The core principle of this update is that a lessee should recognize the assets and liabilities that arise from leases. This update requires adoption under the modified retrospective approach and becomes effective for us in our quarter ending June 30, 2019. Early adoption is permitted. We are currently evaluating the impact of this update on our financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments- Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The amendments in this update replace the incurred loss impairment methodology in current US GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. This update requires adoption under a modified retrospective approach and becomes effective for us in our quarter ending June 30, 2020. Early adoption is permitted beginning in our quarter ending June 30, 2019. We are currently evaluating the impact of this update on our financial statements.

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3. FINANCING RECEIVABLES AND OPERATING LEASES

Our financing receivables and operating leases consist of assets that we finance for our customers, which we manage as a portfolio of investments. Equipment financed for our customers is accounted for as investments in direct financing, sales-type or operating leases in accordance with Accounting Standards Codification ("ASC") Topic 840, Leases. We also finance third-party software, maintenance, and services for our customers, which are classified as notes receivables. Our notes receivables are interest bearing and are often due over a period of time that corresponds with the terms of the leased products.

FINANCING RECEIVABLES—NET

Our financing receivables, net consist of the following (in thousands):

December 31, 2017	Notes Receivables	Lease-Related Receivables	Total Financing Receivables
Minimum payments	$ 59,444	$ 73,022	$ 132,466
Estimated unguaranteed residual value (1)	-	13,358	13,358
Initial direct costs, net of amortization (2)	369	321	690
Unearned income	-	(6,034)	