

INTRICON CORP
Form 10-Q
May 09, 2008

Table of Contents

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 March 31, 2008

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 1-5005

INTRICON CORPORATION

Edgar Filing: INTRICON CORP - Form 10-Q

(Exact Name of Registrant as specified in its charter)

Pennsylvania

(State or other jurisdiction of incorporation or organization)

23-1069060

(IRS Employer Identification No.)

**1260 Red Fox Road,
Arden Hills, Minnesota**

(Address of principal executive offices)

55112

(Zip Code)

Registrant's telephone number, including area code **(651) 636-9770**

Former name, former address and former fiscal year, if changed since last report: N/A

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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 by Rule 12b-2 of the Exchange Act)

Yes No

The number of outstanding shares of the registrant's common shares, \$1.00 Par Value, on April 18, 2008 was 5,309,908 (net of 515,754 treasury shares).

INTRICON CORPORATION

INDEX

	Page Numbers
PART I: FINANCIAL INFORMATION	
Item 1.	Financial Statements
	<u>Consolidated Condensed Balance Sheets as of March 31, 2008 (Unaudited) and December 31, 2007</u> 3-4
	<u>Consolidated Condensed Statements of Operations (Unaudited) for the Three Months Ended March 31, 2008 and 2007</u> 5
	<u>Consolidated Condensed Statements of Cash Flows (Unaudited) for the Three Months Ended March 31, 2008 and 2007</u> 6
	<u>Notes to Consolidated Condensed Financial Statements (Unaudited)</u> 7-15
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 16-23
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u> 24
Item 4.	<u>Controls and Procedures</u> 24
PART II: OTHER INFORMATION	
Item 1.	<u>Legal Proceedings</u> 25
Item 1A.	<u>Risk Factors</u> 25
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u> 25
Item 3.	<u>Defaults Upon Senior Securities</u> 25
Item 4.	<u>Submission of Matters to a Vote of Security Holders</u> 25
Item 5.	<u>Other Information</u> 25
Item 6.	<u>Exhibits</u> 26

Table of Contents**PART I: FINANCIAL INFORMATION****ITEM 1. Financial Statements****INTRICON CORPORATION****Consolidated Condensed Balance Sheets****Assets**

	March 31, 2008 (Unaudited)	December 31, 2007
Current assets:		
Cash	\$ 1,511,202	\$ 1,651,145
Restricted cash	75,463	72,231
Accounts receivable, less allowance for doubtful accounts of \$255,000 at March 31, 2008 and \$259,000 at December 31, 2007	9,634,764	8,408,149
Inventories	9,661,228	9,835,060
Refundable income tax	37,945	28,297
Note receivable from sale of discontinued operations, less allowance of \$225,000 at March 31, 2008 and December 31, 2007		75,000
Other current assets	728,874	775,206
Total current assets	21,649,476	20,845,088
Machinery and equipment	37,410,216	36,959,184
Less: Accumulated depreciation	29,077,884	28,500,318
Net machinery and equipment	8,332,332	8,458,866
Goodwill	8,266,438	8,238,020
Investment in partnerships	1,612,582	1,590,426
Other assets, net	1,499,601	1,543,127
Total Assets	\$ 41,360,429	\$ 40,675,527

(See accompanying notes to the consolidated condensed financial statements)

Table of Contents**INTRICON CORPORATION****Consolidated Condensed Balance Sheets****Liabilities and Shareholders' Equity**

	March 31, 2008 (Unaudited)	December 31, 2007
Current liabilities:		
Checks written in excess of cash	\$ 813,366	\$ 1,209,642
Current maturities of long-term debt	1,362,591	1,476,665
Accounts payable	3,933,011	3,965,914
Customers' advance payments on contracts		190,062
Income taxes payable	73,021	74,549
Deferred gain on building sale	110,084	110,084
Partnership payable	260,000	260,000
Other accrued liabilities	3,343,710	4,192,693
Total current liabilities	9,895,783	11,479,609
Long term debt, less current maturities	8,918,464	6,963,410
Other postretirement benefit obligations	776,181	816,532
Long term partnership payable	1,020,000	1,020,000
Note payable, net of current portion	259,360	259,360
Deferred income taxes	92,273	89,273
Accrued pension liabilities	650,031	624,517
Deferred gain on building sale	798,110	825,631
Total liabilities	22,410,202	22,078,332
Commitments and contingencies (Note 12)		
Shareholders' equity:		

Edgar Filing: INTRICON CORP - Form 10-Q

Common shares, \$1.00 par value per share; 10,000,000 shares authorized; 5,825,308 and 5,813,491 shares issued; 5,309,554 and 5,297,737 outstanding	5,825,308	5,813,491
Additional paid-in capital	13,609,571	13,391,449
Retained earnings	1,027,549	877,733
Accumulated other comprehensive loss	(247,123)	(220,400)
Less: 515,754 common shares held in treasury, at cost	(1,265,078)	(1,265,078)
Total shareholders' equity	18,950,227	18,597,195
	\$ 41,360,429	\$ 40,675,527

(See accompanying notes to the consolidated condensed financial statements)

4

Table of Contents

INTRICON CORPORATION

Consolidated Condensed Statements of Operations

(Unaudited)

	Three Months Ended	
	March 31,	March 31,
	2008	2007
	(Unaudited)	(Unaudited)
Sales, net	\$ 16,591,380	\$ 14,579,267
Cost of sales	12,746,689	11,368,010
Gross margin	3,844,691	3,211,257
Operating expenses:		
Selling expense	996,226	842,766
General and administrative expense	1,652,379	1,420,264
Research and development expense	787,773	732,681
Total operating expenses	3,436,378	2,995,711
Operating income	408,313	215,546
Interest expense	(195,625)	(153,277)
Interest income	7,260	38,736

Edgar Filing: INTRICON CORP - Form 10-Q

Equity in earnings of partnerships	22,156	(20,000)
Other expense, net	(5,458)	(25,737)
Income before income taxes	236,646	55,268
Income tax expense	86,830	27,760
Net income	\$ 149,816	\$ 27,508

Earnings per share:

Basic and diluted	\$.03	\$.01
-------------------	--------	--------

Average shares outstanding:

Basic	5,303,083	5,196,903
Diluted	5,589,894	5,358,986

(See accompanying notes to the consolidated condensed financial statements)

5

Table of Contents

INTRICON CORPORATION

Consolidated Condensed Statements of Cash Flows

(Unaudited)

	Three months Ended	
	March 31,	March 31,
	2008	2007
	(Unaudited)	(Unaudited)
Cash flows from operating activities:		
Net income	\$ 149,816	\$ 27,508
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	582,520	456,907
Stock-based compensation	128,351	73,073
Gain on disposition of property	(1,900)	(2,653)
Change in deferred gain	(27,521)	(27,521)
Change in allowance for doubtful accounts	(4,353)	(29,144)
Equity in earnings of partnerships	(22,156)	20,000
Provision for deferred income taxes	3,000	
Changes in operating assets and liabilities:		
Accounts receivable	(1,194,441)	728,627
Inventories	174,131	(645,459)
Other assets	83,045	(431)
Accounts payable	(46,387)	(1,502,793)

Edgar Filing: INTRICON CORP - Form 10-Q

Accrued expenses	(969,581)	(224,323)
Customer advances	(190,062)	
Other liabilities	1,211	10,566
Net cash used by operating activities	(1,334,327)	(1,115,643)
Cash flows from investing activities:		
Purchases of property, plant and equipment	(457,546)	(697,764)
Proceeds from sales of property, plant and equipment	1,900	
Proceeds from note receivable	75,000	75,000
Net cash used by investing activities	(380,646)	(622,764)
Cash flows from financing activities:		
Proceeds from short-term bank borrowings		193,844
Proceeds from long-term borrowings	1,953,480	1,009,699
Repayments of long-term borrowings	(112,500)	(21,755)
Proceeds from employee stock purchases and exercise of stock options	98,531	8,500
Change in restricted cash	(3,232)	
Change in checks written in excess of cash	(396,276)	687,807
Net cash provided by financing activities	1,540,003	1,878,095
Effect of exchange rate changes on cash	35,027	4,647
Net increase (decrease) in cash	(139,943)	144,335
Cash, beginning of period	1,651,145	599,459
Cash, end of period	\$ 1,511,202	\$ 743,794

(See accompanying notes to the consolidated condensed financial statements)

6

Table of Contents

INTRICON CORPORATION

Notes to Consolidated Condensed Financial Statements (Unaudited)

1. General

In the opinion of management, the accompanying consolidated condensed financial statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly IntriCon Corporation's consolidated financial position as of March 31, 2008 and December 31, 2007, and the consolidated results of its operations for the three months ended March 31, 2008 and 2007. Results of operations for the interim periods are not necessarily indicators of the results of the operations expected for the full year.

2. New Accounting Pronouncements

Edgar Filing: INTRICON CORP - Form 10-Q

FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159) in February 2007. This statement expands the use of fair value measurement by permitting entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 is effective beginning with the first fiscal year that begins after November 15, 2007. The adoption of SFAS 159 did not have a material impact on the Company's consolidated financial statements.

On December 4, 2007, the FASB issued FASB Statement No. 141 (Revised 2007), *Business Combinations*. FAS 141(R) will significantly change the accounting for business combinations. Under Statement 141(R), an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. FAS 141R will change the accounting treatment for certain specific items, including:

Acquisition costs will be generally expensed as incurred;

Noncontrolling interests (formerly known as minority interests) will be valued at fair value at the acquisition date);

Acquired contingent liabilities will be recorded at fair value at the acquisition date and subsequently measured at either the higher of such amount or the amount determined under existing guidance for non-acquired contingencies;

In-process research and development will be recorded at fair value as an indefinite-lived intangible asset at the acquisition date;

Restructuring costs associated with a business combination will be generally expensed subsequent to the acquisition date; and

Changes in deferred tax asset valuation allowances and income tax uncertainties after the acquisition date generally will affect income tax expense.

FAS 141(R) also includes a substantial number of new disclosure requirements. The statement applies to the Company prospectively for business combinations for which the acquisition date is on or after January 1, 2009. Earlier adoption is prohibited.

On December 4, 2007, the FASB issued FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements - An Amendment of ARB No. 51*. Statement 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of a noncontrolling interest (minority interest) as equity in the consolidated financial statements and separate from the parent's equity. The amount of net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement. Statement 160 clarifies that changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidation date. Statement 160 also includes expanded disclosure requirements regarding the interests of the parent and its noncontrolling interest.

Statement 160 is effective for the Company for fiscal years, and interim periods within those fiscal years, beginning with the year ended December 31, 2009. Earlier adoption is prohibited.

Edgar Filing: INTRICON CORP - Form 10-Q

In March 2008, the Financial Accounting Standards Board (FASB) issued Statement No. 161. Disclosures about Derivative Instruments and Hedging Activities. SFAS 161 requires additional disclosures related to the use of derivative instruments, the accounting for derivatives and how derivatives impact financial statements. SFAS No. 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company does not expect the adoption of SFAS 161 to have a material effect on the consolidated financial statements.

3. Acquisitions

On May 22, 2007, the Company completed the acquisition of substantially all of the assets, other than real estate, of Tibbetts Industries, Inc. (Tibbetts), a privately held designer and manufacturer of components used in hearing aids and medical devices, based in Camden, Maine. The acquisition expanded the Company's component technology and customer base.

Pursuant to an asset purchase agreement, dated as of April 19, 2007, by and among the Company and Tibbetts and certain of the principal shareholders of Tibbetts, the Company purchased substantially all of the assets of Tibbetts, other than real estate, for cash of \$4,500,000, subject to a closing adjustment, and the assumption of certain liabilities (total purchase price of \$5,569,000 including acquisition costs of \$228,000). Certain escrow amounts will be distributed to the seller at the conclusion of the respective escrow periods. The acquisition was financed with borrowings under the Company's new credit facility, as further described in Note 7.

In addition, the Company entered into a five year lease and a ten year lease, respectively, for Tibbetts' two facilities in Camden, Maine, in each case with an option to renew for two additional periods of five years each.

The Company has accounted for the Tibbetts acquisition, utilizing the generally accepted accounting principles of SFAS Nos. 141, Business Combinations, and 142, Goodwill and Other Intangible Assets. Under the purchase method of accounting, the assets and liabilities of Tibbetts were recorded as of the acquisition date at their respective fair values and consolidated with those of the Company. Likewise, the results of operations of the Tibbetts' operations since May 22, 2007 have been included in the accompanying consolidated statements of operations. The preliminary allocation of the net purchase price of the acquisition resulted in goodwill of approximately \$2,317,000. The goodwill represents operating and market synergies that the Company expects to be realized as a result of the acquisition and future opportunities and is also deductible for tax purposes based on a 15 year amortization schedule. The purchase price allocation is based on estimates of fair values of assets acquired and liabilities assumed. The valuation required the use of significant assumptions and estimates. These estimates were based on assumptions the Company believed to be reasonable. However, actual results may differ from these estimates.

The purchase price was as follows (amounts in thousands):

Cash	\$4,500
Liabilities assumed	841
Acquisition costs	228
Total purchase price	\$5,569

The following table summarizes the purchase price allocation for the Tibbetts acquisition (amounts in thousands):

Cash	\$ 130
Other current assets	1,964
Intangible assets subject to amortization (through 2022)	108

Edgar Filing: INTRICON CORP - Form 10-Q

Goodwill	2,317
Other long-term assets	1,050
Current liabilities	(841)
Total purchase price allocation, net of liabilities assumed	\$4,728

8

Table of Contents

The following unaudited pro forma information presents a summary of consolidated results of operations of the Company as if the acquisition of Tibbetts had occurred at January 1, 2007. All amounts presented are in thousands. The historical consolidated financial information has been adjusted to give effect to pro forma events that are directly attributable to the acquisition and are factually supportable, including the increase in interest expense related to the borrowings used to fund the acquisition and the increase in depreciation expense of Tibbetts related to the step-up of fixed assets to fair value. The unaudited pro forma condensed consolidated financial information is presented for informational purposes only. The pro forma information is not necessarily indicative of what the financial position or results of operations actually would have been had the acquisition been completed on the dates indicated. In addition, the unaudited pro forma condensed consolidated financial information does not purport to project the future financial position or operating results of the Company after completion of the acquisition.

(amounts in thousands)	Three months ended March 31, 2007
Net sales	\$ 16,115
Cost of sales	12,700
S, G & A	3,510
Interest expense	267
Other expense	11
Loss from continuing operations before income taxes	\$ (373)
Earnings per share:	
Basic and diluted	\$ (0.08)
Weighted average number of shares outstanding:	
Basic	5,197
Diluted	5,197

The pro forma income from continuing operations for the period presented includes the increase in interest expense related to the borrowings used to fund the acquisition and the increase in depreciation expense of Tibbetts related to the step-up of fixed assets to fair value.

4. Product Warranty

In general, the Company warrants its products to be free from defects in material and workmanship and will fully conform to and perform to specifications for a period of one year. The following table presents changes in the Company's warranty liability for the three months ended March 31, 2008:

**For the three
months ended**

Edgar Filing: INTRICON CORP - Form 10-Q

	March 31, 2008
Beginning balance (December 31, 2007)	\$ 136,000
Warranty expense	8,900
Closed warranty claims	(33,500)
Ending balance (March 31, 2008)	\$ 111,400

5. Geographic Information

The geographical distribution of long-lived assets to geographical areas consisted of the following at:

Long-lived Assets

	March 31, 2008	December 31, 2007
United States	\$ 18,614,695	\$ 18,737,623
Other	1,096,258	1,092,816
Consolidated	\$ 19,710,953	\$ 19,830,439

9

Table of Contents

Long-lived assets consist primarily of property and equipment, investments in partnerships, patents, license agreements and goodwill. The Company capitalizes long-lived assets pertaining to the production of specialized parts. These assets are periodically reviewed to assure the net realizable value from the estimated future production based on forecasted sales exceeds the carrying value of the assets.

The geographical distribution of net sales to geographical areas for the three months ended March 31, 2008 and 2007 were as follows:

Net Sales to Geographical Areas:	Three months ended	
	March 31, 2008	March 31, 2007
United States	\$ 11,866,581	\$ 10,382,938
Germany	988,950	680,801
China	811,882	762,079
France	386,812	60,727
Switzerland	384,685	581,505
Japan	187,185	449,483

Edgar Filing: INTRICON CORP - Form 10-Q

United Kingdom	182,006	198,047
Turkey	170,835	49,165
Singapore	162,399	331,141
Russia	152,310	100,944
All other countries	1,297,735	982,437
Consolidated	\$ 16,591,380	\$ 14,579,267

Geographic net sales are allocated based on the location of the customer. All other countries include net sales primarily to various countries in Europe and in the Asian Pacific.

For the three months ended March 31, 2008, one customer accounted for 11 percent of the Company's consolidated net sales. For the three months ended March 31, 2007, one customer accounted for 13 percent of consolidated net sales.

At March 31, 2008, one customer accounted for 16 percent of the Company's consolidated accounts receivable. At December 31, 2007, one customer accounted for 14 percent of the Company's consolidated accounts receivable.

6. Inventories

Inventories consisted of the following at:

	March 31, 2008	December 31, 2007
Raw materials	\$ 4,767,833	\$ 4,936,949
Work-in-process	3,005,871	2,822,784
Finished products and components	1,887,524	2,075,327
Total Inventories	\$ 9,661,228	\$ 9,835,060

10

Table of Contents

7. Short and Long Term Debt

Short and long term debt is summarized as follows:

	March 31, 2008	December 31, 2007
Domestic Asset-Based Revolving Credit Facility	\$ 5,100,000	\$ 3,000,000

Edgar Filing: INTRICON CORP - Form 10-Q

Foreign Overdraft and Letter of Credit Facility	937,234	1,071,009
Domestic Term Loan	4,162,500	4,275,000
Domestic Capital Equipment Leases	81,321	94,066
Total Debt	10,281,055	8,440,075
Less: Current maturities	(1,362,591)	(1,476,665)
Total Long Term Debt	\$ 8,918,464	\$ 6,963,410

The Company and its subsidiaries, Resistance Technology, Inc., RTI Electronics, Inc. and IntriCon Tibbetts Corporation, referred to as the borrowers, entered into a credit facility with LaSalle Bank, National Association, referred to as the lender, on May 22, 2007 replacing the prior credit facilities with M & I Business Credit (formerly known as Diversified Business Credit, Inc.). The credit facility provides for:

a \$10,000,000 revolving credit facility, with a \$200,000 subfacility for letters of credit. Under the revolving credit facility, the availability of funds depends on a borrowing base composed of stated percentages of our eligible trade receivables and eligible inventory, less a reserve.

a \$4,500,000 term loan, which was used to fund the Tibbetts acquisition.

Loans under the new credit facility are secured by a security interest in substantially all of the assets of the borrowers including a pledge of the stock of the subsidiaries. All of the borrowers are jointly and severally liable for all borrowings under the new credit facility.

As of March 31, 2008, the Company was in compliance with all financial covenants under the credit facility, as amended.

8. Income Taxes

Income tax expense for the three months ended March 31, 2008 and 2007 was \$86,830 and \$27,760, respectively. The expense for the three months ended March 31, 2008 and 2007 was primarily due to foreign taxes on German and Singapore operations. The Company is in a net operating loss position for U.S. federal income tax purposes and, consequently, minimal federal expense from the current period domestic operations was recognized as the deferred tax asset has a full valuation allowance.

The following was the income (loss) before income taxes for each jurisdiction that the Company has operations for the three months ended March 31, 2008 and 2007:

	Three months ended	
	March 31, 2008	March 31, 2007
United States	\$(14,678)	\$(13,737)
Singapore	145,845	33,825
Germany	105,479	35,180
Income before income taxes	\$236,646	\$55,268

9. Stockholders Equity and Stock-based Compensation

The Company applies the provisions of SFAS 123R, which establishes the accounting for stock-based awards.

Edgar Filing: INTRICON CORP - Form 10-Q

The Company has a 1994 stock option plan, a 2001 stock option plan, a non-employee directors' stock option plan and a 2006 equity incentive plan. New grants may not be made under the 1994, the 2001 and the non-employee directors' stock option plans, however certain option grants under these plans remain exercisable as of March 31, 2008. The aggregate number of shares of common stock for which awards could be granted under the 2006 Equity Incentive Plan as of the date of adoption was 698,500 shares. Additionally, as outstanding options under the 2001 stock option plan and non-employee directors' stock option plan expire, the shares of the Company's common stock subject to the expired options will become available for issuance under the 2006 Equity Incentive Plan.

11

Table of Contents

Under the various plans, executives, employees and outside directors receive awards of options to purchase common stock. Additionally, the board has established the non-employee directors stock fee election program, referred to as the program, as an award under the 2006 equity incentive plan. The program gives each non-employee director the right under the 2006 equity incentive plan to elect to have some or all of his quarterly director fees paid in common shares rather than cash. There were 237 shares issued in lieu of cash for director fees under the program for the three months ended March 31, 2008. Under the 2006 equity incentive plan, the Company may also grant stock awards, stock appreciation rights, restricted stock units and other equity-based awards, although no such awards, other than awards under the program, had been granted as of March 31, 2008.

Under all awards, the terms are fixed on the grant date. Generally, the exercise price equals the market price of the Company's stock on the date of the grant. Options under the plans generally vest over three years, and have a maximum term of 10 years.

Stock option activity as of and during the three months ended March 31, 2008 was as follows:

	Number of Shares	Weighted- average Exercise Price	Aggregate Intrinsic Value
Outstanding at December 31, 2007	854,231	\$ 5.83	\$ 5,680,636
Options forfeited	(16,631)	10.50	
Options granted	44,950	11.09	
Options exercised	(1,900)	2.51	
Outstanding at March 31, 2008	880,650	\$ 6.02	\$ 1,814,139
Exercisable at March 31, 2008	505,867	\$ 3.48	\$ 2,870,587
Available for future grant at December 31, 2007	424,746		
Available for future grant at March 31, 2008	379,559		

The number of shares available for future grant at March 31, 2008, does not include a total of up to 415,700 shares subject to options outstanding under the 2001 stock option plan and non-employee directors' stock option plan as of March 31, 2008, which will become available for grant under the 2006 Equity Incentive Plan in the event of the expiration of said options.

The fair value of each stock option granted is estimated on the date of grant using the Black-Scholes option-pricing model. The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option-pricing models require the input of subjective assumptions, including the expected stock price volatility. Because the Company's options have characteristics different from those of traded options, in the opinion of management, the existing models do not necessarily provide a reliable single measure of the fair value of its options.

The Company calculates expected volatility for stock options and awards using both historical volatility as well as the average volatility of our peer competitors. Historical volatility is not strictly used due to the material changes in the Company's operations as a result of the sales of business segments that occurred in 2004 and 2005 (see Note 2 to the Company's consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007).

The Company currently estimates a nine percent forfeiture rate for stock options, but will continue to review this estimate in future periods.

The risk-free rates for the expected terms of the stock options and awards and the employee stock purchase plan is based on the U.S. Treasury yield curve in effect at the time of grant.

The weighted average remaining contractual life of options exercisable at March 31, 2008, was 6.6 years.

As of March 31, 2008, there was \$1,053,766 of total unrecognized compensation costs related to non-vested awards that are expected to be recognized over a weighted-average period of 2.4 years.

At the 2007 annual meeting of shareholders, the shareholders approved the IntriCon Corporation 2007 Employee Stock Purchase Plan (the Purchase Plan). A maximum of 100,000 shares may be sold under the Purchase Plan. There were 9,680 shares purchased under the plan as of March 31, 2008.

12

Table of Contents

10. Income (Loss) Per Share

The following table presents a reconciliation of the denominators used in the computation of basic and diluted earnings per share related to the Company's employee stock option and equity plans:

Edgar Filing: INTRICON CORP - Form 10-Q

	Three months ended	
	March 31, 2008	March 31, 2007
Basic weighted shares outstanding	5,303,083	5,196,903
Weighted shares assumed upon exercise of stock options	286,811	162,083
Diluted weighted shares outstanding	5,589,894	5,358,986

The dilutive impact summarized above relates to the periods when the average market price of Company stock exceeded the exercise price of the potentially dilutive option securities granted. Earnings per common share was based on the weighted average number of common shares outstanding during the periods when computing the basic earnings per share. When dilutive, stock options are included as equivalents using the treasury stock market method when computing the diluted earnings per share. There were dilutive common stock equivalents of 286,811 shares for the three months ended March 31, 2008 compared to 162,083 shares of dilutive common stock equivalents for the three months ended March 31, 2007, respectively.

Excluded from the computation of diluted earnings per share for the three months ended March 31, 2008 and 2007, were options to purchase approximately 218,500 common shares with an average exercise price of \$13.27 and options to purchase approximately 196,000 common shares with an average exercise price of \$8.66, respectively, because the effect would have been anti-dilutive.

11. Derivative Financial Instruments

Derivative financial instruments are used by the Company in the management of its interest rate exposure. The Company does not hold or issue derivative financial instruments for trading purposes. When entered into, the Company formally designates the derivative financial instrument as a hedge of a specific underlying exposure if such criteria are met, and documents both the risk management objectives and strategies for undertaking the hedge. The Company formally assesses, both at inception and at least quarterly thereafter, whether the derivative financial instruments that are used in hedging transactions are effective at offsetting changes in either the fair value or cash flows of the related underlying exposure. Because of the high correlation between the derivative financial instrument and the underlying exposure being hedged, fluctuations in the value of the derivative financial instruments are generally offset by changes in the fair values or cash flows of the underlying exposures being hedged. Any ineffective portion of a derivative financial instrument's change in fair value would be immediately recognized in earnings.

The Company uses interest rate swaps to manage its interest rate risk. The swaps are designated as cash flow hedges with the changes in fair value recorded in accumulated other comprehensive loss and as a derivative hedge asset or liability, as applicable. The swaps settle periodically in arrears with the related amounts for the current settlement period payable to, or receivable from, the counter-parties included in accrued liabilities or accounts receivable and recognized in earnings as an adjustment to interest expense from the underlying debt to which the swap is designated. During the three month period ended March 31, 2008 approximately \$1,000 of said adjustments were recorded to interest expense. During the three months ended March 31, 2008, ineffectiveness from such hedges was \$0.

At March 31, 2008, the Company had a United States Dollar (USD) denominated interest rate swap outstanding which effectively fixed the interest rate on floating rate debt, exclusive of lender spreads, at 5.36% for a notional principal amount of \$2,000,000 through December 2010. The derivative net loss on this contract recorded in accumulated other comprehensive loss at March 31, 2008 was \$39,882, which is expected to be reclassified from Accumulated other comprehensive loss into earnings over the next 18 months.

Table of Contents**12. Comprehensive Income**

The components of comprehensive income, as required to be reported by SFAS No. 130, Reporting Comprehensive Income, were as follows:

	Three months ended	
	March 31, 2008	March 31, 2007
Net income	\$ 149,816	\$ 27,508
Change in fair value of interest rate swap	(58,524)	
Gain on foreign currency translation adjustment	31,797	6,012
Comprehensive income	\$ 123,089	\$ 33,520

Accumulated other comprehensive loss totaled \$247,123 and \$220,400 at March 31, 2008 and December 31, 2007, respectively and principally related to foreign currency translations and change in fair value of interest rate swap.

13. Legal Proceedings

We are a defendant along with a number of other parties in approximately 122 lawsuits as of March 31, 2008, (approximately 122 lawsuits as of December 31, 2007) alleging that plaintiffs have or may have contracted asbestos-related diseases as a result of exposure to asbestos products or equipment containing asbestos sold by one or more named defendants. Due to the noninformative nature of the complaints, we do not know whether any of the complaints state valid claims against us. Certain insurance carriers have informed us that the primary policies for the period August 1, 1970-1973, have been exhausted and that the carriers will no longer provide a defense under those policies. We have requested that the carriers substantiate this situation. We believe we have additional policies available for other years which have been ignored by the carriers. As settlement payments are applied to all years a litigant was deemed to have been exposed to asbestos, we believe when settlement payments are applied to these additional policies, we will have availability under the years deemed exhausted. We do not believe that the asserted exhaustion of the primary insurance coverage for this period will have a material adverse effect on our financial condition, liquidity, or results of operations. Management believes that the number of insurance carriers involved in the defense of the suits and the significant number of policy years and policy limits, to which these insurance carriers are insuring us, make the ultimate disposition of these lawsuits not material to our consolidated financial position or results of operations.

The Company's former wholly owned French subsidiary, Selas SAS, filed for insolvency in France and is being managed by a court appointed administrator. The Company may be subject to additional litigation or liabilities as a result of the French insolvency proceeding.

We are also involved in other lawsuits arising in the normal course of business. While it is not possible to predict with certainty the outcome of these matters, management is of the opinion that the disposition of these lawsuits and claims will not materially affect our consolidated financial position, liquidity or results of operations.

14. Related-Party Transactions

Edgar Filing: INTRICON CORP - Form 10-Q

One of the Company's subsidiaries leases office and factory space from a partnership consisting of three present or former officers of the subsidiary, including Mark Gorder, the President and Chief Executive Officer of the Company. The subsidiary is required to pay all real estate taxes and operating expenses. In the opinion of management, the terms of the lease agreement are comparable to those which could be obtained from unaffiliated third parties. The total base rent expense incurred under the lease was approximately \$92,000 for each of the three months ended March 31, 2008 and 2007. Annual lease commitments approximate \$475,000 through October 2011.

The Company uses the law firm of Blank Rome LLP for legal services. A partner of that firm is the son-in-law of the Chairman of the Company's Board of Directors. For the three months ended March 31, 2008, the Company paid that firm approximately \$43,000 for legal services and costs. The Chairman of our Board of Directors is considered independent under applicable Nasdaq and SEC rules because (i) no payments were made to the Chairman or the partner directly in exchange for the services provided by the law firm and (ii) the amounts paid to the law firm did not exceed the thresholds contained in the Nasdaq standards. Furthermore, the aforementioned partner does not provide any legal services to the Company and is not involved in billing matters.

14

Table of Contents

15. Statements of Cash Flows

The following table provides supplemental disclosures of cash flow information:

	Three months ended	
	March 31, 2008	March 31, 2007
Interest received	\$ 11,525	\$ 38,570
Interest paid	159,423	99,480
Income taxes paid	64,506	7,122

16. Investment in Equity Instruments

The Company owns a 9% partnership interest in the Hearing Instrument Manufacturers Patent Partnership (HIMPP), and is a party to a license agreement that grants the Company access to over 45 US registered patents. The Company has recorded a \$37,000 decrease in the carrying amount of the investment, reflecting amortization of the patents, other intangibles and the Company's portion of the partnership's operating results for the three months ended March 31, 2008.

The Company's subsidiary, IntriCon Tibbetts Corporation, owns a 50% interest in a joint venture with a Swiss company to market, design, manufacture, and sell audio coils to the hearing health industry. The Company has recorded a \$59,000 increase in the carrying amount of the investment, reflecting the Company's portion of the joint venture's operating results for the three months ended March 31, 2008.

Table of Contents

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

Business Overview

Headquartered in Arden Hills, Minnesota, IntriCon Corporation (formerly Selas Corporation of America) (IntriCon, the Company, we, us or our) is an international firm engaged in the designing, developing, engineering and manufacturing of body-worn devices. The Company serves the body-worn device market by designing, developing, engineering and manufacturing micro-miniature components, systems and molded plastic parts primarily for the hearing instrument, electronics, telecommunications, computer and medical equipment industries. In addition to its operations in Minnesota, the Company has facilities in California, Maine, Singapore, and Germany.

The Company has one operating segment, its precision miniature medical and electronics products segment. Our expertise is focused on four main markets within this segment: medical, hearing health, professional audio and electronics. Within these chosen markets, we combine ultra-miniature mechanical and electronics capabilities with proprietary technology that enhances the performance of body-worn devices.

In the hearing health market, IntriCon manufactures hybrid amplifiers and integrated circuit components (hybrid amplifiers), along with faceplates for in-the-ear and in-the-canal hearing instruments. IntriCon is a leading manufacturer and supplier of microminiature electromechanical components to hearing instrument manufacturers. These components consist of volume controls, microphones, receivers, trimmer potentiometers and switches. Components are offered in a variety of sizes, colors and capacities in order to accommodate a hearing manufacturer's individualized specifications.

Hearing instruments, which fit behind or in a person's ear to amplify and process sound for a hearing impaired person, generally are composed of four basic parts and several supplemental components for control or fitting purposes. The four basic parts are microphones, amplifier circuits, miniature receivers/speakers and batteries, all of which IntriCon manufactures, with the exception of the battery. IntriCon's hybrid amplifiers are a type of amplifier circuit. Supplemental components include volume controls, trimmer potentiometers, which shape sound frequencies to respond to the particular nature of a person's hearing loss, and switches used to turn the instrument on and off and to go from telephone to normal speech modes. Faceplates and an ear shell, molded to fit the user's ear, often serve as housing for hearing instruments. IntriCon manufactures its components on a short lead-time basis in order to supply just-in-time delivery to its customers and, consequently, order backlog amounts are not meaningful.

Edgar Filing: INTRICON CORP - Form 10-Q

Using our proprietary digital signal processing technology, nanoDSP, IntriCon is building a new generation of affordable, high-quality hearing aids and similar amplifier devices under contracts for original equipment manufacturers (OEMs). DSP devices have better clarity, attractive pricing points and an improved ability to filter out background noise.

In the medical market, the Company is focused on sales of biotelemetry devices, microelectronics, micromechanical assemblies and high-precision plastic molded components to medical device manufacturers. Targeted customers include medical product manufacturers of portable and lightweight battery powered devices, as well as a variety of sensors designed to connect a patient to an electronic device.

The medical industry is faced with pressures to reduce the costs of healthcare. IntriCon currently serves this market by offering medical manufacturers the capabilities to design, develop and manufacture components for medical devices that are easier to use, measure with greater accuracy and provide more functions while reducing the costs to manufacture these devices. IntriCon manufactures and supplies bubble sensors and flow restrictors that monitor and control the flow of fluid in an intravenous infusion system. IntriCon also manufactures a family of safety needle products for an OEM customer that utilizes IntriCon's insert and straight molding capabilities. These products are assembled using full automation including built-in quality checks within the production lines. Other examples include sensors used to detect pathologies in specific organs of the body and monitoring devices to detect cardiac and respiratory functions. The early and accurate detection of pathologies allows for increased likelihood for successful treatment of chronic diseases and cancers. Accurate monitoring of multiple functions of the body, such as heart rate and breathing, aids in generating more accurate diagnosis and treatments for patients.

In addition, there has been an industry-wide trend toward further miniaturization and ambulatory operation enabled by wireless connectivity, which is also referred to as bio-telemetry. Through the development of our ultra low power (ULP) wireless technology, Bodynet, we believe that bio-telemetry offers a significant future opportunity. Increasingly, the medical industry is looking for wireless, low-power capabilities in their devices. We believe our strategic partnership with AME will allow us to develop new bio-telemetry devices that better connect patients and care givers, providing critical information and feedback. Current examples of IntriCon bio-telemetry products used by medical device manufacturers include components found in wireless glucose sensor pumps that introduce drugs into the bloodstream.

16

Table of Contents

IntriCon entered the high-quality audio communication device market in 2001, and now has a line of miniature, professional audio headset products used by performers and support staff in the music and stage performance markets. For customers focusing on homeland security needs, the line includes several communication devices that are more portable and perform well in noisy or hazardous environments. These products are also well suited for applications in the fire, law enforcement, safety, aviation and military markets. In addition, our May 2007 acquisition of Tibbett's Industries provides the Company access to homeland security agencies in this market.

Our RTIE subsidiary manufactures and sells thermistors and thermistor assemblies, which are solid state devices that produce precise changes in electrical resistance as a function of any change in absolute body temperature. The balance of sales represents various industrial, commercial and military sales for thermistor and thermistor assemblies to domestic and international markets.

On May 22, 2007, the Company completed the acquisition of substantially all of the assets of Tibbetts Industries, Inc., other than real estate.

The acquisition was financed with borrowings under the Company's new credit facility, as further described in Liquidity and Capital Resources.

The addition of Tibbetts provides us with incremental gains in both our medical and professional audio businesses. We believe the benefits of this acquisition will eventually carry over to hearing health, where we expect to incorporate Tibbetts' pioneering magnetic telecoil and miniature transducer technology into key hearing aid components. Tibbetts' surveillance capabilities also expand our markets to include security products, which are reflected in our professional audio performance.

Forward-Looking and Cautionary Statements

Certain statements included in this Quarterly Report on Form 10-Q or documents the Company files with the Securities and Exchange Commission, which are not historical facts, are forward-looking statements (as such term is defined in Section 21E of the Securities Exchange Act of 1934 and Section 27A of the Securities Act of 1933, and the regulations thereunder), which are intended to be covered by the safe harbors created thereby. These statements may include, but are not limited to statements in Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes to the Company's Condensed Consolidated Financial Statements such as, net operating loss carryforwards, the ability to meet cash requirements for operating needs, the ability to meet liquidity needs, assumptions used to calculate future level of funding of employee benefit plans, the adequacy of insurance coverage, the impact of new accounting pronouncements and litigation.

Forward-looking statements also include, without limitation, statements as to the Company's expected future results of operations and growth, the Company's ability to meet working capital requirements, the Company's business strategy, the expected increases in operating efficiencies, anticipated trends in the Company's precision miniature medical and electronic products markets, estimates of goodwill impairments and amortization expense of other intangible assets, the effects of changes in accounting pronouncements, the effects of litigation and the amount of insurance coverage, and statements as to trends or the Company's or management's beliefs, expectations and opinions.

Forward-looking statements are subject to risks and uncertainties and may be affected by various factors that may cause actual results to differ materially from those in the forward-looking statements. In addition to the factors discussed in this Quarterly Report on Form 10-Q, certain risks, uncertainties and other factors can cause actual results and developments to be materially different from those expressed or implied by such forward-looking statements, including, without limitation, the following:

- risks related to the Tibbetts acquisition, including unanticipated liabilities and expenses;
- the ability to successfully implement the Company's business and growth strategy;
- risks arising in connection with the insolvency of our former subsidiary, Selas SAS, and potential liabilities and actions arising in connection therewith;
- the volume and timing of orders received by the Company;
- changes in estimated future cash flows;
- ability to collect on our accounts receivable;

Table of Contents

foreign currency movements in markets the Company services;
 changes in the global economy and financial markets;
 changes in the mix of products sold;
 ability to meet increasing demand;
 changes in customer requirements;
 timing and extent of research and development expenses;
 acceptance of the Company's products;
 competitive pricing pressures;
 pending and potential future litigation;
 availability of electronic components for the Company's products;
 ability to create and market products in a timely manner and develop products that are inexpensive to manufacture;
 ability to repay debt when it comes due;
 the loss of one or more of our major customers;
 ability to identify and integrate acquisitions;
 effects of legislation;
 effects of foreign operations;
 ability to recruit and retain engineering and technical personnel;
 loss of members of our senior management team; and
 our ability and the ability of our customers to protect intellectual property.

For a description of these and other risks, see "Risk Factors" in Part I, Item 1A: Risk Factors in the Company's Annual Report on Form 10-K for the year ended December 31, 2007 or in other filings the Company makes from time to time with the Securities and Exchange Commission. The Company does not undertake to update any forward-looking statement that may be made from time to time by or on behalf of the Company.

Results of Operations

Sales, net

Consolidated net sales for the three months ended March 31, were as follows (in thousands):

	2008	2007	Change Dollars	Percent	
Three months ended March 31	\$ 16,591	\$ 14,579	\$ 2,012	13.8	%

Edgar Filing: INTRICON CORP - Form 10-Q

Our net sales are comprised of four main sectors: hearing health, medical, professional audio device and electronics. Sales for the first quarter were up 13.8 percent over the prior year driven by our focus on enhancing the mobility and effectiveness of body-worn devices. Exclusive of net sales resulting from the Tibbetts acquisition, net sales increased 3 percent from 2007.

We experienced an increase of 27 percent in net sales in the medical equipment market in 2008 as a direct result of increased sales to existing original equipment manufacturer, or OEM, customers. Management believes there is an industry-wide trend toward further miniaturization and ambulatory operation enabled by wireless connectivity which resulted in further growth in our medical business. Exclusive of net sales resulting from the Tibbetts acquisition, net medical sales increased 11 percent from 2007.

Net sales to the professional audio device sector grew 95 percent fueled by higher demand for microphones from existing customers and additional sales resulting from the acquisition of Tibbetts. Excluding the results from Tibbetts, professional audio device net sales grew 39 percent.

Net sales in our hearing health business decreased 4 percent from 2007 primarily due to lower demand from our customers in this market.

Electronics net sales decreased 15 percent from 2007 primarily due to lower demand from one customer.

18

Table of Contents

Gross profit

Gross profit margins for the three months ended March 31, were as follows (in thousands):

	2008		2007		Change		
	Dollars	Percent of Sales	Dollars	Percent of Sales	Dollars	Percent	
Three months ended March 31	\$3,845	23.2	% \$3,211	22.0	% \$634	19.7	%

The gross profit margin as a percentage of sales, increased for the three months ended March 31, 2008 compared to the previous year periods primarily due to a lower volume of new product introductions combined with a higher margin product mix.

Selling, general and administrative expenses (SG&A)

Edgar Filing: INTRICON CORP - Form 10-Q

Selling, general and administrative expenses (SG&A) for the three months ended March 31 were as follows (in thousands):

	2008		2007		Change			
	Dollars	Percent of Sales	Dollars	Percent of Sales	Increase Dollars	Increase Percent		
Selling	\$ 996	6.0	% \$ 843	5.8	% \$ 153	18.2	%	
General and Administrative	1,652	10.0	1,420	9.7	232	16.3		
Research and Development	788	4.7	733	5.0	55	7.5		

The increased selling, general and administrative, and research and development expenses for three months ended March 31, 2008 as compared to the prior year periods were primarily driven by \$252,000 of additional operating expenses from the May 2007 acquisition of Tibbetts. In addition, we continued to place significant emphasis on investing in research and development to develop new products and technology to further enhance our product portfolio.

Net interest expense

Net interest expense for the three months ended March 31, 2008, was \$188,000 compared to \$115,000 for the same period in 2007. The increase in net interest expense was due to increased amounts of outstanding debt related to the refinancing of the credit facility in connection with the Tibbetts acquisition in May 2007 and decreased interest income as a result of lower balance of note receivable.

Equity in earnings of partnerships

The equity in earnings of partnerships for the three months ended March 31, 2008 was income of \$22,000 compared to expense of \$20,000 for the same period in 2007.

The Company recorded a \$37,000 decrease in the carrying amount of the investment in HIMPP, reflecting amortization of the patents and other intangibles for the three months ended March 31, 2008.

The Company recorded a \$59,000 increase in the carrying amount of Tibbetts investment in joint venture, reflecting the Company's portion of the joint venture's operating results for the period ended March 31, 2008.

Other expense, net

Other expense, net for the three months ended March 31, 2008, was \$5,000 compared to \$26,000 for the same period in 2007. The change in other expense, net primarily related to the changes in foreign currency exchange.

Table of Contents**Income taxes**

Income tax expense for the three months ended March 31, 2008, was \$87,000 compared to \$28,000 for the same period in 2007. The increased expense in 2008 was primarily due to additional foreign taxes on German and Singapore earnings. The Company is in a net operating loss position for U.S. federal income tax purposes and, consequently, minimal expense from the current period domestic operations was recognized.

Liquidity and Capital Resources

As of March 31, 2008, we had approximately \$1.5 million of cash on hand. Sources of our cash for the three months ended March 31, 2008 have been from our operations and our credit facility, as described below.

The Company's cash flows from operating, investing and financing activities, as reflected in the statement of cash flows, are summarized as follows (in thousands):

	Three months Ended	
	March 31,	March 31,
	2008	2007
Cash provided (used) by:		
Continuing operations	\$ (1,334)	\$ (1,116)
Investing activities	(381)	(623)
Financing activities	1,540	1,878
Effect of exchange rate changes on cash	35	5
Increase (decrease) in cash and cash equivalents	\$ (140)	\$ 144

The Company had the following bank arrangements (in thousands):

	March 31,	December
	2008	31,
		2007
Total borrowing capacity under existing facilities	\$ 13,638	\$ 13,623
Facility Borrowings:		
Domestic revolving credit facility	5,100	3,000

Edgar Filing: INTRICON CORP - Form 10-Q

Domestic term loan	4,163	4,275
Foreign overdraft and letter of credit facility	937	1,071
Domestic capital equipment leases	81	94
Total Borrowings	10,281	8,440
Total borrowing availability under existing facilities	\$ 3,357	\$ 5,183

We and our subsidiaries, Resistance Technology, Inc., RTI Electronics, Inc. and IntriCon Tibbetts Corporation, referred to as the borrowers, entered into a credit facility with LaSalle Bank, National Association, referred to as the lender, on May 22, 2007 replacing the prior credit facilities with M & I Business Credit (formerly known as Diversified Business Credit, Inc.). The credit facility provides for:

a \$10,000,000 revolving credit facility, with a \$200,000 subfacility for letters of credit. Under the revolving credit facility, the availability of funds depends on a borrowing base composed of stated percentages of our eligible trade receivables and eligible inventory, less a reserve; and
a \$4,500,000 term loan which was used to fund the Tibbetts acquisition.

Loans under the new credit facility are secured by a security interest in substantially all of the assets of the borrowers including a pledge of the stock of the subsidiaries. All of the borrowers are jointly and severally liable for all borrowings under the new credit facility.

20

Table of Contents

Loans under the new credit facility bear interest, at the option of the Company, at:

the London InterBank Offered Rate (LIBOR) plus 1.90%, in the case of revolving line of credit loans, or LIBOR plus 2.15%, in the case of the term loan, or
the base rate, which is the higher of (a) the rate publicly announced from time to time by the lender as its prime rate and (b) the Federal Funds Rate plus 0.5%.

Interest is payable monthly in arrears, except that interest on LIBOR based loans is payable at the end of the one, two or three month interest periods applicable to LIBOR based loans, or every three months in the case of LIBOR based loans with a six month interest period.

Weighted average interest on the domestic revolving credit facilities (including the prior credit facility) was 6.55% and 8.75% for the three months ended March 31, 2008 and 2007, respectively.

The new credit facility will expire and all outstanding loans will become due and payable on June 30, 2012. The term loan requires quarterly principal payments, commencing on September 30, 2007, based on an increasing installment schedule, with any balance due on June 30, 2012.

The outstanding balance of the revolving credit facilities was \$5,100,000 and \$3,000,000 at March 31, 2008 and December 31, 2007, respectively. The total remaining availability on the revolving credit facility was approximately \$2,409,000 at March 31, 2008.

Edgar Filing: INTRICON CORP - Form 10-Q

The revolving facility carries a non-use fee equal to 0.25% per year of the unused portion of the revolving line of credit facility, payable quarterly in arrears.

We are subject to various covenants under the credit facility, including financial covenants relating to tangible net worth, funded debt to EBITDA, fixed charge coverage ratio and capital expenditures. Under the credit facility, except as otherwise permitted, the borrowers may not, among other things, incur or permit to exist any indebtedness; grant or permit to exist any liens or security interests on their assets or pledge the stock of any subsidiary; make investments; be a party to any merger or consolidation, or purchase of all or substantially all of the assets or equity of any other entity; sell, transfer, convey or lease all or any substantial part of its assets or capital securities; sell or assign, with or without recourse, any receivables; issue any capital securities; make any distribution or dividend (other than stock dividends), whether in cash or otherwise, to any of its equityholders; purchase or redeem any of its equity interests or any warrants, options or other rights in respect thereof; enter into any transaction with any of its affiliates or with any director, officer or employee of any borrower; be a party to any unconditional purchase obligations; cancel any claim or debt owing to it; enter into any agreement inconsistent with the provisions of the credit facility or other agreements and documents entered into in connection with the credit facility; engage in any line of business other than the businesses engaged in on the date of the credit facility and businesses reasonably related thereto; or permit its charter, bylaws or other organizational documents to be amended or modified in any way which could reasonably be expected to materially adversely affect the interests of the lender. Effective as of September 30, 2007, the credit facility was amended to change the tangible net worth covenant. As of March 31, 2008 the Company was in compliance with all financial covenants under the credit facility, as amended.

Upon the occurrence and during the continuance of an event of default (as defined in the credit facility), the lender may, among other things: terminate its commitments to the borrowers (including terminating or suspending its obligation to make loans and advances); declare all outstanding loans, interest and fees to be immediately due and payable; take possession of and sell any pledged assets and other collateral; and exercise any and all rights and remedies available to it under the Uniform Commercial Code or other applicable law. In the event of the insolvency or bankruptcy of any borrower, all commitments of the lender will automatically terminate and all outstanding loans, interest and fees will be immediately due and payable. Events of default include, among other things, failure to pay any amounts when due; material misrepresentation; default in the performance of any covenant, condition or agreement to be performed that is not cured within 20 days after notice from the lender; default in the payment of other indebtedness or other obligation with an outstanding principal balance of more than \$50,000, or of any other term, condition or covenant contained in the agreement under which such obligation is created, the effect of which is to allow the other party to accelerate such payment or to terminate the agreements; the insolvency or bankruptcy of any borrower; the entrance of any judgment against any borrower in excess of \$50,000, which is not fully covered by insurance; the occurrence of a change in control (as defined in the credit facility); certain collateral impairments; and a contribution failure with respect to any employee benefit plan that gives rise to a lien under ERISA.

21

Table of Contents

The prior credit facility provided for:

a \$5,500,000 domestic revolving credit facility, bearing interest at an annual rate equal to the greater of 5.25%, or 0.5% over prime. Under the revolving credit facility, the availability of funds depended on a borrowing base composed of stated percentages of our eligible trade receivables and eligible inventory, less a reserve; and
a \$1,000,000 domestic equipment term loan, bearing interest at an annual rate equal to the greater of 5.25%, or 0.75% over the prime rate.

The revolving facility carried a commitment fee of 0.25% per year, payable on the unborrowed portion of the line. Additionally, the credit facility required an annual fee of \$27,500 due on August 31, 2007, and 2008. Upon termination of the credit facility by us prior to maturity, we

Edgar Filing: INTRICON CORP - Form 10-Q

were required to pay a termination fee equal to 2% of the total of the maximum amount available under the revolving credit facility plus the amounts then outstanding under the term loan, equal to \$110,000.

The credit facility originally included a real estate loan with an original principal balance of \$1,500,000, which was associated with our Vadnais Heights manufacturing facility. In June 2006, we completed a sale-leaseback of the Vadnais Heights manufacturing facility. The transaction generated proceeds of \$2,650,000, of which \$1,388,000 was used to repay the associated real estate loan and the remainder to pay down our domestic revolver. The remaining gain on the sale of \$908,000 is being recognized over the initial 10-year lease term as the renewal options in the lease are not assured and a penalty does not exist if we do not exercise the renewal options.

In addition to our domestic credit facilities, on August 15, 2005, our wholly-owned subsidiary, IntriCon PTE LTD., entered into an international senior secured credit agreement with Oversea-Chinese Banking Corporation Ltd. that provides for a \$1.6 million line of credit. Borrowings bear interest at a rate of 6.47%. The outstanding balance was \$937,000 and \$1,071,000 at March 31, 2008 and December 31, 2007, respectively. The total remaining availability on the international senior secured credit agreement was \$949,000 at March 31, 2008.

We believe that funds expected to be generated from operations, the available borrowing capacity through our revolving credit loan facilities and the control of capital spending will be sufficient to meet our anticipated cash requirements for operating needs through April 2009. If, however, we do not generate sufficient cash from operations, or if we incur additional unanticipated liabilities, we may be required to seek additional financing or sell equity or debt on terms which may not be as favorable as we could have otherwise obtained. No assurance can be given that any refinancing, additional borrowing or sale of equity or debt will be possible when needed or that we will be able to negotiate acceptable terms. In addition, our access to capital is affected by prevailing conditions in the financial and equity capital markets, as well as our own financial condition. While management believes that we will meet our liquidity needs through April 2009, no assurance can be given that we will be able to do so.

During 2005, the Company entered into several capital lease agreements to fund the acquisition of machinery and equipment. For 2005, the total principal amount of these leases was \$314,000 with effective interest rates ranging from 6.7% to 8.0%. These agreements range from 3 to 5 years. The outstanding balance under these capital lease agreements at March 31, 2008 and December 31, 2007 was \$81,000 and \$94,000, respectively. The accumulated amortization on leased equipment was \$130,000 and \$119,000 at March 31, 2008 and December 31, 2007, respectively. The amortization of capital leases is included in depreciation expense for 2008 and 2007.

Recent Accounting Pronouncements

As previously discussed under note 2 to the Consolidated Condensed Financial Statements, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159) in February 2007. This statement expands the use of fair value measurement by permitting entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 is effective beginning with the first fiscal year that begins after November 15, 2007. The adoption of SFAS 159 did not have a material impact on the Company's consolidated financial statements.

Edgar Filing: INTRICON CORP - Form 10-Q

On December 4, 2007, the FASB issued FASB Statement No. 141 (Revised 2007), Business Combinations. FAS 141(R) will significantly change the accounting for business combinations. Under Statement 141(R), an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. FAS 141R will change the accounting treatment for certain specific items, including:

Acquisition costs will be generally expensed as incurred;

Noncontrolling interests (formerly known as minority interests) will be valued at fair value at the acquisition date);

Acquired contingent liabilities will be recorded at fair value at the acquisition date and subsequently measured at either the higher of such amount or the amount determined under existing guidance for non-acquired contingencies;

In-process research and development will be recorded at fair value as an indefinite-lived intangible asset at the acquisition date;

Restructuring costs associated with a business combination will be generally expensed subsequent to the acquisition date; and

Changes in deferred tax asset valuation allowances and income tax uncertainties after the acquisition date generally will affect income tax expense.

FAS 141(R) also includes a substantial number of new disclosure requirements. The statement applies to the Company prospectively for business combinations for which the acquisition date is on or after January 1, 2009. Earlier adoption is prohibited.

On December 4, 2007, the FASB issued FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements - An Amendment of ARB No. 51. Statement 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of a noncontrolling interest (minority interest) as equity in the consolidated financial statements and separate from the parent's equity. The amount of net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement. Statement 160 clarifies that changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidation date. Statement 160 also includes expanded disclosure requirements regarding the interests of the parent and its noncontrolling interest.

Statement 160 is effective for the Company for fiscal years, and interim periods within those fiscal years, beginning with the year ended December 31, 2009. Earlier adoption is prohibited.

In March 2008, the Financial Accounting Standards Board (FASB) issued Statement No. 161, Disclosures about Derivative Instruments and Hedging Activities. SFAS 161 requires additional disclosures related to the use of derivative instruments, the accounting for derivatives and how derivatives impact financial statements. SFAS No. 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company does not expect the adoption of SFAS 161 to have a material effect on the consolidated financial statements.

Critical Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make certain assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period.

Certain accounting estimates and assumptions are particularly sensitive because their significance to the consolidated condensed financial statements and the possibility that future events affecting them may differ markedly. The accounting policies of the Company with significant estimates and assumptions include the Company's revenue recognition, accounts receivable reserves, inventory reserves, discontinued operations,

goodwill, long-lived assets and deferred taxes policies. These and other significant accounting policies are described in and incorporated by reference from Management's Discussion and Analysis of Financial Condition and Results of Operations, and Note 1 to the financial statements contained in or incorporated by reference in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

23

Table of Contents

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

For information regarding the Company's exposure to certain market risks, see Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in the Company's Annual Report on Form 10-K for the year ended December 31, 2007. There have been no material changes in the Company's portfolio of financial instruments or market risk exposures which have occurred since December 31, 2007.

ITEM 4. Controls and Procedures

The Company's management, with the participation of its chief executive officer and chief financial officer, conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures, as defined in Exchange Act Rule 13a-15(e), as of March 31, 2008 (the Disclosure Controls Evaluation). Based on the Disclosure Controls Evaluation, the Company's chief executive officer and chief financial officer concluded that the Company's disclosure controls and procedures were effective to provide a reasonable level of assurance that: (i) information required to be disclosed by the Company in the reports the Company files or submits under the Exchange Act is recorded, processed, summarized and reported within the specific time periods in the Securities and Exchange Commission's rules and forms and (ii) information required to be disclosed in the reports the Company files or submits under Exchange Act is accumulated and communicated to management, including the chief executive officer and chief financial officer, to allow timely decisions regarding required disclosure, all in accordance with Exchange Act Rule 13a-15(e).

There were no changes in the Company's internal control over financial reporting, as defined in Exchange Act Rule 13a-15(f), during the quarter ended March 31, 2008, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

24

Table of Contents

PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

The information contained in note 13 to the Consolidated Condensed Financial Statements in Part I of this quarterly report is incorporated by reference herein.

ITEM 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2007, which could materially affect the Company's business, financial condition or future results. The risk factors in the Company's Annual Report on Form 10-K have not materially changed. The risks described in our Annual Report on Form 10-K are not the only risks facing the Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

ITEM 3. Defaults upon Senior Securities

None.

ITEM 4. Submission of Matters to a Vote of Security Holders

None.

ITEM 5. Other Information

None.

25

Table of Contents

ITEM 6. Exhibits

(a) Exhibits

31.1 Certification of principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1

Edgar Filing: INTRICON CORP - Form 10-Q

Certification of principal executive officer pursuant to U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

- 32.2 Certification of principal financial officer to U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

26

Table of Contents

INTRICON CORPORATION

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

INTRICON CORPORATION
(Registrant)

Date: May 9, 2008

By: /s/ Mark S. Gorder
Mark S. Gorder
President and Chief Executive Officer
(principal executive officer)

Date: May 9, 2008

By: /s/ Scott Longval
Scott Longval
Chief Financial Officer and Treasurer
(principal financial officer)

27

Table of Contents

EXHIBIT INDEX

- 31.1 Certification of principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of principal executive officer pursuant to U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of principal financial officer to U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

