Compass Diversified Holdings
Form 10-K
March 11, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2013

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: 001-34927

Compass Diversified Holdings

(Exact name of registrant as specified in its charter)

Delaware	**57-6218917**
(Jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

Commission File Number: 001-34926

Compass Group Diversified Holdings LLC

(Exact name of registrant as specified in its charter)

Delaware	**20-3812051**
(Jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
Sixty One Wilton Road	
Second Floor	
Westport, CT	**06880**
(Address of principal executive offices)	**(Zip Code)**

(203) 221-1703

(Registrants telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Shares representing beneficial interests in Compass Diversified Holdings (trust shares)	New York Stock Exchange

Securities registered pursuant to Section 12 (g) of the Act: None

Indicate by check mark if the registrants are collectively a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No þ

Indicate by check mark if the registrants are collectively not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No þ

Indicate by check mark whether the registrants (1) have 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 registrants were required to file such reports), and (2) have been subject to such filing requirements for the past 90 days. Yes þ No ¨

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrants knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

Indicate by check mark whether the registrants are collectively 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. (Check one):

Large accelerated filer	¨	Accelerated filer	þ
Non-accelerated filer	¨	Smaller reporting company	¨

Indicate by check mark whether the registrants are collectively a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No þ

The aggregate market value of the outstanding shares of trust stock held by non-affiliates of Compass Diversified Holdings at June 30, 2013 was $689,963,270 based on the closing price on the New York Stock Exchange on that date. For purposes of the foregoing calculation only, all directors and officers of the registrant have been deemed affiliates. There were 48,300,000 shares of trust stock without par value outstanding at February 25, 2014.

Documents Incorporated by Reference

Certain information in the registrant s definitive proxy statement to be filed with the Commission relating to the registrant s 2014 Annual Meeting of Stockholders is incorporated by reference into Part III.

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NOTE TO READER

In reading this Annual Report on Form 10-K, references to:

- the Trust and Holdings refer to Compass Diversified Holdings;
- businesses , operating segments , subsidiaries and reporting units all refer to, collectively, the businesses controlled by the Company;
- the Company refer to Compass Group Diversified Holdings LLC;
- the Manager refer to Compass Group Management LLC (CGM);
- the initial businesses refer to, collectively, Staffmark Holdings, Inc., Crosman Acquisition Corporation, Compass AC Holdings, Inc. and Silvue Technologies Group, Inc.;
- the 2007 acquisitions refer to, collectively, the acquisitions of Aeroglide Corporation, HALO Branded Solutions and American Furniture Manufacturing;
- the 2008 acquisitions refer to, collectively, the acquisitions of Fox Factory Inc. and Staffmark Investment LLC;
- the 2010 acquisitions refer to, collectively, the acquisitions of Liberty Safe and Security Products, LLC and Ergobaby Carrier, Inc.;
- the 2011 acquisition refer to the acquisition of CamelBak Products, LLC;
- the 2012 acquisition refer to the acquisition of Arnold Magnetic Technologies;
- the 2007 disposition refer to the sale of Crosman Acquisition Corporation;
- the 2008 dispositions refer to, collectively, the sales of Aeroglide Corporation and Silvue Technologies Group, Inc.;
- the 2011 disposition refer to the sale of Staffmark Holdings, Inc.;
- the 2012 disposition refer to the sale of HALO Branded Solutions.;
- the Trust Agreement refer to the amended and restated Trust Agreement of the Trust dated as of April 25, 2007;

the Prior Credit Agreement refer to the Credit Agreement with a group of lenders led by Madison Capital, LLC which provided for a Prior Revolving Credit Facility and a Prior Term Loan Facility ;

the Credit Facility refer to the Credit Facility with a group of lenders led by TD Securities (USA) LLC (TD Securities) which provides for a Revolving Credit Facility and a Term Loan Facility;

the Revolving Credit Facility refer to the $320 million Revolving Credit Facility provided by the Credit Facility that matures in April 2017;

the Term Loan Facility refer to the $279.8 million Term Loan Facility outstanding as of December 31, 2013, provided by the Credit Facility that matures in October 2017;

the LLC Agreement refer to the fourth amended and restated operating agreement of the Company dated as of January 1, 2012;

we , us and our refer to the Trust, the Company and the businesses together.

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Statement Regarding Forward-Looking Disclosure

This Annual Report on Form 10-K, including the sections entitled Risk Factors, Management s Discussion and Analysis of Financial Condition and Results of Operations and Business, contains forward-looking statements. We may, in some cases, use words such as project, predict, believe, anticipate, plan, expect, estimate, intend, should, would, could, potentially, or may or other words that convey unc events or outcomes to identify these forward-looking statements. Forward-looking statements in this Annual Report on Form 10-K are subject to a number of risks and uncertainties, some of which are beyond our control, including, among other things:

- our ability to successfully operate our businesses on a combined basis, and to effectively integrate and improve any future acquisitions;
- our ability to remove our Manager and our Manager s right to resign;
- our trust and organizational structure, which may limit our ability to meet our dividend and distribution policy;
- our ability to service and comply with the terms of our indebtedness;
- our cash flow available for distribution and our ability to make distributions in the future to our shareholders;
- our ability to pay the management fee, and profit allocation when due;
- our ability to make and finance future acquisitions;
- our ability to implement our acquisition and management strategies;
- the regulatory environment in which our businesses operate;
- trends in the industries in which our businesses operate;
- changes in general economic or business conditions or economic or demographic trends in the United States and other countries in which we have a presence, including changes in interest rates and inflation;
- environmental risks affecting the business or operations of our businesses;
- our and our Manager s ability to retain or replace qualified employees of our businesses and our Manager;
- costs and effects of legal and administrative proceedings, settlements, investigations and claims; and

extraordinary or force majeure events affecting the business or operations of our businesses.

Our actual results, performance, prospects or opportunities could differ materially from those expressed in or implied by the forward-looking statements. A description of some of the risks that could cause our actual results to differ appears under the section Risk Factors . Additional risks of which we are not currently aware or which we currently deem immaterial could also cause our actual results to differ.

In light of these risks, uncertainties and assumptions, you should not place undue reliance on any forward-looking statements. The forward-looking events discussed in this Annual Report on Form 10-K may not occur. These forward-looking statements are made as of the date of this Annual Report. We undertake no obligation to publicly update or revise any forward-looking statements to reflect subsequent events or circumstances, whether as a result of new information, future events or otherwise, except as required by law.

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PART I

ITEM 1. BUSINESS

Compass Diversified Holdings, a Delaware statutory trust (Holdings , or the Trust), was incorporated in Delaware on November 18, 2005. Compass Group Diversified Holdings, LLC, a Delaware limited liability Company (the Company), was also formed on November 18, 2005. The Trust and the Company (collectively CODI) were formed to acquire and manage a group of small and middle-market businesses headquartered in North America. The Trust is the sole owner of 100% of the Trust Interests, as defined in our LLC Agreement, of the Company. Pursuant to the LLC Agreement, the Trust owns an identical number of Trust Interests in the Company as exist for the number of outstanding shares of the Trust. Accordingly, our shareholders are treated as beneficial owners of Trust Interests in the Company and, as such, are subject to tax under partnership income tax provisions.

The Company is the operating entity with a board of directors whose corporate governance responsibilities are similar to that of a Delaware corporation. The Company s board of directors oversees the management of the Company and our businesses and the performance of Compass Group Management LLC (CGM or our Manager). Certain members of our Manager receive a profit allocation as owners of 53.6% of the Allocation Interests in us, as defined in our LLC Agreement.

Overview

We acquire controlling interests in and actively manage businesses that we believe (i) operate in industries with long-term macroeconomic growth opportunities, (ii) have positive and stable cash flows, (iii) face minimal threats of technological or competitive obsolescence and, (iv) have strong management teams largely in place.

Our unique public structure provides investors with an opportunity to participate in the ownership and growth of companies which have historically been owned by private equity firms, wealthy individuals or families. Through the acquisition of a diversified group of businesses with these characteristics, we believe we offer investors an opportunity to diversify their own portfolio risk while participating in the ongoing cash flows of those businesses through the receipt of quarterly distributions.

Our disciplined approach to our target market provides opportunities to methodically purchase attractive businesses at values that are accretive to our shareholders. For sellers of businesses, our unique financial structure allows us to acquire businesses efficiently with little or no third party financing contingencies and, following acquisition, to provide our businesses with substantial access to growth capital.

We believe that private company operators and corporate parents looking to sell their business units may consider us an attractive purchaser because of our ability to:

- provide ongoing strategic and financial support for their businesses;
- maintain a long-term outlook as to the ownership of those businesses where such an outlook is required for maximization of our shareholders return on investment; and
- consummate transactions efficiently without being dependent on third-party transaction financing.

In particular, we believe that our outlook on length of ownership and active management on our part may alleviate the concern that many private company operators and parent companies may have with regard to their businesses going through multiple sale processes in a short period of time. We believe this outlook reduces both the risk that businesses may be sold at unfavorable points in the overall market cycle and enhances our ability to develop a comprehensive strategy to grow the earnings and cash flows of each of our businesses, which we expect will better enable us to meet our long-term objective of continuing to pay distributions to our shareholders while increasing shareholder value. Finally, it has been our experience, that our ability to acquire businesses without the cumbersome delays and conditions typical of third party transactional financing is appealing to sellers of businesses who are interested in confidentiality and certainty to close.

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We believe our management team s strong relationships with industry executives, accountants, attorneys, business brokers, commercial and investment bankers, and other potential sources of acquisition opportunities offer us substantial opportunities to assess small to middle market businesses available for acquisition. In addition, the flexibility, creativity, experience and expertise of our management team in structuring transactions allows us to consider non-traditional and complex transactions tailored to fit a specific acquisition target.

In terms of the businesses in which we have a controlling interest as of December 31, 2013, we believe that these businesses have strong management teams, operate in strong markets with defensible market niches and maintain long standing customer relationships. We believe that the strength of this model, which provides for significant industry, customer and geographic diversity, has become even more apparent in the recent challenging economic environment.

2013 Highlights

Debt Re-pricing

On April 3, 2013, we exercised an option to increase our Term Loan Facility by $30 million. Net proceeds from this incremental term loan were used to reduce outstanding loans on our Revolving Credit Facility. In connection with the increase, we amended the pricing of our Credit Facility so that borrowings under the Term Loan Facility now bear interest at LIBOR plus 4.0% with a floor of 1.0% and borrowings under the Revolving Credit Facility now bear interest at LIBOR plus 2.5% - 3.5%. In addition, the amendment provided for a reduction in commitment fees on revolving loan availability to 0.75% and extended the maturity date on our Revolving Credit Facility to April 2017.

On August 6, 2013, we exercised an option under our Credit Facility to expand our Revolving Credit Facility by $30 million, increasing the total amount available under the facility to $320 million subject to borrowing base restrictions. We intend to utilize the incremental borrowing capacity under the Revolving Credit Facility to fund future growth opportunities and provide for working capital and general corporate purposes.

FOX IPO

On August 13, 2013 Fox Factory Holding Corp. (FOX) completed an initial public offering of its common stock pursuant to a registration statement on Form S-1 (the FOX IPO). In the FOX IPO, FOX sold 2,857,143 shares and certain of its shareholders sold 7,000,000 shares (including 5,800,238 shares held by CODI) at an initial offering price of $15.00 per share. FOX trades on The NASDAQ Stock Market LLC (the NASDAQ) stock market under the ticker FOXF . We received approximately $80.9 million in net proceeds from the sale of our FOX shares. FOX used a portion of their net proceeds received from the sale of their shares as well as proceeds from a new credit facility with a third party lender to repay $61.5 million in outstanding indebtedness to us under their credit facility.

As a result of the FOX IPO, we currently own approximately 53.9% of the outstanding shares of FOX common stock.

2013 Distributions

For the 2013 fiscal year we declared and paid distributions to our shareholders totaling $1.44 per share.

The following is a brief summary of the businesses in which we own a controlling interest at December 31, 2013:

Branded Products Businesses

CamelBak

CamelBak Products LLC (CamelBak), headquartered in Petaluma, California, is a diversified hydration and personal protection platform offering products for outdoor, recreation and military applications. CamelBak offers a broad range of recreational / military hydration packs, reusable water bottles, specialized military gloves and performance accessories. We made loans to, and purchased a controlling interest in, CamelBak on August 24, 2011 for approximately $211.6 million. We currently own 89.9% of the outstanding stock of CamelBak on a primary basis and 79.7% on a fully diluted basis.

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Ergobaby

Ergobaby Carrier, Inc. (Ergobaby), headquartered in Los Angeles, California, is a premier designer, manufacturer and distributor of wearable baby carriers and related baby wearing products, as well as stroller travel systems and accessories. Ergobaby s reputation for product innovation, reliability and safety has led to numerous awards and accolades from consumers, industry experts and publications. Ergobaby offers a broad range of wearable baby carriers, stroller travel systems and related products that are sold through more than 450 retailers and web shops in the United States and internationally. We made loans to, and purchased a controlling interest in, Ergobaby on September 16, 2010 for approximately $85.2 million. We currently own 81.0% of the outstanding stock of Ergobaby on a primary basis and 75.0% on a fully diluted basis.

FOX

FOX headquartered in Scotts Valley, California, is a designer, manufacturer and marketer of high-performance suspension products used primarily on mountain bikes, side-by-side vehicles, on-road vehicles with off-road capabilities, off-road vehicles and trucks, all-terrain vehicles, or ATVs, snowmobiles, specialty vehicles and applications, and motorcycles. FOX s products offer innovative design, performance, durability and reliability that enhance ride dynamics by improving performance and control. The FOX brand is associated with high-performance and technologically advanced products. We made loans to and purchased a controlling interest in FOX on January 4, 2008, for approximately $80.4 million. We currently own 53.9% of the outstanding common stock on a primary basis and 49.8% on a fully diluted basis.

Liberty Safe

Liberty Safe and Security Products, Inc. (Liberty Safe or Liberty), headquartered in Payson, Utah, is a designer, manufacturer and marketer of premium home and gun safes in North America. From it s over 200,000 square foot manufacturing facility, Liberty produces a wide range of home and gun safe models in a broad assortment of sizes, features and styles. We made loans to and purchased a controlling interest in Liberty Safe on March 31, 2010 for approximately $70.2 million. We currently own 96.2% of the outstanding stock of Liberty Safe on a primary basis and 84.8% on a fully diluted basis.

Niche Industrial Businesses

Advanced Circuits

Compass AC Holdings, Inc. (Advanced Circuits or ACI), headquartered in Aurora, Colorado, is a provider of prototype, quick-turn and volume production rigid printed circuit boards, or PCBs , throughout the United States. PCBs are a vital component of virtually all electronic products. The prototype and quick-turn portions of the PCB industry are characterized by customers requiring high levels of responsiveness, technical support and timely delivery. We made loans to and purchased a controlling interest in Advanced Circuits, on May 16, 2006, for approximately $81.0 million. We currently own 69.4% of the outstanding stock of Advanced Circuits on a primary and fully diluted basis.

American Furniture

AFM Holding Corporation (American Furniture or AFM) headquartered in Ecru, Mississippi, is a leader in the manufacturing of low-cost upholstered stationary and motion furniture, including sofas, loveseats, sectionals, recliners and complementary products to the promotional furniture market. We made loans to and purchased a controlling interest in AFM on August 31, 2007 for approximately $97.0 million. We currently own approximately 99.9% of AFM s outstanding stock on a primary basis and fully diluted basis.

Arnold

AMT Acquisition Corporation (Arnold or Arnold Magnetics), headquartered in Rochester, NY, with nine additional facilities worldwide, is a manufacturer of engineered, application specific permanent magnets. Arnold Magnetics products are used in applications such as general industrial, reprographic systems, aerospace and defense, advertising and promotional, consumer and appliance, energy, automotive and medical technology. Arnold Magnetics is the largest U.S. manufacturer of engineered magnets as well as only one of two domestic producers to design, engineer and manufacture rare earth magnetic solutions. We made loans to, and purchased a controlling interest in Arnold on March 5, 2012 for approximately $128.8 million. We currently own 96.7% of the outstanding stock of Arnold on a primary basis and 87.2% on a fully diluted basis.

Tridien

Anodyne Medical Device, Inc. (Anodyne , which was rebranded as Tridien in September 2010) headquartered in Coral Springs, Florida, is a leading designer and manufacturer of powered and non-powered medical therapeutic support services and patient positioning devices serving the acute care, long-term care and home health care markets. Tridien is one of the nation s leading designers and manufacturers of specialty therapeutic support surfaces and is able to manufacture products in multiple locations to better serve a national customer base. We made loans to and purchased a controlling interest in Tridien from CGI on August 1, 2006 for approximately $31.0 million. We currently own 81.3% of the outstanding capital stock on a primary basis and 66.5% on a fully diluted basis.

Our businesses also represent our operating segments. See Our Businesses and Note F Operating Segment Data to our Consolidated Financial Statements for further discussion of our businesses as our operating segments.

Tax Reporting

Information returns will be filed by the Trust and the Company with the IRS, as required, with respect to income, gain, loss, deduction and other items derived from the Company s activities. The Company has and will file a partnership return with the IRS and intends to issue a Schedule K-1 to the trustee. The trustee intends to provide information to each holder of shares using a monthly convention as the calculation period. For 2013, and future years, the Trust has, and will continue to file a Form 1065 and issue Schedule K-1 to shareholders. For 2013, we delivered the Schedule K-1 to shareholders within the same time frame as we delivered the schedule to shareholders for the 2012 and 2011 taxable year. The relevant and necessary information for tax purposes is readily available electronically through our website. Each holder will be deemed to have consented to provide relevant information, and if the shares are held through a broker or other nominee, to allow such broker or other nominee to provide such information as is reasonably requested by us for purposes of complying with our tax reporting obligations.

WHERE YOU CAN FIND ADDITIONAL INFORMATION

We have filed with the SEC Forms S-1 and S-3 under the Securities Act, and Forms 10-Q, 10-K, and 8-K under the Exchange Act, which include exhibits, schedules and amendments. In addition, copies of such reports are available free of charge that can be accessed indirectly through our website http://www.compassdiversifiedholdings.com and are available as soon as reasonably practicable after such documents are electronically filed or furnished with the SEC.

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1) CGI and its affiliates beneficially own approximately 16.4% of the Trust shares and is our single largest holder. Mr. Offenberg is not a director, officer or member of CGI or any of its affiliates.
2) 53.6% owned by certain members of our Manager. Mr. Day and CGI are non-managing members.
3) Mr. Offenberg is a partner of this entity.
4) The Allocation Interests, which carry the right to receive a profit allocation, represent less than 0.1% equity interest in the Company.

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Our Manager

Our Manager, CGM, has been engaged to manage the day-to-day operations and affairs of the Company and to execute our strategy, as discussed below. Our management team has worked together since 1998. Collectively, our management team has extensive experience in acquiring and managing small and middle market businesses. We believe our Manager is unique in the marketplace in terms of the success and experience of its employees in acquiring and managing diverse businesses of the size and general nature of our businesses. We believe this experience will provide us with an advantage in executing our overall strategy. Our management team devotes a majority of its time to the affairs of the Company.

We have entered into a management services agreement, (the Management Services Agreement or MSA) pursuant to which our Manager manages the day-to-day operations and affairs of the Company and oversees the management and operations of our businesses. We pay our Manager a quarterly management fee for the services it performs on our behalf. In addition, certain members of our Manager receive a profit allocation with respect to its Allocation Interests in us. All of the Allocation Interests in us are owned by Sostratus LLC. See Part III, Item 13 Certain Relationships and Related Transactions for further descriptions of the management fees and profit allocations.

The Company s Chief Executive Officer and Chief Financial Officer are employees of our Manager and have been seconded to us. Neither the Trust nor the Company has any other employees. Although our Chief Executive Officer and Chief Financial Officer are employees of our Manager, they report directly to the Company s board of directors. The management fee paid to our Manager covers all expenses related to the services performed by our Manager, including the compensation of our Chief Executive Officer and other personnel providing services to us. The Company reimburses our Manager for the salary and related costs and expenses of our Chief Financial Officer and his staff, who dedicate substantially all of their time to the affairs of the Company.

See Part III, Item 13, Certain Relationships and Related Party Transactions and Director Independence.

Market Opportunity

We acquire and actively manage small and middle market businesses. We characterize small to middle market businesses as those that generate annual cash flows of up to $60 million. We believe that the merger and acquisition market for small to middle market businesses is highly fragmented and provides opportunities to purchase businesses at attractive prices. We believe that the following factors contribute to lower acquisition multiples for small and middle market businesses:

- there are fewer potential acquirers for these businesses;
- third-party financing generally is less available for these acquisitions;
- sellers of these businesses frequently consider non-economic factors, such as continuing board membership or the effect of the sale on their employees; and
- these businesses are less frequently sold pursuant to an auction process.

Frequently opportunities exist to augment existing management at such businesses and improve the performance of these businesses upon their acquisition. In the past, our management team has acquired businesses that were owned by entrepreneurs or large corporate parents. In these cases, our management team has frequently found that there have been opportunities to further build upon the management teams of acquired businesses beyond those that existed at the time of acquisition. In addition, our management team has frequently found that financial reporting and management information systems of acquired businesses may be improved, both of which can lead to improvements in earnings and cash flow. Finally, because these businesses tend to be too small to have their own corporate development efforts, opportunities frequently exist to assist these businesses as they pursue organic or external growth strategies that were often not pursued by their previous owners.

Our Strategy

We have two primary strategies that we use in order to provide distributions to our shareholders and increase shareholder value. First, we focus on growing the earnings and cash flow from our acquired businesses. We believe that the scale and scope of our businesses give us a diverse base of cash flow upon which to further build. Second, we identify, perform due diligence on, negotiate and consummate additional platform acquisitions of small to middle market businesses in attractive industry sectors in accordance with acquisition criteria established by the board of directors

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Management Strategy

Our management strategy involves the proactive financial and operational management of the businesses we own in order to increase cash flow, pay distributions to our shareholders and increase shareholder value. Our Manager oversees and supports the management teams of each of our businesses by, among other things:

- recruiting and retaining talented managers to operate our businesses using structured incentive compensation programs, including non-controlling equity ownership, tailored to each business;
- regularly monitoring financial and operational performance, instilling consistent financial discipline, and supporting management in the development and implementation of information systems to effectively achieve these goals;
- assisting management in their analysis and pursuit of prudent organic growth strategies;
- identifying and working with management to execute attractive external growth and acquisition opportunities;
- assisting management in controlling and right-sizing overhead costs, particularly in the current challenging economic environment; and
- forming strong subsidiary level boards of directors to supplement management in their development and implementation of strategic goals and objectives.

Specifically, while our businesses have different growth opportunities and potential rates of growth, we expect our Manager to work with the management teams of each of our businesses to increase the value of, and cash generated by, each business through various initiatives, including:

- making selective capital investments to expand geographic reach, increase capacity, or reduce manufacturing costs of our businesses;
- investing in product research and development for new products, processes or services for customers;
- improving and expanding existing sales and marketing programs;
- pursuing reductions in operating costs through improved operational efficiency or outsourcing of certain processes and products; and
- consolidating or improving management of certain overhead functions.

Our businesses typically acquire and integrate complementary businesses. We believe that complementary add-on acquisitions improve our overall financial and operational performance by allowing us to:

leverage manufacturing and distribution operations;

leverage branding and marketing programs, as well as customer relationships;

add experienced management or management expertise;

increase market share and penetrate new markets; and

realize cost synergies by allocating the corporate overhead expenses of our businesses across a larger number of businesses and by implementing and coordinating improved management practices.

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We incur third party debt financing almost entirely at the Company level, which we use, in combination with our equity capital, to provide debt financing to each of our businesses and to acquire additional businesses. FOX maintains its own credit facility. Refer to Liquidity and Capital Resources FOX Credit Facility. We believe this financing structure is beneficial to the financial and operational activities of each of our businesses by aligning our interests as both equity holders of, and lenders to, our businesses, in a manner that we believe is more efficient than each of our businesses borrowing from third-party lenders.

Acquisition Strategy

Our acquisition strategy involves the acquisition of businesses that we expect to produce stable and growing earnings and cash flow. In this respect, we expect to make acquisitions in industries other than those in which our businesses currently operate if we believe an acquisition presents an attractive opportunity. We believe that attractive opportunities will continue to present themselves, as private sector owners seek to monetize their interests in longstanding and privately-held businesses and large corporate parents seek to dispose of their non-core operations.

Our ideal acquisition candidate has the following characteristics:

- is an established North American based company;
- maintains a significant market share in defensible industry niche (i.e., has a reason to exist);
- has a solid and proven management team with meaningful incentives;
- has low technological and/or product obsolescence risk; and
- maintains a diversified customer and supplier base.

We benefit from our Manager s ability to identify potential diverse acquisition opportunities in a variety of industries. In addition, we rely upon our management team s experience and expertise in researching and valuing prospective target businesses, as well as negotiating the ultimate acquisition of such target businesses. In particular, because there may be a lack of information available about these target businesses, which may make it more difficult to understand or appropriately value such target businesses, on our behalf, our Manager:

- engages in a substantial level of internal and third-party due diligence;
- critically evaluates the target management team;
- identifies and assesses any financial and operational strengths and weaknesses of the target business;
- analyzes comparable businesses to assess financial and operational performances relative to industry competitors;
- actively researches and evaluates information on the relevant industry; and

thoroughly negotiates appropriate terms and conditions of any acquisition.

The process of acquiring new businesses is both time-consuming and complex. Our management team historically has taken from two to twenty-four months to perform due diligence, negotiate and close acquisitions. Although our management team is always at various stages of evaluating several transactions at any given time, there may be periods of time during which our management team does not recommend any new acquisitions to us. Even if an acquisition is recommended by our management team, our board of director s may not approve it.

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A component of our acquisition financing strategy that we utilize in acquiring the businesses we own and manage is to provide both equity capital and debt capital, raised at the parent company level largely through our existing credit facility, to close acquisitions. We believe, and it has been our experience, that having the ability to finance our acquisitions with capital resources raised by us, rather than negotiating separate third party financing, provides us with an advantage in successfully acquiring attractive businesses by minimizing delay and closing conditions that are often related to acquisition-specific financings. In addition, our strategy of providing this intercompany debt financing within the capital structure of the businesses we acquire and manage allows us the ability to distribute cash to the parent company through monthly interest payments and amortization of principle on these intercompany loans.

Upon acquisition of a new business, we rely on our Manager s experience and expertise to work efficiently and effectively with the management of the new business to jointly develop and execute a successful business plan.

We believe our financing structure, in which both equity and debt capital are raised at the Company level, allows us to acquire businesses without transaction specific financing and is conducive to our ability to consummate transactions that may be attractive in both the short- and long-term.

In addition to acquiring businesses, we sell those businesses that we own from time to time when attractive opportunities arise that outweigh the value that we believe we will be able to bring such businesses consistent with our long-term investment strategy. As such, our decision to sell a business is based on our belief that doing so will increase shareholder value to a greater extent than through our continued ownership of that business. Upon the sale of a business, we may use the proceeds to retire debt or retain proceeds for acquisitions or general corporate purposes. We do not expect to make special distributions at the time of a sale of one of our businesses; instead, we expect to pay shareholder distributions over time solely through the earnings and cash flows of our businesses.

Since our inception in May 2006, we have recorded gains on sales of our businesses of approximately $198 million. We sold Crosman Acquisition Company (Crosman) in January 2007, Aeroglide Company (Aeroglide) and Silvue Technologies Group, Inc. (Silvue) in June 2008, Staffmark Holdings Inc. (Staffmark) in 2011 and HALO Branded Solutions (HALO) in 2012. We sold Crosman, our majority owned recreational products company for approximately $143 million and our net proceeds and gain on sale were approximately $110 million and $36 million, respectively. We sold Aeroglide, our majority owned designer and manufacturer of industrial drying and cooling equipment for approximately $95 million and our net proceeds and gain on sale were approximately $78 million and $34 million, respectively. We sold Silvue, our majority owned developer and producer of proprietary, high performance liquid coating systems for approximately $95 million and our net proceeds and gain on sale were approximately $64 million and $39 million, respectively. We sold Staffmark, our majority-owned provider of temporary staffing solutions subsidiary for approximately $295 million and our net proceeds and gain on sale were approximately $217 million and $89 million, respectively We sold HALO, our majority owned fulfillment provider of promotional items for $76.5 million and our net proceeds upon sale were approximately $66.0 million and our loss on sale was approximately $0.5 million.

On August 13, 2013 FOX completed an initial public offering of its common stock. We sold a portion of our shares of common stock in FOX in this offering and received net proceeds totaling $80.9 million. Our ownership position was diluted as a result of the offering. We currently own 53.9% of FOX on a primary basis and 48.9% on a fully diluted basis. No gain was reflected as a result of the sale of our FOX shares because our majority ownership classification of FOX did not change.

Strategic Advantages

Based on the experience of our management team and its ability to identify and negotiate acquisitions, we believe we are well-positioned to acquire additional businesses. Our management team has strong relationships with business brokers, investment and commercial bankers, accountants, attorneys and other potential sources of acquisition opportunities. In addition, our management team also has a successful track record of acquiring and managing small to middle market businesses in various industries. In negotiating these acquisitions, we believe our management team has been able to successfully navigate complex situations surrounding acquisitions, including corporate spin-offs, transitions of family-owned businesses, management buy-outs and reorganizations.

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Our management team has a large network of approximately 2,000 deal intermediaries who we expect to expose us to potential acquisitions. Through this network, as well as our management team s proprietary transaction sourcing efforts, we have a substantial pipeline of potential acquisition targets. Our management team also has a well-established network of contacts, including professional managers, attorneys, accountants and other third-party consultants and advisors, who may be available to assist us in the performance of due diligence and the negotiation of acquisitions, as well as the management and operation of our acquired businesses.

Finally, because we intend to fund acquisitions through the utilization of our Revolving Credit Facility, we expect to minimize the delays and closing conditions typically associated with transaction specific financing, as is typically the case in such acquisitions. We believe this advantage can be a powerful one, especially in a tight credit environment, and is highly unusual in the marketplace for acquisitions in which we operate.

Valuation and Due Diligence

When evaluating businesses or assets for acquisition, our management team performs a rigorous due diligence and financial evaluation process. In doing so, we evaluate the operations of the target business as well as the outlook for the industry in which the target business operates. While valuation of a business is, by definition, a subjective process, we define valuations under a variety of analyses, including:

- discounted cash flow analyses;
- evaluation of trading values of comparable companies;
- expected value matrices; and
- examination of comparable recent transactions.

One outcome of this process is a projection of the expected cash flows from the target business. A further outcome is an understanding of the types and levels of risk associated with those projections. While future performance and projections are always uncertain, we believe that with detailed due diligence, future cash flows will be better estimated and the prospects for operating the business in the future better evaluated. To assist us in identifying material risks and validating key assumptions in our financial and operational analysis, in addition to our own analysis, we engage third-party experts to review key risk areas, including legal, tax, regulatory, accounting, insurance and environmental. We also engage technical, operational or industry consultants, as necessary.

A further critical component of the evaluation of potential target businesses is the assessment of the capability of the existing management team, including recent performance, expertise, experience, culture and incentives to perform. Where necessary, and consistent with our management strategy, we actively seek to augment, supplement or replace existing members of management who we believe are not likely to execute our business plan for the target business. Similarly, we analyze and evaluate the financial and operational information systems of target businesses and, where necessary, we enhance and improve those existing systems that are deemed to be inadequate or insufficient to support our business plan for the target business.

Financing

We have a Credit Facility with a group of lenders led by TD Securities that we entered into on October 27, 2011 and further amended on April 2, 2012, April 3 and August 6, 2013. The Credit Facility provides for a Revolving Credit Facility totaling $320 million, subject to