

MOTORCAR PARTS AMERICA INC

Form 10-Q

February 09, 2017

---

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

FOR THE QUARTERLY PERIOD ENDED DECEMBER 31, 2016

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

FOR THE TRANSITION PERIOD FROM TO

Commission File No. 001-33861

MOTORCAR PARTS OF AMERICA, INC.

(Exact name of registrant as specified in its charter)

New York

(State or other jurisdiction of incorporation or organization)

11-2153962

(I.R.S. Employer Identification No.)

2929 California Street, Torrance, California 90503

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (310) 212-7910

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

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

There were 18,693,779 shares of Common Stock outstanding at February 2, 2017.



MOTORCAR PARTS OF AMERICA, INC.

TABLE OF CONTENTS

PART I — FINANCIAL INFORMATION

<u>Item 1. Financial Statements</u>	4
<u>Consolidated Balance Sheets</u>	4
<u>Consolidated Statements of Operations</u>	5
<u>Consolidated Statements of Comprehensive Income</u>	6
<u>Consolidated Statements of Cash Flows</u>	7
<u>Condensed Notes to Consolidated Financial Statements</u>	8
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	22
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	32
<u>Item 4. Controls and Procedures</u>	32

PART II — OTHER INFORMATION

<u>Item 1. Legal Proceedings</u>	34
<u>Item 1A. Risk Factors</u>	34
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	34
<u>Item 3. Defaults Upon Senior Securities</u>	34
<u>Item 5. Other Information</u>	34
<u>Item 6. Exhibits</u>	35

Table of Contents

MOTORCAR PARTS OF AMERICA, INC.

GLOSSARY

The following terms are frequently used in the text of this report and have the meanings indicated below.

“Used Core” — An automobile part which has been used in the operation of a vehicle. Generally, the Used Core is an original equipment (“OE”) automobile part installed by the vehicle manufacturer and subsequently removed for replacement. Used Cores contain salvageable parts which are an important raw material in the remanufacturing process. We obtain most Used Cores by providing credits to our customers for Used Cores returned to us under our core exchange program. Our customers receive these Used Cores from consumers who deliver a Used Core to obtain credit from our customers upon the purchase of a newly remanufactured automobile part. When sufficient Used Cores cannot be obtained from our customers, we will purchase Used Cores from core brokers, who are in the business of buying and selling Used Cores. The Used Cores purchased from core brokers or returned to us by our customers under the core exchange program, and which have been physically received by us, are part of our raw material or work in process inventory included in long-term core inventory.

“Remanufactured Core” — The Used Core underlying an automobile part that has gone through the remanufacturing process and through that process has become part of a newly remanufactured automobile part. The remanufacturing process takes a Used Core, breaks it down into its component parts, replaces those components that cannot be reused and reassembles the salvageable components of the Used Core and additional new components into a remanufactured automobile part. Remanufactured Cores are included in our on-hand finished goods inventory and in the remanufactured finished good product held for sale at customer locations. Used Cores returned by consumers to our customers but not yet returned to us continue to be classified as Remanufactured Cores until we physically receive these Used Cores. All Remanufactured Cores are included in our long-term core inventory or in our long-term core inventory deposit.

Table of Contents

## PART I — FINANCIAL INFORMATION

## Item 1. Financial Statements

MOTORCAR PARTS OF AMERICA, INC. AND SUBSIDIARIES  
Consolidated Balance Sheets

	December 31, 2016 (Unaudited)	March 31, 2016
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$3,941,000	\$ 21,897,000
Short-term investments	1,966,000	1,813,000
Accounts receivable — net	22,667,000	8,548,000
Inventory— net	71,340,000	58,060,000
Inventory unreturned	5,098,000	10,520,000
Deferred income taxes	34,723,000	33,347,000
Prepaid expenses and other current assets	7,478,000	5,900,000
Total current assets	147,213,000	140,085,000
Plant and equipment — net	18,243,000	16,099,000
Long-term core inventory — net	257,198,000	241,100,000
Long-term core inventory deposits	5,569,000	5,569,000
Long-term deferred income taxes	456,000	236,000
Goodwill	2,551,000	2,053,000
Intangible assets — net	4,150,000	4,573,000
Other assets	7,649,000	3,657,000
<b>TOTAL ASSETS</b>	<b>\$443,029,000</b>	<b>\$ 413,372,000</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$77,552,000	\$ 72,152,000
Accrued liabilities	8,716,000	9,101,000
Customer finished goods returns accrual	12,567,000	26,376,000
Accrued core payment	11,791,000	8,989,000
Revolving loan	18,001,000	7,000,000
Other current liabilities	11,579,000	4,698,000
Current portion of term loan	3,064,000	3,067,000
Total current liabilities	143,270,000	131,383,000
Term loan, less current portion	17,691,000	19,980,000
Long-term accrued core payment	15,181,000	17,550,000
Long-term deferred income taxes	13,577,000	14,315,000
Other liabilities	13,374,000	19,336,000
Total liabilities	203,093,000	202,564,000
Commitments and contingencies		
Shareholders' equity:		
Preferred stock; par value \$.01 per share, 5,000,000 shares authorized; none issued...	-	-
Series A junior participating preferred stock; par value \$.01 per share, 20,000 shares authorized; none issued	-	-
Common stock; par value \$.01 per share, 50,000,000 shares authorized; 18,693,779 and 18,531,751 shares issued and outstanding at December 31, 2016 and March 31, 2016, respectively	187,000	185,000

Edgar Filing: MOTORCAR PARTS AMERICA INC - Form 10-Q

Additional paid-in capital	206,619,000	203,650,000
Retained earnings	40,478,000	11,825,000
Accumulated other comprehensive loss	(7,348,000 )	(4,852,000 )
Total shareholders' equity	239,936,000	210,808,000
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$443,029,000	\$ 413,372,000

The accompanying condensed notes to consolidated financial statements are an integral part hereof.

Table of Contents

## MOTORCAR PARTS OF AMERICA, INC. AND SUBSIDIARIES

## Consolidated Statements of Operations

(Unaudited)

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	2015	2016	2015
Net sales	\$ 112,595,000	\$ 94,022,000	\$ 306,843,000	\$ 271,527,000
Cost of goods sold	80,225,000	65,123,000	223,424,000	194,817,000
Gross profit	32,370,000	28,899,000	83,419,000	76,710,000
Operating expenses:				
General and administrative	7,952,000	8,802,000	21,446,000	38,381,000
Sales and marketing	3,234,000	2,671,000	8,575,000	7,583,000
Research and development	1,039,000	711,000	2,813,000	2,093,000
Total operating expenses	12,225,000	12,184,000	32,834,000	48,057,000
Operating income	20,145,000	16,715,000	50,585,000	28,653,000
Interest expense, net	3,357,000	2,516,000	9,365,000	13,566,000
Income before income tax expense	16,788,000	14,199,000	41,220,000	15,087,000
Income tax expense	5,678,000	6,451,000	13,459,000	6,821,000
Net income	\$ 11,110,000	\$ 7,748,000	\$ 27,761,000	\$ 8,266,000
Basic net income per share	\$0.59	\$0.42	\$1.49	\$0.45
Diluted net income per share	\$0.57	\$0.41	\$1.43	\$0.44
Weighted average number of shares outstanding:				
Basic	18,675,125	18,319,531	18,587,946	18,180,039
Diluted	19,441,265	19,095,704	19,399,857	18,981,421

The accompanying condensed notes to consolidated financial statements are an integral part hereof.

Table of Contents

## MOTORCAR PARTS OF AMERICA, INC. AND SUBSIDIARIES

## Consolidated Statements of Comprehensive Income

(Unaudited)

	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	2015	2016	2015
Net income	\$ 11,110,000	\$ 7,748,000	\$ 27,761,000	\$ 8,266,000
Other comprehensive income (loss), net of tax:				
Unrealized gain (loss) on short-term investments (net of tax of \$7,000, \$29,000, \$66,000, and \$(11,000))	10,000	42,000	98,000	(17,000 )
Foreign currency translation loss	(1,252,000 )	(422,000 )	(2,594,000 )	(2,195,000 )
Total other comprehensive loss, net of tax	(1,242,000 )	(380,000 )	(2,496,000 )	(2,212,000 )
Comprehensive income	\$ 9,868,000	\$ 7,368,000	\$ 25,265,000	\$ 6,054,000

The accompanying condensed notes to consolidated financial statements are an integral part hereof.



Table of Contents

## MOTORCAR PARTS OF AMERICA, INC. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

(Unaudited)

	Nine Months Ended	
	December 31,	
	2016	2015
Cash flows from operating activities:		
Net income	\$27,761,000	\$8,266,000
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation	2,262,000	1,737,000
Amortization of intangible assets	456,000	476,000
Amortization of debt issuance costs	538,000	635,000
Write-off of debt issuance costs	-	5,108,000
Amortization of interest on accrued core payments	545,000	566,000
(Gain) loss due to change in fair value of the warrant liability	(5,727,000 )	3,077,000
Gain due to change in fair value of the contingent consideration	(16,000 )	-
Gain due to change in estimate of stock adjustment accrual	(4,066,000 )	-
Net provision for inventory reserves	2,327,000	3,439,000
Net provision for (recovery of) customer payment discrepancies	612,000	(270,000 )
Net (recovery of) provision for doubtful accounts	(1,000 )	4,552,000
Deferred income taxes	(1,620,000 )	(3,264,000 )
Share-based compensation expense	2,555,000	1,786,000
Loss on disposal of plant and equipment	1,000	-
Changes in current assets and liabilities:		
Accounts receivable	(14,685,000)	11,481,000
Inventory	(13,696,000)	2,905,000
Inventory unreturned	227,000	(2,815,000 )
Prepaid expenses and other current assets	(1,917,000 )	2,462,000
Other assets	(4,045,000 )	(359,000 )
Accounts payable and accrued liabilities	3,945,000	(3,830,000 )
Customer finished goods returns accrual	(4,548,000 )	3,680,000
Long-term core inventory	(17,893,000)	(47,731,000)
Long-term core inventory deposits	-	26,002,000
Accrued core payments	(113,000 )	(8,896,000 )
Other liabilities	6,288,000	956,000
Net cash (used in) provided by operating activities	(20,810,000)	9,963,000
Cash flows from investing activities:		
Purchase of plant and equipment	(4,127,000 )	(3,168,000 )
Purchase of business	(705,000 )	(2,701,000 )
Change in short-term investments	11,000	(838,000 )
Net cash used in investing activities	(4,821,000 )	(6,707,000 )
Cash flows from financing activities:		
Borrowings under revolving loan	37,001,000	22,000,000
Repayments of revolving loan	(26,000,000)	(15,000,000)
Borrowings under term loan	-	25,000,000
Repayments of term loan	(2,344,000 )	(85,281,000)
Payments for debt issuance costs	(444,000 )	(2,337,000 )
Payments on capital lease obligations	(406,000 )	(268,000 )
Payment of contingent consideration	(314,000 )	-

Edgar Filing: MOTORCAR PARTS AMERICA INC - Form 10-Q

Exercise of stock options	1,475,000	3,051,000
Excess tax benefits from stock-based compensation	-	3,106,000
Cash used to net share settle equity awards	(1,058,000 )	(913,000 )
Net cash provided by (used in) financing activities	7,910,000	(50,642,000)
Effect of exchange rate changes on cash and cash equivalents	(235,000 )	(143,000 )
Net decrease in cash and cash equivalents	(17,956,000)	(47,529,000)
Cash and cash equivalents — Beginning of period	21,897,000	61,230,000
Cash and cash equivalents — End of period	\$3,941,000	\$13,701,000
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest, net	\$8,212,000	\$7,405,000
Income taxes, net of refunds	9,971,000	3,684,000
Non-cash investing and financing activities:		
Plant and equipment acquired under capital lease	\$802,000	\$1,591,000
Contingent consideration	-	1,320,000

The accompanying condensed notes to consolidated financial statements are an integral part hereof.

Table of Contents

MOTORCAR PARTS OF AMERICA, INC. AND SUBSIDIARIES

Condensed Notes to Consolidated Financial Statements

December 31, 2016

(Unaudited)

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended December 31, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ending March 31, 2017. This report should be read in conjunction with the Company’s audited consolidated financial statements and notes thereto for the fiscal year ended March 31, 2016, which are included in the Company’s Annual Report on Form 10-K filed with the Securities and Exchange Commission (“SEC”) on June 14, 2016, as amended by the Form 10-K/A filed with the SEC on July 29, 2016.

The accompanying consolidated financial statements have been prepared on a consistent basis with, and there have been no material changes to, except as noted below, the accounting policies described in Note 2, Summary of Significant Accounting Policies, to the consolidated financial statements that are presented in the Company’s Annual Report on Form 10-K for the fiscal year ended March 31, 2016.

1. Company Background and Organization

Motorcar Parts of America, Inc. and its subsidiaries (the “Company”, or “MPA”) is a leading manufacturer, remanufacturer, and distributor of aftermarket automotive parts. These replacement parts are sold for use on vehicles after initial vehicle purchase. These automotive parts are sold to automotive retail chain stores and warehouse distributors throughout North America and to major automobile manufacturers for both their aftermarket programs and warranty replacement programs (“OES”). The Company’s products include (i) rotating electrical products such as alternators and starters, (ii) wheel hub assemblies and bearings, (iii) brake master cylinders, and (iv) other products which include turbochargers and brake power boosters. The Company added turbochargers with its acquisition in July 2016. The Company began selling brake power boosters in August 2016.

The Company obtains used automotive parts, commonly known as Used Cores, primarily from its customers under the Company’s core exchange program. It also purchases Used Cores from vendors (core brokers). The customers grant credit to the consumer when the used part is returned to them, and the Company in turn provides a credit to the customers upon return to the Company. These Used Cores are an essential material needed for the remanufacturing operations.

The Company has remanufacturing, warehousing and shipping/receiving operations for automotive parts in North America and Asia. In addition, the Company utilizes various third party warehouse distribution centers in North America.

Pursuant to the guidance provided under the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”), for segment reporting, the Company has identified its chief executive officer as its chief operating decision maker (“CODM”), has reviewed the documents used by the CODM, and understands how such documents are used by the CODM to make financial and operating decisions. The Company has determined through this review process that it has one reportable segment for purposes of recording and reporting its financial results.



Table of Contents

2. New Accounting Pronouncements

Recently Adopted Accounting Standards

Share-based Compensation

In March 2016, the FASB issued guidance that simplifies several aspects of the accounting for share-based payment transactions and states that, among other things, all excess tax benefits and tax deficiencies should be recognized as income tax expense or benefit in the income statement and an entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. The new guidance is effective for interim and annual reporting periods beginning after December 15, 2016 with early adoption permitted. The Company early adopted this guidance effective April 1, 2016 which resulted in a cumulative-effect adjustment of \$892,000 through retained earnings and current deferred tax assets to record excess tax benefits not previously recognized. The Company has also elected to account for forfeitures as they occur using the modified retrospective approach which did not have any material impact on its consolidated balance sheets. In addition, the Company is now required to present excess tax benefits as an operating activity (combined with other income tax cash flows) on the statements of cash flows rather than as a financing activity and has elected to adopt this change prospectively.

Extraordinary Items

In January 2015, the FASB issued guidance that simplifies income statement presentation by eliminating the concept of extraordinary items. This guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. A reporting entity may apply the amendments prospectively or retrospectively to all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. There was no impact on the Company's consolidated financial statements from the adoption of this guidance.

Accounting Standards Not Yet Adopted

Revenue Recognition

In May 2014, the FASB issued guidance codified in ASC 606, "Revenue Recognition - Revenue from Contracts with Customers", which amends the guidance in the former ASC 605, "Revenue Recognition". The new guidance is effective for annual periods beginning after December 15, 2016, and interim periods within that reporting period for a public company. A full or modified retrospective transition method is required. In August 2015, the FASB delayed the effective date by one year to annual periods beginning after December 15, 2017, and interim periods within that reporting period for a public company. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. Accordingly, the updated standard is effective for the Company in the first quarter of fiscal 2019 and the Company does not plan to early adopt. The Company has not yet selected a transition method and is currently evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures.

Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern

In August 2014, the FASB issued guidance which requires an entity to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued). If conditions or events raise substantial doubt that is not alleviated, an entity should disclose that there is substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or

available to be issued), along with the principal conditions or events that raise substantial doubt, management's evaluation of the significance of those conditions or events in relation to the entity's ability to meet its obligations and management's plans that are intended to mitigate those conditions. The new guidance is effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. The Company does not expect any impact on its financial position, results of operations or cash flows from the adoption of this guidance.

## Table of Contents

### Inventory

In July 2015, the FASB issued guidance that requires an entity to measure inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. Subsequent measurement is unchanged for inventory measured using LIFO or the retail inventory method. The amendments in this update are effective for financial statements issued for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The amendments in this update should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period. The Company is currently evaluating the impact the provisions of this guidance will have on its consolidated financial statements.

### Income Taxes

In November 2015, the FASB issued guidance that requires deferred tax liabilities and assets to be classified as noncurrent in the consolidated balance sheet. The guidance is effective for fiscal years beginning after December 15, 2016 including interim periods within those fiscal years with early adoption permitted. A reporting entity should apply the amendment prospectively or retrospectively. The Company is currently evaluating the impact the provisions of this guidance will have on its consolidated financial statements.

### Financial Instruments

In January 2016, the FASB issued guidance that addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. A reporting entity should apply the new guidance by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The Company is currently evaluating the impact the provisions of this guidance will have on its consolidated financial statements.

### Leases

In February 2016, the FASB issued new guidance that requires balance sheet recognition of a right-of-use asset and lease liability by lessees for operating leases. The new guidance also requires new disclosures providing additional qualitative and quantitative information about the amounts recorded in the financial statements. The new guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The new guidance requires a modified retrospective approach with optional practical expedients. The Company is currently evaluating the impact the provisions of this guidance will have on its consolidated financial statements.

### Statement of Cash Flows

In August 2016, the FASB issued guidance which adds and/or clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. The new guidance is intended to reduce diversity in practice in how certain transactions are presented and classified in the statement of cash flows. The new guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years; early adoption is permitted. The Company does not expect any impact on its consolidated statements of cash flows from the adoption of this guidance.

### Business Combinations

In January 2017, the FASB issued guidance which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The new

guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. A reporting entity should apply the amendment prospectively. The Company is currently evaluating the impact the provisions of this guidance will have on its consolidated financial statements.



Table of Contents

## 3. Intangible Assets

The following is a summary of acquired intangible assets subject to amortization:

	Weighted Average Amortization Period	December 31, 2016		March 31, 2016	
		Gross Carrying Value	Accumulated Amortization	Gross Carrying Value	Accumulated Amortization
Intangible assets subject to amortization					
Trademarks	11 years	\$705,000	\$175,000	\$705,000	\$127,000
Non-compete agreement	1 year	33,000	21,000	-	-
Customer relationships	13 years	5,900,000	2,292,000	5,900,000	1,905,000
Total		\$6,638,000	\$2,488,000	\$6,605,000	\$2,032,000

Amortization expense for acquired intangible assets is as follows:

	Three Months Ended		Nine Months Ended	
	December 31, 2016	2015	December 31, 2016	2015
Amortization expense	\$166,000	\$145,000	\$456,000	\$476,000

The estimated future amortization expense for acquired intangible assets subject to amortization is as follows:

Year Ending March 31,

2017 - remaining three months	\$157,000
2018	580,000
2019	580,000
2020	580,000
2021	580,000
Thereafter	1,673,000
Total	\$4,150,000

## 4. Accounts Receivable — Net

Included in accounts receivable — net are significant offset accounts related to customer allowances earned, customer payment discrepancies, returned goods authorizations (“RGA”) issued for in-transit unit returns, estimated future credits to be provided for Used Cores returned by the customers and potential bad debts. Due to the forward looking nature and the different aging periods of certain estimated offset accounts, the offset accounts may not, at any point in time, directly relate to the balances in the accounts receivable-trade account.

Table of Contents

Accounts receivable — net is comprised of the following:

	December 31, 2016	March 31, 2016
Accounts receivable — trade	\$ 71,428,000	\$ 62,206,000
Allowance for bad debts	(4,137,000)	(4,284,000)
Customer allowances earned	(9,274,000)	(12,029,000)
Customer payment discrepancies	(1,173,000)	(703,000)
Customer returns RGA issued	(10,645,000)	(6,561,000)
Customer core returns accruals	(23,532,000)	(30,081,000)
Less: total accounts receivable offset accounts	(48,761,000)	(53,658,000)
Total accounts receivable — net	\$ 22,667,000	\$ 8,548,000

## Customer Finished Goods Returns Accrual

The Company allows its customers to return goods that their customers have returned to them, whether or not the returned item is defective (“warranty returns”). The Company accrues an estimate of its exposure to warranty returns based on a historical analysis of the level of this type of return as a percentage of total unit sales. Amounts charged to expense for these warranty returns are considered in arriving at the Company’s net sales. At December 31, 2016 and March 31, 2016, the Company’s total warranty return accrual was \$11,865,000 and \$10,845,000, respectively, of which \$6,444,000 and \$4,612,000, respectively, was included in the customer returns RGA issued balance in the above table for expected credits to be issued against accounts receivable and \$5,421,000 and \$6,233,000, respectively, was included in the customer finished goods returns accrual in the consolidated balance sheets for estimated future warranty returns.

Under customer agreements and general industry practice, customers are allowed stock adjustments if the inventory of certain product lines exceeds the inventory necessary to support sales to end-user consumers (“stock adjustment returns”). Customers have various contractual rights for stock adjustment returns which are typically less than 5% of units sold. In some instances, the Company allows a higher level of returns in connection with significant restocking orders. Stock adjustment returns do not occur at any specific time during the year.

As is standard in the industry, the Company only accepts returns from on-going customers. If a customer ceases doing business, the Company has no further obligation to accept additional product returns from that customer. Similarly, the Company accepts product returns and grants appropriate credits to new customers from the inception of the customer relationship. Based on information about stock levels, sell through information and return rate estimates for a particular customer obtained during the three months ended December 31, 2016, the Company updated its estimate for anticipated stock adjustment returns. This adjustment resulted in an increase in net sales and cost of goods sold for the unit value related to this inventory of \$9,261,000 and \$5,195,000, respectively, during the three months ended December 31, 2016. The impact on operating income from this change in estimate was \$4,066,000 for the three and nine months ended December 31, 2016. The impact on net income was \$2,551,000, which represents an increase in basic net income per share of \$0.14 and diluted net income per share of \$0.13 for both the three and nine months ended December 31, 2016.

The following summarizes the changes in the Company’s warranty return accrual:

	Three Months Ended		Nine Months Ended	
	December 31, 2016	December 31, 2015	December 31, 2016	December 31, 2015
Balance at beginning of period	\$ 13,707,000	\$ 10,204,000	\$ 10,845,000	\$ 10,904,000
Charged to expense/additions	22,930,000	18,463,000	73,803,000	58,276,000
Amounts processed	(24,772,000)	(20,307,000)	(72,783,000)	(60,820,000)

Balance at end of period	\$ 11,865,000	\$ 8,360,000	\$ 11,865,000	\$ 8,360,000
--------------------------	---------------	--------------	---------------	--------------

12

---

Table of Contents

## 5. Inventory

Inventory is comprised of the following:

	December 31, 2016	March 31, 2016
Non-core inventory		
Raw materials	\$ 23,074,000	\$ 17,394,000
Work-in-process	581,000	135,000
Finished goods	50,556,000	42,982,000
	74,211,000	60,511,000
Less allowance for excess and obsolete inventory	(2,871,000)	) (2,451,000)
Total	\$ 71,340,000	\$ 58,060,000
Inventory unreturned	\$ 5,098,000	\$ 10,520,000
Long-term core inventory		
Used cores held at the Company's facilities	\$ 42,036,000	\$ 34,405,000
Used cores expected to be returned by customers	12,104,000	10,781,000
Remanufactured cores held in finished goods	25,671,000	24,489,000
Remanufactured cores held at customers' locations (1)	178,607,000	172,600,000
	258,418,000	242,275,000
Less allowance for excess and obsolete inventory	(1,220,000)	) (1,175,000)
Total	\$ 257,198,000	\$ 241,100,000
Long-term core inventory deposits	\$ 5,569,000	\$ 5,569,000

---

(1) Remanufactured cores held at customers' locations represent the core portion of the Company's customers' finished goods at the Company's customers' locations.

## 6. Significant Customer and Other Information

## Significant Customer Concentrations

The Company's largest customers accounted for the following total percentage of net sales:

Sales	Three Months Ended		Nine Months Ended			
	December 31,		December 31,			
	2016	2015	2016	2015	2016	2015
Customer A	42 %	49 %	46 %	48 %		
Customer B	21 %	16 %	19 %	19 %		
Customer C	14 %	16 %	17 %	18 %		
Customer D	5 %	3 %	4 %	3 %		
Customer E	10 %	4 %	5 %	3 %		

The Company's largest customers accounted for the following total percentage of accounts receivable—trade:

Accounts receivable - trade	December 31, 2016	March 31, 2016
Customer A	45 %	37 %
Customer B	13 %	17 %
Customer C	9 %	15 %

Customer D	13	%	9	%
Customer E	2	%	4	%

13

---

Table of Contents

## Geographic and Product Information

The Company's products are predominantly sold in the U.S. and accounted for the following total percentage of net sales:

	Three Months Ended				Nine Months Ended			
	December 31,		December 31,		December 31,		December 31,	
	2016	2015	2016	2015	2016	2015	2016	2015
Rotating electrical products	81	%	78	%	78	%	80	%
Wheel hub products	15	%	19	%	18	%	19	%
Brake master cylinders products	3	%	3	%	4	%	1	%
Other products	1	%	-	%	-	%	-	%
	100	%	100	%	100	%	100	%

## Significant Supplier Concentrations

The Company had no suppliers that accounted for more than 10% of inventory purchases for the three and nine months ended December 31, 2016 and 2015.

## 7. Debt

The Company has the following credit agreements.

## Credit Facility

The Company is party to a \$125,000,000 senior secured financing (the "Credit Facility") with the lenders party thereto, and PNC Bank, National Association, as administrative agent, consisting of (i) a \$100,000,000 revolving loan facility, subject to borrowing base restrictions and a \$15,000,000 sublimit for letters of credit (the "Revolving Facility") and (ii) a \$25,000,000 term loan facility (the "Term Loans"). The loans under the Credit Facility mature on June 3, 2020. In connection with the Credit Facility, the lenders were granted a security interest in substantially all of the assets of the Company. The Credit Facility permits the payment of up to \$10,000,000 of dividends per calendar year, subject to a minimum availability threshold and pro forma compliance with financial covenants.

In May 2016, the Company entered into a consent and second amendment to the Credit Facility (the "Second Amendment") which, among other things, (i) increased the borrowing capacity of the Revolving Facility from \$100,000,000 to \$120,000,000, subject to certain borrowing base restrictions and a \$15,000,000 sublimit for letters of credit, (ii) amended the definition and calculation of consolidated EBITDA, (iii) increased the maximum of amount of capital expenditures, and (iv) made certain other amendments and modifications.

The Term Loans require quarterly principal payments of \$781,250. The Credit Facility bears interest at rates equal to either LIBOR plus a margin of 2.50%, 2.75% or 3.00% or a reference rate plus a margin of 1.50%, 1.75% or 2.00%, in each case depending on the senior leverage ratio as of the applicable measurement date. There is also a facility fee of 0.25% to 0.375%, depending on the senior leverage ratio as of the applicable measurement date. The interest rate on the Company's Term Loans and Revolving Facility was 3.12% and 4.09%, respectively, at December 31, 2016 and 2.94% and 3.53%, respectively, at March 31, 2016.

The Credit Facility, among other things, requires the Company to maintain certain financial covenants including a maximum senior leverage ratio and a minimum fixed charge coverage ratio. The Company was in compliance with all financial covenants as of December 31, 2016.

In addition to other covenants, the Credit Facility places limits on the Company's ability to incur liens, incur additional indebtedness, make loans and investments, engage in mergers and acquisitions, engage in asset sales, redeem or repurchase capital stock, alter the business conducted by the Company and its subsidiaries, transact with affiliates, prepay, redeem or purchase subordinated debt, and amend or otherwise alter debt agreements.

Table of Contents

The following summarizes information about the Company's Term Loans at:

	December 31, 2016	March 31, 2016
Principal amount of term loan	\$ 21,094,000	\$ 23,438,000
Unamortized financing fees	(339,000)	(391,000)
Net carrying amount of term loan	20,755,000	23,047,000
Less current portion of term loan	(3,064,000)	(3,067,000)
Long-term portion of term loan	\$ 17,691,000	\$ 19,980,000

Future repayments of the Company's Term Loans are as follows:

Year Ending March 31,

2017 - remaining three months	781,000
2018	3,125,000
2019	3,125,000
2020	3,125,000
2021	10,938,000
Total payments	\$21,094,000

The Company had \$18,001,000 and \$7,000,000 outstanding under the Revolving Facility at December 31, 2016 and March 31, 2016, respectively. In addition, \$260,000 was reserved for standby letters of credit for workers' compensation insurance and \$600,000 for commercial letters of credit at December 31, 2016. At December 31, 2016, \$101,139,000, subject to certain adjustments, was available under the Revolving Facility.

## WX Agreement

In August 2012, the Company entered into a Revolving Credit/Strategic Cooperation Agreement (the "WX Agreement") with Wanxiang America Corporation (the "Supplier") and the discontinued subsidiaries. In connection with the WX Agreement, the Company also issued a warrant (the "Supplier Warrant") to the Supplier to purchase up to 516,129 shares of the Company's common stock for an initial exercise price of \$7.75 per share exercisable at any time after August 22, 2014 and on or prior to September 30, 2017. The exercise price is subject to adjustments, among other things, for sales of common stock by the Company at a price below the exercise price.

The fair value of the Supplier Warrant using level 3 inputs and the Monte Carlo simulation model was \$9,916,000 and \$15,643,000 at December 31, 2016 and March 31, 2016, respectively. These amounts are included in other liabilities in the consolidated balance sheets. The warrant liability continues to be classified as a noncurrent liability at December 31, 2016 as the Company does not expect to settle this amount in cash. During the three months ended December 31, 2016 and 2015, a gain of \$962,000 and a loss of \$1,275,000, respectively, were recorded in general and administrative expenses due to the change in the fair value of this warrant liability. During the nine months ended December 31, 2016 and 2015, a gain of \$5,727,000 and a loss of \$3,017,000, respectively, were recorded in general and administrative expenses due to the change in the fair value of this warrant liability.

## 8. Accounts Receivable Discount Programs

The Company uses receivable discount programs with certain customers and their respective banks. Under these programs, the Company may sell those customers' receivables to those banks at a discount to be agreed upon at the time the receivables are sold. These discount arrangements allow the Company to accelerate receipt of payment on customers' receivables.





Table of Contents

The following is a summary of the Company's accounts receivable discount programs:

	Nine Months Ended			
	December 31,			
	2016	2015		
Receivables discounted	\$254,795,000	\$248,443,000		
Weighted average days	341	342		
Annualized weighted average discount rate	2.9	%	2.2	%
Amount of discount as interest expense	\$6,864,000	\$5,241,000		

## 9. Net Income Per Share

Basic net income per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted net income per share includes the effect, if any, from the potential exercise or conversion of securities, such as stock options and warrants, which would result in the issuance of incremental shares of common stock.

The following presents a reconciliation of basic and diluted net income per share:

	Three Months Ended		Nine Months Ended	
	December 31,		December 31,	
	2016	2015	2016	2015
Net income	\$11,110,000	\$7,748,000	\$27,761,000	\$8,266,000
Basic shares	18,675,125	18,319,531	18,587,946	18,180,039
Effect of potentially dilutive securities	766,140	776,173	811,911	801,382
Diluted shares	19,441,265	19,095,704	19,399,857	18,981,421
Net income per share:				
Basic net income per share	\$0.59	\$0.42	\$1.49	\$0.45
Diluted net income per share	\$0.57	\$0.41	\$1.43	\$0.44

The effect of dilutive options excludes (i) 292,415 shares subject to options with exercise prices ranging from \$26.47 to \$34.17 per share for the three months ended December 31, 2016, (ii) 291,215 shares subject to options with exercise prices ranging from \$28.68 to \$34.17 per share for the nine months ended December 31, 2016, and (iii) 1,100 shares subject to options with an exercise price of \$34.17 per share for the nine months ended December 31, 2015, which were anti-dilutive. There were no anti-dilutive options or warrants for the three months ended December 31, 2015.

## 10. Income Taxes

The Company recorded income tax expenses for the three months ended December 31, 2016 and 2015 of \$5,678,000, or an effective tax rate of 33.8%, and \$6,451,000, or an effective tax rate of 45.4%. The Company recorded income tax expenses for the nine months ended December 31, 2016 and 2015 of \$13,459,000, or an effective tax rate of 32.7%, and \$6,821,000, or an effective tax rate of 45.2%, respectively. The Company's income tax rates for the three and nine months ended December 31, 2016 were positively impacted by \$34,000 and \$624,000, respectively, of excess tax benefits reflected in income tax expense as a result of the early adoption of the FASB's new guidance on share-based compensation. The income tax rates for the three and nine months ended December 31, 2016 were further impacted by a non-taxable gain in connection with the fair value adjustment on the warrants compared to a non-deductible loss for the three and nine months ended December 31, 2015. In addition, the income tax rates for all periods are increased by the inclusion of state income taxes and non-deductible executive compensation under Internal

Revenue Code Section 162(m). These increases in all periods were partially offset by the benefit of lower statutory tax rates in foreign taxing jurisdictions.

## Table of Contents

The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions with varying statutes of limitations. The Internal Revenue Services (“IRS”) audit for the fiscal years ended March 31, 2011, 2012, 2013, and 2014 were collectively concluded in May 2016. It was primarily agreed that the Company’s approximately \$80,000,000 of ordinary bad debt deduction would be disallowed on its March 31, 2013 return and instead would be reclassified as deductible section 165(g)(3) loss on its March 31, 2014 return. Pursuant to this IRS exam adjustment, and certain other less significant findings, the disallowed losses which were carried back to offset taxable income on the Company’s March 31, 2011 return were reclaimed by the IRS. However the same losses, reclassified as noted above, were carried back two years to offset taxable income on the Company’s March 31, 2012 and 2013 tax returns. The remaining net operating losses were carried forward on to the Company’s March 31, 2014 tax return, and to the extent additional net operating losses remain will also offset taxable income in future years.

The impact of the reclassification and other findings resulted in no material increase in tax expense from changes in taxable income, but the Company incurred additional interest charges of approximately \$460,000. These charges were accrued for in the final quarter of the year ended March 31, 2016. There is no impact from the conclusion of these audits in the income tax expenses for the current period ended December 31, 2016.

The Company is also under examination by the State of California for the years ended March 31, 2013 and 2014. The Company is not under examination in any another jurisdiction. The Company believes no significant changes in the unrecognized tax benefits will occur within the next 12 months.

## 11. Financial Risk Management and Derivatives

Purchases and expenses denominated in currencies other than the U.S. dollar, which are primarily related to the Company’s facilities overseas, expose the Company to market risk from material movements in foreign exchange rates between the U.S. dollar and the foreign currencies. The Company’s primary risk exposure is from fluctuations in the value of the Mexican peso and to a lesser extent the Chinese yuan. To mitigate these risks, the Company enters into forward foreign currency exchange contracts to exchange U.S. dollars for these foreign currencies. The extent to which forward foreign currency exchange contracts are used is modified periodically in response to the Company’s estimate of market conditions and the terms and length of anticipated requirements.

The Company enters into forward foreign currency exchange contracts in order to reduce the impact of foreign currency fluctuations and not to engage in currency speculation. The use of derivative financial instruments allows the Company to reduce its exposure to the risk that the eventual cash outflow resulting from funding the expenses of the foreign operations will be materially affected by changes in exchange rates between the U.S. dollar and the foreign currencies. The Company does not hold or issue financial instruments for trading purposes. The forward foreign currency exchange contracts are designated for forecasted expenditure requirements to fund foreign operations.

The Company had forward foreign currency exchange contracts with a U.S. dollar equivalent notional value of \$27,433,000 and \$18,917,000 at December 31, 2016 and March 31, 2016, respectively. These contracts generally have a term of one year or less, at rates agreed at the inception of the contracts. The counterparty to this derivative transaction is a major financial institution with investment grade credit rating; however, the Company is exposed to credit risk with this institution. The credit risk is limited to the potential unrealized gains (which offset currency fluctuations adverse to the Company) in any such contract should this counterparty fail to perform as contracted. Any changes in the fair values of forward foreign currency exchange contracts are reflected in current period earnings and accounted for as an increase or offset to general and administrative expenses.

Table of Contents

The following shows the effect of the Company's derivative instruments on its consolidated statements of operations:

Derivatives Not Designated as Hedging Instruments	Gain (Loss) Recognized within General and Administrative Expenses			
	Three Months Ended December 31,		Nine Months Ended December 31,	
	2016	2015	2016	2015
Forward foreign currency exchange contracts	\$ (964,000	) \$ 245,000	\$ (2,150,000	) \$ (104,000

The fair value of the forward foreign currency exchange contracts of \$2,566,000 and \$416,000 is included in other current liabilities in the consolidated balance sheets at December 31, 2016 and March 31, 2016, respectively.

## 12. Fair Value Measurements

The following summarizes the Company's financial assets and liabilities measured at fair value, by level within the fair value hierarchy:

	December 31, 2016				March 31, 2016			
	Fair Value Measurements Using Inputs Considered as				Fair Value Measurements Using Inputs Considered as			
	Fair Value	Level 1	Level 2	Level 3	Fair Value	Level 1	Level 2	Level 3
<b>Assets</b>								
<b>Short-term investments</b>								
Mutual funds	\$ 1,966,000	\$ 1,966,000	-	-	\$ 1,813,000	\$ 1,813,000	-	-
<b>Liabilities</b>								
<b>Accrued liabilities</b>								
Contingent consideration	-	-	-	-	224,000	-	-	\$ 224,000
<b>Other current liabilities</b>								
Deferred compensation	1,966,000	1,966,000	-	-	1,813,000	1,813,000	-	-
<b>Forward foreign currency exchange contracts</b>								
	2,566,000	-	\$ 2,566,000	-	416,000	-	\$ 416,000	-
<b>Other liabilities</b>								
Warrant liability	9,916,000	-	-	\$ 9,916,000	15,643,000	-	-	15,643,000
Contingent consideration	-	-	-	-	106,000	-	-	106,000

## Short-term Investments and Deferred Compensation

The Company's short-term investments, which fund its deferred compensation liabilities, consist of investments in mutual funds. These investments are classified as Level 1 as the shares of these mutual funds trade with sufficient

frequency and volume to enable the Company to obtain pricing information on an ongoing basis.

#### Forward Foreign Currency Exchange Contracts

The forward foreign currency exchange contracts are primarily measured based on the foreign currency spot and forward rates quoted by the banks or foreign currency dealers. During the three months ended December 31, 2016 and 2015, a loss of \$964,000 and a gain of \$245,000, respectively, were recorded in general and administrative expenses due to the change in the value of the forward foreign currency exchange contracts. During the nine months ended December 31, 2016 and 2015, a loss of \$2,150,000 and \$104,000, respectively, were recorded in general and administrative expenses due to the change in the value of the forward foreign currency exchange contracts.

#### Warrant Liability

The Company estimates the fair value of the warrant liability using level 3 inputs and the Monte Carlo simulation model at each balance sheet date. This warrant liability is included in other liabilities in the consolidated balance sheets. Any subsequent changes from the initial recognition in the fair value of the warrant liability are recorded in current period earnings as a general and administrative expense. During the three months ended December 31, 2016 and 2015, a gain of \$962,000 and a loss of \$1,275,000, respectively, were recorded in general and administrative expenses due to the change in the fair value of this warrant liability. During the nine months ended December 31, 2016 and 2015, a gain of \$5,727,000 and a loss of \$3,017,000, respectively, were recorded in general and administrative expenses due to the change in the fair value of this warrant liability.

Table of Contents

The following assumptions were used to determine the fair value of the Supplier Warrant:

	Supplier Warrant	
Risk free interest rate	0.74	%
Expected life in years	0.75	
Expected volatility	39.90	%
Dividend yield	-	
Probability of future financing	0	%

The risk free interest rate used was based on U.S. treasury-note yields with terms commensurate with the remaining term of the warrant. The expected life is based on the remaining contractual term of the warrant and the expected volatility is based on the Company's daily historical volatility over a period commensurate with the remaining term of the warrant.

## Contingent Consideration

The Company estimated the fair value of the contingent consideration liability using level 3 inputs and an option-pricing model at each balance sheet date. This amount was recorded in accrued expenses in the Company's consolidated balance sheet at March 31, 2016. Any subsequent changes from the initial recognition in the fair value of the contingent consideration were recorded in current period earnings as a general and administrative expense. On June 21, 2016, the Company entered into a full release and settlement agreement with former owners of OE Plus Ltd., pursuant to which the Company agreed to pay \$314,000 in full and complete satisfaction of all payments of any sort otherwise owed by the Company in connection with the May 2015 asset purchase agreement. This amount was paid in full on July 6, 2016. During the nine months ended December 31, 2016, a gain of \$16,000 was recorded in general and administrative expenses due to the change in the fair value of the contingent consideration. During the three and nine months ended December 31, 2015, a loss of \$40,000 and \$60,000, respectively, was recorded in general and administrative expenses due to the change in the fair value of the contingent consideration.

The following summarizes the activity for Level 3 fair value measurements:

	Three Months Ended December 31,				Nine Months Ended December 31,			
	2016		2015		2016		2015	
	Supplier Warrant	Contingent Consideration	Supplier Warrant	Contingent Consideration	Supplier Warrant	Contingent Consideration	Supplier Warrant	Contingent Consideration
Beginning balance	\$10,878,000	\$-	\$12,248,000	\$1,340,000	\$15,643,000	\$330,000	\$10,506,000	\$-
Newly issued	-	-	-	-	-	-	-	1,320,000
Total (gain) loss included in net income (loss)	(962,000 )	-	1,275,000	40,000	(5,727,000 )	(16,000 )	3,017,000	60,000
Exercises/settlements	-	-	-	-	-	(314,000)	-	-
Net transfers in (out) of Level 3	-	-	-	-	-	-	-	-
Ending balance	\$9,916,000	\$-	\$13,523,000	\$1,380,000	\$9,916,000	\$-	\$13,523,000	\$1,380,000

During the three and nine months ended December 31, 2016, the Company had no significant measurements of assets or liabilities at fair value on a nonrecurring basis subsequent to their initial recognition.

The carrying amounts of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate their fair value due to the short-term nature of these instruments. The carrying amounts of the revolving loan, term loan and other long-term liabilities approximate their fair value based on the variable nature of interest rates

and current rates for instruments with similar characteristics.

19

---



Table of Contents

## 13. Share-based Payments

## Stock Options

The Company granted options to purchase 184,000 and 111,222 shares of common stock during the nine months ended December 31, 2016 and 2015, respectively. The cost associated with stock options is estimated using the Black-Scholes option-pricing model. This model requires the input of subjective assumptions including the expected volatility of the underlying stock and the expected holding period of the option. These subjective assumptions are based on both historical and other information. Changes in the values assumed and used in the model can materially affect the estimate of fair value.

The following assumptions were used to derive the weighted average fair value of the stock options granted:

	Nine Months Ended	
	December 31,	
	2016	2015
Weighted average risk free interest rate	1.38 %	1.73 %
Weighted average expected holding period (years)	5.84	5.76
Weighted average expected volatility	47.42 %	46.84 %
Weighted average expected dividend yield	-	-
Weighted average fair value of options granted	\$ 13.07	\$ 14.14

The following is a summary of stock option transactions:

	Number of Shares	Weighted Average Exercise Price
Outstanding at March 31, 2016	984,066	\$ 11.98
Granted	184,000	\$ 28.67
Exercised	(108,997 )	\$ 13.53
Cancelled	-	\$ -
Outstanding at December 31, 2016	1,059,069	\$ 14.72

At December 31, 2016, options to purchase 283,102 shares of common stock were unvested at the weighted average exercise price of \$13.02.

At December 31, 2016, there was \$3,025,000 of total unrecognized compensation expense related to unvested stock option awards. The compensation expense is expected to be recognized over a weighted average vesting period of approximately 2.1 years.

## Restricted Stock or Restricted Stock Units (collectively "RS")

During the nine months ended December 31, 2016 and 2015, the Company granted 55,469 and 49,702 shares of RS, respectively, with an estimated grant date fair value of \$1,574,000 and \$1,566,000, respectively, which was based on the closing market price on the grant date.

The following is a summary of non-vested RS:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-vested at March 31, 2016	153,527	\$ 22.28

Edgar Filing: MOTORCAR PARTS AMERICA INC - Form 10-Q

Granted	55,469	\$	28.37
Vested	(89,617 )	\$	18.14
Cancelled	-	\$	-
Non-vested at December 31, 2016	119,379	\$	28.22

At December 31, 2016, there was \$2,573,000 of unrecognized compensation expense related to these awards, which will be recognized over the remaining vesting period of approximately 1.8 years.

Table of Contents

## 14. Accumulated Other Comprehensive Income (Loss)

The following summarizes changes in accumulated other comprehensive income (loss):

	Three Months Ended December 31, 2016			Three Months Ended December 31, 2015		
	Unrealized Gain on Short-Term Investments	Foreign Currency Translation	Total	Unrealized Gain (Loss) on Short-Term Investments	Foreign Currency Translation	Total
Balance at beginning of period	\$ 420,000	\$ (6,526,000 )	\$ (6,106,000 )	\$ 286,000	\$ (4,636,000 )	\$ (4,350,000 )
Other comprehensive income (loss), net of tax	10,000	(1,252,000 )	(1,242,000 )	42,000	(422,000 )	(380,000 )
Amounts reclassified from accumulated other comprehensive loss, net of tax	-	-	-	-	-	-
Balance at end of period	\$ 430,000	\$ (7,778,000 )	\$ (7,348,000 )	\$ 328,000	\$ (5,058,000 )	\$ (4,730,000 )

	Nine Months Ended December 31, 2016			Nine Months Ended December 31, 2015		
	Unrealized Gain on Short-Term Investments	Foreign Currency Translation	Total	Unrealized Gain (Loss) on Short-Term Investments	Foreign Currency Translation	Total
Balance at beginning of period	\$ 332,000	\$ (5,184,000 )	\$ (4,852,000 )	\$ 345,000	\$ (2,863,000 )	\$ (2,518,000 )
Other comprehensive income (loss), net of tax	98,000	(2,594,000 )	(2,496,000 )	(17,000 )	(2,195,000 )	(2,212,000 )
Amounts reclassified from accumulated other comprehensive loss, net of tax	-	-	-	-	-	-
Balance at end of period	\$ 430,000	\$ (7,778,000 )	\$ (7,348,000 )	\$ 328,000	\$ (5,058,000 )	\$ (4,730,000 )

## 15. Acquisitions

On July 21, 2016, the Company completed the acquisition of certain assets and assumption of certain liabilities of Zor Industries USA LLC (“ZOR”), a privately held manufacturer and remanufacturer of turbochargers based in Winchester, Virginia. The acquisition was consummated pursuant to an asset purchase agreement for a purchase price of \$705,000. The assets and results of operations of ZOR were not significant to the Company’s consolidated financial position or results of operations, and thus pro forma information is not presented.

Table of Contents

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

The following discussion and analysis presents factors that Motorcar Parts of America, Inc. and its subsidiaries ("our," "we" or "us") believe are relevant to an assessment and understanding of our consolidated financial position and results of operations. This financial and business analysis should be read in conjunction with our March 31, 2016 audited consolidated financial statements included in our Annual Report on Form 10-K filed with the SEC on June 14, 2016, as amended by the Form 10-K/A filed with the SEC on July 29, 2016.

Disclosure Regarding Private Securities Litigation Reform Act of 1995

This report contains certain forward-looking statements with respect to our future performance that involve risks and uncertainties. Various factors could cause actual results to differ materially from those projected in such statements. These factors include, but are not limited to: concentration of sales to a small number of customers, changes in the financial condition of or our relationship with any of our major customers, increases in the average accounts receivable collection period, the loss of sales to customers, delays in payments by customers, the increasing customer pressure for lower prices and more favorable payment and other terms, lower revenues than anticipated from new and existing contracts, the increasing demands on our working capital, the significant strain on working capital associated with large inventory purchases from customers, any meaningful difference between expected production needs and ultimate sales to our customers, investments in operational changes or acquisitions, our ability to obtain any additional financing we may seek or require, our ability to achieve positive cash flows from operations, potential future changes in our previously reported results as a result of the identification and correction of errors in our accounting policies or procedures or the potential material weaknesses in our internal controls over financial reporting, our failure to meet the financial covenants or the other obligations set forth in our credit agreement and the lenders' refusal to waive any such defaults, increases in interest rates, the impact of high gasoline prices, consumer preferences and general economic conditions, increased competition in the automotive parts industry including increased competition from Chinese and other offshore manufacturers, difficulty in obtaining Used Cores and component parts or increases in the costs of those parts, political, criminal or economic instability in any of the foreign countries where we conduct operations, currency exchange fluctuations, unforeseen increases in operating costs, risks associated with cyber-attacks, risks associated with conflict minerals, and other factors discussed herein and in our other filings with the SEC.

Management Overview

We are a leading manufacturer, remanufacturer, and distributor of aftermarket automotive parts for import and domestic cars, light trucks, heavy duty, agricultural and industrial applications. We sell our products predominantly in North America to the largest auto parts retail and traditional warehouse chains and to major automobile manufacturers for both their aftermarket programs and their OES programs. Our products include (i) rotating electrical products such as alternators and starters, (ii) wheel hub assemblies and bearings, (iii) brake master cylinders, and (iv) other products which include turbochargers and brake power boosters. We added turbochargers with our acquisition in July 2016. We began selling brake power boosters in August 2016.

The aftermarket for automobile parts is divided into two markets. The first is the DIY market, which is generally serviced by the large retail chain outlets. Consumers who purchase parts from the DIY channel generally install parts into their vehicles themselves. In most cases, this is a less expensive alternative than having the repair performed by a professional installer. The second is the professional installer market, commonly known as the DIFM market. This market is generally serviced by the traditional warehouse distributors, the dealer networks, and the commercial divisions of retail chains. Generally, the consumer in this channel is a professional parts installer. Our products are distributed to both the DIY and DIFM markets.

Pursuant to the guidance provided under the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”), for segment reporting, we have identified our chief executive officer as our chief operating decision maker (“CODM”), have reviewed the documents used by the CODM, and understand how such documents are used by the CODM to make financial and operating decisions. We have determined through this review process that we have one reportable segment for purposes of recording and reporting our financial results.

Table of Contents

## Results of Operations for the Three Months Ended December 31, 2016 and 2015

The following discussion and analysis should be read in conjunction with the financial statements and notes thereto appearing elsewhere herein.

The following summarizes certain key operating data:

	Three Months Ended			
	December 31,			
	2016		2015	
Gross profit percentage	28.7	%	30.7	%
Cash flow provided by (used in) operations	\$1,506,000		\$(9,214,000)	
Finished goods turnover (annualized) (1)	6.3		6.6	

---

(1) Annualized finished goods turnover for the fiscal quarter is calculated by multiplying cost of goods sold for the quarter by 4 and dividing the result by the average between beginning and ending non-core finished goods inventory values for the fiscal quarter. We believe this provides a useful measure of our ability to turn our inventory into revenues.

## Net Sales and Gross Profit

The following summarizes net sales and gross profit:

	Three Months Ended			
	December 31,			
	2016		2015	
Net sales	\$112,595,000		\$94,022,000	
Cost of goods sold	80,225,000		65,123,000	
Gross profit	32,370,000		28,899,000	
Gross profit percentage	28.7	%	30.7	%

Net Sales. Our net sales for the three months ended December 31, 2016 increased by \$18,573,000, or 19.8%, to \$112,595,000 compared to net sales for the three months ended December 31, 2015 of \$94,022,000. The increase in our net sales was attributable to higher sales of rotating electrical products, brake master cylinders and the introduction of brake power boosters. \$9,261,000 of this increase is due to the change in estimate in our accrual for anticipated stock adjustment returns.

Gross Profit. Our gross profit percentage was 28.7% for the three months ended December 31, 2016 compared to 30.7% for the three months ended December 31, 2015. Our gross profit for the three months ended December 31, 2016 was impacted by volume and stock update discounts for rotating electrical products. In addition, our gross profit percentage for the three months ended December 31, 2016 was further impacted by \$258,000 for customer allowances related to new business. This decrease was partially offset by a 1.3% increase from the change in estimate relating to stock adjustments. In the prior year's three months ended December 31, 2015, the gross profit included a cost of goods sold impact of \$176,000 for inventory step-up amortization.

Table of Contents

## Operating Expenses

The following summarizes operating expenses:

	Three Months Ended December 31,	
	2016	2015
General and administrative	\$7,952,000	\$8,802,000
Sales and marketing	3,234,000	2,671,000
Research and development	1,039,000	711,000

## Percent of net sales

General and administrative	7.1	%	9.4	%
Sales and marketing	2.9	%	2.8	%
Research and development	0.9	%	0.8	%

**General and Administrative.** Our general and administrative expenses for the three months ended December 31, 2016 were \$7,952,000, which represents a decrease of \$850,000, or 9.7%, from general and administrative expenses for the three months ended December 31, 2015 of \$8,802,000. The reduction was primarily due to (i) \$4,624,000 of decreased bad debt expense as compared to the three months ended December 31, 2015, which included expense resulting from the bankruptcy filing by one of our customers, (ii) a \$962,000 gain recorded due to the change in the fair value of the warrant liability during the three months ended December 31, 2016 compared to a \$1,275,000 loss recorded during the three months ended December 31, 2015, and (iii) \$732,000 of decreased legal expense. These decreases were partially offset by (i) a \$5,800,000 gain in connection with the settlement of litigation with Fenwick Automotive Products Limited and various of its subsidiaries during the three months ended December 31, 2015 and (ii) a \$964,000 loss recorded due to the change in the fair value of the forward foreign currency exchange contracts during the three months ended December 31, 2016 compared to a \$245,000 gain recorded during the three months ended December 31, 2015.

**Sales and Marketing.** Our sales and marketing expenses for the three months ended December 31, 2016 increased \$563,000, or 21.1%, to \$3,234,000 from \$2,671,000 for the three months ended December 31, 2015. The increase was due primarily to our growth initiatives and increased commissions.

**Research and Development.** Our research and development expenses increased by \$328,000, or 46.1%, to \$1,039,000 for the three months ended December 31, 2016 from \$711,000 for the three months ended December 31, 2015, due primarily to our growth initiatives.

## Interest Expense

**Interest Expense, net.** Our interest expense, net for the three months ended December 31, 2016 increased \$841,000, or 33.4%, to \$3,357,000 from \$2,516,000 for the three months ended December 31, 2015. The increase in interest expense was due primarily to higher interest rates on (i) our accounts receivable discount programs and (ii) higher average outstanding balances on our revolving facility.

## Provision for Income Taxes

**Income Tax.** Our income tax expense for the three months ended December 31, 2016 and 2015 was \$5,678,000, or an effective tax rate of 33.8%, and \$6,451,000, or an effective tax rate of 45.4%, respectively. Our income tax rate for the three months ended December 31, 2016 was positively impacted by (i) a non-taxable gain in connection with the fair

value adjustments on the warrants compared to a non-deductible loss for the three months ended December 31, 2015 and (ii) \$34,000 of excess tax benefits as a result of the early adoption of the FASB's new guidance on share-based compensation. In addition, the income tax rates for all periods are increased by the inclusion of state income taxes and non-deductible executive compensation under Internal Revenue Code Section 162(m). These increases in all periods were partially offset by the benefit of lower statutory tax rates in foreign taxing jurisdictions.



Table of Contents

## Results of Operations for the Nine Months Ended December 31, 2016 and 2015

The following discussion and analysis should be read in conjunction with the financial statements and notes thereto appearing elsewhere herein.

The following summarizes certain key operating data:

	Nine Months Ended			
	December 31,			
	2016		2015	
Gross profit percentage	27.2	%	28.3	%
Cash flow (used in) provided by operations	\$(20,810,000)		\$9,963,000	
Finished goods turnover (annualized) (1)	6.4		6.5	

---

Annualized finished goods turnover for the period is calculated by multiplying cost of goods sold for the period by (1) 1.33 and dividing the result by the average between beginning and ending non-core finished goods inventory values for the period. We believe this provides a useful measure of our ability to turn our inventory into revenues.

## Net Sales and Gross Profit

The following summarizes net sales and gross profit:

	Nine Months Ended			
	December 31,			
	2016		2015	
Net sales	\$306,843,000		\$271,527,000	
Cost of goods sold	223,424,000		194,817,000	
Gross profit	83,419,000		76,710,000	
Gross profit percentage	27.2	%	28.3	%

Net Sales. Our net sales for the nine months ended December 31, 2016 increased by \$35,316,000, or 13.0%, to \$306,843,000 compared to net sales for the nine months ended December 31, 2015 of \$271,527,000. The increase in our net sales was across all existing product lines. \$9,261,000 of this increase is due to the change in estimate in our accrual for anticipated stock adjustment returns. This increase was partially offset by allowances and returns related to new business as discussed below in the Gross Profit paragraph.

Gross Profit. Our gross profit percentage decreased to 27.2% for the nine months ended December 31, 2016 from 28.3% for the nine months ended December 31, 2015. Our gross profit for the nine months ended December 31, 2016 was impacted by \$12,215,000 for customer allowances and initial return and stock adjustment accruals related to new business less a cost of goods sold offset of \$568,000, and a cost of goods sold impact of \$140,000 for start-up costs incurred related to our launch of brake power boosters. This decrease was partially offset by a 0.5% increase from the change in estimate relating to stock adjustments. Our gross profit for the nine months ended December 31, 2015 was impacted by \$10,863,000 for customer allowances related to new business less a cost of goods sold offset of \$809,000, and a cost of goods sold impact of \$321,000 for inventory step-up amortization.

Table of Contents

## Operating Expenses

The following summarizes operating expenses:

	Nine Months Ended December 31,	
	2016	2015
General and administrative	\$21,446,000	\$38,381,000
Sales and marketing	8,575,000	7,583,000
Research and development	2,813,000	2,093,000

## Percent of net sales

General and administrative	7.0	%	14.1	%
Sales and marketing	2.8	%	2.8	%
Research and development	0.9	%	0.8	%

**General and Administrative.** Our general and administrative expenses for the nine months ended December 31, 2016 were \$21,446,000, which represents a decrease of \$16,935,000, or 44.1%, from general and administrative expenses for the nine months ended December 31, 2015 of \$38,381,000. The reduction was primarily due to (i) a \$5,727,000 gain recorded due to the change in the fair value of the warrant liability during the nine months ended December 31, 2016 compared to a loss of \$3,017,000 recorded during the nine months ended December 31, 2015, (ii) \$7,251,000 of decreased legal expense as compared to the nine months ended December 31, 2015, which included \$9,250,000 accrued for the litigation settlement in the bankruptcy cases related to the discontinued subsidiaries partially offset by a \$5,800,000 gain in connection with the settlement of litigation with Fenwick Automotive Products Limited and various of its subsidiaries, and (iii) \$4,553,000 of decreased bad debt expense as compared to the nine months ended December 31, 2015, which included expense resulting from the bankruptcy filing by one of our customers. These decreases were partially offset by (i) \$2,046,000 of increased loss recorded due to the change in the fair value of the forward foreign currency exchange contracts, (ii) \$797,000 of increased general and administrative expenses at our offshore locations due primarily to our growth initiatives, and (iii) \$769,000 of increased share-based compensation.

**Sales and Marketing.** Our sales and marketing expenses for the nine months ended December 31, 2016 increased \$992,000, or 13.1%, to \$8,575,000 from \$7,583,000 for the nine months ended December 31, 2015. The increase was due primarily to our growth initiatives.

**Research and Development.** Our research and development expenses increased by \$720,000, or 34.4%, to \$2,813,000 for the nine months ended December 31, 2016 from \$2,093,000 for the nine months ended December 31, 2015, due primarily to our growth initiatives.

## Interest Expense

**Interest Expense, net.** Our interest expense, net for the nine months ended December 31, 2016 decreased \$4,201,000, or 31.0%, to \$9,365,000 from \$13,566,000 for the nine months ended December 31, 2015. The decrease in interest expense was due primarily to (i) the write-off of previous debt issuance costs of \$5,108,000 in connection with the financing agreement which was terminated when we entered into a new credit facility in June 2015 and (ii) lower interest rates and lower average outstanding balances on our loans. These decreases in interest expense were partially offset by higher interest rates and increased use of our accounts receivable discount programs during the nine months ended December 31, 2016.

## Provision for Income Taxes

Income Tax. Our income tax expense for the nine months ended December 31, 2016 and 2015 was \$13,459,000, or an effective tax rate of 32.7%, and \$6,821,000, or an effective tax rate of 45.2%, respectively. Our income tax rate for the nine months ended December 31, 2016 was positively impacted by (i) a non-taxable gain in connection with the fair value adjustments on the warrants compared to a non-deductible loss for the nine months ended December 31, 2015 and (ii) \$624,000 of excess tax benefits as a result of the early adoption of the FASB's new guidance on share-based compensation. In addition, the income tax rates for all periods are increased by the inclusion of state income taxes and non-deductible executive compensation under Internal Revenue Code Section 162(m). These increases in all periods were partially offset by the benefit of lower statutory tax rates in foreign taxing jurisdictions.

Table of Contents

## Liquidity and Capital Resources

## Overview

At December 31, 2016, we had working capital of \$3,943,000, a ratio of current assets to current liabilities of 1.03:1.00, and cash of \$3,941,000, compared to working capital of \$8,702,000, a ratio of current assets to current liabilities of 1.10:1.00, and cash of \$21,897,000 at March 31, 2016. We generated cash during the nine months ended December 31, 2016 from the use of receivable discount programs with certain of our major customers and their respective banks, as well as from our credit facility. The cash generated from these activities was used primarily to make payments for certain customer allowances and initial return and stock adjustment accruals in connection with new business and to build our inventory levels to support higher sales.

We believe our cash and cash equivalents, short-term investments, use of receivable discount programs, amounts available under our credit facility, and other sources are sufficient to satisfy our expected future working capital needs, repayment of the current portion of our term loans, capital lease commitments, and capital expenditure obligations over the next 12 months.

## Share Repurchase Program

On June 9, 2016, our board of directors approved a stock repurchase program of up to \$10,000,000 of our outstanding common stock, at prices deemed appropriate by management. This program replaces our existing \$5,000,000 repurchase program, announced in March 2010, pursuant to which we had purchased 67,347 shares for a total of \$389,000, which leaves \$9,611,000 available for repurchases under the new stock repurchase program.

## Cash Flows

The following summarizes cash flows as reflected in the consolidated statements of cash flows:

	Nine Months Ended December 31,	
	2016	2015
Cash provided by (used in):		
Operating activities	\$(20,810,000)	\$9,963,000
Investing activities	(4,821,000 )	(6,707,000 )
Financing activities	7,910,000	(50,642,000)
Effect of exchange rates on cash and cash equivalents	(235,000 )	(143,000 )
Net decrease in cash and cash equivalents	\$(17,956,000)	\$(47,529,000)
Additional selected cash flow data:		
Depreciation and amortization	\$2,718,000	\$2,213,000
Capital expenditures	4,127,000	3,168,000

Net cash used in operating activities was \$20,810,000 during the nine months ended December 31, 2016 compared to net cash provided by operating activities of \$9,963,000 during the nine months ended December 31, 2015. The significant changes in our operating activities were due primarily to (i) an increase in accounts receivable during the nine months ended December 31, 2016 compared to a decrease during the nine months ended December 31, 2015, (ii) payments made in connection with new business, and (iii) increased inventory levels to support our future growth.

Net cash used in investing activities was \$4,821,000 and \$6,707,000 during the nine months ended December 31, 2016 and 2015, respectively. This change was due primarily to a decrease in cash used for the acquisition related

activities during the nine months ended December 31, 2016 as compared to the nine months ended December 31, 2015.

27

---

Table of Contents

Net cash provided by financing activities was \$7,910,000 during the nine months ended December 31, 2016 compared to net cash used in financing activities during the nine months ended December 31, 2015 of \$50,642,000. This change was due mainly to (i) the net repayment of our long-term debt in connection with the financing agreement which was terminated when we entered into a new credit facility in June 2015, (ii) the payment of debt issuance costs associated with this new credit facility, and (iii) fewer stock options exercised during the nine months ended December 31, 2016 as compared to the nine months ended December 31, 2015.

Capital Resources

Debt

We are party to the following credit agreements.

Credit Facility

We are a party to a \$125,000,000 senior secured financing (the “Credit Facility”) with the lenders party thereto, and PNC Bank, National Association, as administrative agent, consisting of (i) a \$100,000,000 revolving loan facility, subject to borrowing base restrictions and a \$15,000,000 sublimit for letters of credit (the “Revolving Facility”) and (ii) a \$25,000,000 term loan facility (the “Term Loans”). The loans under the Credit Facility mature on June 3, 2020. In connection with the Credit Facility, the lenders were granted a security interest in substantially all of our assets. Our Credit Facility permits the payment of up to \$10,000,000 of dividends per calendar year, subject to a minimum availability threshold and pro forma compliance with financial covenants.

In May 2016, we entered into a consent and second amendment to the Credit Facility (the “Second Amendment”) which, among other things, (i) increased the borrowing capacity of the Revolving Facility from \$100,000,000 to \$120,000,000, subject to certain borrowing base restrictions and a \$15,000,000 sublimit for letters of credit, (ii) amended the definition and calculation of consolidated EBITDA, (iii) increased the maximum of amount of capital expenditures, and (iv) made certain other amendments and modifications.

The Term Loans require quarterly principal payments of \$781,250. The Credit Facility bears interest at rates equal to either LIBOR plus a margin of 2.50%, 2.75% or 3.00% or a reference rate plus a margin of 1.50%, 1.75% or 2.00%, in each case depending on the senior leverage ratio as of the applicable measurement date. There is also a facility fee of 0.25% to 0.375%, depending on the senior leverage ratio as of the applicable measurement date. The interest rate on our Term Loans and Revolving Facility was 3.12% and 4.09%, respectively, at December 31, 2016 compared to 2.94% and 3.53%, respectively, at March 31, 2016.

The Credit Facility, among other things, requires us to maintain certain financial covenants including a maximum senior leverage ratio and a minimum fixed charge coverage ratio. We were in compliance with all financial covenants as of December 31, 2016.

The following summarizes the financial covenants required under the Credit Facility:

	Calculation as of December 31, 2016	Financial covenants required per the Credit Facility
Maximum senior leverage ratio	0.41	2.50
Minimum fixed charge coverage ratio	1.44	1.05

In addition to other covenants, the Credit Facility places limits on our ability to incur liens, incur additional indebtedness, make loans and investments, engage in mergers and acquisitions, engage in asset sales, redeem or

repurchase capital stock, alter the business conducted by us and our subsidiaries, transact with affiliates, prepay, redeem or purchase subordinated debt, and amend or otherwise alter debt agreements.

Table of Contents

We had \$18,001,000 and \$7,000,000 outstanding under the Revolving Facility at December 31, 2016 and March 31, 2016, respectively. In addition, \$260,000 was reserved for standby letters of credit for workers' compensation insurance and \$600,000 for commercial letters of credit at December 31, 2016. At December 31, 2016, \$101,139,000, subject to certain adjustments, was available under the Revolving Facility.

WX Agreement

In August 2012, we entered into a Revolving Credit/Strategic Cooperation Agreement (the "WX Agreement") with Wanxiang America Corporation (the "Supplier") and the discontinued subsidiaries. In connection with the WX Agreement, we also issued a warrant (the "Supplier Warrant") to the Supplier to purchase up to 516,129 shares of our common stock for an initial exercise price of \$7.75 per share exercisable at any time after August 22, 2014 and on or prior to September 30, 2017. The exercise price is subject to adjustments, among other things, for sales of common stock by us at a price below the exercise price.

The fair value of the Supplier Warrant using level 3 inputs and the Monte Carlo simulation model was \$9,916,000 and \$15,643,000 at December 31, 2016 and March 31, 2016, respectively. These amounts are included in other liabilities in the consolidated balance sheets. The warrant liability continues to be classified as a noncurrent liability at December 31, 2016 as we do not expect to settle this amount in cash. During the three months ended December 31, 2016 and 2015, a gain of \$962,000 and a loss of \$1,275,000, respectively, were recorded in general and administrative expenses due to the change in the fair value of this warrant liability. During the nine months ended December 31, 2016 and 2015, a gain of \$5,727,000 and a loss of \$3,017,000, respectively, were recorded in general and administrative expenses due to the change in the fair value of this warrant liability.

Receivable Discount Programs

We use receivable discount programs with certain customers and their respective banks. Under these programs, we have options to sell those customers' receivables to those banks at a discount to be agreed upon at the time the receivables are sold. These discount arrangements allows us to accelerate receipt of payment on customers' receivables. While these arrangements have reduced our working capital needs, there can be no assurance that these programs will continue in the future. Interest expense resulting from these programs would increase if interest rates rise, if utilization of these discounting arrangements expands, if customers extend their payment to us, or if the discount period is extended to reflect more favorable payment terms to customers.

The following is a summary of the receivable discount programs:

	Nine Months Ended December 31,			
	2016		2015	
Receivables discounted	\$254,795,000		\$248,443,000	
Weighted average days	341		342	
Annualized weighted average discount rate	2.9	%	2.2	%
Amount of discount as interest expense	\$6,864,000		\$5,241,000	

Off-Balance Sheet Arrangements

At December 31, 2016, we had no off-balance sheet financing or other arrangements with unconsolidated entities or financial partnerships (such as entities often referred to as structured finance or special purpose entities) established for purposes of facilitating off-balance sheet financing or other debt arrangements or for other contractually narrow or limited purposes.





Table of Contents

Capital Expenditures and Commitments

Capital Expenditures

Our capital expenditures were \$4,127,000 and \$3,168,000 for the nine months ended December 31, 2016 and 2015, respectively. These capital expenditures represent the purchase of equipment for our office, manufacturing and warehouse facilities. We expect our fiscal 2017 capital expenditures to be approximately \$5,000,000 to support our current operations. In addition, we expect to invest additional amounts in connection with the expansion of our operations in Mexico. We expect to use our working capital and incur additional capital lease obligations to finance these capital expenditures.

Related Party Transactions

There have been no material changes to our related party transactions that are presented in our Annual Report on Form 10-K for the year ended March 31, 2016, which was filed on June 14, 2016 and as amended by the Form 10-K/A filed with the SEC on July 29, 2016.

Litigation

There have been no material changes to our litigation matters that are presented in our Annual Report on Form 10-K for the year ended March 31, 2016, which was filed on June 14, 2016 and as amended by the Form 10-K/A filed with the SEC on July 29, 2016.

Critical Accounting Policies

There have been no material changes to our critical accounting policies and estimates that are presented in our Annual Report on Form 10-K for the year ended March 31, 2016, which was filed on June 14, 2016, except as discussed below.

Recently Adopted Accounting Standards

Share-based Compensation

In March 2016, the FASB issued guidance that simplifies several aspects of the accounting for share-based payment transactions and states that, among other things, all excess tax benefits and tax deficiencies should be recognized as income tax expense or benefit in the income statement and an entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. The new guidance is effective for interim and annual reporting periods beginning after December 15, 2016 with early adoption permitted. We early adopted this guidance effective April 1, 2016 which resulted in a cumulative-effect adjustment of \$892,000 through retained earnings and current deferred tax assets to record excess tax benefits not previously recognized. We have also elected to account for forfeitures as they occur using the modified retrospective approach which did not have any material impact on our consolidated balance sheets. In addition, we are now required to present excess tax benefits as an operating activity (combined with other income tax cash flows) on the statements of cash flows rather than as a financing activity and have elected to adopt this change prospectively.

Extraordinary Items

In January 2015, the FASB issued guidance that simplifies income statement presentation by eliminating the concept of extraordinary items. This guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. A reporting entity may apply the amendments prospectively or retrospectively to

all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. There was no impact on our consolidated financial statements from the adoption of this guidance.

## Table of Contents

### Accounting Standards Not Yet Adopted

#### Revenue Recognition

In May 2014, the FASB issued guidance codified in ASC 606, “Revenue Recognition - Revenue from Contracts with Customers”, which amends the guidance in the former ASC 605, “Revenue Recognition”. The new guidance is effective for annual periods beginning after December 15, 2016, and interim periods within that reporting period for a public company. A full or modified retrospective transition method is required. In August 2015, the FASB delayed the effective date by one year to annual periods beginning after December 15, 2017, and interim periods within that reporting period for a public company. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. Accordingly, the updated standard is effective for us in the first quarter of fiscal 2019 and we do not plan to early adopt. We have not yet selected a transition method and are currently evaluating the effect that the updated standard will have on our consolidated financial statements and related disclosures.

#### Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern

In August 2014, the FASB issued guidance which requires an entity to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued). If conditions or events raise substantial doubt that is not alleviated, an entity should disclose that there is substantial doubt about the entity’s ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued), along with the principal conditions or events that raise substantial doubt, management’s evaluation of the significance of those conditions or events in relation to the entity’s ability to meet its obligations and management’s plans that are intended to mitigate those conditions. The new guidance is effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. We do not expect any impact on our financial position, results of operations or cash flows from the adoption of this guidance.

#### Inventory

In July 2015, the FASB issued guidance that requires an entity to measure inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. Subsequent measurement is unchanged for inventory measured using LIFO or the retail inventory method. The amendments in this update are effective for financial statements issued for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The amendments in this update should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period. We are currently evaluating the impact the provisions of this guidance will have on our consolidated financial statements.

#### Income Taxes

In November 2015, the FASB issued guidance that requires deferred tax liabilities and assets to be classified as noncurrent in the consolidated balance sheet. The guidance is effective for fiscal years beginning after December 15, 2016 including interim periods within those fiscal years with early adoption permitted. A reporting entity should apply the amendment prospectively or retrospectively. We are currently evaluating the impact the provisions of this guidance will have on our consolidated financial statements.

#### Financial Instruments

In January 2016, the FASB issued guidance that addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. A reporting entity should apply the new guidance by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. We are currently evaluating the impact the provisions of this guidance will have on our consolidated financial statements.

## Table of Contents

### Leases

In February 2016, the FASB issued new guidance that requires balance sheet recognition of a right-of-use asset and lease liability by lessees for operating leases. The new guidance also requires new disclosures providing additional qualitative and quantitative information about the amounts recorded in the financial statements. The new guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. The new guidance requires a modified retrospective approach with optional practical expedients. We are currently evaluating the impact the provisions of this guidance will have on our consolidated financial statements.

### Statement of Cash Flows

In August 2016, the FASB issued guidance which adds and/or clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. The new guidance is intended to reduce diversity in practice in how certain transactions are presented and classified in the statement of cash flows. The new guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years; early adoption is permitted. We do not expect any impact on our consolidated statements of cash flows from the adoption of this guidance.

### Business Combinations

In January 2017, the FASB issued guidance which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The new guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. A reporting entity should apply the amendment prospectively. We are currently evaluating the impact the provisions of this guidance will have on our consolidated financial statements.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in market risk from the information provided in Item 7A. "Quantitative and Qualitative Disclosures About Market Risk" in our Annual Report on Form 10-K as of March 31, 2016, which was filed with the SEC on June 14, 2016.

### Item 4. Controls and Procedures

#### Evaluation of Disclosure Controls and Procedures

We have established disclosure controls and procedures designed to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms and that such information is accumulated and communicated to management, including our chief executive officer, chief financial officer, and chief accounting officer, as appropriate to allow timely decisions regarding required disclosures.

Under the supervision and with the participation of management, including our chief executive officer, chief financial officer, and chief accounting officer, we have conducted an evaluation of the effectiveness of our disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based on this evaluation, our chief executive officer, chief financial officer, and chief accounting officer concluded that MPA's disclosure controls and procedures were effective as of December 31, 2016.

#### Inherent Limitations Over Internal Controls

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Exchange Act Rules 13a-15(f) and 15d-15(f).

32

---

Table of Contents

Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America, applying certain estimates and judgments as required.

Internal control over financial reporting includes those policies and procedures that:

1. Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company;  
Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and
2. Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.
- 3.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Changes in Internal Control Over Financial Reporting

There were no changes in MPA's internal control over financial reporting during the third quarter ended December 31, 2016 that have materially affected, or are reasonably likely to materially affect, MPA's internal control over financial reporting.



Table of Contents

PART II — OTHER INFORMATION

Item 1. Legal Proceedings

There have been no material changes to our litigation matters that are presented in our Annual Report on Form 10-K for the year ended March 31, 2016, which was filed on June 14, 2016 and as amended by the Form 10-K/A filed with the SEC on July 29, 2016.

Item 1A. Risk Factors

There have been no material changes in the risk factors set forth in Item 1A to Part I of our Annual Report on Form 10-K for the fiscal year ended March 31, 2016, filed on June 14, 2016 and as amended by the Form 10-K/A filed with the SEC on July 29, 2016.

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

Limitation on Payment of Dividends— The Credit Facility permits the payment of up to \$10,000,000 of dividends per calendar year, subject to a minimum availability threshold and pro forma compliance with financial covenants.

Item 3. Defaults Upon Senior Securities

None.

Item 5. Other Information

None.

Table of Contents

## Item 6. Exhibits

## (a) Exhibits:

Number	Description of Exhibit	Method of Filing
3.1	Certificate of Incorporation of the Company	Incorporated by reference to Exhibit 3.1 to the Company's Registration Statement on Form SB-2 declared effective on March 22, 1994 (the "1994 Registration Statement").
3.2	Amendment to Certificate of Incorporation of the Company	Incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form S-1 (No. 33-97498) declared effective on November 14, 1995.
3.3	Amendment to Certificate of Incorporation of the Company	Incorporated by reference to Exhibit 3.3 to the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 1997.
3.4	Amendment to Certificate of Incorporation of the Company	Incorporated by reference to Exhibit 3.4 to the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 1998 (the "1998 Form 10-K").
3.5	Amendment to Certificate of Incorporation of the Company	Incorporated by reference to Exhibit C to the Company's proxy statement on Schedule 14A filed with the SEC on November 25, 2003.
3.6	Amended and Restated By-Laws of Motorcar Parts of America, Inc.	Incorporated by reference to Exhibit 3.1 to Current Report on Form 8-K filed on August 24, 2010.
3.7	Certificate of Amendment of the Certificate of Incorporation of the Company	Incorporated by reference to Exhibit 3.1 to Current Report on Form 8-K filed on April 9, 2014.
3.8	Amendment to the Amended and Restated By-Laws of Motorcar Parts of America, Inc., as adopted on June 9, 2016	Incorporated by reference to Exhibit 3.1 to Current Report on Form 8-K filed on June 14, 2016.
4.1	2003 Long Term Incentive Plan	Incorporated by reference to Exhibit 4.9 to the Company's Registration Statement on Form S-8 filed with the SEC on April 2, 2004.
4.2	2004 Non-Employee Director Stock Option Plan	Incorporated by reference to Appendix A to the Proxy Statement on Schedule 14A for the 2004 Annual Shareholders Meeting.
4.3	2010 Incentive Award Plan	Incorporated by reference to Appendix A to the Proxy Statement on Schedule 14A filed on December 15, 2010.
4.4	Amended and Restated 2010 Incentive Award Plan	Incorporated by reference to Appendix A to the Proxy Statement on Schedule 14A filed on March 5, 2013.
4.5		

Second Amended and Restated 2010  
Incentive Award Plan

Incorporated by reference to Appendix A to the Proxy  
Statement on Schedule 14A filed on March 3, 2014.

Table of Contents

Number	Description of Exhibit	Method of Filing
4.6	2014 Non-Employee Director Incentive Award Plan	Incorporated by reference to Appendix B to the Proxy Statement on Schedule 14A filed on March 3, 2014.
10.1	Consent and Second Amendment to Loan Agreement, dated as of May 19, 2016, among Motorcar Parts of America, Inc., each lender from time to time party thereto and PNC Bank, National Association, as administrative agent	Incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q filed on August 9, 2016.
<u>31.1</u>	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002	Filed herewith.
<u>31.2</u>	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002	Filed herewith.
<u>31.3</u>	Certification of Chief Accounting Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002	Filed herewith.
<u>32.1</u>	Certifications of Chief Executive Officer, Chief Financial Officer and Chief Accounting Officer pursuant to Section 906 of the Sarbanes Oxley Act of 2002	Filed herewith.
101.1	The following financial information from Motorcar Parts of America, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2016, formatted in Extensible Business Reporting Language ("XBRL") and filed electronically herewith: (i) the Consolidated Balance Sheets; (ii) the Consolidated Statements of Operations; (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Cash Flows; and (v) the Condensed Notes to Consolidated Financial Statements	Filed herewith.

Table of Contents

SIGNATURES

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.

MOTORCAR PARTS OF  
AMERICA, INC

Dated: February 9, 2017 By: /s/ David Lee  
David Lee  
Chief Financial Officer

Dated: February 9, 2017 By: /s/ Kevin Daly  
Kevin Daly  
Chief Accounting Officer