

FORWARD AIR CORP
Form 10-K
February 15, 2013

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

FORM 10-K

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

For the Fiscal Year Ended December 31, 2012
Commission File No. 000-22490

FORWARD AIR CORPORATION
(Exact name of registrant as specified in its charter)

Tennessee 62-1120025
(State or other jurisdiction (I.R.S. Employer Identification No.)
of incorporation or organization)

430 Airport Road 37745
Greeneville, Tennessee (Zip Code)
(Address of principal executive offices)
(423) 636-7000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:
Common Stock, \$0.01 par value The NASDAQ Stock Market LLC
(Title of class) (Name of exchange on which registered)

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 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 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 Exchange Act.) Yes No

The aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2012 was approximately \$922,515,140 based upon the \$32.27 closing price of the stock as reported on The NASDAQ Stock Market LLC on that date. For purposes of this computation, all directors and executive officers of the registrant are assumed to be affiliates. This assumption is not a conclusive determination for purposes other than this calculation.

The number of shares outstanding of the registrant's common stock, \$0.01 par value per share as of February 11, 2013 was 29,602,342.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement for the 2013 Annual Meeting of Shareholders are incorporated by reference into Part III of this report.

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Introductory Note

This Annual Report on Form 10-K for the fiscal year ended December 31, 2012 (this “Form 10-K”) contains “forward-looking statements,” as defined in Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Forward-looking statements are statements other than historical information or statements of current condition and relate to future events or our future financial performance. Some forward-looking statements may be identified by use of such terms as “believes,” “anticipates,” “intends,” “plans,” “estimates,” “projects” or “expects.” Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The following is a list of factors, among others, that could cause actual results to differ materially from those contemplated by the forward-looking statements: economic factors such as recessions, inflation, higher interest rates and downturns in customer business cycles, our inability to maintain our historical growth rate because of a decreased volume of freight or decreased average revenue per pound of freight moving through our network, increasing competition and pricing pressure, surplus inventories, loss of a major customer, the creditworthiness of our customers and their ability to pay for services rendered, our ability to secure terminal facilities in desirable locations at reasonable rates, the inability of our information systems to handle an increased volume of freight moving through our network, changes in fuel prices, claims for property damage, personal injuries or workers’ compensation, employment matters including rising health care costs, enforcement of and changes in governmental regulations, environmental and tax matters, the handling of hazardous materials, the availability and compensation of qualified independent owner-operators and freight handlers needed to serve our transportation needs and our inability to successfully integrate acquisitions. As a result of the foregoing, no assurance can be given as to future financial condition, cash flows or results of operations. Except as required by law, we undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Part I

Item 1. Business

We were formed as a corporation under the laws of the State of Tennessee on October 23, 1981. Our operations can be broadly classified into two principal segments: Forward Air, Inc. (“Forward Air”) and Forward Air Solutions, Inc. (“FASI”).

Through our Forward Air segment, we are a leading provider of time-definite surface transportation and related logistics services to the North American expedited ground freight market. We offer our customers local pick-up and delivery (Forward Air Complete™) and scheduled surface transportation of cargo as a cost-effective, reliable alternative to air transportation. We transport cargo that must be delivered at a specific time but is less time-sensitive than traditional air freight. This type of cargo is frequently referred to in the transportation industry as deferred air freight. We operate our Forward Air segment through a network of terminals located on or near airports in 87 cities in the United States and Canada, including a central sorting facility in Columbus, Ohio and 12 regional hubs serving key markets. We also offer our customers an array of logistics and other services including: expedited full truckload (“TLX”); dedicated fleets; warehousing; customs brokerage; and shipment consolidation, deconsolidation and handling.

Through our Forward Air segment, we market our airport-to-airport services primarily to freight forwarders, integrated air cargo carriers, and passenger and cargo airlines. To serve this market, we offer customers a high level of service with a focus on on-time, damage-free deliveries. We serve our customers by locating our terminals on or near airports and maintaining regularly scheduled transportation service between major cities. We either receive shipments at our terminals or if instructed to do so pick up shipments directly from our customers. We then transport the freight

by truck (i) directly to the destination terminal; (ii) to our Columbus, Ohio central sorting facility; or (iii) to one of our 12 regional hubs, where they are unloaded, sorted and reloaded. After reloading the shipments, we deliver them to the terminals nearest their destinations and then, if requested by the customer, on to a final designated site. We ship freight directly between terminals when justified by the tonnage volume.

During 2012, approximately 23.9% of the freight we handled was for overnight delivery, approximately 61.3% was for delivery within two to three days and the balance was for delivery in four or more days. We generally do not market our airport-to-airport services directly to shippers (where such services might compete with our freight forwarder customers). Also, because we do not place significant size or weight restrictions on airport-to-airport shipments, we generally do not compete directly with integrated air cargo carriers such as United Parcel Service and Federal Express in the overnight delivery of small parcels. In 2012, Forward Air's ten largest customers accounted for approximately 47.2% of Forward Air's operating revenue and no single customer accounted for more than 10.0% of Forward Air's operating revenue.

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We continue to develop and implement complimentary services to the airport-to-airport network. Our complimentary services including TLX full truckload; dedicated fleets; local pick-up and delivery; warehousing; customs brokerage; and shipment consolidation, deconsolidation and handling are critical to helping meet the changing needs of our customers and for efficiently using the people and resources of our airport-to-airport network.

Through our FASI segment, which we formed in July 2007, we provide pool distribution services throughout the Mid-Atlantic, Southeast, Midwest and Southwest continental United States. Pool distribution involves managing high-frequency, last mile handling and distribution of time-sensitive product to numerous destinations in specific geographic regions. Our primary customers for pool distribution are regional and nationwide distributors and specialty retailers, such as mall, strip mall and outlet-based retail chains. We service these customers through a network of terminals and service centers located in 19 cities. FASI's three largest customers accounted for approximately 61.9% of FASI's 2012 operating revenue, but revenues from these three customers did not exceed 10.0% of our consolidated revenue. No other customers accounted for more than 10.0% of FASI's operating revenue.

Our Industry

As businesses minimize inventory levels, close regional and local distribution centers, perform manufacturing and assembly operations in multiple locations and distribute their products through multiple channels, they have an increased need for expedited or time-definite delivery services. Expedited or time-definite shipments are those shipments for which the customer requires delivery the next day or within two to three days, usually by a specified time or within a specified time window.

Shippers with expedited or time-definite delivery requirements have several principal alternatives to transport freight: freight forwarders; integrated air cargo carriers; less-than-truckload carriers; full truckload carriers, and passenger and cargo airlines.

Freight forwarders obtain requests for shipments from customers, make arrangements for transportation of the cargo by a third-party carrier and usually arrange for both delivery from the shipper to the carrier and from the carrier to the recipient.

Integrated air cargo carriers provide pick-up and delivery services primarily using their own fleet of trucks and provide transportation services generally using their own fleet of aircraft.

Less-than-truckload carriers also provide pick-up and delivery services through their own fleet of trucks. These carriers operate terminals where a single shipment is unloaded, sorted and reloaded multiple times. This additional handling increases transit time, handling costs and the likelihood of cargo damage or theft.

Full truckload carriers provide transportation services generally using their own fleet of trucks. A freight forwarder or shipper must have a shipment of sufficient size to justify the cost of a full truckload. These cost benefit concerns can inhibit the flexibility often required by freight forwarders or shippers.

Passenger or cargo airlines provide airport-to-airport service, but have limited cargo space and generally accept only shipments weighing less than 150 pounds.

Competitive Advantages

We believe that the following competitive advantages are critical to our success in both our Forward Air and FASI segments:

Focus on Specific Freight Markets. Our Forward Air segment focuses on providing time-definite surface transportation and related logistics services to the North American expedited ground freight market. Our FASI segment focuses on providing high-quality pool distribution services to retailers and nationwide distributors of retail products. This focused approach enables us to provide a higher level of service in a more cost-effective manner than our competitors.

Expansive Network of Terminals and Sorting Facilities. We have developed a network of Forward Air terminals and sorting facilities throughout the United States and Canada located on or near airports. We believe it would be difficult for a competitor to duplicate our Forward Air network with the expertise and strategic facility locations we have acquired without expending significant capital and management resources. Our expansive Forward Air network enables us to provide regularly scheduled service between most markets with low levels of freight damage or loss, all at rates which in general are significantly below air freight rates.

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We have established a FASI network of terminals and service centers throughout the Mid-Atlantic, Southeast, Midwest and Southwest continental United States. The pool distribution market is very fragmented and our competition primarily consists of regional and local providers. We believe that through our network of FASI terminals and service locations we can offer our pool distribution customers comprehensive, high-quality, consistent service across the majority of the continental United States.

Concentrated Marketing Strategy. Forward Air provides our expedited ground freight services mainly to freight forwarders, integrated air cargo carriers, and passenger and cargo airlines rather than directly serving shippers. Forward Air does not place significant size or weight restrictions on shipments and, therefore, it does not compete with delivery services such as United Parcel Service and Federal Express in the overnight small parcel market. We believe that Forward Air customers prefer to purchase their transportation services from us because, among other reasons, we generally do not market Forward Air's services to their shipper customers and, therefore, do not compete directly with them for customers.

FASI provides pool distribution services primarily to regional and nationwide distributors and specialty retailers, such as mall, strip mall and outlet-based retail chains.

Superior Service Offerings. Forward Air's published expedited ground freight schedule for transit times with specific cut-off and arrival times generally provides Forward Air customers with the predictability they need. In addition, our network of Forward Air terminals allows us to offer our customers later cut-off times, a higher percentage of direct shipments (which reduces damage and shortens transit times) and earlier delivery times than most of our competitors. Our network of FASI terminals allows us the opportunity to provide precision deliveries to a wider range of locations than most pool distribution providers with increased on-time performance. Recent economic uncertainty resulted in reduced inventory levels and increased shippers' need for reliable, expedited delivery. We believe the trend of minimal inventories and increased expedited shipping will continue, and that our network of terminals and expedited capabilities put us in an excellent position to benefit from these trends.

Flexible Business Model. Rather than owning and operating our own fleet of trucks, Forward Air purchases most of its transportation requirements from owner-operators or truckload carriers. Due to the nature of pool distribution services, FASI utilizes a higher percentage of Company-employed drivers and Company-owned equipment than Forward Air. However, as the conditions of individual markets and requirements of our customers allow, we utilize owner-operators in our pool distribution business. This approach allows us to respond quickly to changing demands and opportunities in our industry and to generate higher returns on assets because of the lower capital requirements.

Comprehensive Logistic and Other Service Offerings. Through our two segments we offer an array of logistic and other services including: TLX, pick-up and delivery (Forward Air Complete™), dedicated fleet, warehousing, customs brokerage and shipment consolidation and handling. These services are an essential part of many of our customers' transportation needs and are not offered by many of our competitors. We are often able to provide these services utilizing existing infrastructure and thereby earning additional revenue without incurring significant additional fixed costs.

Leading Technology Platform. We are committed to using information technology to improve our operations. Through improved information technology, we believe we can increase the volume of freight we handle in our networks, improve visibility of shipment information and reduce our operating costs. Our technology allows us to provide our customers with electronic bookings and real-time tracking and tracing of shipments while in our network, complete shipment history, proof of delivery, estimated charges and electronic bill presentment. We continue to enhance our systems to permit us and our customers to access vital information through both the Internet and electronic data interchange. We have continued to invest in information technology to the benefit of our customers and our business processes.

Strong Balance Sheet and Availability of Funding. Our asset-light business model and strong market position in the expedited ground freight market provides the foundation for operations that have produced excellent cash flow from operations even in challenging conditions. Our strong balance sheet can also be a competitive advantage. Our competitors, particularly in the pool distribution market, are mainly regional and local operations and may struggle to maintain operations in an uncertain economic environment. The threat of financial instability may encourage new and existing customers to use a more financially secure transportation provider, such as FASI.

Growth Strategy

Our growth strategy is to take advantage of our competitive strengths in order to increase our profits and shareholder returns. Our goal is to use our established networks as the base from which to expand and launch new services that will allow us to grow in any economic environment. Principal components of our efforts include:

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Increase Freight Volume from Existing Customers. Many of our customers currently use us for only a portion of their overall transportation needs. We believe we can increase freight volumes from existing customers by offering more comprehensive services that address all of the customer's transportation needs, such as Forward Air Complete™ ("Complete"), our direct to door pick-up and delivery service. By offering additional services that can be integrated with our existing services, we believe we will attract additional business from existing customers. In 2012, 23.1% of airport-to-airport linehaul shipments had a Complete component. We believe increasing this Complete attachment rate is a key to growing the revenue of our airport-to-airport service.

Develop New Customers. We continue to actively market our services to potential new customers. In our Forward Air segment, we believe freight forwarders will continue to move away from integrated air cargo carriers because those carriers charge higher rates, and away from less-than-truckload carriers because those carriers provide less reliable service and compete for the same customers as do the freight forwarders. In addition, we believe Forward Air's comprehensive North American network and related logistics services are attractive to domestic and international airlines. Forward Air Complete™ can also help attract business from new customers who require pick-up and delivery for their shipments. In our pool distribution business, we are emphasizing the development of relationships with customers who have peak volume seasons outside of the traditional fourth quarter peak season in order to stabilize FASI's earnings throughout the calendar year. We are currently targeting customers from industries such as hospitality, healthcare, lawn and garden and publishing. We continue to evaluate plans to expand FASI's terminal footprint by opening FASI operations in select Forward Air terminals. We believe the utilization of existing Forward Air terminals will allow us to increase our FASI revenues with minimal addition of fixed costs.

Improve Efficiency of Our Transportation Network. We constantly seek to improve the efficiency of our networks. Regional hubs and direct shuttles improve Forward Air's efficiency by reducing the number of miles freight must be transported and the number of times freight must be handled and sorted. As the volume of freight between key markets increases, we intend to continue adding direct shuttles. In key gateway cities we have constructed or expanded terminals. With these expanded facilities, we believe we have the necessary space to grow our business in key gateway cities and to offer additional services. We are working to improve our FASI operations by increasing the efficiencies of our daily and weekly transportation routes and the cartons handled per hour on our docks. We are constantly looking to improve FASI route efficiencies by consolidating loads and utilizing owner-operators when available. We are investing in conveyor systems for certain FASI terminals to increase the productivity of our cargo handlers. Finally, we are actively looking to reduce or eliminate the number of duplicate facilities in cities which have both Forward Air and FASI terminals. We have combined Forward Air and FASI facilities in Dallas/Fort Worth, Texas, Des Moines, Iowa, Denver, Colorado, Kansas City, Missouri, Nashville, Tennessee, Richmond, Virginia and Tulsa, Oklahoma, and will continue this process in upcoming years as the expiration of leases and business volumes allow.

Expand Logistics and Other Services. We continue to expand our logistics and other services to increase revenue and improve utilization of our terminal facilities and labor force. Because of the timing of the arrival and departure of cargo, our facilities are under-utilized during certain portions of the day, allowing us to add logistics services without significantly increasing our costs. Therefore, we have added a number of logistic services in the past few years, such as TLX, dedicated fleet, warehousing, customs brokerage and shipment consolidation and handling services. These services directly benefit our existing customers and increase our ability to attract new customers, particularly those customers that cannot justify providing the services directly. These services are not offered by many transportation providers with whom we compete and are attractive to customers who prefer to use one provider for all of their transportation needs.

Expand Pool Distribution Services and Integrate with our Forward Air Services. In addition to increasing our revenue from traditional pool distribution services, we are working to expand FASI's customer base beyond retail and to integrate our Forward Air and FASI service offerings. Through this process, we are able to offer customers linehaul or truckload services, with handling and sorting at the origin and destination terminal, and final distribution to one or many locations utilizing FASI pool distribution and Forward Air Complete™.

Enhance Information Systems. We are committed to the continued development and enhancement of our information systems in ways that will continue to provide us competitive service advantages and increased productivity. We

believe our enhanced systems have and will assist us in capitalizing on new business opportunities with existing customers and developing relationships with new customers.

Pursue Strategic Acquisitions. We continue to evaluate and pursue acquisitions that can increase our penetration of a geographic area, add new customers, add new business verticals, increase freight volume and add new service offerings. In addition, we expect to explore acquisitions that may enable us to offer additional services. Acquisitions may affect our short-term cash flow and net income as we expend funds, potentially increase indebtedness and incur additional expenses.

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Operations

We operate in two reportable segments, based on differences in the services provided: Forward Air and FASI. Through Forward Air, we are a leading provider of time-definite transportation and related logistics services to the North American expedited ground freight market. Forward Air's activities can be broadly classified into three categories of services: airport-to-airport, logistics and other.

Through our FASI segment, we provide pool distribution services throughout the Mid-Atlantic, Southeast, Midwest and Southwest continental United States. Pool distribution involves managing high-frequency handling and distribution of time-sensitive product to numerous destinations in specific geographic regions.

Forward Air

Airport-to-airport

We receive freight from freight forwarders, integrated air cargo carriers and passenger and cargo airlines at our terminals, which are located on or near airports in the United States and Canada. We also pick up freight from customers at designated locations via our Forward Air Complete™ service. We consolidate and transport these shipments by truck through our network to our terminals nearest the ultimate destinations of the shipments. We operate regularly scheduled service to and from each of our terminals through our Columbus, Ohio central sorting facility, through one of our 12 regional hubs or, as volumes require, direct point-to-point service. We also operate regularly scheduled shuttle service directly between terminals where the volume of freight warrants bypassing the Columbus, Ohio central sorting facility or a regional hub. When a shipment arrives at our terminal nearest its destination, the customer arranges for the shipment to be picked up and delivered to its final destination, or we, in the alternative, through our Forward Air Complete™ service, deliver the freight for the customer to its final destination.

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Terminals

Our airport-to-airport network consists of terminals located in the following 87 cities:

City	Airport Served	City	Airport Served
Albany, NY	ALB	Louisville, KY	SDF
Albuquerque, NM*	ABQ	Memphis, TN	MEM
Allentown, PA*	ABE	McAllen, TX	MFE
Atlanta, GA	ATL	Miami, FL	MIA
Austin, TX	AUS	Milwaukee, WI	MKE
Baltimore, MD	BWI	Minneapolis, MN	MSP
Baton Rouge, LA*	BTR	Mobile, AL*	MOB
Birmingham, AL*	BHM	Moline, IA	MLI
Blountville, TN*	TRI		