

SIMPSON MANUFACTURING CO INC /CA/
Form 10-Q
November 09, 2006

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: **September 30, 2006**

OR

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

For the transition period from _____ to _____

Commission file number: **0-23804**

Simpson Manufacturing Co., Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation
or organization)

94-3196943
(I.R.S. Employer
Identification No.)

5956 W. Las Positas Blvd., Pleasanton, CA 94588

(Address of principal executive offices)

(Registrant's telephone number, including area code): **(925) 560-9000**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

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Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares of the Registrant's common stock outstanding as of September 30, 2006: **48,170,928**

PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

Simpson Manufacturing Co., Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(In thousands, unaudited)

	September 30, 2006	2005	December 31, 2005
ASSETS			
Current assets			
Cash and cash equivalents	\$ 104,605	\$ 104,360	\$ 131,203
Short-term investments		6,303	
Trade accounts receivable, net	132,946	129,590	101,621
Inventories	229,703	174,783	181,492
Deferred income taxes	11,622	10,160	10,088
Other current assets	5,257	3,598	10,051
Total current assets	484,133	428,794	434,455
Property, plant and equipment, net			
Goodwill	190,311	151,724	166,480
Equity method investment	44,297	42,901	42,681
Other noncurrent assets		222	244
Total assets	15,156	16,952	15,855
	\$ 733,897	\$ 640,593	\$ 659,715
LIABILITIES AND STOCKHOLDERS EQUITY			
Current liabilities			
Current portion of long-term debt	\$ 326	\$ 545	\$ 2,186
Trade accounts payable	40,134	41,290	29,485
Accrued liabilities	37,704	30,471	39,076
Income taxes payable		3,313	
Accrued profit sharing trust contributions	6,708	6,013	7,721
Accrued cash profit sharing and commissions	12,213	15,449	10,229
Accrued workers compensation	3,312	2,724	3,262
Total current liabilities	100,397	99,805	91,959
Long-term debt, net of current portion	490	1,874	2,928
Other long-term liabilities	1,643	1,352	1,362
Total liabilities	102,530	103,031	96,249
Commitments and contingencies (Note 7)			
Minority interest in consolidated variable interest entities			5,337
Stockholders equity			
Common stock, at par value	482	482	483
Additional paid-in capital	108,033	89,383	94,398
Retained earnings	511,552	438,773	456,474
Accumulated other comprehensive income	11,300	8,924	6,774
Total stockholders equity	631,367	537,562	558,129
Total liabilities and stockholders equity	\$ 733,897	\$ 640,593	\$ 659,715

The accompanying notes are an integral part of these condensed consolidated financial statements.

Simpson Manufacturing Co., Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(In thousands except per-share amounts, unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2006	2005	2006	2005
Net sales	\$ 226,718	\$ 233,809	\$ 683,607	\$ 642,359
Cost of sales	139,803	140,607	409,259	388,640
Gross profit	86,915	93,202	274,348	253,719
Operating expenses (income):				
Research and development and other engineering	4,531	3,519	15,337	10,722
Selling	17,955	15,679	54,105	47,057
General and administrative	22,468	27,282	72,143	76,995
Loss (gain) on sale of assets	(3)	(2,027)	110	(2,124)
	44,951	44,453	141,695	132,650
Income from operations	41,964	48,749	132,653	121,069
Income (loss) in equity method investment, before tax	(1)	54	(130)	222
Interest income, net	831	373	2,610	595
Income before income taxes	42,794	49,176	135,133	121,886
Provision for income taxes	15,704	17,569	51,151	45,057
Minority interest			166	
Net income	\$ 27,090	\$ 31,607	\$ 83,816	\$ 76,829
Net income per common share				
Basic	\$ 0.56	\$ 0.66	\$ 1.74	\$ 1.60
Diluted	\$ 0.56	\$ 0.65	\$ 1.71	\$ 1.58
Cash dividends declared per common share	\$ 0.08	\$ 0.05	\$ 0.24	\$ 0.15
Number of shares outstanding				
Basic	48,120	48,091	48,295	48,024
Diluted	48,587	48,658	48,935	48,532

The accompanying notes are an integral part of these condensed consolidated financial statements.

Simpson Manufacturing Co., Inc. and Subsidiaries
Condensed Consolidated Statements of Stockholders' Equity
for the nine months ended September 30, 2005 and 2006 and the three months ended December 31, 2005
(In thousands except per-share amounts, unaudited)

	Common Stock Shares	Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Total
Balance, January 1, 2005	47,929	\$ 479	\$ 79,877	\$ 369,154	\$ 13,415	\$	\$ 462,925
Comprehensive income:							
Net income				76,829			76,829
Other comprehensive income:							
Change in net unrealized gains or losses on available-for-sale investments					46		46
Translation adjustment					(4,537)		(4,537)
Comprehensive income							72,338
Options exercised	214	3	2,409				2,412
Stock compensation			4,414				4,414
Tax benefit of options exercised			1,976				1,976
Cash dividends declared on Common stock (\$0.15 per share)				(7,210)			(7,210)
Common stock issued at \$34.30 per share	21		707				707
Balance, September 30, 2005	48,164	482	89,383	438,773	8,924		537,562
Comprehensive income:							
Net income				21,565			21,565
Other comprehensive income:							
Change in net unrealized gains or losses on available-for-sale investments					12		12
Translation adjustment					(2,162)		(2,162)
Comprehensive income							19,415
Options exercised	158	1	1,682				1,683
Stock compensation			1,459				1,459
Tax benefit of options exercised			1,867				1,867
Cash dividends declared on Common stock (\$0.08 per share)				(3,864)			(3,864)
Common stock issued at \$38.65 per share			7				7
Balance, December 31, 2005	48,322	483	94,398	456,474	6,774		558,129
Comprehensive income:							
Net income				83,816			83,816
Other comprehensive income:							
Translation adjustment, net of tax of \$129					4,526		4,526
Comprehensive income							88,342
Options exercised	343	4	5,431				5,435
Stock compensation			5,681				5,681
Tax benefit of options exercised			2,294				2,294
	(500)					(17,166)	(17,166)

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Repurchase of common stock								
Retirement of common stock		(5)		(17,161)			17,166	
Cash dividends declared on Common stock (\$0.24 per share)				(11,577)			(11,577)	
Common stock issued at \$36.35 per share	6		229				229	
Balance, September 30, 2006	48,171	\$ 482	\$ 108,033	\$ 511,552	\$ 11,300	\$	\$ 631,367	

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Simpson Manufacturing Co., Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(In thousands, unaudited)

	Nine Months Ended September 30,	
	2006	2005
Cash flows from operating activities		
Net income	\$ 83,816	\$ 76,829
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Loss (gain) on sale of assets	110	(2,124)
Depreciation and amortization	19,100	17,850
Deferred income taxes	(2,610)	(3,794)
Noncash compensation related to stock plans	5,708	4,798
Loss (income) in equity method investment	130	(222)
Tax benefit of options exercised		1,976
Excess tax benefit of options exercised	(2,048)	
Provision for obsolete inventory	188	808
Provision for (recovery of) doubtful accounts	277	(143)
Minority interest	166	
Changes in operating assets and liabilities, net of effects of acquisitions:		
Trade accounts receivable	(30,153)	(41,221)
Inventories	(46,604)	15,697
Trade accounts payable	6,430	7,340
Income taxes payable	4,843	8,493
Accrued profit sharing trust contributions	(1,053)	(1,006)
Accrued cash profit sharing and commissions	1,969	7,250
Other current assets	(1,672)	(667)
Accrued liabilities	1,893	4,015
Other long-term liabilities	410	(97)
Accrued workers compensation	50	(36)
Other noncurrent assets	(9)	(245)
Net cash provided by operating activities	40,941	95,501
Cash flows from investing activities		
Capital expenditures	(36,934)	(31,074)
Acquisition of minority interest	(9,135)	
Proceeds from sale of capital assets	79	4,025
Distributions from equity investment	114	
Maturities of available-for-sale investments		7,000
Sales of available-for-sale investments		3,500
Net cash used in investing activities	(45,876)	(16,549)
Cash flows from financing activities		
Line of credit borrowings	712	724
Repayment of debt and line of credit borrowings	(1,413)	(1,047)
Repurchase of common stock	(17,166)	
Issuance of Company's common stock	5,435	2,412
Excess tax benefit of options exercised	2,048	
Dividends paid	(11,591)	(7,198)
Net cash used in financing activities	(21,975)	(5,109)
Effect of exchange rate changes on cash	312	(400)
Net increase (decrease) in cash and cash equivalents	(26,598)	73,443
Cash and cash equivalents at beginning of period	131,203	30,917
Cash and cash equivalents at end of period	\$ 104,605	\$ 104,360
Noncash activity during the period		
Noncash capital expenditures	\$ 3,425	\$ 2,376
Dividends declared but not paid	\$ 3,820	\$ 2,410
Issuance of Company's common stock for compensation	\$ 229	\$ 707

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Simpson Manufacturing Co., Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation

Principles of Consolidation

The consolidated financial statements include the accounts of Simpson Manufacturing Co., Inc. and its subsidiaries (the Company). Investments in 50% or less owned affiliates are generally accounted for using either cost or the equity method. The Company consolidates all variable interest entities where it is the primary beneficiary. All significant intercompany transactions have been eliminated.

Interim Period Reporting

The accompanying unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations for reporting on Form 10-Q. Accordingly, certain information and footnotes required by accounting principles generally accepted in the United States of America have been condensed or omitted. These interim statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's 2005 Annual Report on Form 10-K (the 2005 Annual Report).

The unaudited quarterly condensed consolidated financial statements have been prepared on the same basis as the audited annual consolidated financial statements and, in the opinion of management, contain all adjustments (consisting of only normal recurring adjustments) necessary to state fairly the financial information set forth therein, in accordance with accounting principles generally accepted in the United States of America. The year-end condensed consolidated balance sheet data were derived from audited financial statements, but do not include all disclosures required by accounting principles generally accepted in the United States of America. The Company's quarterly results fluctuate. As a result, the Company believes the results of operations for the interim periods are not necessarily indicative of the results to be expected for any future period.

Revenue Recognition

The Company recognizes revenue when the earnings process is complete, net of applicable provision for discounts, returns and incentives, whether actual or estimated based on the Company's experience. This generally occurs when products are shipped to the customer in accordance with the sales agreement or purchase order, ownership and risk of loss pass to the customer, collectibility is reasonably assured and pricing is fixed or determinable. The Company's general shipping terms are F.O.B. shipping point, where title is transferred and revenue is recognized when the products are shipped to customers. When the Company sells F.O.B. destination point, title is transferred and the Company recognizes revenue on delivery or customer acceptance, depending on terms of the sales agreement. Service sales, representing aftermarket repair and maintenance and engineering activities, though significantly less than 1% of net sales and not material to the consolidated financial statements, are recognized as the services are completed. If the actual costs of sales returns, incentives, and discounts were to significantly exceed the recorded estimated allowance, the Company's sales would be adversely affected.

Net Income Per Common Share

Basic net income per common share is computed based on the weighted average number of common shares outstanding. Potentially dilutive securities, using the treasury stock method, are included in the diluted per-share calculations for all periods when the effect of their inclusion is dilutive.

The following is a reconciliation of basic net income (earnings) per share (EPS), to diluted EPS:

<i>(in thousands, except per-share amounts)</i>	Three Months Ended, September 30, 2006			Three Months Ended, September 30, 2005		
	Income	Shares	Per Share	Income	Shares	Per Share
Basic EPS						
Income available to common stockholders	\$ 27,090	48,120	\$ 0.56	\$ 31,607	48,091	\$ 0.66
Effect of Dilutive Securities						
Stock options		467			567	(0.01)
Diluted EPS						
Income available to common stockholders	\$ 27,090	48,587	\$ 0.56	\$ 31,607	48,658	\$ 0.65
	Nine Months Ended September 30, 2006			Nine Months Ended, September 30, 2005		
	Income	Shares	Per Share	Income	Shares	Per Share
Basic EPS						
Income available to common stockholders	\$ 83,816	48,295	\$ 1.74	\$ 76,829	48,024	\$ 1.60
Effect of Dilutive Securities						
Stock options		640	(0.03)		508	(0.02)
Diluted EPS						
Income available to common stockholders	\$ 83,816	48,935	\$ 1.71	\$ 76,829	48,532	\$ 1.58

Anti-dilutive shares attributable to outstanding stock options were excluded from the calculation of diluted net income per share. For the three months ended September 30, 2006 and 2005, 989 thousand and 512 thousand shares subject to stock options were anti-dilutive, respectively. For the nine months ended September 30, 2006 and 2005, 989 thousand and 896 thousand shares subject to stock options were anti-dilutive, respectively.

Accounting for Stock-Based Compensation

The Company maintains two stock option plans under which it may grant incentive stock options and non-qualified stock options, though the Company has granted only non-qualified stock options under these plans. The Simpson Manufacturing Co., Inc. 1994 Stock Option Plan (the 1994 Plan) is principally for the Company's employees and the Simpson Manufacturing Co., Inc. 1995 Independent Director Stock Option Plan (the 1995 Plan) is for its independent directors. The Company generally grants options under each of the 1994 Plan and the 1995 Plan once each year. The exercise price per share under each option granted in January 2006 under the 1994 Plan equaled or exceeded the closing market price per share of the Company's Common Stock as reported by the New York Stock Exchange for the date when the Company first publicly announced its financial results for 2005. In prior years, stock options were granted under the 1994 Plan with the exercise price equal to or in excess of the closing market price per share of the Company's Common Stock as reported by the New York Stock Exchange on the last trading day of the preceding year. The exercise price per share under each option granted under the 1995 Plan is at the fair market value on the date specified in the 1995 Plan. Options vest and expire according to terms established at the grant date.

Under the 1994 Plan, no more than 16 million shares of the Company's common stock may be sold (including shares already sold) pursuant to all options granted under the 1994 Plan. Under the 1995 Plan, no more than 320 thousand

shares of common stock may be sold (including shares already sold) pursuant to all options granted under the 1995 Plan. Options granted under the 1994 Plan typically vest evenly over the requisite service period of four years and have a term of seven years. The vesting of options granted under the 1994 Plan will be accelerated if there is a change in control of the Company. Options granted under the 1995 Plan are fully vested on the date of grant.

As of January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123R, Share Based Payment (Revised 2004), using the modified prospective application approach as the transition method. Prior periods are not restated under this method. The cash flow presentation changed whereby cash inflow from excess tax benefits from the exercise of stock options are presented in the consolidated statements of cash flows as a financing activity, where applicable, rather than as an operating activity, as previously presented. Prior to the adoption of SFAS 123R and since January 1, 2003, when the Company adopted SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure, and SFAS No. 123, Accounting for Stock Based Compensation, the Company accounted for stock options on a fair value basis and used the prospective method of applying SFAS No. 123 for the transition. As of January 1, 2006, the Company had no unvested options which were accounted for using the intrinsic value method prescribed in Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations.

The following table represents the Company's stock option activity for the three and nine months ended September 30, 2006 and 2005:

<i>(in thousands)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Stock option expense recognized in operating expenses	\$ 1,887	\$ 1,404	\$ 5,442	\$ 4,414
Tax benefit of stock option expense in provision for income taxes	692	501	2,063	1,633
Stock option expense, net of tax	\$ 1,195	\$ 903	\$ 3,379	\$ 2,781
Fair value of shares vested	\$ 1,846	\$ 1,404	\$ 5,681	\$ 4,414
Proceeds to the Company from the exercise of stock options	\$ 869	\$ 1,534	\$ 5,435	\$ 2,412
Excess tax benefit from exercise of stock options	\$ 289	\$ 1,527	\$ 2,294	\$ 1,976
	At September 30,			
	2006	2005		
Stock option cost capitalized in inventory	\$ 239	\$		

The amounts included in cost of sales, selling, or general and administrative expenses depend on the job functions performed by the employees to whom the stock options were granted. Shares of common stock issued on exercise of stock options under the plans are registered under the Securities Act of 1933.

The adoption of SFAS No. 123R had no material effect on the Company's income from continuing operations, income before tax, net income, or net income per share. The adoption of SFAS No. 123R resulted in \$2.0 million in additional cash flows from financing activities for the nine months ended September 30, 2006, which previously would have been reported as cash flows from operating activities under SFAS No. 123.

Had compensation cost for the Company's stock options for all grants prior to January 1, 2003, been recognized based on the estimated fair value on the grant date under the fair value methodology prescribed by SFAS No. 123, as amended by SFAS No. 148, the Company's net income and net income per share would have been as follows:

<i>(in thousands, except per-share amounts)</i>	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net income, as reported	\$ 31,607	\$ 76,829
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	903	2,781
Deduct: Total stock-based employee compensation expense determined under the fair value method for all awards granted prior to January 1, 2003, net of related tax effects	910	2,803
Net income, pro forma	\$ 31,600	76,807
Net income per share		
Basic, as reported	\$ 0.66	\$ 1.60
Basic, pro forma	0.66	1.60
Diluted, as reported	0.65	1.58
Diluted, pro forma	0.65	1.58

The assumptions used to calculate the fair value of options granted are evaluated and revised, as necessary, to reflect market conditions and the Company's experience.

Under the 1994 Stock Option plan, the Company allows for full vesting on retirement if the employee becomes retirement-eligible by reaching age sixty. Prior to the adoption of SFAS 123R, stock-based employee compensation expense was recorded over the nominal vesting period and if a retirement-eligible employee retired before the end of the vesting period, the Company recorded unrecognized compensation cost at the date of retirement (the nominal vesting period approach). The nominal vesting period is four years of service subsequent to the grant date. The non-substantive vesting period approach specifies that awards, in substance, become vested when the employee's retention of the award is no longer contingent on providing service. Under this approach, the unrecorded compensation cost is expensed when that condition is met even if the employee continues providing service to the Company. This would be the case for existing grants when an employee becomes retirement-eligible, as well as when a retirement-eligible employee is granted an award. With the adoption of SFAS No. 123R on January 1, 2006, the Company adopted the non-substantive vesting period approach for new grants that have retirement eligibility provisions. The accounting treatment of options granted to retirement-eligible employees prior to the Company's adoption of SFAS 123R has not changed and financial statements for periods prior to adoption have not been restated for the effects of adopting SFAS 123R. Therefore, the expense recorded in 2006 comprises stock options that vest under both the non-substantive vesting period approach and the nominal vesting period approach. In contrast, the 2005 expense was calculated using the nominal vesting period approach. The effect on net income of applying the nominal vesting period approach versus the non-substantive vesting period approach was not material to the Company's results of operations for the three and nine months ended September 30, 2006 and 2005.

Recently Issued Accounting Standards

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation 48 (FIN 48), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 will be

effective for fiscal years beginning after December 15, 2006. Management has not yet determined the effect, if any, on the Company's financial statements for its fiscal year ending December 31, 2007.

In March 2006, the Emerging Issues Task Force (EITF) issued EITF 06-3 How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation). The Task Force agreed that a company should disclose its accounting policy regarding the gross or net presentation of certain taxes. If taxes included in gross revenues are significant, a company should disclose the amount of such taxes for each annual or interim period for which an income statement is presented. Taxes within the scope of EITF 06-3 are those that are imposed on and concurrent with a specific revenue-producing transaction. Taxes assessed on an entity's activities over a period of time, such as income taxes or gross receipts taxes, are not within the scope of EITF 06-3. EITF 06-3 will be effective for periods beginning after December 15, 2006. Management estimates that the effect on the Company's financial statements for its fiscal year ending December 31, 2007, or for any quarter of that year will be immaterial.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 will be effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Management has not yet determined the effect, if any, on the Company's financial statements for its fiscal year ending December 31, 2008, or its fiscal quarters within that year. SFAS No. 157 will be applied prospectively as of the beginning of the fiscal year in which it is initially applied.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108). SAB 108 expresses the SEC's views regarding the process of quantifying financial statement misstatements. The interpretations in SAB 108 were issued to address diversity in practice in quantifying financial statement misstatements and the potential under current practice for the build-up of improper amounts on the balance sheet. This statement is effective for the Company's annual financial statements starting this year. Management continues to evaluate SAB 108 and its effect on the Company's consolidated financial statements and results of operations. Based on current information, management does not believe that the effect will be material.

Revision in Classification

Historically, the Company has reported research and development and other engineering expenses as a component of cost of sales because of the integration of these departments within the manufacturing environment. On analysis of the current production environment, the Company has determined that it is more appropriate to report these amounts as operating expenses. The Company has elected to make this change to the condensed consolidated statement of operations beginning with the first quarter of 2006. Management has concluded that the effect of this revision in classification for the three and nine months ended September 30, 2005, which was an increase in gross profit of \$3.5 million and \$10.7 million, respectively, was immaterial. The revision in classification had no effect on the Company's consolidated income from operations, net income, net income per share, cash flows, or any balance sheet item for any period. The Company believes this change enhances the transparency of its financial statements and is appropriate given the organizational changes that have occurred as the Company has grown.

2. Trade Accounts Receivable, net

Trade accounts receivable consist of the following:

<i>(in thousands)</i>	At September 30,		At December 31,	
	2006	2005	2005	
Trade accounts receivable	\$ 137,917	\$ 133,799	\$ 105,940	
Allowance for doubtful accounts	(2,312)	(2,196)	(2,131)	
Allowance for sales discounts and returns	(2,659)	(2,013)	(2,188)	
	\$ 132,946	\$ 129,590	\$ 101,621	

3. Inventories

Inventories consist of the following:

<i>(in thousands)</i>	At September 30, 2006	2005	At December 31, 2005
Raw materials	\$ 102,288	\$ 63,740	\$ 65,163
In-process products	26,639	25,221	30,207
Finished products	100,776	85,822	86,122
	\$ 229,703	\$ 174,783	\$ 181,492

4. Property, Plant and Equipment, net

Property, plant and equipment, net, consists of the following:

<i>(in thousands)</i>	At September 30, 2006	2005	At December 31, 2005
Land	\$ 22,786	\$ 18,451	\$ 21,720
Buildings and site improvements	114,363	88,045	93,751
Leasehold improvements	4,710	5,921	5,945
Machinery and equipment	174,909	159,819	161,357
	316,768	272,236	282,773
Less accumulated depreciation and amortization	(151,646)	(134,323)	(135,570)
	165,122	137,913	147,203
Capital projects in progress	25,189	13,811	19,277
	\$ 190,311	\$ 151,724	\$ 166,480

Included in property, plant and equipment at December 31, 2005, are land, buildings, building improvements and construction-in-progress of consolidated variable interest entities with a net book value of \$9.0 million.

5. Investments

Equity Method Investment

The Company has a 35% equity interest in Keymark Enterprises, LLC (Keymark), for which it accounts using the equity method. Keymark develops software that assists in the design and engineering of residential structures. The Company's relationship with Keymark includes the specification of the Company's products in the Keymark software. The Company has no obligation to make any additional future capital contributions, nor does it intend to provide additional funding, to Keymark. Due to equity losses through September 30, 2006, the carrying amount of the Company's investment in Keymark has been written down to zero.

Available-for-Sale Investments

As of December 31, 2005, the Company's available-for-sale investments had either matured or were redeemed. Prior to that, the Company's investments in all debt securities were classified as available-for-sale investments. As of September 30, 2005, the Company's investments, classified as short-term investments, were as follows:

<i>(in thousands)</i>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt investments				
Municipal bonds	\$ 6,315	\$	\$ 12	\$ 6,303

6. Debt

Outstanding debt at September 30, 2006 and 2005, and December 31, 2005, and the available credit at September 30, 2006, consisted of the following:

(dollar amounts in thousands)

	Available Credit at September 30, 2006	Debt Outstanding at September 30, 2006	2005	at December 31, 2005
Revolving line of credit, interest at bank's reference rate less 0.50% (at September 30, 2006, the bank's reference rate less 0.50% was 7.75%), expires November 2006	\$ 13,800	\$	\$	\$
Revolving term commitment, interest at bank's prime rate less 0.50% (at September 30, 2006, the bank's prime rate less 0.50% was 7.75%), expires October 2007	9,200			
Revolving line of credit, interest at the bank's base rate plus 2% (at September 30, 2006, the bank's base rate plus 2% was 6.75%), expires September 2007	1,296			
Revolving lines of credit, interest rates between 3.3768% and 4.50%	5,359			
Term loan, interest at 7.70%, collateralized by real estate, repaid June 2006				1,941
Term loan, interest at bank's base rate plus 1.65% (at September 30, 2006, the bank's base rate plus 1.65% was 6.177%), collateralized by real estate, repaid March 2006				1,691
Term loan, interest at LIBOR plus 1.375% (at September 30, 2006, LIBOR plus 1.375% was 6.775%), matures May 2008		600	900	750
Term loans, interest rates between 4.00% and 5.50%, expirations between 2006 and 2018		216	1,519	732
	29,655	816	2,419	5,114
Less current portion of long-term debt		(326)	(545)	(2,186)
Long-term debt, net of current portion		\$ 490	\$ 1,874	\$ 2,928
Available credit	\$ 29,655			

7. Commitments and Contingencies

Note 9 to the consolidated financial statements in the 2005 Annual Report provides information concerning commitments and contingencies. From time to time, the Company is involved in various legal proceedings and other matters arising in the normal course of business. The resolution of claims and litigation is subject to inherent uncertainty and could have a material adverse effect on the Company's financial condition, cash flows and results of operations.

The Company's policy with regard to environmental liabilities is to accrue for future environmental assessments and remediation costs when information becomes available that indicates that it is probable that the Company is liable for any related claims and assessments and the amount of the liability is reasonably estimable. The Company does not believe that these matters will have a material adverse effect on the Company's financial condition, cash flows or results of operations.

Corrosion, hydrogen embrittlement, cracking, material hardness, wood pressure-treating chemicals, misinstallations, environmental conditions or other factors can contribute to failure of fasteners, connectors and tools. On occasion, some of the fasteners that the Company sells have failed, although the Company has not incurred any material liability resulting from those failures. The Company attempts to avoid such failures by establishing and monitoring appropriate product specifications, manufacturing quality control procedures, inspection procedures and information on appropriate installation methods and conditions. The Company subjects its products to extensive testing, with results and conclusions published in Company catalogues and on its websites (see www.strongtie.com/info and www.duravent.com). Based on test results to date, the Company believes that, generally, if its products are appropriately selected and installed in accordance with the Company's guidance, they may be reliably used in appropriate applications.

8. Stock Option Plans

The Company currently has two stock option plans (see Note 1 *Accounting for Stock-Based Compensation*). Participants are granted stock options only if the applicable company-wide or profit-center operating goals, or both, established by the Compensation Committee of the Board of Directors at the beginning of the year, are met.

The fair value of each option award was estimated on the date of grant using the Black-Scholes option pricing model. Expected volatility is based on historical volatilities of the Company's common stock measured monthly over the expected life of the option. The expected term of options granted is estimated based on the Company's prior exercise experience and future expectations of the exercise and termination behavior of the grantees. The risk-free rate is based on the yield of U.S. Treasury zero-coupon bonds with maturities comparable to the expected life in effect at the time of grant. The dividend yield is based on the expected dividend rate on the grant date.

Black-Scholes option pricing model assumptions for options granted in 2006 and 2005 are as follows:

Number of options granted (in thousands)	Grant Date	Risk free interest rate	Dividend yield	Expected life	Volatility	Exercise Price Range	Weighted average fair value
1994 Plan							
1	05/30/06	4.97%	0.90%	6.3 years	27.2%	\$35.75	\$12.25
489	01/26/06	4.46%	0.79%	6.3 years	27.2%	\$40.72 to \$44.79	\$13.68
515	01/01/05	3.87%	0.57%	6.4 years	28.0%	\$34.90 to \$38.39	\$11.91
1995 Plan							
5	02/15/06	4.46%	0.81%	6.3 years	27.2%	\$39.27	\$13.14
14	02/14/05	3.87%	0.57%	6.3 years	28.0%	\$36.00	\$12.18

The following table summarizes the Company's stock option activity for the nine months ended September 30, 2006:

Non-Qualified Stock Options	Shares (in thousands)	Weighted Average Exercise Price	Weighted- Average Remaining Contractual Life	Aggregate Intrinsic Value * (in thousands)
Outstanding at January 1, 2006	2,950	\$ 22.46		
Granted	495	40.70		
Exercised	(343)	15.86		
Forfeited	(20)	31.62		
Outstanding at September 30, 2006	3,082	\$ 26.06	4.2	\$ 13,611
Exercisable at September 30, 2006	1,895	\$ 22.11	3.6	\$ 12,002

* The intrinsic value represents the amount by which the fair market value of the underlying common stock exceeds the exercise price of the option, using the closing price per share of \$27.03 on September 30, 2006.

The total intrinsic value of options exercised during the nine months ended September 30, 2006 and 2005, was \$7.2 million and \$5.4 million, respectively.

A summary of the status of unvested options as of September 30, 2006, and changes during the nine months ended September 30, 2006, are presented below:

Unvested Options	Shares (in thousands)	Weighted Average Grant-Date Fair Value
Unvested at January 1, 2006	1,290	\$ 9.52
Granted	495	13.67
Vested	(578)	9.40
Forfeited	(20)	11.05
Unvested at September 30, 2006	1,187	\$ 11.28

As of September 30, 2006, there was \$11.6 million of total unrecognized compensation cost related to unvested share-based compensation arrangements granted under the 1994 Plan. This cost is expected to be recognized over a weighted-average period of 2.4 years. Options granted under the 1995 Plan are fully vested and expensed to income on the date of grant.

9. Segment Information

The Company is organized into two primary operating segments. The segments are defined by types of products manufactured, marketed and distributed to the Company's customers. The two product segments are connector products and venting products. These segments are differentiated in several ways, including the types of materials, the production processes, the distribution channels and the product applications. Transactions between the two segments were immaterial for each of the periods presented.

The following table illustrates certain measurements used by management to assess the performance of the segments described above as of or for the following periods:

<i>(in thousands)</i>	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2006	2005	2006	2005
<i>Net Sales</i>				
Connector products	\$ 201,739	\$ 209,453	\$ 614,901	\$ 582,194
Venting products	24,979	24,356	68,706	60,165