COMTECH TELECOMMUNICATIONS CORP /DE/
Form 10-Q
March 08, 2012
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 January 31, 2012

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-7928
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation /organization)	11-2139466 (I.R.S. Employer Identification Number)
68 South Service Road, Suite 230, Melville, NY (Address of principal executive offices)	11747 (Zip Code)

(631) 962-7000
(Registrant's telephone number, including area code)

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

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

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

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

Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS:

As of March 5, 2012, the number of outstanding shares of Common Stock, par value $.10 per share, of the registrant was 19,014,817 shares.

COMTECH TELECOMMUNICATIONS CORP.
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PART I
FINANCIAL INFORMATION
COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

Item 1.

Assets	January 31, 2012 (Unaudited)	July 31, 2011
Current assets:		
Cash and cash equivalents	$400,216,000	558,804,000
Accounts receivable, net	60,902,000	70,801,000
Inventories, net	75,207,000	74,661,000
Prepaid expenses and other current assets	8,747,000	7,270,000
Deferred tax asset, net	11,892,000	11,529,000
Total current assets	556,964,000	723,065,000
Property, plant and equipment, net	24,515,000	26,638,000
Goodwill	137,354,000	137,354,000
Intangibles with finite lives, net	42,059,000	45,470,000
Deferred financing costs, net	3,326,000	3,823,000
Other assets, net	1,182,000	1,159,000
Total assets	$765,400,000	937,509,000
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$18,668,000	23,501,000
Accrued expenses and other current liabilities	36,427,000	49,858,000
Dividends payable	5,352,000	6,100,000
Customer advances and deposits	8,048,000	11,011,000
Interest payable	1,553,000	1,531,000
Income taxes payable	-	4,056,000
Total current liabilities	70,048,000	96,057,000
Convertible senior notes	200,000,000	200,000,000
Other liabilities	6,306,000	6,360,000
Income taxes payable	3,235,000	3,811,000
Deferred tax liability	1,697,000	2,101,000
Total liabilities	281,286,000	308,329,000
Commitments and contingencies (See Note 20)		
Stockholders' equity:		
Preferred stock, par value $.10 per share; shares authorized and unissued 2,000,000	-	-
Common stock, par value $.10 per share; authorized 100,000,000 shares; issued 28,869,089 shares and 28,731,265 shares at January 31, 2012 and July 31, 2011, respectively	2,887,000	2,873,000
Additional paid-in capital	358,697,000	355,001,000
Retained earnings	400,077,000	393,109,000
	761,661,000	750,983,000

Less:		
Treasury stock, at cost (9,574,737 shares and 4,508,445 shares at January 31, 2012 and July 31, 2011, respectively)	(277,547,000)	(121,803,000)
Total stockholders' equity	484,114,000	629,180,000
Total liabilities and stockholders' equity	$765,400,000	937,509,000

See accompanying notes to condensed consolidated financial statements.

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three months ended January 31,		Six months ended January 31,	
	2012	2011	2012	2011
Net sales	$99,141,000	162,811,000	212,502,000	340,971,000
Cost of sales	57,725,000	101,901,000	119,806,000	215,827,000
Gross profit	41,416,000	60,910,000	92,696,000	125,144,000
Expenses:				
Selling, general and administrative	19,626,000	23,175,000	43,744,000	47,190,000
Research and development	9,444,000	10,467,000	19,128,000	21,218,000
Amortization of intangibles	1,692,000	2,004,000	3,411,000	3,891,000
Merger termination fee, net	-	-	-	(12,500,000)
	30,762,000	35,646,000	66,283,000	59,799,000
Operating income	10,654,000	25,264,000	26,413,000	65,345,000
Other expenses (income):				
Interest expense	2,183,000	2,090,000	4,329,000	4,153,000
Interest income and other	(434,000)	(626,000)	(930,000)	(1,320,000)
Income before provision for income taxes	8,905,000	23,800,000	23,014,000	62,512,000
Provision for income taxes	3,084,000	7,704,000	4,592,000	20,760,000
Net income	$5,821,000	16,096,000	18,422,000	41,752,000
Net income per share (See Note 6):				
Basic	$0.29	0.59	0.85	1.51
Diluted	$0.27	0.52	0.75	1.32
Weighted average number of common shares outstanding – basic	20,087,000	27,209,000	21,672,000	27,664,000
Weighted average number of common and common equivalent shares outstanding – diluted	26,056,000	32,983,000	27,588,000	33,403,000
Dividends declared per issued and outstanding common share as of the applicable dividend record date	$0.275	0.25	0.55	0.50

See accompanying notes to condensed consolidated financial statements.

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COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME
SIX MONTHS ENDED JANUARY 31, 2012 AND 2011
(Unaudited)

	Common Stock		Additional		Treasury Stock			
			Paid-in	Retained			Stockholders'	Comprehensive
	Shares	Amount	Capital	Earnings	Shares	Amount	Equity	Income
Balance July 31, 2010	28,542,535	$2,854,000	$347,514,000	$351,449,000	210,937	$(185,000)	$701,632,000	
Equity-classified stock award compensation	-	-	2,807,000	-	-	-	2,807,000	
Proceeds from exercise of options	66,945	7,000	1,005,000	-	-	-	1,012,000	
Proceeds from issuance of employee stock purchase plan shares	25,170	2,000	585,000	-	-	-	587,000	
Cash dividends	-	-	-	(13,614,000)	-	-	(13,614,000)	
Excess income tax benefit from stock-based award exercises	-	-	113,000	-	-	-	113,000	
Reversal of deferred tax assets associated with expired and unexercised stock-based awards	-	-	(1,237,000)	-	-	-	(1,237,000)	
Repurchases of common stock	-	-	-	-	1,628,848	(46,804,000)	(46,804,000)	
Net income	-	-	-	41,752,000	-	-	41,752,000	$4
Balance January 31, 2011	28,634,650	$2,863,000	$350,787,000	$379,587,000	1,839,785	$(46,989,000)	$686,248,000	$4
Balance July 31, 2011	28,731,265	$2,873,000	$355,001,000	$393,109,000	4,508,445	$(121,803,000)	$629,180,000	
Equity-classified stock award	-	-	1,834,000	-	-	-	1,834,000	

compensation								
Proceeds from exercise of options	114,160	12,000	2,575,000	-	-	-	2,587,000	
Proceeds from issuance of employee stock purchase plan shares	23,664	2,000	554,000	-	-	-	556,000	
Cash dividends	-	-	-	(11,454,000)	-	-	(11,454,000)	
Income tax shortfall from stock-based award exercises	-	-	(81,000)	-	-	-	(81,000)	
Reversal of deferred tax assets associated with expired and unexercised stock-based awards	-	-	(1,186,000)	-	-	-	(1,186,000)	
Repurchases of common stock	-	-	-	-	5,066,292	(155,744,000)	(155,744,000)	
Net income	-	-	-	18,422,000	-	-	18,422,000	$1
Balance January 31, 2012	28,869,089	$2,887,000	$358,697,000	$400,077,000	9,574,737	$(277,547,000)	$484,114,000	$1

See accompanying notes to condensed consolidated financial statements.

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six months ended January 31, 2012	2011
Cash flows from operating activities:		
Net income	$18,422,000	41,752,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property, plant and equipment	4,781,000	6,620,000
Amortization of intangible assets with finite lives	3,411,000	3,891,000
Amortization of stock-based compensation	1,909,000	2,859,000
Deferred financing costs	746,000	699,000
Loss (gain) on disposal of property, plant and equipment	2,000	(1,000)
(Benefit from) provision for allowance for doubtful accounts	(50,000)	315,000
Provision for excess and obsolete inventory	1,616,000	932,000
Excess income tax benefit from stock-based award exercises	(82,000)	(113,000)
Deferred income tax (benefit) expense	(1,953,000)	358,000
Changes in assets and liabilities, net of effects of acquisition:		
Accounts receivable	9,949,000	54,661,000
Inventories	(5,007,000)	(7,350,000)
Prepaid expenses and other current assets	(255,000)	1,520,000
Other assets	(23,000)	711,000
Accounts payable	(4,833,000)	(54,453,000)
Accrued expenses and other current liabilities	(9,003,000)	(11,075,000)
Customer advances and deposits	(2,963,000)	6,087,000
Other liabilities	446,000	350,000
Interest payable	22,000	-
Income taxes payable	(5,935,000)	(3,523,000)
Net cash provided by operating activities	11,200,000	44,240,000
Cash flows from investing activities:		
Purchases of property, plant and equipment	(2,660,000)	(3,350,000)
Purchases of other intangibles with finite lives	-	(50,000)
Payments for business acquisitions	-	(2,550,000)
Net cash used in investing activities	(2,660,000)	(5,950,000)
Cash flows from financing activities:		
Repurchases of common stock	(157,745,000)	(46,804,000)
Cash dividends paid	(12,202,000)	(6,915,000)
Proceeds from exercises of stock options	2,587,000	1,012,000
Proceeds from issuance of employee stock purchase plan shares	556,000	587,000
Excess income tax benefit from stock-based award exercises	82,000	113,000
Payment of contingent consideration related to business acquisition	(157,000)	-
Origination fees related to line of credit	(249,000)	(539,000)
Net cash used in financing activities	(167,128,000)	(52,546,000)
Net decrease in cash and cash equivalents	(158,588,000)	(14,256,000)

Cash and cash equivalents at beginning of period	558,804,000	607,594,000
Cash and cash equivalents at end of period	$400,216,000	593,338,000

See accompanying notes to condensed consolidated financial statements.

(Continued)

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
(Unaudited)

	Six months ended January 31,	
	2012	2011
Supplemental cash flow disclosures:		
Cash paid during the period for:		
Interest	$3,193,000	3,215,000
Income taxes	$12,481,000	24,204,000
Non cash investing and financing activities:		
Business acquisition liabilities (See Note 18)	$-	4,103,000
Cash dividends declared	$5,352,000	6,699,000

See accompanying notes to condensed consolidated financial statements.

COMTECH TELECOMMUNICATIONS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(1) General

The accompanying condensed consolidated financial statements of Comtech Telecommunications Corp. and Subsidiaries ("Comtech," "we," "us," or "our") as of and for the three and six months ended January 31, 2012 and 2011 are unaudited. In the opinion of management, the information furnished reflects all material adjustments (which include normal recurring adjustments) necessary for a fair presentation of the results for the unaudited interim periods. Our results of operations for such periods are not necessarily indicative of the results of operations to be expected for the full fiscal year.

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amount of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual results may differ from those estimates.

Our condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements, filed with the Securities and Exchange Commission ("SEC"), for the fiscal year ended July 31, 2011 and the notes thereto contained in our Annual Report on Form 10-K, and all of our other filings with the SEC.

(2) Adoption of Accounting Standards Updates

The Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC") is subject to updates by FASB, which are known as Accounting Standards Updates ("ASUs"). The following are FASB ASUs which have been issued and incorporated into the FASB ASC and adopted by us:

On August 1, 2011, we adopted FASB ASU No. 2010-06, which amends the disclosure requirements of FASB ASC 820-10, "Fair Value Measurements and Disclosures – Overall." This FASB ASU requires that information about purchases, sales, issuances and settlements be presented separately, on a gross basis, in Level 3 fair value measurement reconciliations. Our adoption of this ASU did not have any impact on our condensed consolidated financial statements, as we have historically valued our money market mutual funds and U.S. Treasury securities using Level 1 inputs and do not have any other assets or liabilities in our Condensed Consolidated Balance Sheets at estimated fair value.

On August 1, 2011, we adopted FASB ASU No. 2010-28, which amends the factors considered in determining if goodwill is impaired in FASB ASC 350, "Intangibles – Goodwill and Other." This ASU requires entities that have reporting units with carrying amounts that are zero or negative to assess whether it is more likely than not that the reporting unit's goodwill is impaired and, if an impairment is likely, to perform Step 2 of the goodwill impairment test for the reporting unit(s). On August 1, 2011, the date we performed our annual goodwill impairment test for fiscal 2012, none of our reporting units with goodwill had a zero or negative carrying value and, as such, our adoption of this ASU did not have any impact on our condensed consolidated financial statements.

On August 1, 2011, we adopted FASB ASU No. 2010-29, which amends the presentation and disclosure requirements of FASB ASC 805, "Business Combinations." This ASU requires a public entity that presents comparative financial statements to disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. This ASU also expands the supplemental proforma disclosures required. Our adoption of this

ASU did not have any impact on our condensed consolidated financial statements, as we did not acquire any businesses during the six months ended January 31, 2012.

On August 1, 2011, we adopted FASB ASU No. 2010-20, which amends ASC 310, “Receivables” by requiring additional disclosures regarding troubled debt restructuring. In addition, we also adopted FASB ASU No. 2011-02, which amends the previously issued guidance on evaluation of whether or not a restructuring constitutes a troubled debt restructuring. Our adoption of these ASUs did not have any impact on our condensed consolidated financial statements given that substantially all of our receivables are classified as trade receivables.

(3) Reclassifications

Certain reclassifications have been made to previously reported financial statements to conform to our current financial statement format.

(4) Stock-Based Compensation

We issue stock-based awards to certain of our employees and our Board of Directors and we recognize related stock-based compensation for both equity and liability-classified stock-based awards in our condensed consolidated financial statements. These awards are issued pursuant to our 2000 Stock Option Plan and our 2001 Employee Stock Purchase Plan (the "ESPP").

Stock-based compensation for equity-classified awards is measured at the date of grant, based on an estimate of the fair value of the award and is generally expensed over the vesting period of the grant. Stock-based compensation for liability-classified awards is determined the same way, except that the fair value of liability-classified awards is remeasured at the end of each reporting period until the award is settled, with changes in fair value recognized pro-rata for the portion of the requisite service period rendered.

Stock-based compensation for awards issued is reflected in the following line items in our Condensed Consolidated Statements of Operations:

	Three months ended January 31,		Six months ended January 31,	
	2012	2011	2012	2011
Cost of sales	$ 125,000	151,000	178,000	273,000
Selling, general and administrative expenses	795,000	953,000	1,440,000	2,051,000
Research and development expenses	116,000	247,000	291,000	535,000
Stock-based compensation expense before income tax benefit	1,036,000	1,351,000	1,909,000	2,859,000
Income tax benefit	(394,000)	(489,000)	(701,000)	(1,031,000)
Net stock-based compensation expense	$ 642,000	862,000	1,208,000	1,828,000

Of the total stock-based compensation expense before income tax benefit recognized in the three months ended January 31, 2012 and 2011, $59,000 and $79,000, respectively, related to awards issued pursuant to our ESPP. Of the total stock-based compensation expense before income tax benefit recognized in the six months ended January 31, 2012 and 2011, $120,000 and $148,000, respectively, related to awards issued pursuant to our ESPP.

Included in total stock-based compensation expense before income tax benefit in the three months ended January 31, 2012 and 2011 is a benefit of $14,000 and $7,000, respectively, as a result of the required fair value remeasurement of our liability-classified stock appreciation rights ("SARs") at the end of each of the respective reporting periods. Included in total stock-based compensation expense before income tax benefit in the six months ended January 31, 2012 and 2011 is an expense of $6,000 and $10,000, respectively, related to SARs.

Stock-based compensation that was capitalized and included in ending inventory at January 31, 2012 and July 31, 2011 was $48,000 and $117,000, respectively.

We estimate the fair value of stock-based awards using the Black-Scholes option pricing model. The Black-Scholes option pricing model includes assumptions regarding dividend yield, expected volatility, expected option term and risk-free interest rates. The assumptions used in computing the fair value of stock-based awards reflect our best estimates, but involve uncertainties relating to market and other conditions, many of which are outside of our control. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by the employees who receive stock-based awards.

The per share weighted average grant-date fair value of stock-based awards granted during the three months ended January 31, 2012 approximated $6.34. There were no stock-based awards granted during the three months ended January 31, 2011. The per share weighted average grant-date fair value of stock-based awards granted during the six months ended January 31, 2012 and 2011 approximated $5.93 and $6.67, respectively. In addition to the exercise and grant-date prices of these awards, we utilized certain weighted average assumptions to estimate the initial fair value of stock-based awards.

Weighted average assumptions related to our stock-based awards are listed in the table below:

	Three months ended January 31,			Six months ended January 31,			
	2012		2011	2012		2011	
Expected dividend yield	3.68	%	-	4.00	%	3.66	%
Expected volatility	37.70	%	-	36.20	%	38.00	%
Risk-free interest rate	0.42	%	-	0.83	%	1.27	%
Expected life (years)	3.81		-	5.24		5.18	

Stock-based awards granted have exercise prices equal to the fair market value of the stock on the date of grant, a contractual term of five or ten years and a vesting period of three or five years. We settle employee stock option exercises with new shares. All SARs granted through January 31, 2012 may only be settled with cash. Included in accrued expenses at January 31, 2012 and July 31, 2011 is $28,000 and $22,000, respectively, relating to the potential cash settlement of SARs.

The expected dividend yield is the expected annual dividend as a percentage of the fair market value of the stock on the date of grant. For the stock-based awards granted during the six months ended January 31, 2012 and 2011, the expected dividend yield was equal to our targeted annual dividend of $1.10 per share and $1.00 per share, respectively, divided by the quoted market price of our common stock on the date of the grant. We estimate expected volatility by considering the historical volatility of our stock, the implied volatility of publicly traded call options on our stock, the implied volatility of call options embedded in our 3.0% convertible senior notes and our expectations of volatility for the expected life of stock-based awards. The risk-free interest rate is based on the U.S. treasury yield curve in effect at the time of grant for an instrument which closely approximates the expected option term. The expected option term is the number of years we estimate that stock-based awards will be outstanding prior to exercise. The expected life of awards issued is determined by employee groups with sufficiently distinct behavior patterns.

The following table provides the components of the actual income tax benefit recognized for tax deductions relating to the exercise of stock-based awards:

		Six months ended January 31,			
		2012		2011	
Actual income tax benefit recorded for the tax deductions relating to the exercise of stock-based awards	$	235,000		215,000	
Less: Tax benefit initially recognized on exercised stock-based awards vesting subsequent to the adoption of accounting standards that require us to expense stock-based awards, excluding income tax shortfalls		(151,000	)	(102,000	)
Excess income tax benefit recorded as an increase to additional paid-in capital		84,000		113,000	
		(2,000	)	-	

Less: Tax benefit initially disclosed but not previously recognized on exercised equity-classified stock-based awards vesting prior to the adoption of accounting standards that require us to expense stock-based awards			
Excess income tax benefit from exercised equity-classified stock-based awards reported as a cash flow from financing activities in our Condensed Consolidated Statements of Cash Flows	$	82,000	113,000

At January 31, 2012, total remaining unrecognized compensation cost related to unvested stock-based awards was $7,527,000, net of estimated forfeitures of $587,000. The net cost is expected to be recognized over a weighted average period of approximately 3.5 years.

As of January 31, 2012, the amount of hypothetical tax benefits related to stock-based awards was $22,851,000. During the six months ended January 31, 2012 and 2011, we recorded $1,186,000 and $1,237,000, respectively, as a reduction to additional paid-in capital, which represented the reversal of unrealized deferred tax assets associated with certain vested equity-classified stock-based awards that expired during the period.

(5) Fair Value Measurements and Financial Instruments

In accordance with FASB ASC 825, “Financial Instruments,” we determined that, as of January 31, 2012 and July 31, 2011, the fair value of our 3.0% convertible senior notes was approximately $221,080,000 and $207,680,000, respectively, based on a quoted market price in an active market. Our 3.0% convertible senior notes are not marked-to-market and are shown in our accompanying Condensed Consolidated Balance Sheets at their original issuance value. As such, changes in the estimated fair value of our 3.0% convertible senior notes are not recorded in our condensed consolidated financial statements.

As of January 31, 2012 and July 31, 2011, we had approximately $104,068,000 and $152,878,000, respectively, of money market mutual funds which are classified as cash and cash equivalents in our Condensed Consolidated Balance Sheets. These money market mutual funds are recorded at their current fair value. FASB ASC 820, “Fair Value Measurements and Disclosures,” requires us to define fair value as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, using the fair value hierarchy described in FASB ASC 820, we valued our money market mutual funds using Level 1 inputs that were based on quoted market prices. As of January 31, 2012 and July 31, 2011, we had no other assets included in our Condensed Consolidated Balance Sheets that are recorded at current fair value. If we acquire different types of assets or incur different types of liabilities in the future, we might be required to use different FASB ASC fair value methodologies.

(6) Earnings Per Share

Our basic earnings per share (“EPS”) is computed based on the weighted average number of shares outstanding during each respective period. Our diluted EPS reflects the dilution from potential common stock issuable pursuant to the exercise of equity-classified stock-based awards and convertible senior notes, if dilutive, outstanding during each respective period. When calculating our diluted EPS, we consider (i) the amount an employee must pay upon assumed exercise of stock-based awards; (ii) the amount of stock-based compensation cost attributed to future services and not yet recognized; and (iii) the amount of excess tax benefits, if any, that would be credited to additional paid-in capital assuming exercise of in-the-money stock-based awards. This excess tax benefit is the amount resulting from a tax deduction for compensation in excess of compensation expense, based on the Black Scholes option pricing model, recognized for financial reporting purposes.

Equity-classified stock-based awards to purchase 2,147,000 and 2,435,000 shares, for the three months ended January 31, 2012 and 2011, respectively, were not included in our diluted EPS calculation because their effect would have been anti-dilutive. Equity-classified stock-based awards to purchase 2,647,000 and 2,464,000 shares, for the six months ended January 31, 2012 and 2011, respectively, were not included in our diluted EPS calculation because their effect would have been anti-dilutive. Liability-classified stock-based awards do not impact and are not included in the denominator for EPS calculations.

In addition, the weighted-average basic and diluted shares outstanding for the three months ended January 31, 2012 and 2011 reflect a reduction of approximately 1,544,000 and 475,000 shares as a result of the repurchase of our common shares during the respective periods. The weighted-average basic and diluted shares outstanding for the six months ended January 31, 2012 and 2011 reflect a reduction of approximately 2,627,000 and 711,000 shares as a result of the repurchase of our common shares during the respective periods. See Note (19) – “Stockholders’ Equity” for more information on our stock repurchase program.

The following table reconciles the numerators and denominators used in our basic and diluted EPS calculations:

	Three months ended January 31,		Six months ended January 31,	
	2012	2011	2012	2011
Numerator:				
Net income for basic calculation	$ 5,821,000	16,096,000	18,422,000	41,752,000
Effect of dilutive securities:				
Interest expense (net of tax) on 3.0% convertible senior notes	1,117,000	1,117,000	2,234,000	2,234,000
Numerator for diluted calculation	$ 6,938,000	17,213,000	20,656,000	43,986,000
Denominator:				
Denominator for basic calculation	20,087,000	27,209,000	21,672,000	27,664,000
Effect of dilutive securities:				
Stock options	228,000	234,000	200,000	223,000
Conversion of 3.0% convertible senior notes	5,741,000	5,540,000	5,716,000	5,516,000
Denominator for diluted calculation	26,056,000	32,983,000	27,588,000	33,403,000

(7) Accounts Receivable

Accounts receivable consist of the following:

	January 31, 2012	July 31, 2011
Billed receivables from commercial customers	$ 35,402,000	38,245,000
Billed receivables from the U.S. government and its agencies	19,538,000	22,075,000
Unbilled receivables on contracts-in-progress	7,139,000	11,701,000
Total accounts receivable	62,079,000	72,021,000
Less allowance for doubtful accounts	1,177,000	1,220,000
Accounts receivable, net	$ 60,902,000	70,801,000

Unbilled receivables on contracts-in-progress include $2,594,000 and $4,487,000 at January 31, 2012 and July 31, 2011, respectively, due from the U.S. government and its agencies. There was $28,000 of retainage included in unbilled receivables at both January 31, 2012 and July 31, 2011. In the opinion of management, substantially all of the unbilled balances will be billed and collected within one year.

(8) Inventories

Inventories consist of the following:

	January 31, 2012	July 31, 2011
Raw materials and components	$ 56,919,000	53,678,000
Work-in-process and finished goods	33,460,000	34,299,000
Total inventories	90,379,000	87,977,000
Less reserve for excess and obsolete inventories	15,172,000	13,316,000
Inventories, net	$ 75,207,000	74,661,000

At January 31, 2012 and July 31, 2011, the amount of inventory directly related to long-term contracts (including contracts-in-progress) was $2,871,000 and $8,041,000, respectively.

At January 31, 2012, $320,000 of our long-term contract inventory relates to our BFT-1 contract. Our BFT-1 contract is known as an “indefinite delivery/indefinite quantity” type contract; thus, the U.S. Army is not obligated to purchase any additional products or services from us in the future. Almost the entire long-term BFT-1 inventory relates to BFT-1 orders already in our backlog. The remaining portion is expected to be used for incidental purchases and customer repairs. If we are left with inventories of unusable parts, we would likely have to write-off the remaining balance in the period that we make such determination.

At January 31, 2012 and July 31, 2011, $1,043,000 and $1,339,000, respectively, of the total inventory balance above related to contracts from third party commercial customers who outsource their manufacturing to us.

(9) Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following:

		January 31, 2012	July 31, 2011
Accrued wages and benefits	$	12,681,000	19,751,000
Accrued warranty obligations		8,852,000	9,120,000
Accrued commissions and royalties		4,093,000	3,295,000
Accrued business acquisition payments		1,070,000	726,000
Other		9,731,000	16,966,000
Accrued expenses and other current liabilities	$	36,427,000	49,858,000

We provide warranty coverage for most of our products for a period of at least one year from the date of shipment. We record a liability for estimated warranty expense based on historical claims, product failure rates and other factors. Some of our product warranties are provided under long-term contracts, the costs of which are incorporated into our estimates of total contract costs.

Changes in our product warranty liability during the six months ended January 31, 2012 and 2011 were as follows:

		January 31, 2012	January 31, 2011
Balance at beginning of period	$	9,120,000	10,562,000
Provision for warranty obligations		3,194,000	3,680,000
Reversal of warranty liability		-	(525,000)
Charges incurred		(3,462,000)	(3,986,000)
Balance at end of period	$	8,852,000	9,731,000

(10) Cost Reduction Actions

Fiscal 2011 and Fiscal 2012 Cost Reduction Actions

During the six months ended January 31, 2012, we continued to implement certain cost reduction actions that we initiated in prior periods in all of our reportable operating segments.

Costs (almost all of which have been for severance) for each respective period are included in our Condensed Consolidated Statements of Operations and have not been material in the aggregate.

Fiscal 2009 Radyne Acquisition-Related Restructuring Plan

In connection with our August 1, 2008 acquisition of Radyne, we immediately adopted a restructuring plan to achieve operating synergies for which we recorded $2,713,000 of estimated restructuring costs. Of this amount, $613,000 relates to severance for Radyne employees which was paid in fiscal 2009. The remaining estimated amounts relate to facility exit costs and were determined as follows:

		At August 1, 2008
Total non-cancelable lease obligations	$	12,741,000
Less: Estimated sublease income		(8,600,000)
Total net estimated facility exit costs		4,141,000
Less: Interest expense to be accreted		(2,041,000)
Present value of estimated facility exit costs	$	2,100,000

Our total non-cancelable lease obligations were based on the actual lease term which runs from November 1, 2008 through October 31, 2018. We estimated sublease income based on (i) the terms of a fully executed sublease agreement, whose lease term runs from November 1, 2008 through October 31, 2015 and (ii) our assessment of future uncertainties relating to the commercial real estate market. Based on our assessment of commercial real estate market conditions, we currently believe that it is not probable that we will be able to sublease the facility beyond the current sublease terms. As such, in accordance with grandfathered accounting standards that were not incorporated into the FASB's ASC, we recorded these costs, at fair value, as assumed liabilities as of August 1, 2008, with a corresponding increase to goodwill.

As of January 31, 2012, the amount of the acquisition-related restructuring reserve is as follows:

	Cumulative Activity Through January 31, 2012
Present value of estimated facility exit costs at August 1, 2008	$ 2,100,000
Cash payments made	(3,795,000)
Cash payments received	3,889,000
Accreted interest recorded	521,000
Net liability as of January 31, 2012	2,715,000
Amount recorded as prepaid expenses in the Condensed Consolidated Balance Sheet	406,000
Amount recorded as other liabilities in the Condensed Consolidated Balance Sheet	$ 3,121,000

As of July 31, 2011, the present value of the estimated facility exit costs was $2,518,000. During the six months ended January 31, 2012, we made cash payments of $499,000 and we received cash payments of $605,000. Interest accreted for the three and six months ended January 31, 2012 and 2011 was $46,000 and $91,000, respectively, and $40,000 and $78,000, respectively, and is included in interest expense for each of the respective fiscal periods.

As of January 31, 2012, future cash payments associated with our restructuring plan are summarized below:

	As of January 31, 2012
Future lease payments to be made in excess of anticipated sublease payments	$ 3,121,000
Less net cash to be received in next twelve months	(406,000)
Interest expense to be accreted in future periods	1,519,000
Total remaining net cash payments	$ 4,234,000

(11) Credit Facility

We have a committed $150,000,000 secured revolving credit facility (the "Credit Facility") with a syndicate of bank lenders that expires on January 31, 2014. The Credit Facility provides for the extension of credit to us in the form of revolving loans, including letters of credit, at any time and from time to time during its term, in an aggregate principal amount at any time outstanding not to exceed $150,000,000 for both revolving loans and letters of credit, with sub-limits of $15,000,000 for commercial letters of credit and $35,000,000 for standby letters of credit. The Credit Facility may be used for acquisitions, equity securities repurchases, dividends, working capital and other general corporate purposes.

At our election, borrowings under the Credit Facility will bear interest either at LIBOR plus an applicable margin or at the base rate plus an applicable margin. The interest rate margin over LIBOR ranges from 2.25 percent, up to a maximum amount of 2.75 percent. The base rate is a fluctuating rate equal to the highest of (i) the Prime Rate; (ii) the Federal Funds Effective Rate from time to time plus 0.5 percent; and (iii) two hundred (200) basis points in excess of the floating rate of interest determined, on a daily basis, in accordance with the terms of the agreement. The interest rate margin over the base rate ranges from 1.25 percent up to a maximum amount of 1.75 percent. In both cases, the applicable interest rate margin is based on the ratio of our consolidated total indebtedness to our consolidated earnings before interest, taxes, depreciation and amortization ("Consolidated Adjusted EBITDA"). As defined in the Credit Facility, Consolidated Adjusted EBITDA is adjusted for certain items and, in the event of an acquisition, provides for the inclusion of the last twelve months of consolidated EBITDA of a target.

The Credit Facility contains covenants, including covenants limiting certain debt, certain liens on assets, certain sales of assets and receivables, certain payments (including dividends), certain repurchases of equity securities, certain sale and leaseback transactions, certain guaranties and certain investments. The Credit Facility also contains financial condition covenants requiring that we (i) not exceed a maximum ratio of consolidated total indebtedness to Consolidated Adjusted EBITDA (each as defined in the Credit Facility); (ii) not exceed a maximum ratio of consolidated senior secured indebtedness to Consolidated Adjusted EBITDA (each as defined in the Credit Facility); (iii) maintain a minimum fixed charge ratio (as defined in the Credit Facility); (iv) maintain a minimum consolidated net worth; in each case measured on the last day of each fiscal quarter and (v) in the event total consolidated indebtedness (as defined in the Credit Facility) is less than $200,000,000, we maintain a minimum level of Consolidated Adjusted EBITDA (as defined in the Credit Facility).

At January 31, 2012, we had $1,748,000 of standby letters of credit outstanding related to our guarantees of future performance on certain customer contracts and no outstanding commercial letters of credit.

At January 31, 2012, had borrowings been outstanding under the Credit Facility, the applicable interest rate margin above LIBOR and base rate borrowings would have been 2.75 percent and 1.75 percent, respectively. We are also subject to an undrawn line fee based on the ratio of our consolidated total indebtedness to our Consolidated Adjusted EBITDA, as defined and adjusted for certain items in the Credit Facility. Interest expense, including amortization of deferred financing costs, related to our credit facility recorded during the three and six months ended January 31, 2012 was $244,000 and $451,000, respectively, as compared to $158,000 and $368,000 during the three and six months ended January 31, 2011, respectively.

At January 31, 2012, based on our Consolidated Adjusted EBITDA (as defined in the Credit Facility) and our business outlook and related business plans, we believe we will be able to meet or obtain waivers for the applicable financial covenants that we are required to maintain.

(12) 3.0% Convertible Senior Notes

In May 2009, we issued $200,000,000 of our 3.0% convertible senior notes in a private offering pursuant to Rule 144A under the Securities Act of 1933, as amended. The net proceeds from this transaction were $194,541,000 after deducting the initial purchasers' discount and other transaction costs of $5,459,000.

The 3.0% convertible senior notes bear interest at an annual rate of 3.0% and, effective January 20, 2012 (the record date of our dividend declared on December 8, 2011), are convertible into shares of our common stock at a conversion price of $34.56 per share (a conversion rate of 28.9360 shares per $1,000 original principal amount of notes) at any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, subject to adjustment in certain circumstances. Pursuant to the terms of the 3.0% convertible senior notes indenture, cash dividends require an adjustment to the conversion rate, effective on the record date.

We may, at our option, redeem some or all of the 3.0% convertible senior notes on or after May 5, 2014. Holders of the 3.0% convertible senior notes will have the right to require us to repurchase some or all of the outstanding 3.0% convertible senior notes, solely for cash, on May 1, 2014, May 1, 2019 and May 1, 2024 and upon certain events, including a change in control. If not redeemed by us or repaid pursuant to the holders' right to require repurchase, the 3.0% convertible senior notes mature on May 1, 2029.

The 3.0% convertible notes are senior unsecured obligations of Comtech.

(13) Income Taxes

Our effective tax rate was 20.0% for the six months ended January 31, 2012, which includes a net discrete tax benefit of $3,463,000 principally relating to the effective settlement of certain federal and state income tax audits and the reversal of previously recorded tax liabilities no longer required due to the expiration of applicable statutes of limitations. Excluding the impact of discrete tax items, our fiscal 2012 estimated tax rate is expected to approximate 35.0%. Our effective tax rate during fiscal 2012 only includes five months of benefit associated with the federal research and experimentation credit which expired on December 31, 2011.

At January 31, 2012 and July 31, 2011, total unrecognized tax benefits, excluding interest, were $3,454,000 and $6,763,000, respectively. Of these amounts, $2,791,000 and $5,719,000, respectively, net of the reversal of the federal benefit recognized as a deferred tax asset relating to state reserves, would positively impact our effective tax rate, if recognized. Unrecognized tax benefits result from income tax positions taken or expected to be taken on our income tax returns for which a tax benefit has not been recorded in our financial statements. Of the total unrecognized tax benefits, $3,235,000 and $3,811,000, including interest, were recorded as non-current income taxes payable in our Condensed Consolidated Balance Sheets at January 31, 2012 and July 31, 2011, respectively.

Our policy is to recognize interest and penalties relating to uncertain tax positions in income tax expense. At January 31, 2012 and July 31, 2011, interest accrued relating to income taxes was $133,000 and $545,000, respectively, net of the related income tax benefit.

In August 2011, we reached an effective settlement with the IRS relating to its audit of our federal income tax returns for fiscal 2007, fiscal 2008 and fiscal 2009. Although adjustments relating to the settlement of our prior year completed audits were immaterial, a resulting tax assessment or settlement for other potential later periods, or for other tax jurisdictions, could have a material adverse effect on our consolidated results of operations and financial condition. The IRS is not currently examining any of the federal income tax returns filed by Radyne for the tax years prior to August 1, 2008, which was the date we acquired Radyne. Our federal income tax returns for fiscal 2010 and fiscal 2011 and the federal income tax return filed by Radyne for 2008 are subject to potential future IRS audit.

(14) Stock Option Plan and Employee Stock Purchase Plan

We issue stock-based awards pursuant to the following plan:

2000 Stock Incentive Plan – The 2000 Stock Incentive Plan, as amended, provides for the granting to all employees and consultants of Comtech (including prospective employees and consultants) non-qualified stock options, SARs, restricted stock, restricted stock units (“RSUs”), performance shares, performance units and other stock-based awards. In addition, our employees are eligible to be granted incentive stock options. Our non-employee directors are eligible to receive non-discretionary grants of non-qualified stock options, restricted stock, RSUs and other stock-based awards subject to certain limitations. The aggregate number of shares of common stock which may be issued may not exceed 8,962,500. Grants of incentive and non-qualified stock awards may not have a term exceeding ten years or, in the case of an incentive stock award granted to a stockholder who owns stock representing more than 10% of the voting power, no more than five years.

As of January 31, 2012, we had granted stock-based awards representing the right to purchase an aggregate of 6,912,543 shares (net of 1,577,760 canceled awards) at prices ranging between $3.13 - $51.65, of which 3,222,718 were outstanding at January 31, 2012. As of January 31, 2012, 3,690,225 stock-based awards have been exercised, of which 750 were SARs. All stock-based awards have exercise prices equal to the fair market value of the stock on the date of grant. RSUs, restricted stock and stock units are generally valued at the fair market value of our common stock at the grant date.

The following table summarizes certain stock option plan activity during the six months ended January 31, 2012:

	Number of Shares Underlying Stock-Based Awards	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at July 31, 2011	3,580,168	$ 31.86		
Granted	52,000	27.16		
Expired/canceled	(241,043)	36.64		
Exercised	(99,260)	22.57		
Outstanding at October 31, 2011	3,291,865	31.71		
Granted	6,753	29.89		
Expired/canceled	(61,000)	34.24		
Exercised	(14,900)	23.24		
Outstanding at January 31, 2012	3,222,718	$ 31.70	4.24	$ 9,750,000
Exercisable at January 31, 2012	1,895,465	$ 34.06	1.92	$ 6,393,000
Vested and expected to vest at January 31, 2012	3,156,151	$ 31.77	4.14	$ 9,581,000

Included in the number of shares underlying stock-based awards outstanding at January 31, 2012, in the above table, are 37,500 SARs with an aggregate intrinsic value of $8,800. As of January 31, 2012, there were no awards of RSUs, restricted stock or stock units outstanding.

The total intrinsic value of stock-based awards exercised during the three months ended January 31, 2012 and 2011 was $145,000 and $490,000, respectively. The total intrinsic value of stock-based awards exercised during the six months ended January 31, 2012 and 2011 was $1,009,000 and $987,000, respectively.

2001 Employee Stock Purchase Plan – The ESPP was approved by the shareholders on December 12, 2000, and 675,000 shares of our common stock were reserved for issuance. The ESPP is intended to provide our eligible employees the opportunity to acquire our common stock at 85% of fair market value at the date of issuance through participation in the payroll-deduction based ESPP. Through the second quarter of fiscal 2012, we issued 452,413 shares of our common stock to participating employees in connection with the ESPP.

(15) Customer and Geographic Information

Sales by geography and customer type, as a percentage of consolidated net sales, are as follows:

	Three months ended January 31,		Six months ended January 31,	
	2012	2011	2012	2011
United States				
U.S. government	46.5 %	62.7 %	47.5 %	68.3 %
Commercial customers	12.1 %	7.7 %	12.5 %	7.0 %
Total United States	58.6 %	70.4 %	60.0 %	75.3 %
International	41.4 %	29.6 %	40.0 %	24.7 %

International sales for the three months ended January 31, 2012 and 2011, which include sales to U.S. domestic companies for inclusion in products that will be sold to international customers, were $40,990,000 and $48,254,000, respectively. International sales for the six months ended January 31, 2012 and 2011, which include sales to U.S. domestic companies for inclusion in products that will be sold to international customers, were $84,968,000 and $84,318,000, respectively.

For the three and six months ended January 31, 2012 and 2011, except for sales to the U.S. government (including sales to prime contractors of the U.S. government), no other customer or individual country, including sales to U.S. domestic companies for inclusion in products that will be sold to a foreign country, represented more than 10% of consolidated net sales.

(16) Segment Information

Reportable operating segments are determined based on Comtech's management approach. The management approach, as defined by accounting standards which have been codified into FASB ASC 280, "Segment Reporting," is based on the way that the chief operating decision-maker organizes the segments within an enterprise for making decisions about resources to be allocated and assessing their performance. Our chief operating decision-maker is our President and Chief Executive Officer.

While our results of operations are primarily reviewed on a consolidated basis, the chief operating decision-maker also manages the enterprise in three operating segments: (i) telecommunications transmission, (ii) RF microwave amplifiers, and (iii) mobile data communications.

Telecommunications transmission products include satellite earth station products (such as analog and digital modems, frequency converters, power amplifiers, transceivers and voice gateways) and over-the-horizon microwave communications products and systems (such as digital troposcatter modems).

RF microwave amplifier products include traveling wave tube amplifiers and solid-state, high-power broadband amplifier products that use the microwave and radio frequency spectrums.

Mobile data communications products include satellite-based mobile location tracking and messaging hardware (such as mobile satellite transceivers and third-party produced ruggedized computers) and related services and the design and production of microsatellites.

Corporate management defines and reviews segment profitability based on the same allocation methodology as presented in the segment data tables below:

	Three months ended January 31, 2012				
	Telecommunications Transmission	RF Microwave Amplifiers	Mobile Data Communications	Unallocated	Total
Net sales	$51,328,000	22,437,000	25,376,000	-	$99,141,000
Operating income (loss)	8,319,000	1,195,000	4,408,000	(3,268,000)	10,654,000
Interest income and other (expense)	14,000	(3,000)	7,000	416,000	434,000
Interest expense	166,000	-	-	2,017,000	2,183,000
Depreciation and amortization	2,507,000	1,101,000	397,000	1,084,000	5,089,000
Expenditures for long-lived assets, including intangibles	799,000	369,000	49,000	-	1,217,000
Total assets at January 31, 2012	241,369,000	103,445,000	25,160,000	395,426,000	765,400,000

	Three months ended January 31, 2011				
	Telecommunications Transmission	RF Microwave Amplifiers	Mobile Data Communications	Unallocated	Total
Net sales	$ 62,268,000	23,889,000	76,654,000	-	$ 162,811,000
Operating income (loss)	15,450,000	407,000	14,320,000	(4,913,000)	25,264,000
Interest income and other (expense)	16,000	(5,000)	12,000	603,000	626,000
Interest expense	159,000	-			