

SAFEGUARD SCIENTIFICS INC

Form 10-Q

October 26, 2012

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SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the Quarter Ended September 30, 2012

Commission File Number 1-5620

Safeguard Scientifics, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania
(State or other jurisdiction of
incorporation or organization)

23-1609753
(I.R.S. Employer
ID No.)

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435 Devon Park Drive

Building 800

Wayne, PA

(Address of principal executive offices)

19087

(Zip Code)

(610) 293-0600

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 and 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 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 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 (Do not check if a smaller reporting company) Smaller reporting company

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

Number of shares outstanding as of October 25, 2012

Common Stock 20,950,057

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QUARTERLY REPORT ON FORM 10-Q

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Table of Contents**SAFEGUARD SCIENTIFICS, INC.****CONSOLIDATED BALANCE SHEETS**

	September 30, 2012	December 31, 2011
	(In thousands except	
	per share data) (Unaudited)	
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 71,151	\$ 83,187
Cash held in escrow	6,433	6,433
Marketable securities	120,317	158,098
Restricted cash equivalents	5,310	5,137
Prepaid expenses and other current assets	1,834	1,081
Total current assets	205,045	253,936
Property and equipment, net	175	228
Ownership interests in and advances to partner companies and funds	118,131	114,169
Loan participations receivable	8,860	7,587
Available-for-sale securities	9,648	5,184
Long-term marketable securities	37,811	16,287
Long-term restricted cash equivalents	2,376	7,128
Other assets	1,978	2,117
Total Assets	\$ 384,024	\$ 406,636
LIABILITIES AND EQUITY		
Current Liabilities:		
Accounts payable	\$ 225	\$ 243
Accrued compensation and benefits	3,443	4,583
Accrued expenses and other current liabilities	2,617	3,690
Total current liabilities	6,285	8,516
Other long-term liabilities	3,970	4,146
Convertible senior debentures - non-current	46,215	45,694
Commitments and contingencies		
Equity:		
Preferred stock, \$0.10 par value; 1,000 shares authorized		
Common stock, \$0.10 par value; 83,333 shares authorized; 20,910 and 20,752 shares issued and outstanding in 2012 and 2011, respectively	2,091	2,075
Additional paid-in capital	814,120	810,956
Accumulated deficit	(493,264)	(464,710)
Accumulated other comprehensive income (loss)	4,607	(41)
Total equity	327,554	348,280
Total Liabilities and Equity	\$ 384,024	\$ 406,636

See Notes to Consolidated Financial Statements.

Table of Contents**SAFEGUARD SCIENTIFICS, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS**

Three Months Ended September 30, 2012 **Three Months Ended September 30, 2011**
2012 **2011** **2012** **2011**
(In thousands except per share data)
(Unaudited)

General and administrative expense	\$ 4,790	\$ 5,100	\$ 14,681	\$ 15,554
Operating loss	(4,790)	(5,100)	(14,681)	(15,554)
Other income (loss), net	91	(324)	7,994	(1,391)
Interest income	696	278	2,190	969
Interest expense	(1,461)	(1,445)	(4,369)	(4,522)
Equity income (loss)	(3,293)	28,922	(19,688)	155,634
Net income (loss) before income taxes	(8,757)	22,331	(28,554)	135,136
Income tax benefit (expense)				
Net income (loss)	\$ (8,757)	\$ 22,331	\$ (28,554)	\$ 135,136
Net income (loss) per share:				
Basic	\$ (0.42)	\$ 1.07	\$ (1.36)	\$ 6.52
Diluted	\$ (0.42)	\$ 0.98	\$ (1.36)	\$ 5.68
Average shares used in computing net income (loss) per share:				
Basic	20,999	20,790	20,935	20,737
Diluted	20,999	24,291	20,935	24,573

See Notes to Consolidated Financial Statements.

Table of Contents**SAFEGUARD SCIENTIFICS, INC.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(In thousands)			
	(Unaudited)			
Net income (loss)	\$ (8,757)	\$ 22,331	\$ (28,554)	\$ 135,136
Other comprehensive income (loss), before taxes:				
Unrealized net gain (loss) on available-for-sale securities	(1,390)	(14,552)	4,410	(19,787)
Reclassification adjustment for other than temporary impairment of available-for-sale securities included in net income (loss)	94	389	238	1,520
Total comprehensive income (loss)	\$ (10,053)	\$ 8,168	\$ (23,906)	\$ 116,869

See Notes to Consolidated Financial Statements.

Table of Contents**SAFEGUARD SCIENTIFICS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Nine Months Ended September 30,	
	2012	2011
	(In thousands)	
	(Unaudited)	
Cash Flows from Operating Activities:		
Net cash used in operating activities	\$ (12,616)	\$ (13,584)
Cash Flows from Investing Activities:		
Proceeds from sales of and distributions from companies and funds	14,526	171,167
Advances and loans to companies	(13,315)	(3,150)
Origination fees on mezzanine loans	74	
Acquisitions of ownership interests in companies and funds	(21,719)	(74,692)
Increase in marketable securities	(209,876)	(160,032)
Decrease in marketable securities	226,133	66,306
Repayment of advances to companies	3,214	5,000
Capital expenditures	(25)	(58)
Other, net		108
Net cash provided by (used in) investing activities	(988)	4,649
Cash Flows from Financing Activities:		
Repurchase of convertible senior debentures		(30,848)
Issuance of Company common stock, net	1,568	605
Net cash provided by (used in) financing activities	1,568	(30,243)
Net Decrease in Cash and Cash Equivalents	(12,036)	(39,178)
Cash and Cash Equivalents at beginning of period	83,187	183,419
Cash and Cash Equivalents at end of period	\$ 71,151	\$ 144,241

See Notes to Consolidated Financial Statements.

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SAFEGUARD SCIENTIFICS, INC.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Total	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss) (In thousands) (Unaudited)	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital
Balance December 31, 2011	\$ 348,280	\$ (464,710)	\$ (41)	20,752	\$ 2,075	\$ 810,956
Net loss	(28,554)	(28,554)				
Stock options exercised, net	1,568			154	16	1,552
Issuance of restricted stock, net	66			4		66
Stock-based compensation expense	1,546					1,546
Other comprehensive income	4,648		4,648			
Balance September 30, 2012	\$ 327,554	\$ (493,264)	\$ 4,607	20,910	\$ 2,091	\$ 814,120

See Notes to Consolidated Financial Statements.

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SAFEGUARD SCIENTIFICS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. General

The accompanying unaudited interim Consolidated Financial Statements of Safeguard Scientifics, Inc. (the Company) were prepared in accordance with accounting principles generally accepted in the United States of America and the interim financial statement rules and regulations of the SEC. In the opinion of management, these statements include all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the Consolidated Financial Statements. The interim operating results are not necessarily indicative of the results for a full year or for any interim period. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations relating to interim financial statements. The Consolidated Financial Statements included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this Form 10-Q and with the Company's Consolidated Financial Statements and Notes thereto included in the Company's 2011 Annual Report on Form 10-K.

Table of Contents**SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2. Ownership Interests in and Advances to Partner Companies and Funds**

The following summarizes the carrying value of the Company's ownership interests in and advances to partner companies and private equity funds.

	September 30, 2012	December 31, 2011
	(In thousands)	
	(Unaudited)	
Equity Method:		
Partner companies	\$ 101,337	\$ 104,545
Private equity funds	5,868	5,784
	107,205	110,329
Cost Method:		
Private equity funds	2,634	2,984
	2,634	2,984
Advances to partner companies	8,292	856
	\$ 118,131	\$ 114,169
Loan participations receivable	\$ 8,860	\$ 7,587
Available-for-sale securities	\$ 9,648	\$ 5,184

The Company recognized an impairment charge of \$3.7 million related to PixelOptics, Inc. (PixelOptics) in the second quarter of 2012 which is reflected in Equity income (loss) in the Consolidated Statement of Operations. The impairment was based upon launch delays and related supply chain issues that PixelOptics is addressing, as well as the pricing of a transaction between other institutional shareholders in PixelOptics.

The Company recorded an impairment charge of \$0.7 million related to its Penn Mezzanine debt and equity participations in the second quarter of 2012, which is reflected in Other income (loss), net in the Consolidated Statement of Operations. The charge included \$0.2 million related to loan participations, \$0.4 million related to equity participations and \$0.1 million representing an adjustment to the fair value of the Company's participation in warrants.

The Company recognized an impairment charge of \$0.4 million related to its interest in a legacy private equity fund in the first quarter of 2012, which is reflected in Other income (loss), net in the Consolidated Statement of Operations.

The Company accounts for its holdings in NuPathe, Inc. (NuPathe) and Tengion, Inc. (Tengion) as available-for-sale securities. The Company recognized an impairment charge of \$0.1 million in the three months ended September 30, 2012, which is reflected in Other income (loss), net, in the Consolidated Statements of Operations, representing the unrealized loss on the mark-to-market of its ownership interest in Tengion, which was previously recorded as a separate component of equity. The Company previously recognized an impairment charge of \$0.1 million in the second quarter of 2012 related to its ownership interest in Tengion. The Company determined that the decline in the value of its public holdings in Tengion was other than temporary. The Company's holdings of available-for-sale securities in NuPathe generated an unrealized loss of \$1.3 million and an unrealized gain of \$4.6 million for the three and nine months ended September 30, 2012, respectively. As of September 30, 2012, the Company's adjusted cost basis in NuPathe and Tengion securities was \$5.0 million and \$0.1 million, respectively.

Table of Contents**SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following unaudited summarized results of operations for the six months ended June 30, 2012 and 2011 for PixelOptics have been compiled from the unaudited financial statements of PixelOptics. The results of PixelOptics are reported on a one quarter lag.

	Six Months Ended	Six Months Ended
	June 30, 2012	June 30, 2011
	(In thousands) (Unaudited)	
Results of Operations:		
Revenue	\$ 569	\$ 864
Operating loss	\$ (16,172)	\$ (13,803)
Net loss	\$ (16,925)	\$ (14,992)

Table of Contents**SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. Acquisitions of Ownership Interests in Partner Companies and Funds**

In September 2012, the Company deployed an additional \$5.0 million in ThingWorx, Inc. (ThingWorx). The Company previously deployed \$5.0 million in ThingWorx in February 2011. ThingWorx offers a platform designed to accelerate the development of applications connecting people, systems and devices. The Company accounts for its holdings in ThingWorx under the equity method. The difference between the Company's cost and its interest in the underlying net assets of ThingWorx was preliminarily allocated to intangible assets and goodwill as reflected in the carrying value in Ownership interests in and advances to partner companies and funds on the Consolidated Balance Sheets.

In September, July and April 2012, the Company funded an aggregate of \$6.6 million of a convertible bridge loan to PixelOptics. The Company previously deployed \$25.0 million in PixelOptics in April 2011. PixelOptics provides electronic corrective eyeglasses designed to substantially reduce or eliminate the visual distortion and other limitations associated with multifocal lenses. The Company accounts for its interest in PixelOptics under the equity method. The difference between the Company's cost and its interest in the underlying net assets of PixelOptics was allocated to intangible assets and goodwill as reflected in the carrying value in Ownership interests in and advances to partner companies and funds on the Consolidated Balance Sheets.

In August 2012, the Company funded \$1.7 million of a convertible debt facility to MediaMath, Inc. (MediaMath). The Company previously deployed an aggregate of \$16.9 million in MediaMath. MediaMath is an online media trading company that enables advertising agencies and their advertisers to optimize their ad spending across various exchanges through its proprietary algorithmic bidding platform and data integration technology. The Company accounts for its holdings in MediaMath under the equity method.

In August 2012, the Company funded \$1.7 million for participations in loan and equity interests initiated by Penn Mezzanine. Included in this funding was \$1.5 million for participation in a loan, \$0.1 million for participation in equity of the borrower and \$0.1 million for participation in warrants to acquire common stock of the borrower. In January 2012, the Company funded \$2.5 million for participations in loan and equity interests initiated by Penn Mezzanine. Included in this funding was \$2.3 million for participation in a loan and \$0.2 million for participation in equity of the borrower acquired by Penn Mezzanine. The loan principal was repaid in March 2012.

In August 2012, the Company funded \$0.4 million into New York Digital Health Accelerator in exchange for a 9.4% limited partnership interest in a fund run by the New York eHealth Collaborative and the New York City Investment Fund for early- and growth-stage digital health companies that are developing technology products in care coordination, patient engagement, analytics and message alerts for healthcare providers. The Company accounts for its limited partnership interest in New York Digital Health Accelerator under the equity method.

In July 2012 and February 2012, the Company funded an aggregate of \$1.2 million of convertible bridge loans to Alverix, Inc. (Alverix). The Company previously deployed an aggregate of \$7.6 million in Alverix. Alverix provides next-generation instrument and connectivity platforms for diagnostic Point-of-Care (POC) testing. The Company accounts for its interest in Alverix under the equity method.

In March 2012, the Company deployed an additional \$3.7 million in Good Start Genetics, Inc. (Good Start). The Company had previously acquired an interest in Good Start in 2010 for \$6.8 million. Good Start has developed and launched pre-pregnancy genetic tests, which utilize an advanced DNA sequencing technology to screen for a panel of genetic disorders, including those recommended by the American Congress of Obstetricians and Gynecologists and the American College of Medical Genetics. The Company accounts for its interest in Good Start under the equity method. The difference between the Company's cost and its interest in the underlying net assets of Good Start was allocated to intangible assets and goodwill as reflected in the carrying value in Ownership interests in and advances to partner companies and funds on the Consolidated Balance Sheets.

In February 2012, the Company acquired a 23.1% ownership interest in Spongecell, Inc. (Spongecell) for \$10.0 million. Spongecell is a digital advertising technology company that enhances standard banner ads with rich interactive features. The Company accounts for its ownership interest in Spongecell under the equity method. The difference between the Company's cost and its interest in the underlying net assets of Spongecell was preliminarily allocated to intangible assets and goodwill as reflected in the carrying value in Ownership interests in and advances to partner companies and funds on the Consolidated Balance Sheets.

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In February 2012, the Company acquired a 31.6% ownership interest in Lumesis, Inc. (Lumesis) for \$2.2 million. Lumesis is a financial technology company that is dedicated to delivering timely data and robust analytical tools for the fixed income marketplace. The Company accounts for its interest in Lumesis under the equity method. The difference between the Company's cost and its interest in the underlying net assets of Lumesis was preliminarily allocated to intangible assets and goodwill as reflected in the carrying value in Ownership interests in and advances to partner companies and funds on the Consolidated Balance Sheets.

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SAFEGUARD SCIENTIFICS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Fair Value Measurements

The Company categorizes its financial instruments into a three-level fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure fair value fall within different levels of the hierarchy, the category level is based on the lowest priority level input that is significant to the fair value measurement of the instrument. Financial assets recorded at fair value on the Company's Consolidated Balance Sheets are categorized as follows:

Level 1 Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 Include other inputs that are directly or indirectly observable in the marketplace.

Level 3 Unobservable inputs which are supported by little or no market activity.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

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The following table provides the carrying value and fair value of certain financial instruments including assets and liabilities measured at fair value on a recurring basis as of September 30, 2012 and December 31, 2011:

	Carrying Value	Fair Value Measurement at September 30, 2012		
		Level 1 (In thousands) (Unaudited)	Level 2	Level 3
Cash and cash equivalents	\$ 71,151	\$ 71,151		
Cash held in escrow	\$ 6,433	\$ 6,433		
Restricted cash equivalents	\$ 7,686	\$ 7,686		
Available-for-sale securities	\$ 9,648	\$ 9,648		
Warrant participations	\$ 423			\$ 423
Marketable securities - held-to-maturity:				
Commercial paper	\$ 59,406	\$ 59,406		
U.S. Treasury Bills	15,182	15,182		
Government agency bonds	53,278	53,278		
Corporate bonds	281	281		
Certificates of deposit	29,981	29,981		
	\$ 158,128	\$ 158,128		
	Carrying Value	Fair Value Measurement at December 31, 2011		
		Level 1 (In thousands) (Unaudited)	Level 2	Level 3
Cash and cash equivalents	\$ 83,187	\$ 83,187		
Cash held in escrow	\$ 6,433	\$ 6,433		
Restricted cash equivalents	\$ 12,265	\$ 12,265		
Available-for-sale securities	\$ 5,184	\$ 5,184		
Warrant participations	\$ 276			\$ 276
Marketable securities - held-to-maturity:				
Commercial paper	\$ 42,919	\$ 42,919		
U.S. Treasury Bills	17,555	17,555		
Government agency bonds	80,712	80,712		
Corporate bonds	1,296	1,296		
Certificates of deposit	31,903	31,903		
	\$ 174,385	\$ 174,385		

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SAFEGUARD SCIENTIFICS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

As of September 30, 2012, \$120.3 million of marketable securities had contractual maturities which were less than one year and \$37.8 million of marketable securities had contractual maturities greater than one year. Held-to-maturity securities are carried at amortized cost, which, due to the short-term maturity of these instruments, approximates fair value using quoted prices in active markets for identical assets or liabilities defined as Level 1 inputs under the fair value hierarchy.

The Company recorded an impairment charge of \$3.7 million related to PixelOptics in the second quarter of 2012 measured as the amount by which PixelOptics' carrying value exceeded its estimated fair value. The fair market value of the Company's equity ownership in PixelOptics was determined to be \$11.4 million based on Level 3 inputs as defined above. The inputs and valuation techniques used included discounted cash flows as well as the pricing of a transaction between other institutional shareholders in PixelOptics debt and equity securities.

The Company recorded a gain of \$0.2 million associated with mark-to-market adjustments related to its warrant participations in Penn Mezzanine in the three months ended September 30, 2012 which is reflected in Other income (loss), net in the Consolidated Statement of Operations. The Company recorded an impairment charge of \$0.7 million related to its Penn Mezzanine debt and equity participations in the second quarter of 2012 measured as the amount by which the carrying value of the Company's participation in the debt and equity interests acquired by Penn Mezzanine exceeded their estimated fair values. The fair market values of the Company's participating interests in debt, equity and warrants acquired by Penn Mezzanine were determined based on Level 3 inputs as defined above. The inputs and valuation techniques used included discounted cash flows and valuations of comparable public companies.

The Company recognized an impairment charge of \$0.4 million related to a legacy private equity fund in the first quarter of 2012, measured as the amount by which the carrying value of the Company's interest in the fund exceeded its estimated fair value. The fair market value of the Company's interest in the fund was determined to be \$1.9 million based on the value of the Company's pro rata portion of the fair value of the fund's net assets, which is a Level 3 input under the fair value hierarchy.

The Company accounts for its holdings in NuPathe and Tengion as available-for-sale securities. The value of the Company's available-for-sale securities is measured by reference to quoted prices for NuPathe and Tengion's common stock as traded on the NASDAQ Capital Market, which is considered a Level 1 input under the valuation hierarchy.

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The carrying values of the Company's convertible senior debentures were as follows:

	September 30, 2012	December 31, 2011
	(In thousands)	
	(Unaudited)	
Convertible senior debentures due 2024	\$ 441	\$ 441
Convertible senior debentures due 2014	45,774	45,253
	\$ 46,215	\$ 45,694

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SAFEGUARD SCIENTIFICS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Convertible Senior Debentures due 2024

In 2004, the Company issued an aggregate of \$150 million in face value of convertible senior debentures with a stated maturity date of March 15, 2024 (the 2024 Debentures). The Company has \$0.4 million of the 2024 Debentures outstanding at September 30, 2012. On March 21, 2011, the Company repurchased \$30.8 million of the 2024 Debentures as required by the 2024 Debenture holders. Interest on the 2024 Debentures is payable semi-annually. At the debentures holders' option, the 2024 Debentures are convertible into the Company's common stock through March 14, 2024, subject to certain conditions. The adjusted conversion rate of the debentures is \$43.3044 of principal amount per share. The closing price of the Company's common stock at September 30, 2012 was \$15.69. The remaining 2024 Debentures holders have the right to require the Company to repurchase the 2024 Debentures on March 20, 2014 or March 20, 2019 at a repurchase price equal to 100% of their face amount, plus accrued and unpaid interest. Subject to certain conditions, the Company has the right to redeem all or some of the 2024 Debentures.

At September 30, 2012, the fair value of the \$0.4 million outstanding 2024 Debentures approximated their carrying value based on quoted market prices as of such date.

Convertible Senior Debentures due 2014

In March 2010, the Company issued an aggregate of \$46.9 million in face value of 10.125% convertible senior debentures with a stated maturity of March 15, 2014 (the 2014 Debentures). Interest on the 2014 Debentures is payable semi-annually on March 15 and September 15. In the first quarter of 2010, as required under the terms of the 2014 Debentures, the Company placed approximately \$19.0 million in a restricted escrow account to make all scheduled interest payments on the 2014 Debentures through their maturity. In the nine months ended September 30, 2012, interest payments of \$4.8 million were made out of the restricted escrow account and are considered non-cash investing activities. Including accrued interest, a total of \$7.7 million was reflected in Restricted cash equivalents on the Consolidated Balance Sheet at September 30, 2012, of which \$5.3 million was classified as a current asset.

At the debentures holders' option, the 2014 Debentures are convertible into the Company's common stock at anytime after March 15, 2013; and, prior to March 15, 2013, under any of the following conditions:

During any fiscal quarter commencing after June 30, 2010 if the closing sale price per share of Company common stock is greater than or equal to 120% of the conversion price for at least 20 trading days during the period of 30 trading days ending on the last day of the preceding fiscal quarter;

During the five day period immediately following any 10 consecutive trading day period in which the trading price per \$1,000 principal amount of 2014 Debentures for each trading day of such period was less than 100% of the product of the closing sale price per share of Company common stock multiplied by the conversion rate on each such trading day;

If a fundamental change (as defined) occurs, including sale of all or substantially all of the Company's common stock or assets, liquidation, dissolution or a change in control.

The conversion price is \$16.50 of principal amount per share, equivalent to a conversion rate of 60.6061 shares of Company common stock per \$1,000 principal amount of the 2014 Debentures. The closing price of the Company's common stock at September 30, 2012 was \$15.69. The 2014 Debentures holders have the right to require repurchase of the 2014 Debentures upon a fundamental change, including sale of all or substantially all of the Company's common stock or assets, liquidation, dissolution or a change in control or the delisting of the Company's common stock from the New York Stock Exchange if the Company were unable to obtain a listing for its common stock on another national or regional securities exchange. None of the above conditions required for conversion were met as of September 30, 2012.

Table of Contents**SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The Company may mandatorily convert all or some of the 2014 Debentures at any time after March 15, 2012 if the closing sale price per share of Company common stock exceeds 130% of the conversion price for at least 20 trading days in a period of 30 consecutive trading days. If the Company elects to mandatorily convert any of the 2014 Debentures, the Company will be required to pay any interest that would have accrued and become payable on the debentures through their maturity. Upon a conversion of the 2014 Debentures, the Company has the right to settle the conversion in stock, cash or a combination thereof.

Because the 2014 Debentures may be settled in cash or partially in cash upon conversion, the Company separately accounts for the liability and equity components of the 2014 Debentures. The carrying amount of the liability component was determined at the exchange date by measuring the fair value of a similar liability that does not have an associated equity component. The carrying amount of the equity component represented by the embedded conversion option was determined by deducting the fair value of the liability component from the carrying value of the 2014 Debentures as a whole at the exchange date. The carrying value of the 2014 Debentures as a whole at the exchange date was equal to their fair value of \$55.2 million determined using a convertible bond valuation model. At September 30, 2012, the fair value of the \$46.9 million outstanding 2014 Debentures was approximately \$58.9 million based on the midpoint of bid and ask prices as of such date. At September 30, 2012, the carrying amount of the equity component was \$10.8 million, the principal amount of the liability component was \$46.9 million, the unamortized discount was \$1.2 million and the net carrying value of the liability component was \$45.8 million. The Company is amortizing the excess of the face value of the 2014 Debentures over their carrying value to interest expense over their term. The effective interest rate on the 2014 Debentures is 12.5%.

Credit Arrangements

The Company is party to a loan agreement which provides it with a revolving credit facility in the maximum aggregate amount of \$50 million in the form of borrowings, guarantees and issuances of letters of credit (subject to a \$20 million sublimit). Actual availability under the credit facility is based on the amount of cash maintained at the bank as well as the value of the Company's public and private partner company interests. This credit facility bears interest at the prime rate for outstanding borrowings, subject to an increase in certain circumstances. Other than for limited exceptions, the Company is required to maintain all of its depository and operating accounts and the lesser of \$80 million or 75% of its investment and securities accounts at the lending bank. The credit facility matures on December 31, 2012. Under the credit facility, the Company provided a \$6.3 million letter of credit expiring on March 19, 2019 to the landlord of CompuCom Systems, Inc.'s Dallas headquarters as required in connection with the sale of CompuCom Systems in 2004. Availability under the Company's revolving credit facility at September 30, 2012 was \$43.7 million.

6. Stock-Based Compensation

Stock-based compensation expense was recognized in the Consolidated Statements of Operations as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(In thousands)		(In thousands)	
	(Unaudited)		(Unaudited)	
General and administrative expense	\$ 317	\$ 844	\$ 1,546	\$ 2,845
	\$ 317	\$ 844	\$ 1,546	\$ 2,845

The fair value of the Company's stock-based awards to employees was estimated at the date of grant using the Black-Scholes option-pricing model. The risk-f