Mistras Group, Inc.
Form 10-Q
January 08, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
(Mark One)

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

For the quarterly period ended November 30, 2015

Or

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

For the transition period to

Commission file number 001- 34481

Mistras Group, Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	22-3341267 (I.R.S. Employer Identification No.)
195 Clarksville Road Princeton Junction, New Jersey (Address of principal executive offices)	08550 (Zip Code)

(609) 716-4000

(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.
ý Yes o 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).
ý Yes o No

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

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of January 1, 2016, the registrant had 28,890,796 shares of common stock outstanding.

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PART I—FINANCIAL INFORMATION

ITEM 1. Financial Statements

Mistras Group, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(in thousands, except share and per share data)

	(unaudited) November 30, 2015	May 31, 2015
ASSETS		
Current Assets		
Cash and cash equivalents	$10,579	$10,555
Accounts receivable, net	149,173	133,228
Inventories	9,676	10,841
Deferred income taxes	4,816	5,144
Prepaid expenses and other current assets	12,181	11,698
Total current assets	186,425	171,466
Property, plant and equipment, net	76,429	79,256
Intangible assets, net	46,759	51,276
Goodwill	167,649	166,414
Deferred income taxes	827	1,208
Other assets	1,975	2,107
Total assets	$480,064	$471,727
LIABILITIES AND EQUITY		
Current Liabilities		
Accounts payable	$9,169	$10,529
Accrued expenses and other current liabilities	58,933	55,914
Current portion of long-term debt	13,772	17,902
Current portion of capital lease obligations	6,853	8,646
Income taxes payable	2,083	532
Total current liabilities	90,810	93,523
Long-term debt, net of current portion	87,946	95,557
Obligations under capital leases, net of current portion	10,240	10,717
Deferred income taxes	18,247	16,984
Other long-term liabilities	8,477	9,934
Total liabilities	215,720	226,715
Commitments and contingencies		
Equity		
Preferred stock, 10,000,000 shares authorized	—	—
Common stock, $0.01 par value, 200,000,000 shares authorized	289	287
Additional paid-in capital	210,222	208,064
Retained earnings	75,872	57,581
Accumulated other comprehensive loss	(22,149)	(21,113)
Total Mistras Group, Inc. stockholders’ equity	264,234	244,819
Noncontrolling interests	110	193
Total equity	264,344	245,012

Total liabilities and equity	$480,064	$471,727

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

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Mistras Group, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Income
(in thousands, except per share data)

	Three months ended November 30,		Six months ended November 30,	
	2015	2014	2015	2014
Revenue	$194,786	$206,893	$374,639	$373,466
Cost of revenue	132,720	142,940	256,120	262,662
Depreciation	5,141	4,914	10,320	9,771
Gross profit	56,925	59,039	108,199	101,033
Selling, general and administrative expenses	34,008	37,180	69,844	72,400
Research and engineering	601	629	1,222	1,278
Depreciation and amortization	2,822	3,472	5,603	6,894
Acquisition-related (benefit), net	(75)	(434)	(971)	(1,395)
Income from operations	19,569	18,192	32,501	21,856
Interest expense	1,335	1,352	3,257	2,257
Income before provision for income taxes	18,234	16,840	29,244	19,599
Provision for income taxes	6,804	6,428	10,967	7,516
Net income	11,430	10,412	18,277	12,083
Less: net loss (income) attributable to noncontrolling interests, net of taxes	(5)	15	20	10
Net income attributable to Mistras Group, Inc.	$11,425	$10,427	$18,297	$12,093
Earnings per common share				
Basic	$0.40	$0.36	$0.64	$0.42
Diluted	$0.39	$0.35	$0.62	$0.41
Weighted average common shares outstanding:				
Basic	28,869	28,619	28,796	28,547
Diluted	29,594	29,397	29,641	29,551

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

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Mistras Group, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Comprehensive Income
(in thousands)

	Three months ended November 30,		Six months ended November 30,	
	2015	2014	2015	2014
Net income	$11,430	$10,412	$18,277	$12,083
Other comprehensive (loss):				
Foreign currency translation adjustments	(384)	(6,011)	(1,036)	(7,916)
Comprehensive income	11,046	4,401	17,241	4,167
Less: comprehensive loss (income) attributable to noncontrolling interest	(5)	15	20	10
Comprehensive income attributable to Mistras Group, Inc.	$11,041	$4,416	$17,261	$4,177

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

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Mistras Group, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Cash Flows
(in thousands)

	Six months ended November 30,	
	2015	2014 Note 1
Cash flows from operating activities		
Net income	$18,277	$12,083
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	15,923	16,665
Deferred income taxes	1,809	1,192
Share-based compensation expense	3,227	4,257
Fair value adjustment to contingent consideration liabilities	(1,068)	(1,546)
Other	(259)	968
Changes in operating assets and liabilities, net of effect of acquisitions of businesses:		
Accounts receivable	(17,641)	(24,196)
Inventories	1,496	601
Prepaid expenses and other current assets	(790)	(2,952)
Other assets	(9)	(478)
Accounts payable	(1,248)	(972)
Accrued expenses and other current liabilities	5,226	(2,074)
Income taxes payable	1,581	(395)
Net cash provided by operating activities	26,524	3,153
Cash flows from investing activities		
Purchase of property, plant and equipment	(7,753)	(7,862)
Purchase of intangible assets	(480)	(433)
Acquisition of businesses, net of cash acquired	(1,709)	(32,661)
Proceeds from sale of equipment	319	596
Net cash used in investing activities	(9,623)	(40,360)
Cash flows from financing activities		
Repayment of capital lease obligations	(3,681)	(4,183)
Proceeds from borrowings of long-term debt	1,968	872
Repayment of long-term debt	(15,870)	(10,726)
Proceeds of revolver	39,200	86,500
Repayments of revolver	(36,800)	(23,200)
Payment of contingent consideration for business acquisitions	(394)	(700)
Taxes paid related to net share settlement of share-based awards	(951)	(1,384)
Excess tax benefit from share-based compensation	(303)	283
Proceeds from the exercise of stock options	187	—
Net cash (used in) provided by financing activities	(16,644)	47,462
Effect of exchange rate changes on cash and cash equivalents	(233)	(676)
Net change in cash and cash equivalents	24	9,579
Cash and cash equivalents		
Beginning of period	10,555	10,020
End of period	$10,579	$19,599
Supplemental disclosure of cash paid		
Interest	$3,010	$1,815

Income taxes	$6,223	$8,028
Noncash investing and financing		
Equipment acquired through capital lease obligations	$1,555	$3,533
Issuance of notes payable	$—	$20,500

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

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Mistras Group, Inc. and Subsidiaries
Notes to Unaudited Condensed Consolidated Financial Statements
(tabular dollars in thousands, except per share data)

1. Description of Business and Basis of Presentation

Description of Business

Mistras Group, Inc. and subsidiaries (the Company) is a leading "one source" global provider of technology-enabled asset protection solutions used to evaluate the structural integrity and reliability of critical energy, industrial and public infrastructure. The Company combines industry-leading products and technologies, expertise in mechanical integrity (MI) and non-destructive testing (NDT) services and proprietary data analysis software to deliver a comprehensive portfolio of customized solutions, ranging from routine inspections to complex, plant-wide asset integrity assessments and management. These mission critical solutions enhance customers' ability to extend the useful life of their assets, increase productivity, minimize repair costs, comply with governmental safety and environmental regulations, manage risk and avoid catastrophic disasters. The Company serves a global customer base of companies with asset-intensive infrastructure, including companies in the oil and gas, fossil and nuclear power, alternative and renewable energy, public infrastructure, chemicals, commercial aerospace and defense, transportation, primary metals and metalworking, pharmaceutical/biotechnology and food processing industries and research and engineering institutions.

Basis of Presentation

The condensed consolidated financial statements contained in this report are unaudited. In the opinion of management, the condensed consolidated financial statements include all adjustments, which are of a normal recurring nature, necessary for a fair presentation of the results for the interim periods of the fiscal years ending May 31, 2016 and 2015. Reference to a fiscal year means the fiscal year ended May 31. Certain items included in these statements are based on management's estimates. Actual results may differ from those estimates. The results of operations for any interim period are not necessarily indicative of the results expected for the year. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the notes to consolidated financial statements contained in the Company's Annual Report on Form 10-K ("Annual Report") for fiscal 2015, as filed with the Securities and Exchange Commission on August 12, 2015.

Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements include the accounts of Mistras Group, Inc. and its wholly and majority-owned subsidiaries. For subsidiaries in which the Company's ownership interest is less than 100%, the noncontrolling interests are reported in stockholders' equity in the accompanying consolidated balance sheets. The noncontrolling interests in net income, net of tax, is classified separately in the accompanying consolidated statements of income.

All significant intercompany accounts and transactions have been eliminated in consolidation. Mistras Group, Inc.'s and its subsidiaries' fiscal years end on May 31 except for the subsidiaries in the International segment, which end on April 30. Accordingly, the Company's International segment subsidiaries are consolidated on a one month lag. Therefore, in the quarter and year of acquisition, results of acquired subsidiaries in the International segment are generally included in consolidated results for one less month than the actual number of months from the acquisition date to the end of the reporting period. Management does not believe that any events occurred during the one-month lag period that would have a material effect on the Company's consolidated financial statements.

Reclassification

Certain amounts in prior periods have been reclassified to conform to the current year presentation. Such reclassifications did not have a material effect on the Company's financial condition or results of operations as previously reported.

Immaterial Correction

Subsequent to the issuance of its interim consolidated financial statements as of and for the three and six months ended November 30, 2014, the Company identified errors related to the classification of amounts reported in the Consolidated Statement of Cash Flows for that period. In accordance with the SEC Staff Accounting Bulletin (SAB) No. 99, Materiality, and SAB No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements, management evaluated the materiality of the errors from qualitative and quantitative perspectives, and concluded

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(tabular dollars in thousands, except per share data)

that the errors were immaterial. Accordingly, management has corrected the presentation of the affected line items of the accompanying consolidated statement of cash flows for the six-months ended November 30, 2014, as summarized below. These changes did not impact the Company’s net income, balance sheet, or stockholders’ equity for any period previously reported.

	Previously Reported	Revised
Cash flows from operating activities		
Fair value adjustment to contingent consideration liabilities	(808)	(1,546)
Accounts payable	(666)	(972)
Accrued expenses and other current liabilities	(3,041)	(2,074)
Net cash provided by operating activities	3,230	3,153
Cash flows from investing activities		
Acquisition of businesses, net of cash acquired	(32,967)	(32,661)
Net cash used in investing activities	(40,666)	(40,360)
Cash flows from financing activities		
Proceeds from long-term debt	—	872
Repayment of long-term debt	(9,854)	(10,726)
Net borrowings against revolver	62,648	63,300
Net cash provided by financing activities	46,810	47,462
Effect of exchange rate changes on cash and cash equivalents	205	(676)

Significant Accounting Policies

The Company’s significant accounting policies are disclosed in Note 2 — Summary of Significant Accounting Policies in the Company's Annual Report. On an ongoing basis, the Company evaluates its estimates and assumptions, including, among other things those related to revenue recognition, valuations of accounts receivable, long-lived assets, goodwill, deferred tax assets and uncertain tax positions. Since the date of the 2015 Annual Report, there have been no material changes to the Company's significant accounting policies.

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Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for fiscal years and interim periods within those fiscal years beginning December 15, 2017, as a result of a one year deferral in the standard issued by the FASB in August 2015 with ASU 2015-14, Revenue from Contracts with Customers - Deferral of the Effective Date. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures.

In February 2015, the FASB issued ASU No. 2015-02, Consolidation (Topic 810): Amendments to the Consolidations Analysis, which changes the guidance for evaluating whether to consolidate certain legal entities. Specifically, the amendments modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities ("VIEs") or voting interest entities. Further, the amendments eliminate the presumption that a general partner should consolidate a limited partnership, as well as affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships. The updated guidance is effective for fiscal years, and interim periods within those fiscal years beginning after December 15, 2015. Early adoption is permitted. The Company does not expect this update to have a material impact on the consolidated financial statements and related disclosures.

In September 2015, the FASB issued ASU No. 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments. This amendment will simplify the accounting for adjustments made to provisional amounts recognized in a business combination and eliminates the requirement to retrospectively account for those adjustments in previous reporting periods. This update will require on the face of the income statement or in the notes to the financial statements the amount recorded in current-period earnings that would have previously been recorded if the adjustment to the provisional amounts had been recognized as of the acquisition date. ASU 2015-16 is effective for fiscal years, and interim periods within those fiscal years beginning after December 15, 2015. This update should be applied prospectively and earlier adoption is permitted for financial statements that have not been issued. The Company is evaluating the effect that ASU 2015-16 will have on its consolidated financial statements and related disclosures.

In November 2015, the FASB issued ASU No. 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. This amendment will simplify the presentation of deferred tax assets and liabilities on the balance sheet and require all deferred tax assets and liabilities to be treated as non-current. ASU 2015-17 is effective for fiscal years, and interim periods within those fiscal years beginning after December 15, 2016, with early adoption permitted. The Company is evaluating the effect that ASU 2015-17 will have on its consolidated financial statements and related disclosures.

2. Share-Based Compensation

The Company has share-based incentive awards outstanding to its eligible employees and Directors under two equity incentive plans: (i) the 2007 Stock Option Plan (the 2007 Plan), and (ii) the 2009 Long-Term Incentive Plan (the 2009 Plan). No further awards may be granted under the 2007 Plan, although awards granted under the 2007 Plan remain outstanding in accordance with their terms. Awards granted under the 2009 Plan may be in the form of stock options, restricted stock units and other forms of share-based incentives, including performance restricted stock units, stock appreciation rights and deferred stock rights.

Stock Options

For the three months ended November 30, 2015 and 2014, the Company recognized share-based compensation expense related to stock option awards of less than $0.1 million for each period respectively. For the six months ended November 30, 2015 and 2014, the Company recognized share-based compensation expense related to stock option awards of less than $0.1 million for each period respectively. As of November 30, 2015, there was less than $0.1 million of unrecognized compensation costs, net of estimated forfeitures, related to stock option awards, which are expected to be recognized over a remaining weighted average period of 0.3 years.

No stock options were granted during the six months ended November 30, 2015 and 2014.

Restricted Stock Unit Awards

Mistras Group, Inc. and Subsidiaries
Notes to Unaudited Condensed Consolidated Financial Statements
(tabular dollars in thousands, except per share data)

For the three months ended November 30, 2015 and 2014, the Company recognized share-based compensation expense related to restricted stock unit awards of $1.1 million and $1.2 million, respectively. For the six months ended November 30, 2015 and 2014, the Company recognized share-based compensation expense related to restricted stock unit awards of $2.2 million and $2.3 million, respectively. As of November 30, 2015, there was $9.5 million of unrecognized compensation costs, net of estimated forfeitures, related to restricted stock unit awards, which are expected to be recognized over a remaining weighted average period of 2.6 years.

During the first six months of fiscal 2016 and 2015, the Company granted approximately 15,000 and 10,000 shares, respectively, of fully-vested common stock to its five non-employee directors, in connection with its non-employee director compensation plan. These shares had grant date fair values of $0.2 million for each period respectively, which was recorded as share-based compensation expense during the six months ended November 30, 2015 and 2014.

During the first six months of fiscal 2016 and 2015, approximately 217,000 and 226,000 restricted stock units, respectively, vested. The fair value of these units was $3.4 million and $4.9 million, respectively. Upon vesting, restricted stock units are generally net share-settled to cover the required minimum withholding tax and the remaining amount is converted into an equivalent number of shares of common stock.

Performance Restricted Stock Units

Fiscal 2016
In the first quarter of fiscal 2016, the Company modified its equity compensation plan and granted 154,000 performance restricted stock units to its executive and certain other senior officers. These units have requisite service periods of five years and have no dividend rights. The actual payout of these units will vary based on the Company's performance over a one-year period based on three metrics related to the Company's fiscal 2016 performance: (1) Operating Income, (2) Adjusted EBITDAS, which is consistent with Adjusted EBITDA as disclosed in the financial statements, which is net income before interest, taxes, depreciation, amortization, non-cash stock-based compensation expense, acquisition related items, and other non-routine items as determined by the Committee and (3) Revenue. There is also a discretionary portion based on individual performance. During the second quarter of fiscal 2016, the Company evaluated the expected performance metrics and adjusted the estimated performance shares by 80,000 units to 234,000 units.

As a condition for receiving any awards under the revised fiscal 2016 plan, the executive and senior officers surrendered and released all rights to receive any shares under the 2014 and 2015 awards with a three-year performance or market condition. The Company has accounted for the fiscal 2016 awards as modifications in accordance with ASC 718, Compensation - Stock Compensation.

Compensation costs are initially measured assuming that the target performance conditions will be achieved. However, compensation costs related to the performance conditions are adjusted for subsequent changes in the expected outcomes of the performance conditions. The discretionary portion of these awards are liability-classified and adjusted to fair value each reporting period. Compensation costs for the discretionary portion of the awards are recognized over the same five year requisite service period as the awards based on the Company's fiscal 2016 performance. For the three months ended November 30, 2015, the Company recognized share-based compensation

expense related to these units of approximately $0.2 million. For the six months ended November 30, 2015, the Company recognized share-based compensation expense related to these units of approximately $0.2 million. At November 30, 2015, there was $3.8 million of total unrecognized compensation costs related to the 234,000 non-vested performance restricted stock units, which are expected to be recognized over a remaining weighted average period of 4.1 years.

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Mistras Group, Inc. and Subsidiaries
Notes to Unaudited Condensed Consolidated Financial Statements
(tabular dollars in thousands, except per share data)

Fiscal 2015
In the second quarter of fiscal 2015, the Company granted performance restricted stock units to its executive and certain other senior officers. These units were surrendered as part of the revised fiscal 2016 plan as discussed above. For the three and six months ended November 30, 2015, there was $0 and $0.2 million of compensation expense recognized, respectively. For the three and six months ended November 30, 2014, the Company recognized share-based compensation expense related to performance restricted stock units of $0.1 million and $0.1 million, respectively.

Fiscal 2014
In the third quarter of fiscal 2014, the Company granted one-year, two-year and three-year performance restricted stock units to its executive officers and certain other senior officers. The three-year performance restricted stock units were surrendered as part of the revised fiscal 2016 plan as discussed above. For the three and six months ended November 30, 2015, there was $0 and $0.4 million of compensation expense recognized, respectively. For the three and six months ended November 30, 2014, the Company recognized share-based compensation expense related to performance restricted stock units of $0.8 million and $1.6 million, respectively.

3. Earnings per Share

Basic earnings per share is computed by dividing net income by the weighted-average number of shares outstanding during the period. Diluted earnings per share is computed by dividing net income by the sum of (1) the weighted-average number of shares of common stock outstanding during the period, and (2) the dilutive effect of assumed conversion of equity awards using the treasury stock method. With respect to the number of weighted-average shares outstanding (denominator), diluted shares reflects: (i) only the exercise of options to acquire common stock to the extent that the options’ exercise prices are less than the average market price of common shares during the period and (ii) the pro forma vesting of restricted stock units.

The following table sets forth the computations of basic and diluted earnings per share:

	Three months ended November 30,		Six months ended November 30,	
	2015	2014	2015	2014
Basic earnings per share				
Numerator:				
Net income attributable to Mistras Group, Inc.	$11,425	$10,427	$18,297	$12,093
Denominator:				
Weighted average common shares outstanding	28,869	28,619	28,796	28,547
Basic earnings per share	$0.40	$0.36	$0.64	$0.42
Diluted earnings per share:				
Numerator:				
Net income attributable to Mistras Group, Inc.	$11,425	$10,427	$18,297	$12,093
Denominator:				

Weighted average common shares outstanding	28,869	28,619	28,796	28,547
Dilutive effect of stock options outstanding	592	675	610	763
Dilutive effect of restricted stock units outstanding	133	103	235	241
	29,594	29,397	29,641	29,551
Diluted earnings per share	$0.39	$0.35	$0.62	$0.41

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Mistras Group, Inc. and Subsidiaries
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(tabular dollars in thousands, except per share data)

4. Acquisitions

Acquisitions

In the first half of fiscal 2016, the Company completed one acquisition. The Company purchased a company that provides unmanned aerial systems and NDT services, located in the U.S.

In this acquisition, the Company acquired 100% of the common stock of the acquiree in exchange for consideration of $1.8 million in cash and contingent consideration estimated to be $0.9 million to be earned based upon the acquired business achieving specific performance metrics over the initial four years of operations from the acquisition date. The Company accounted for this transaction in accordance with the acquisition method of accounting for business combinations.

The assets and liabilities of the business acquired in fiscal 2016 were included in the Company's consolidated balance sheet based upon their estimated fair values on the date of acquisition as determined in a preliminary purchase price allocation, using available information and making assumptions management believes are reasonable. The Company is still in the process of completing its valuation of the assets, both tangible and intangible, and liabilities acquired. The results of operations for this acquisition is included in the Services segment's results from the date of acquisition. The Company's preliminary purchase price allocations are included in the table below, summarizing the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition:

	Fiscal 2016	
Number of Entities	1	
Consideration transferred:		
Cash paid	$1,750	
Contingent consideration	945	
Consideration transferred	2,695	
Current assets	145	
Property, plant and equipment	485	
Goodwill	2,658	
Current liabilities	(521	)
Long-term deferred tax liability	(72	)
Net assets acquired	$2,695	

In the first half of fiscal 2015, the Company completed three acquisitions. The Company purchased a company, located in Louisiana, a provider of maintenance and inspection services primarily on offshore platforms. This acquisition expanded the service offerings within the Services segment, allowing the Company to provide services to the upstream operations of its customers. The Company also purchased a group of asset protection businesses located in Quebec, Canada to complement service offerings within the Company’s Services segment and continue its market expansion strategy. The Company’s International Segment completed an acquisition of an asset inspection business located in the United Kingdom.

In these acquisitions, the Company acquired 100% of the common stock or certain assets of each acquiree in exchange for aggregate consideration of approximately $34.0 million in cash and $22.7 million in notes payable issued as part of the acquisitions and other liabilities assumed. The Company accounted for these transactions in accordance with the acquisition method of accounting for business combinations. In addition, the acquisition in Quebec provided for contingent consideration of up to $2.7 million to be earned based upon the acquired business achieving specific performance metrics over the initial three years of operation from the acquisition date.

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(tabular dollars in thousands, except per share data)

The amortization period of intangible assets acquired in fiscal 2015 ranges from 3 to 10 years. The Company recorded $43.9 million of goodwill in connection with these acquisitions, reflecting the strategic fit and revenue and earnings growth potential of these business.

Acquisition-Related Expense

During the three and six month periods ended November 30, 2015, the Company incurred acquisition-related costs of less than $0.1 million in connection with due diligence, professional fees, and other expenses for its acquisition activities. Additionally, the Company adjusted the fair value of certain previously recorded acquisition-related contingent consideration liabilities. These adjustments resulted in a net decrease of acquisition-related contingent consideration liabilities and a corresponding increase in income from operations of $0.2 million and $1.1 million, for the three and six month periods ended November 30, 2015, respectively. The Company's aggregate acquisition-related contingent consideration liabilities were $5.7 million and $6.4 million as of November 30, 2015 and May 31, 2015, respectively.

During the three and six month periods ended November 30, 2014, the Company incurred acquisition-related costs of less than $0.2 million in connection with due diligence, professional fees, and other expenses for its acquisition activities. Additionally, the Company adjusted the fair value of certain acquisition-related contingent consideration liabilities. For the three and six month periods ended November 30, 2014, these adjustments resulted in a net decrease of acquisition-related contingent consideration liabilities and a corresponding increase in income from operations of $0.6 million and $1.6 million, respectively.

The fair value adjustments to acquisition-related contingent consideration liabilities and the acquisition-related transaction costs have been classified as acquisition-related expense, net in the condensed consolidated statements of income for the three and six month periods ended November 30, 2015 and 2014.

5. Accounts Receivable, net

Accounts receivable consisted of the following:

	November 30, 2015	May 31, 2015
Trade accounts receivable	$152,545	$136,208
Allowance for doubtful accounts	(3,372)	(2,980)
Accounts receivable, net	$149,173	$133,228

6. Property, Plant and Equipment, net

Property, plant and equipment consisted of the following:

	Useful Life (Years)	November 30, 2015	May 31, 2015
Land		$1,911	$1,856
Buildings and improvements	30-40	18,988	17,712
Office furniture and equipment	5-8	8,547	8,084
Machinery and equipment	5-7	164,980	162,612
		194,426	190,264
Accumulated depreciation and amortization		(117,997)	(111,008)
Property, plant and equipment, net		$76,429	$79,256

Depreciation expense for the three months ended November 30, 2015 and 2014 was $5.5 million and $5.5 million, respectively. Depreciation expense for the six months ended November 30, 2015 and 2014 was $11.1 million and $10.9 million, respectively.

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7. Intangible Assets

The gross amount, accumulated amortization and net carrying amount of intangible assets are as follows:

		November 30, 2015			May 31, 2015		
	Useful Life (Years)	Gross Amount	Accumulated Amortization	Net Carrying Amount	Gross Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	5-12	$80,198	$ (44,040)	$36,158	$81,101	$ (41,009)	$40,092
Software/Technology	3-15	16,692	(11,023)	5,669	15,738	(10,290)	5,448
Covenants not to compete	2-5	11,639	(9,027)	2,612	11,678	(8,605)	3,073
Other	2-5	6,848	(4,528)	2,320	6,910	(4,247)	2,663
Total		$115,377	$ (68,618)	$46,759	$115,427	$ (64,151)	$51,276

Amortization expense for the three months ended November 30, 2015 and 2014 was $2.4 million and $2.9 million, respectively. Amortization expense for the six months ended November 30, 2015 and 2014 was $4.8 million and $5.8 million, respectively.

8. Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following:

	November 30, 2015	May 31, 2015
Accrued salaries, wages and related employee benefits	$28,231	$26,053
Contingent consideration, current portion	2,982	3,543
Accrued workers' compensation and health benefits	7,135	3,630
Deferred revenue	3,591	3,841
Other accrued expenses	16,994	18,847
Total accrued expenses and other liabilities	$58,933	$55,914

9. Long-Term Debt

Long-term debt consists of the following:

	November 30, 2015	May 31, 2015
Senior credit facility	$84,923	$83,062
Notes payable	10,889	24,933
Other	5,906	5,464

Total debt	101,718	113,459
Less: Current portion	(13,772)	(17,902)
Long-term debt, net of current portion	$87,946	$95,557

Senior Credit Facility

On October 31, 2014, the Company entered into a Third Amendment and Modification Agreement, to its revolving line of credit, the Third Amended and Restated Credit Agreement ("Credit Agreement") with Bank of America, N.A., as agent for the lenders and a lender, and JPMorgan Chase Bank, N.A., Keybank, National Association and TD Bank, N.A., as lenders. The Credit Agreement provides the Company's with a $175.0 million revolving line of credit, which, under certain circumstances the line of credit can be increased to $225.0 million. The Company may borrow up to $30.0 million in non-U.S. Dollar

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currencies and use up to $10.0 million of the credit limit for the issuance of letters of credit. The Credit Agreement has a maturity date of October 30, 2019. As of November 30, 2015, the Company had borrowings of $84.9 million and a total of $4.5 million of letters of credit outstanding under the Credit Agreement.

Loans under the Credit Agreement bear interest at LIBOR plus an applicable LIBOR margin ranging from 1% to 1.75%, or a base rate less a margin of 1.25% to 0.375%, at the option of the Company, based upon the Company's Funded Debt Leverage Ratio. Funded Debt Leverage Ratio is generally the ratio of (1) all outstanding indebtedness for borrowed money and other interest-bearing indebtedness as of the date of determination to (2) EBITDA (which is (a) net income, less (b) income (or plus loss) from discontinued operations and extraordinary items, plus (c) income tax expenses, plus (d) interest expense, plus (e) depreciation, depletion, and amortization (including non-cash loss on retirement of assets), plus (f) stock compensation expense, less (g) cash expense related to stock compensation, plus or minus certain other adjustments) for the period of four consecutive fiscal quarters immediately preceding the date of determination. The Company has the benefit of the lowest margin if its Funded Debt Leverage Ratio is equal to or less than 0.5 to 1, and the margin increases as the ratio increases, to the maximum margin if the ratio is greater than 2.0 to 1. The Company will also bear additional costs for market disruption, regulatory changes effecting the lenders' funding costs, and default pricing of an additional 2% interest rate margin on any amounts not paid when due. Amounts borrowed under the Credit Agreement are secured by liens on substantially all of the assets of the Company.

The Credit Agreement contains financial covenants requiring that the Company maintain a Funded Debt Leverage Ratio of no greater than 3.25 to 1 and an Interest Coverage Ratio of at least 3.0 to 1. Interest Coverage Ratio means the ratio, as of any date of determination, of (a) EBITDA for the 12 month period immediately preceding the date of determination, to (b) all interest, premium payments, debt discount, fees, charges and related expenses of the Company and its subsidiaries in connection with borrowed money (including capitalized interest) or in connection with the deferred purchase price of assets, in each case to the extent treated as interest in accordance with GAAP, paid during the 12 month period immediately preceding the date of determination. The Credit Agreement also limits the Company's ability to, among other things, create liens, make investments, incur more indebtedness, merge or consolidate, make dispositions of property, pay dividends and make distributions to stockholders, enter into a new line of business, enter into transactions with affiliates and enter into burdensome agreements. The Credit Agreement does not limit the Company's ability to acquire other businesses or companies except that the acquired business or company must be in the Company's line of business, the Company must be in compliance with the financial covenants on a pro forma basis after taking into account the acquisition, and, if the acquired business is a separate subsidiary, in certain circumstances the lenders will receive the benefit of a guaranty of the subsidiary and liens on its assets and a pledge of its stock.

As of November 30, 2015, the Company was in compliance with the terms of the Credit Agreement, and will continuously monitor its compliance with the covenants contained in its credit agreement.

Notes Payable and Other

In connection with certain of its acquisitions through fiscal 2015, the Company issued subordinated notes payable to the sellers. The maturity of the notes that remain outstanding range from two to five years from the date of acquisition with stated interest rates ranging from 0% to 4%. The Company has discounted these obligations to reflect a 2% to 4% market interest. Unamortized discount on the notes was de minimis as of November 30, 2015 and May 31, 2015.

Amortization is recorded as interest expense in the consolidated statements of income.

The Company has evaluated current market conditions and borrower credit quality and has determined that the carrying value of its long-term debt approximates fair value. The fair value of the Company’s notes payable and capital lease obligations approximates their carrying amounts based on anticipated interest rates which management believes would currently be available to the Company for similar issuances of debt.

10. Fair Value Measurements

The Company performs fair value measurements in accordance with the guidance provided by ASC 820, Fair Value Measurements and Disclosures. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It also establishes a three level hierarchy that prioritizes the inputs used to measure fair value. The three levels of the hierarchy are defined as follows:

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Level 1 — Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2 — Observable inputs other than quoted prices included in Level 1, including quoted prices for similar assets or liabilities in active markets, quoted prices for identical assets or liabilities in inactive markets, inputs other than quoted prices that are observable for the asset or liability and inputs derived principally from or corroborated by observable market data.

Level 3 — Unobservable inputs reflecting the Company's own assumptions about inputs that market participants would use in pricing the asset or liability based on the best information available.

In accordance with the fair value hierarchy described above, the following table shows the fair value of the Company's financial liabilities that are required to be remeasured at fair value on a recurring basis:

	November 30, 2015			
	Level 1	Level 2	Level 3	Total
Liabilities:				
Contingent consideration	$—	$—	$5,664	$5,664
Total Liabilities	$—	$—	$5,664	$5,664

	May 31, 2015			
	Level 1	Level 2	Level 3	Total
Liabilities:				
Contingent consideration	$—	$—	$6,411	$6,411
Total Liabilities	$—	$—	$6,411	$6,411

The fair value of contingent consideration liabilities that was classified as Level 3 in the table above was estimated using a discounted cash flow technique with significant inputs that are not observable in the market and thus represents a Level 3 fair value measurement as defined in ASC 820. The significant inputs in the Level 3 measurement not supported by market activity include the probability assessments of expected future cash flows related to the acquisitions, appropriately discounted considering the uncertainties associated with the obligation, and as calculated in accordance with the terms of the applicable acquisition agreements.

11. Commitments and Contingencies

Litigation and Government Investigations

The Company is subject to periodic lawsuits, investigations and claims that arise in the ordinary course of business. Although the Company cannot predict with certainty the ultimate resolution of lawsuits, investigations and claims asserted against it, the Company does not believe that any currently pending legal proceeding to which the Company is a party will have a material adverse effect on its business, results of operations, cash flows or financial condition, except for the proceedings described below for which the Company is currently unable to determine the likely outcome or reasonably estimate the amount or range of potential liability estimate. The costs of defense and amounts

that may be recovered against the Company in such matters may be covered by insurance, except that the primary claims set forth in the purported class action case in California is excluded from insurance coverage.

Litigation and Commercial Claims

In April 2015, two separate lawsuits were filed in California as purported class action lawsuits on behalf of current and former Mistras employees. The cases are David Kruger v Mistras Group, Inc., filed in the U.S. District Court for the Eastern District of California and Edgar Viceral v Mistras Group, et al, pending in the U.S. District Court for the Northern District of California. Both cases were originally filed in California state court and were removed to the respective U.S. District Courts for the districts in which the state court cases were filed. These two cases have been consolidated, with Kruger dismissing his case and joining the Viceral case. As part of this consolidation, the claims in the Kruger case that were not part of the Viceral case were

added to the Viceral case by the filing of an amended complaint. The consolidated case alleges violations of California statutes primarily, the California Labor Code, and seeks to proceed as a collective action under the U.S. Fair Labor Standards Act. The case is predicated on claims for allegedly missed rest and meal periods, inaccurate wage statements, and failure to pay all wages due, as well as related unfair business practices, and is requesting payment of all damages, including unpaid wages, and various fines and penalties available under California law. The case is in the preliminary stages. The Company is currently unable to determine the likely outcome or reasonably estimate the amount or range of potential liability, if any, related to these matters, and accordingly, has not established any reserves for these matters.

During fiscal 2012 and 2013, the Company performed radiography work on the construction of pipeline projects in the U.S. The Company has received notice that the owner of the pipeline projects contends that certain of the x-ray images the Company’s technicians prepared regarding the projects did not meet the code quality interpretation standards required by API (American Petroleum Institute) 1103. The projects' owner is claiming damages as a result of the alleged quality defects of the Company’s x-ray images. No lawsuit has been filed at this time. The Company is currently unable to determine the likely outcome or reasonably estimate the amount or range of potential liability related to this matter, and accordingly, has not established any reserves for this matter.

Government Investigations

In May 2015, the Company received a notice from the U.S. Environmental Protection Agency (“EPA”) that it performed a preliminary assessment at a leased facility the Company operates in Cudahy, California. Based upon the preliminary assessment, the EPA is conducting an investigation of the site, which includes taking groundwater and soil samples. The purpose of the investigation is to determine whether any hazardous materials were released from the facility. The Company has been informed that certain hazardous materials and pollutants have been found in the ground water in the general vicinity of the site and the EPA is attempting to ascertain the origination or source of these materials and pollutants. Given the historic industrial use of the site, the EPA determined that the site of the Cudahy facility should be examined, along with numerous other sites in the vicinity. At this time, the Company is unable to determine whether it has any liability in connection with this matter and if so, the amount or range of any such liability, and accordingly, has not established any reserves for this matter.

In January 2012, the Company received notice of a governmental investigation concerning an environmental incident which occurred in February 2011 outside on the premises of the Cudahy facility. No human injury or property damage was reported or appears to have been caused as a result of this incident. While management cannot predict the ultimate outcome of this matter, based on its internal investigation to date, the Company does not believe the outcome will have a material effect on its financial condition or results of operations. To the Company’s knowledge, this matter has been dormant since fiscal 2012.

Acquisition-related contingencies

The Company is liable for contingent consideration in connection with certain of its acquisitions. As of November 30, 2015, total potential acquisition-related contingent consideration ranged from zero to approximately $20.0 million and would be payable upon the achievement of specific performance metrics by certain of the acquired companies over the next 3.6 years of operations. See Note 4 - Acquisitions to these consolidated financial statements for further discussion

of the Company’s acquisitions.

12. Segment Disclosure

The Company’s three operating segments are:

- Services. This segment provides asset protection solutions primarily in North America with the largest concentration in the United States and the Canadian services business, consisting primarily of non-destructive testing and inspection and engineering services that are used to evaluate the structural integrity and reliability of critical energy, industrial and public infrastructure.

- International. This segment offers services, products and systems similar to those of the Company’s other two segments to global markets, principally in Europe, the Middle East, Africa, Asia and South America, but not to customers in China and South Korea, which are served by the Products and Systems segment.

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- Products and Systems. This segment designs, manufactures, sells, installs and services the Company's asset protection products and systems, including equipment and instrumentation, predominantly in the United States.

Allocations for general corporate services, including accounting, audit, and contract management, that are provided to the segments are reported within Corporate and eliminations. Sales to the International segment from the Products and Systems segment and subsequent sales by the International segment of the same items are recorded and reflected in the operating performance of both segments. Additionally, engineering charges and royalty fees charged to the Services and International segments by the Products and Systems segment are reflected in the operating performance of each segment. All such intersegment transactions are eliminated in the Company's consolidated financial reporting.

Selected consolidated financial information by segment for the periods shown was as follows:

	Three months ended November 30,		Six months ended November 30,	
	2015	2014	2015	2014
Revenues				
Services	$150,463	$160,874	$287,868	$282,806
International	38,425	41,018	75,284	81,056
Products and Systems	7,791	7,495	16,477	14,062
Corporate and eliminations	(1,893)	(2,494)	(4,990)	(4,458)
	$194,786	$206,893	$374,639	$373,466

	Three months ended November 30,		Six months ended November 30,	
	2015	2014	2015	2014
Gross profit				
Services	$41,118	$44,252	$77,687	$74,023
International	12,106	11,309	22,886	20,777
Products and Systems	3,833	3,328	7,755	5,992
Corporate and eliminations	(132)	150	(129)	241
	$56,925	$59,039	$108,199	$101,033

	Three months ended November 30,		Six months ended November 30,	
	2015	2014	2015	2014
Income (loss) from operations				
Services	$18,815	$20,071	$34,214	$28,951
International	3,971	3,177	5,789	2,478
Products and Systems	1,055	417	2,239	(16)
Corporate and eliminations	(4,272)	(5,473)	(9,741)	(9,557)
	$19,569	$18,192	$32,501	$21,856

Income (loss) by operating segment includes intercompany transactions, which are eliminated in Corporate and eliminations.

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	Three months ended November 30,		Six months ended November 30,	
	2015	2014	2015	2014
Depreciation and amortization				
Services				