INFRASOURCE SERVICES INC
Form 10-Q
August 12, 2005

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended June 30, 2005

OR

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

For the transition period from to

Commission file number 001-32164

INFRASOURCE SERVICES, INC.

(Exact name of registrant as specified in its charter)

Delaware	**03-0523754**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

100 West Sixth Street, Suite 300, Media, PA
(Address of principal executive offices)
19063
(Zip Code)
(610) 480-8000
(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 þ No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

At August 5, 2005, there were 39,395,785 shares of InfraSource Services, Inc. Common Stock, par value of $.001, outstanding.

For the Quarter Ended June 30, 2005
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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

INFRASOURCE SERVICES, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets
(Unaudited)
(In thousands, except share data)

	December 31, 2004	June 30, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 21,222	$ 3,996
Restricted cash	5,000	
Contract receivables (less allowances for doubtful accounts of $3,305 and $3,298, respectively)	104,840	118,903
Costs and estimated earnings in excess of billings	59,517	99,725
Inventories	9,864	10,193
Deferred income taxes	2,886	4,302
Other current assets	10,803	13,490
Current assets discontinued operations	8,959	6,441
Total current assets	223,091	257,050
Property and equipment (less accumulated depreciation of $30,636 and $42,866, respectively)	143,532	144,395
Goodwill	134,478	134,725
Intangible assets (less accumulated amortization of $14,950 and $17,359, respectively)	6,795	3,485
Deferred charges and other assets, net	11,766	13,396
Deferred income taxes	1,187	1,667
Noncurrent assets discontinued operations	1,732	1,876
Total assets	$522,581	$556,594
Current liabilities:		
Current portion of long-term debt and capital lease obligations	$ 900	$ 884
Note payable related party		1,000
Revolving credit facility borrowings		18,000
Other liabilities related parties	3,803	12,351
Accounts payable	33,342	36,494
Accrued compensation and benefits	17,525	17,888
Other current and accrued liabilities	19,570	28,835
Accrued insurance reserves	26,042	28,201
Billings in excess of costs and estimated earnings	10,728	12,187
Deferred revenues	5,359	5,398
Current liabilities discontinued operations	6,786	4,777

Total current liabilities	124,055	166,015
Long-term debt, net of current portion	83,878	83,438
Long-term debt related party	1,000	
Deferred revenues	16,935	16,156
Other long-term liabilities related parties	8,493	
Other long-term liabilities	4,226	4,309
Non-current liabilities discontinued operations	11	11
Total liabilities	238,598	269,929
Commitments and contingencies		
Shareholders equity:		
Preferred stock, $.001 par value (authorized - 12,000,000 shares; 0 shares issued and outstanding)		
Common stock $.001 par value (authorized - 120,000,000 shares; issued and outstanding - 38,942,728 and 39,120,779, respectively)	39	39
Treasury stock at cost (0 and 29,870, respectively)		(137)
Additional paid-in capital	272,954	274,212
Deferred compensation	(329)	(187)
Retained earnings	10,911	12,243
Accumulated other comprehensive income	408	495
Total shareholders equity	283,983	286,665
Total liabilities and shareholders equity	$522,581	$556,594

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

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INFRASOURCE SERVICES, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
(Unaudited)
(In thousands, except per share data)

	Three Months Ended June 30, 2004	Three Months Ended June 30, 2005	Six Months Ended June 30, 2004	Six Months Ended June 30, 2005
Contract revenues	$ 143,311	$ 231,670	$ 288,344	$ 412,300
Cost of revenues	119,671	212,026	240,308	371,559
Gross profit	23,640	19,644	48,036	40,741
Selling, general and administrative expenses	15,340	17,846	30,144	34,637
Merger related costs		76		152
Provision (recoveries) of uncollectible accounts	(464)	4	(471)	84
Amortization of intangible assets	4,022	1,698	8,569	3,310
Income from operations	4,742	20	9,794	2,558
Interest income	68	28	122	222
Interest expense and amortization of debt discount	(2,840)	(2,246)	(6,192)	(3,703)
Loss on early extinguishment of debt	(5,549)		(5,549)	
Other income (expense), net	17	27	160	3,858
Income (loss) before income taxes	(3,562)	(2,171)	(1,665)	2,935
Income tax expense (benefit)	(1,496)	(808)	(718)	1,234
Income (loss) from continuing operations	(2,066)	(1,363)	(947)	1,701
Discontinued operations:				
Income (loss) from discontinued operations (net of income tax provision (benefit) of $28, $(52), $(5) and $(267), respectively)	40	(47)	(8)	(369)
Net income (loss)	$ (2,026)	$ (1,410)	$ (955)	$ 1,332
Basic income (loss) per share:				
Income (loss) from continuing operations	$ (0.06)	$ (0.04)	$ (0.03)	$ 0.04
Income (loss) from discontinued operations				(0.01)
Net income (loss)	$ (0.06)	$ (0.04)	$ (0.03)	$ 0.03

Weighted average basic common shares outstanding	34,755	39,056	31,453	39,018
Diluted income (loss) per share:				
Income (loss) from continuing operations	$ (0.06)	$ (0.04)	$ (0.03)	$ 0.04
Income (loss) from discontinued operations				(0.01)
Net income (loss)	$ (0.06)	$ (0.04)	$ (0.03)	$ 0.03
Weighted average diluted common shares outstanding	34,755	39,056	31,453	39,801

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

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INFRASOURCE SERVICES, INC. AND SUBSIDIARIES
Condensed Consolidated Statement of Shareholders Equity
(Unaudited)
(in thousands, except share amounts)

	Common Stock		Treasury Stock		Additional Paid-In	Deferred	Accumulated Other Comprehensive	Retained	
	Shares	Amount	Shares	Amount	Capital	Compensation	Income	Earnings	Total
Balance as of December 31, 2004	38,942,728	$39		$	$272,954	$ (329)	$ 408	$10,911	$283,983
Treasury stock (see Note 8)	29,870		(29,870)	(137)	137				
Unearned compensation					(108)	108			
Amortization of unearned compensation						34			34
Stock options exercised	71,176				327				327
Income tax benefit from options exercised					219				219
Issuance of shares under employee stock purchase plan	77,005				683				683
Net income								1,332	1,332
Other comprehensive income							87		87
Balance as of June 30, 2005	39,120,779	$39	(29,870)	$(137)	$274,212	$ (187)	$ 495	$12,243	$286,665

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

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INFRASOURCE SERVICES, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Unaudited)
(In thousands)

	Six Months Ended June 30, 2004	Six Months Ended June 30, 2005
Cash flows used in operating activities:		
Income (loss) from continuing operations	$ (947)	$ 1,701
Adjustments to reconcile income (loss) from continuing operations to cash used in operating activities:		
Depreciation	11,314	13,597
Amortization of intangibles	8,569	3,310
Deferred income taxes	(7,490)	(1,988)
Loss on early extinguishment of debt	5,549	
Reversal of litigation judgment		(4,279)
Other	1,489	(1,531)
Changes in operating assets and liabilities, net of effects of acquisitions:		
Contract receivables, net	(3,546)	(14,146)
Contract receivables due from related parties, net	14,617	
Costs and estimated earnings in excess of billings, net	(17,055)	(38,749)
Inventories	(1,533)	(329)
Other current assets	(6,299)	(805)
Deferred charges and other assets	(616)	(1,844)
Accounts payable	(5,527)	3,152
Other current and accrued liabilities	(16,490)	12,427
Accrued insurance reserves	2,253	2,159
Deferred revenue	5,507	(739)
Other liabilities	(201)	(143)
Net cash flows used in operating activities from continuing operations	(10,406)	(28,207)
Net cash flows provided by (used in) operating activities from discontinued operations	2,106	(282)
Net cash flows used in operating activities	(8,300)	(28,489)
Cash flows used in investing activities:		
Acquisitions of businesses, net of cash acquired	(20,101)	(38)
Proceeds from restricted cash		5,000
Proceeds from sales of equipment	2,019	2,871
Additions to property and equipment	(11,634)	(15,404)
Net cash flows used in investing activities from continuing operations	(29,716)	(7,571)
	(928)	(210)

Net cash flows used in investing activities from discontinued operations		
Net cash flows used in investing activities	(30,644)	(7,781)
Cash flows from financing activities:		
Increase in revolving credit facility borrowings		18,000
Repayments of long-term debt and capital lease obligations	(83,620)	(458)
Proceeds from exercise of stock options and employee stock purchase plan	2,250	1,010
Proceeds from sale of common stock	128,093	
Net cash flows provided by financing activities from continuing operations	46,723	18,552
Net cash flows provided by (used in) financing activities from discontinued operations	(1,000)	
Net cash flows provided by financing activities	45,723	18,552
Cash and cash equivalents:		
Net increase (decrease) in cash and cash equivalents	6,779	(17,718)
Cash and cash equivalents transferred (to) from discontinued operations	(178)	492
Cash and cash equivalents beginning of period	12,013	21,222
Cash and cash equivalents end of period	$ 18,614	$ 3,996
Supplemental Disclosure of Non-Cash Investing and Financing Activities:		
Distribution of property and equipment owed to related party	$ 7,218	$
We acquired all of the voting interests of Maslonka for $77,476 in January, 2004		
In conjunction with this acquisition, assets acquired and liabilities assumed were as follows:		
Fair value of assets acquired	41,093	
Goodwill	59,549	
Liability to sellers for taxes and cash holdback	(6,704)	
Liabilities assumed	(23,166)	
Equity issued to sellers	(50,671)	
Cash paid for acquisition, net of cash acquired	(20,101)	

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

INFRASOURCE SERVICES, INC. AND SUBSIDARIES
Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. Organization and Basis of Presentation

InfraSource Services, Inc. (InfraSource) was organized on May 30, 2003 as a Delaware corporation. InfraSource and its wholly owned subsidiaries are referred to herein as the Company, we, us, or our . We operate in two busines segments. Our principal segment, Infrastructure Construction Services (ICS), provides design, engineering, procurement, construction, testing, and maintenance services for utility infrastructure. Our ICS customers include electric power utilities, natural gas utilities, telecommunication customers, government entities and heavy industrial companies, such as petrochemical, processing and refining businesses. Our Telecommunication Services (TS) segment provides design, procurement, construction, and maintenance services for telecommunications infrastructure. Our TS customers include communication service providers, large industrial customers such as pharmaceutical companies, school districts and other entities with high bandwidth telecommunication needs. We operate in multiple territories throughout the United States and do not have significant operations or assets in countries outside the United States.

On September 24, 2003, we acquired all of the voting interests of InfraSource Incorporated and certain of its wholly owned subsidiaries (collectively, the InfraSource Group), pursuant to a merger transaction (the Merger). On May 12, 2004, we completed our initial public offering (IPO) of 8,500,000 shares of common stock. OCM/ GFI Power Opportunities Fund, L.P. and OCM Principal Opportunities Fund, L.P. (collectively, the Principal Stockholders), both Delaware limited partnerships, own approximately 65% of our common stock.

The accompanying unaudited condensed consolidated financial statements reflect our financial position as of December 31, 2004 and June 30, 2005 and our results of operations and cash flows for the three and six months ended June 30, 2004 and 2005. The accompanying condensed consolidated financial statements are unaudited and have been prepared in accordance with the rules and regulations of the U.S. Securities and Exchange Commission (SEC). These financial statements include all adjustments that we consider necessary for a fair presentation of financial position, results of operations and cash flows for the interim periods presented. The December 31, 2004 condensed consolidated balance sheet data were derived from audited financial statements, but do not include all disclosures required by accounting principles generally accepted in the United States of America. The results for interim periods are not necessarily indicative of results to be expected for a full year or future interim periods. These financial statements should be read in conjunction with our financial statements and related notes included in our Report on Form 10-K for the year ended December 31, 2004.

Certain amounts in the accompanying statements have been reclassified for comparative purposes.

2. Recently Issued Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 123R Share Based Payment. SFAS No. 123R is a revision to SFAS No. 123 Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board (APB) Opinion No. 25 Accounting for Stock Issued to Employees, and Related Interpretations and amends FASB Statement No. 95, Statement of Cash Flows. SFAS No. 123R requires a public entity to expense the cost of employee services received in exchange for an award of equity instruments. SFAS No. 123R provides guidance on valuing and expensing these awards, as well as disclosure requirements of these equity arrangements. As modified by the SEC on April 15, 2005, SFAS No. 123R is effective for the first annual or interim reporting period of the registrant s first fiscal year that begins after June 15, 2005. We are required to adopt the provisions of SFAS No. 123R effective January 1, 2006, at which time we will begin recognizing an expense for unvested share-based compensation that has been issued or will be issued after that date. SFAS No. 123R permits an issuer to use either a prospective or one of two modified versions of retrospective application under which financial statements for prior periods are adjusted on a basis consistent with the pro forma disclosures required for those periods by the original SFAS No. 123. Under the retroactive options, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented.

As permitted by SFAS No. 123, we currently account for share-based compensation to employees using the intrinsic value method of APB Opinion No. 25 and, as such, we generally recognize no compensation cost for employee stock options. The impact of the adoption of SFAS No. 123R cannot be predicted at this time because it will be depend on levels of share-based compensation granted in the future. However, valuation of employee stock options under SFAS No. 123R is similar to SFAS No. 123, with minor exceptions. For information about what our reported results of operations and earnings per share would have been had we adopted SFAS No. 123, see the pro forma disclosure in Note 8. Accordingly, the adoption of the fair value method of SFAS No. 123R will likely have a significant impact on our results of operations, although it will have no impact on our overall financial position. We have not yet completed the analysis of the ultimate impact that SFAS No. 123R will have on our results of operations. We plan to adopt SFAS No. 123R using the prospective method.

In December 2004, the FASB issued Staff Position (FSP) No. 109-1, Application of FASB No. 109, Accounting for Income Taxes , to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004 . The American Jobs Creation Act of 2004 (AJCA) introduces a special 3% tax deduction, which is phased up to 9%, on qualified production activities. FSP No. 109-1 clarifies that this tax deduction should be accounted for as a special tax deduction in accordance with SFAS No. 109. Pursuant to the AJCA and the guidance provided to date, we will likely be viewed as engaging in qualified production activities and, thus, be able to claim this tax deduction in 2005. We do not expect these new tax provisions to have a significant impact on our consolidated financial position, results of operations or cash flows.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3 . This Statement replaces APB Opinio