

INTEGRATED ELECTRICAL SERVICES INC  
Form 10-Q  
May 15, 2012  
[Table of Contents](#)

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
WASHINGTON, D.C. 20549

**FORM 10-Q**

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

For the Quarterly Period Ended March 31, 2012

OR

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

For the transition period from                      to

Commission File Number 1-13783

**Integrated Electrical Services, Inc.**

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**76-0542208**  
(I.R.S. Employer  
Identification No.)

**4801 Woodway Drive, Suite 200-E, Houston, Texas 77056**

(Address of principal executive offices and ZIP code)

**Registrant's telephone number, including area code: (713) 860-1500**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes  No

On May 14, 2012, there were 14,994,653 shares of common stock outstanding.

**Table of Contents**

**INTEGRATED ELECTRICAL SERVICES, INC. AND SUBSIDIARIES**

**INDEX**

	<b>Page</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
Item 1. Condensed Consolidated Financial Statements	
<u>Condensed Consolidated Balance Sheets as of March 31, 2012 and September 30, 2011</u>	5
<u>Condensed Consolidated Statements of Operations for the Three and Six Months Ended March 31, 2012 and 2011</u>	6
<u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended March 31, 2012 and 2011</u>	8
<u>Notes to Condensed Consolidated Financial Statements</u>	9
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	40
<u>Item 4. Controls and Procedures</u>	40
<b><u>PART II. OTHER INFORMATION</u></b>	
<u>Item 1. Legal Proceedings.</u>	41
<u>Item 1A. Risk Factors</u>	41
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	41
<u>Item 3. Defaults Upon Senior Securities</u>	42
<u>Item 4. Removed and Reserved</u>	42
<u>Item 5. Other Information</u>	42
<u>Item 6. Exhibits</u>	42
<u>Signatures</u>	43

**Table of Contents**

**PART I**

**DEFINITIONS**

In this quarterly report on Form 10-Q, the words "IES", the "Company", the "Registrant", "we", "our", "ours" and "us" refer to Integrated Electrical Services Inc. and, except as otherwise specified herein, to our subsidiaries.

**DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS**

This quarterly report on Form 10-Q includes certain statements that may be deemed "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, all of which are based upon various estimates and assumptions that the Company believes to be reasonable as of the date hereof. These statements involve risks and uncertainties that could cause the Company's actual future outcomes to differ materially from those set forth in such statements. Such risks and uncertainties include, but are not limited to:

fluctuations in operating activity due to downturns in levels of construction, seasonality and differing regional economic conditions;

competition in the construction industry, both from third parties and former employees, which could result in the loss of one or more customers or lead to lower margins on new contracts;

a general reduction in the demand for our services;

a change in the mix of our customers, contracts and business;

our ability to successfully manage construction projects;

possibility of errors when estimating revenue and progress to date on percentage-of-completion contracts;

inaccurate estimates used when entering into fixed-priced contracts;

challenges integrating new types of work or new processes into our divisions;

the cost and availability of qualified labor;

accidents resulting from the physical hazards associated with our work and the potential for accidents;

success in transferring, renewing and obtaining electrical and construction licenses;

## Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

our ability to pass along increases in the cost of commodities used in our business, in particular, copper, aluminum, steel, fuel and certain plastics;

potential supply chain disruptions due to credit or liquidity problems faced by our suppliers;

loss of key personnel and effective transition of new management;

warranty losses or other latent defect claims in excess of our existing reserves and accruals;

warranty losses or other unexpected liabilities stemming from former divisions which we have sold or closed;

growth in latent defect litigation in states where we provide residential electrical work for home builders not otherwise covered by insurance;

limitations on the availability of sufficient credit or cash flow to fund our working capital needs;

difficulty in fulfilling the covenant terms of our credit facilities;

increased cost of surety bonds affecting margins on work and the potential for our surety providers to refuse bonding or require additional collateral at their discretion;

**Table of Contents**

increases in bad debt expense and days sales outstanding due to liquidity problems faced by our customers;

changes in the assumptions made regarding future events used to value our stock options and performance-based stock awards;

the recognition of potential goodwill, long-lived assets and other investment impairments;

uncertainties inherent in estimating future operating results, including revenues, operating income or cash flow;

disagreements with taxing authorities with regard to tax positions we have adopted;

the recognition of tax benefits related to uncertain tax positions;

complications associated with the incorporation of new accounting, control and operating procedures;

the financial impact of new or proposed accounting regulations;

the ability of our controlling shareholder to take action not aligned with other shareholders;

the possibility that certain tax benefits of our net operating losses may be restricted or reduced in a change in ownership;

credit and capital market conditions, including changes in interest rates that affect the cost of construction financing and mortgages, and the inability for some of our customers to retain sufficient financing which could lead to project delays or cancellations;

the sale or disposition of the shares of our common stock held by our majority shareholder, which, under certain circumstances, would trigger change of control provisions in contracts such as employment agreements and financing and surety arrangements; and

Additional closures or sales of facilities in our Commercial & Industrial segment could result in significant future charges and a significant disruption of our operations.

You should understand that the foregoing, as well as other risk factors discussed in our annual report on Form 10-K/A for the year ended September 30, 2011, could cause future outcomes to differ materially from those experienced previously or those expressed in such forward-looking statements. We undertake no obligation to publicly update or revise information concerning our restructuring efforts, borrowing availability, cash position or any forward-looking statements to reflect events or circumstances that may arise after the date of this report. Forward-looking statements are provided in this quarterly report on Form 10-Q pursuant to the safe harbor established under the Private Securities Litigation Reform Act of 1995 and should be evaluated in the context of the estimates, assumptions, uncertainties and risks described herein.

General information about us can be found at [www.ies-co.com](http://www.ies-co.com) under Investor Relations . Our annual report on Form 10-K/A, quarterly reports on Form 10-Q and current reports on Form 8-K, as well as any amendments to those reports, are available free of charge through our website as soon as reasonably practicable after we file them with, or furnish them to, the Securities and Exchange Commission. You may also contact our Investor Relations department at 713-860-1500, and they will provide you with copies of our public reports.



**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC. AND SUBSIDIARIES****Consolidated Balance Sheets****(In Thousands, Except Share Information)**

	March 31, 2012 (Unaudited)	September 30, 2011 Restated
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 17,766	\$ 35,577
Restricted cash	8,812	
Accounts receivable:		
Trade, net of allowance of \$2,069 and \$2,645, respectively	69,577	85,728
Retainage	16,210	17,944
Inventories	11,718	8,443
Costs and estimated earnings in excess of billings on uncompleted contracts	9,753	9,963
Prepaid expenses and other current assets	6,958	2,840
<b>Total current assets</b>	<b>140,794</b>	<b>160,495</b>
LONG-TERM RECEIVABLE, net of allowance of \$0 and \$59, respectively	259	200
PROPERTY AND EQUIPMENT, net	8,519	8,016
GOODWILL	4,446	4,446
OTHER NON-CURRENT ASSETS, net	5,161	7,087
<b>Total assets</b>	<b>\$ 159,179</b>	<b>\$ 180,244</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Current maturities of long-term debt	\$ 1,644	\$ 209
Accounts payable and accrued expenses	63,420	78,980
Billings in excess of costs and estimated earnings on uncompleted contracts	19,081	19,585
<b>Total current liabilities</b>	<b>84,145</b>	<b>98,774</b>
LONG-TERM DEBT, net of current maturities	10,161	10,289
LONG-TERM DEFERRED TAX LIABILITY	284	284
OTHER NON-CURRENT LIABILITIES	7,266	6,596
<b>Total liabilities</b>	<b>101,856</b>	<b>115,943</b>
<b>STOCKHOLDERS EQUITY:</b>		
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, none issued and outstanding		
Common stock, \$0.01 par value, 100,000,000 shares authorized; 15,407,802 and 15,407,802 shares issued and 14,994,653 and 14,938,071 outstanding, respectively	154	154
Treasury stock, at cost, 413,149 and 451,329 shares, respectively	(4,526)	(5,595)
Additional paid-in capital	163,375	164,262
Retained deficit	(101,680)	(94,520)
<b>Total stockholders equity</b>	<b>57,323</b>	<b>64,301</b>



Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Total liabilities and stockholders' equity	\$ 159,179	\$ 180,244
--	------------	------------

The accompanying notes are an integral part of these Consolidated Financial Statements.

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC. AND SUBSIDIARIES****Consolidated Statements of Operations****(In Thousands, Except Share Information)**

	Three Months Ended March 31,	
	2012	2011 Restated
Revenues	\$ 112,807	\$ 118,326
Cost of services	100,221	112,999
Gross profit	12,586	5,327
Selling, general and administrative expenses	15,222	14,072
Gain on sale of assets	(87)	(87)
Restructuring charges	264	
Loss from operations	(2,813)	(8,658)
Interest and other (income) expense:		
Interest expense	543	576
Interest income	(8)	(24)
Other (income) expense, net	1	(8)
Interest and other expense, net	536	544
Loss from operations before income taxes	(3,349)	(9,202)
Provision (benefit) for income taxes	82	929
Net loss	\$ (3,431)	\$ (10,131)
(Loss) per share:		
Basic	\$ (0.23)	\$ (0.70)
Diluted	\$ (0.23)	\$ (0.70)
Shares used in the computation of loss per share		
Basic	14,638,678	14,481,005
Diluted	14,638,678	14,481,005

The accompanying notes are an integral part of these Consolidated Financial Statements.

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC. AND SUBSIDIARIES****Consolidated Statements of Operations****(In Thousands, Except Share Information)**

	Six Months Ended March 31,	
	2012	2011 Restated
Revenues	\$ 228,101	\$ 228,137
Cost of services	204,606	211,752
Gross profit	23,495	16,385
Selling, general and administrative expenses	28,596	32,724
Gain on sale of assets	(70)	(6,816)
Asset impairment		3,551
Restructuring charges	864	
Loss from operations	(5,895)	(13,074)
Interest and other (income) expense:		
Interest expense	1,088	1,175
Interest income	(15)	(49)
Other (income) expense, net	(64)	(23)
Interest and other expense, net	1,009	1,103
Loss from operations before income taxes	(6,904)	(14,177)
Provision (benefit) for income taxes	250	253
Net loss	\$ (7,154)	\$ (14,430)
(Loss) per share:		
Basic	\$ (0.49)	\$ (1.00)
Diluted	\$ (0.49)	\$ (1.00)
Shares used in the computation of loss per share		
Basic	14,603,693	14,463,996
Diluted	14,603,693	14,463,996

The accompanying notes are an integral part of these Consolidated Financial Statements.

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC. AND SUBSIDIARIES****Consolidated Statements of Cash Flows****(In Thousands)**

	Six Months Ended March 31, 2012 (Unaudited)	2011 Restated
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (7,154)	\$ (14,430)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Bad debt expense	(576)	(466)
Deferred financing cost amortization	(9)	169
Depreciation and amortization	1,058	3,418
Loss (gain) on sale of assets	(9)	(6,816)
Non-cash compensation expense	276	436
Asset impairment		3,551
Equity in losses of investment		96
Changes in operating assets and liabilities		
Accounts receivable	16,829	389
Inventories	(3,276)	(1,640)
Costs and estimated earnings in excess of billings	209	(2,930)
Prepaid expenses and other current assets	(571)	57
Other non-current assets	(40)	2,820
Accounts payable and accrued expenses	(14,130)	6,884
Billings in excess of costs and estimated earnings	(504)	(2,842)
Other non-current liabilities	98	(140)
Net cash (used in) provided by operating activities	(7,799)	(11,444)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(978)	(755)
Proceeds from sales of property and equipment		207
Proceeds from sales of facilities		16,287
Distribution from unconsolidated affiliates		(57)
Net cash (used in) provided by continuing operations	(978)	15,682
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Repayments of debt	(128)	(390)
Purchase of treasury stock	(94)	(65)
Changes in restricted cash	(8,812)	
Net cash used in financing activities	(9,034)	(455)
NET DECREASE IN CASH EQUIVALENTS	(17,811)	3,783
CASH AND CASH EQUIVALENTS, beginning of period	35,577	32,924
CASH AND CASH EQUIVALENTS, end of period	\$ 17,766	\$ 36,707
	2012	2011
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>		

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Cash paid for interest	\$	560	\$	1,009
Cash paid for income taxes	\$	137	\$	106

The accompanying notes are an integral part of these Consolidated Financial Statements.

---

**Table of Contents**

**INTEGRATED ELECTRICAL SERVICES, INC.**

**Notes to Consolidated Financial Statements**

**(All Amounts in Thousands Except Share Amounts)**

**1. BUSINESS**

*Description of the Business*

Integrated Electrical Services, Inc., a Delaware corporation, is a leading national provider of electrical infrastructure services to the communications, residential, commercial and industrial industries. Originally established as IES in 1997, we provide services from 57 locations serving the continental United States as of March 31, 2012. Our operations are organized into three business segments, based upon the nature of its products and services:

**Communications** Nationwide provider of products and services for mission critical infrastructure, such as data centers, of large corporations.

**Residential** Regional provider of electrical installation services for single-family housing and multi-family apartment complexes.

**Commercial & Industrial** Provider of electrical design, construction, and maintenance services to the commercial and industrial markets in various regional markets and nationwide in certain areas of expertise, such as the power infrastructure market.

*Sale of Non-Strategic Manufacturing Facility*

On November 30, 2010, a subsidiary of the Company sold substantially all the assets and certain liabilities of a non-strategic manufacturing facility engaged in manufacturing and selling fabricated metal buildings housing electrical equipment, such as switchgears, motor starters and control systems, to Siemens Energy, Inc. As part of this transaction, Siemens Energy, Inc. also acquired certain real property where the fabrication facilities are located from another subsidiary of the Company. The purchase price of \$10,086 was adjusted to reflect working capital variances. The transaction was completed on December 10, 2010 at which time we recognized a gain of \$6,763.

*Sale of Non-Core Electrical Distribution Facility*

On February 28, 2011, Key Electrical Supply, Inc, a wholly owned subsidiary of the Company, sold substantially all the assets and certain liabilities of a non-core electrical distribution facility engaged in distributing wiring, lighting, electrical distribution, power control and generators for residential and commercial applications to Elliot Electric Supply, Inc. The purchase price of \$6,676 was adjusted to reflect working capital variances. The loss on this transaction was immaterial.

*Controlling Shareholder*

At March 31, 2012, Tontine Capital Partners, L.P. and its affiliates (collectively, "Tontine"), was the controlling shareholder of the Company's common stock. Accordingly, Tontine has the ability to exercise significant control of our affairs, including the election of directors and any action requiring the approval of shareholders, including the approval of any potential merger or sale of all or substantially all assets or divisions of the Company, or the Company itself. In its most recent Schedule 13D, Tontine stated that it has no current plans to make any material change in the Company's business or corporate structure. For a more complete discussion on our relationship with Tontine, please refer to Note 2 "Controlling Shareholder" in the notes to these Consolidated Financial Statements.

*Related Party Transaction*

On March 29, 2012, we entered into a sublease agreement with Tontine Associates, LLC, an affiliate of our controlling shareholder, for corporate office space in Greenwich, Connecticut. The lease extends from April 1, 2012 through March 31, 2014, with monthly payments due in

the amount of \$6.

**Table of Contents**

**INTEGRATED ELECTRICAL SERVICES, INC.**

**Notes to Consolidated Financial Statements**

**(All Amounts in Thousands Except Share Amounts)**

*Summary of Significant Accounting Policies*

These unaudited condensed consolidated financial statements reflect, in the opinion of management, all adjustments necessary to present fairly the financial position as of, and the results of operations for, the periods presented. All adjustments are considered to be normal and recurring unless otherwise described herein. Interim period results are not necessarily indicative of results of operations or cash flows for the full year. During interim periods, we follow the same accounting policies disclosed in our annual report of Form 10-K/A for the year ended September 30, 2011. Please refer to the *Notes to Consolidated Financial Statements* in our annual report on Form 10-K/A for the year ended September 30, 2011, when reviewing our interim financial results set forth herein.

*Revenue Recognition*

As of March 31, 2012 the Company had recognized revenue totaling \$1,098 associated with one contract claim. We recognize revenue associated with unapproved change orders and claims to the extent that related costs have been incurred, recovery is probable and the value can be reliably estimated.

*Fair Value of Financial Instruments*

Our financial instruments consist of cash and cash equivalents, accounts receivable, notes receivable, investments, accounts payable, a line of credit, a note payable issued to finance an insurance policy, and a \$10,000 senior subordinated loan agreement (the "Tontine Term Loan"). We believe that the carrying value of financial instruments, with the exception of the Tontine Term Loan and our cost method investment in EnerTech, in the accompanying Consolidated Balance Sheets approximates their fair value due to their short-term nature. We estimate that the fair value of the Tontine Term Loan is \$10,457 based on comparable debt instruments at March 31, 2012. For additional information, please refer to Note 4, "Debt - The Tontine Term Loan" of this report.

We estimate that the fair value of our investment in EnerTech is \$1,097 at March 31, 2012. For additional information, please refer to Note 8, "Securities and Equity Investments - Investment in EnerTech."

*Asset Impairment*

During the six months ended March 31, 2011 the Company ceased use of certain internally-developed software. As a result, the software has a fair value of zero. The net charge of \$3,551 was recorded separately in the accompanying consolidated statements of operations as a component of loss from operations.

*Use of Estimates and Assumptions*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires the use of estimates and assumptions by management in determining the reported amounts of assets and liabilities, disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Estimates are primarily used in our revenue recognition of construction in progress, fair value assumptions in analyzing goodwill, investments, intangible assets and long-lived asset impairments and adjustments, allowance for doubtful accounts receivable, stock-based compensation, reserves for legal matters, assumptions regarding estimated costs to exit certain divisions, realizability of deferred tax assets, and self-insured claims liabilities and related reserves.

*Cash and Cash Equivalents*

We consider all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. We have restricted cash used to collateralize our letters of credit.



## Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

### *Seasonality and Quarterly Fluctuations*

Results of operations from our Residential construction segment are seasonal, depending on weather trends, with typically higher revenues generated during spring and summer and lower revenues during fall and winter. The Communications and Commercial & Industrial segments of our business are less subject to seasonal trends, as work in these segments generally is

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)**

performed inside structures protected from the weather. Our service and maintenance business is generally not affected by seasonality. In addition, the construction industry has historically been highly cyclical. Our volume of business may be adversely affected by declines in construction projects resulting from adverse regional or national economic conditions. Quarterly results may also be materially affected by the timing of new construction projects. Accordingly, operating results for any fiscal period are not necessarily indicative of results that may be achieved for any subsequent fiscal period.

**2. CONTROLLING SHAREHOLDER**

As of March 31, 2012, \$10,000 remains outstanding on the Tontine Term Loan, with \$274 in accrued interest.

Although Tontine has not indicated any plans to alter its ownership level, should Tontine reconsider its investment plans and sell its controlling interest in the Company, a change in ownership would occur. A change in ownership, as defined by Internal Revenue Code Section 382, could reduce the availability of net operating losses for federal and state income tax purposes. Furthermore, a change in control would trigger the change of control provisions in a number of our material agreements, including our \$40,000 Revolving Credit Facility, bonding agreements with our sureties and certain employment contracts with certain officers and employees of the Company.

Tontine Capital Partners, L.P. and its affiliates own the majority of our common stock. As a significant stakeholder, Tontine provides strategic, general corporate, operational, organizational and financial advice to our board of directors and management. Although such advice may be considered by the board and management, neither the board nor management is under any legal obligation to follow such advice.

**3. STRATEGIC ACTIONS***The 2011 Restructuring Plan*

In the second quarter of our 2011 fiscal year, we began a restructuring program (the 2011 Restructuring Plan) that was designed to consolidate operations within our Commercial & Industrial business. Pursuant to the 2011 Restructuring Plan, we will finalize the sale or closure of certain underperforming facilities within our Commercial & Industrial operations. The 2011 Restructuring Plan is a key element of our commitment to return the Company to profitability.

The facilities directly affected by the 2011 Restructuring Plan are in several locations throughout the country, including Arizona, Florida, Iowa, Massachusetts, Louisiana, Nevada and Texas. These facilities were selected due to current business prospects and the extended time frame needed to return the facilities to a profitable position. We expect that closure costs could range from \$4,500 to \$5,500 in the aggregate. Closure costs associated with the 2011 Restructuring Plan include equipment and facility lease termination expenses, incremental management consulting expenses and severance costs for employees. The Company is in the process of winding down these facilities. As part of our restructuring charges within our Commercial & Industrial segment we recognized \$35 in severance costs, \$764 in consulting services, and \$65 in costs related to lease terminations during the six months ended March 31, 2012.

The following table summarizes the activities related to our restructuring activities by component:

	Severance Charges	Consulting Charges	Lease Termination & Other Charges	Total
Restructuring liability at September 30, 2011	\$ 1,081	\$ 336	\$ 790	\$ 2,207
Restructuring charges incurred	35	764	65	864
Cash payments made	(650)	(1,084)	(268)	(2,002)

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Restructuring liability at March 31, 2012	\$ 466	\$ 16	\$ 587	\$ 1,069
---	--------	-------	--------	----------

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)***Additional Facility Closing*

During the first quarter of fiscal 2012, the Company determined the underperforming Baltimore facility within its Commercial & Industrial and Communications divisions would be either sold or closed over the next three to six months. This closing is a key element of management's overall plan to return the Company to profitability. The Baltimore location was selected based upon current businesses performance and the extended time frame needed to return the operation to profitability. We expect that closure costs could range from \$340 to \$480 in the aggregate.

**4. DEBT**

Debt consists of the following:

	March 31, 2012	September 30, 2011
Tontine Term Loan, due May 15, 2013, bearing interest at 11.00%	\$ 10,000	\$ 10,000
Insurance Financing Agreements	1,367	
Capital leases and other	438	498
Total debt	11,805	10,498
Less Short-term debt and current maturities of long-term debt	(1,644)	(209)
Total long-term debt	\$ 10,161	\$ 10,289

Future payments on debt at March 31, 2012 are as follows:

	Capital Leases and Other	Insurance Financing	Term Debt	Total
2012	\$ 202	\$ 1,367	\$	\$ 1,569
2013	317		10,000	10,317
2014	26			26
2015				
2016				
Thereafter				
Less: Imputed Interest	(107)			(107)
Total	\$ 438	\$ 1,367	\$ 10,000	\$ 11,805

For the three months ended March 31, 2012 and 2011, we incurred interest expense of \$543 and \$576, respectively.

*The Revolving Credit Facility*

On May 12, 2006, we entered into a Loan and Security Agreement (the "Loan and Security Agreement"), for a revolving credit facility (the "Revolving Credit Facility") with Bank of America, N.A. and certain other lenders. On May 7, 2008, we renegotiated the terms of our Revolving Credit Facility and entered into an amended agreement with the same financial institutions. On April 30, 2010, we renegotiated the terms of, and

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

entered into an amendment to, the Loan and Security Agreement pursuant to which the maturity date was extended to May 31, 2012. In connection with the amendment, we incurred an amendment fee of \$200, which is being amortized over 24 months.

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)**

On December 15, 2011, we renegotiated the terms of, and entered into an amendment to, the Loan and Security Agreement without incurring termination charges. Under the terms of the amended Revolving Credit Facility, the size of the facility was reduced to \$40,000 and the maturity date was extended to November 12, 2012. Further, we were required to cash collateralize all of our letters of credit issued by the banks. The cash collateral is added to the borrowing base calculation at 100% throughout the term of the agreement. The Revolving Credit Facility requires that we maintain a fixed charge coverage ratio of not less than 1.0:1.0 at any time that our aggregate amount of unrestricted cash on hand plus availability is less than \$25,000 and, thereafter, until such time as our aggregate amount of unrestricted cash on hand plus availability has been at least \$25,000 for a period of 60 consecutive days. Additionally, if there are any loans outstanding on or after April 30, 2012, the Company's EBITDA for the period from October 2011 through March 2012, may not exceed a negative \$2,500 and we will be required to have a cumulative fixed charge coverage ratio of at least 1.0:1.0 at all times beginning April 1, 2012 to maintain any borrowings under the agreement. The measurement period for this additional test for borrowings begins with the monthly operating results for April 2012 and adds the monthly operating results for each month thereafter to determine the cumulative test during such time as revolving loans are outstanding. Failure to meet this performance test will result in an immediate event of default. The amended Agreement also calls for cost of borrowings of 4.0% over LIBOR per annum. Cost for letters of credit are the same as borrowings and also include a 25 basis point fronting fee. All other terms and conditions remain unchanged. In connection with the amendment, we incurred an amendment fee of \$60 which, together with the unamortized balance of the prior amendment, is being amortized using the straight line method through November 12, 2012.

The Revolving Credit Facility is guaranteed by our subsidiaries and secured by first priority liens on substantially all of our subsidiaries' existing and future acquired assets, exclusive of collateral provided to our surety providers. The Revolving Credit Facility contains customary affirmative, negative and financial covenants. The Revolving Credit Facility also restricts us from paying cash dividends and places limitations on our ability to repurchase our common stock.

Borrowings under the Revolving Credit Facility may not exceed a borrowing base that is determined monthly by our lenders based on available collateral, primarily certain accounts receivables and inventories. Under the terms of the Revolving Credit Facility in effect as of March 31, 2012, interest for loans and letter of credit fees is based on our Total Liquidity, which is calculated for any given period as the sum of average daily availability for such period plus average daily unrestricted cash on hand for such period as follows:

Total Liquidity	Annual Interest Rate for Loans	Annual Interest Rate for Letters of Credit
Greater than or equal to \$60,000	LIBOR plus 3.00% or Base Rate plus 1.00%	3.00% plus 0.25% fronting fee
Greater than \$40,000 and less than \$60,000	LIBOR plus 3.25% or Base Rate plus 1.25%	3.25% plus 0.25% fronting fee
Less than or equal to \$40,000	LIBOR plus 3.50% or Base Rate plus 1.50%	3.50% plus 0.25% fronting fee

At March 31, 2012, we had \$22,009 available to us under the Revolving Credit Facility, with no outstanding borrowings. We had \$8,812 in outstanding letters of credit which were fully collateralized with restricted cash.

At March 31, 2012, our Total Liquidity was \$39,770. For the three months ended March 31, 2012, we paid no interest for loans under the Revolving Credit Facility and had a weighted average interest rate, including fronting fees, of 3.50% for letters of credit. In addition, we are charged monthly in arrears for (1) an unused commitment fee of 0.50%, and (2) certain other fees and charges as specified in the Loan and Security Agreement, as amended.

As of March 31, 2012, we were subject to the financial covenant under the Revolving Credit Facility requiring that we maintain a fixed charge coverage ratio of not less than 1.0:1.0 at any time that our aggregate amount of unrestricted cash on hand plus availability is less than \$25,000 and, thereafter, until such time as our aggregate amount of unrestricted cash on hand plus availability has been at least \$25,000 for a period of 60 consecutive days. As of March 31, 2012, our Total Liquidity was in excess of \$25,000 for the prior 60 day period. Had our Total Liquidity been less than \$25,000 at March 31, 2012, we would not have met the 1.0:1.0 fixed charge coverage ratio test, had it been applicable.



**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)***The Tontine Term Loan*

On December 12, 2007, we entered into the Tontine Term Loan, a \$25,000 senior subordinated loan agreement, with Tontine. The Tontine Term Loan bears interest at 11.0% per annum and is due on May 15, 2013. Interest is payable quarterly in cash or in-kind at our option. Any interest paid in-kind will bear interest at 11.0% in addition to the loan principal. On April 30, 2010, we prepaid \$15,000 of principal on the Tontine Term Loan. On May 1, 2010, Tontine assigned the Tontine Term Loan to TCP Overseas Master Fund II, L.P. We may repay the Tontine Term Loan at any time prior to the maturity date at par, plus accrued interest without penalty. The Tontine Term Loan is subordinated to the Revolving Credit Facility. The Tontine Term Loan is an unsecured obligation of the Company and its subsidiary borrowers. The Tontine Term Loan contains no financial covenants or restrictions on dividends or distributions to stockholders.

**5. PER SHARE INFORMATION**

Basic earnings per share is calculated as income (loss) available to common stockholders, divided by the weighted average number of common shares outstanding during the period. Our restricted shares are considered participating securities, but do not have a contractual obligation to share in the losses in any given period. As a result, these participating securities will not be allocated any losses in the periods of net losses, but will be allocated income in the periods of net income using the two-class method.

The following table reconciles the components of the basic and diluted earnings (loss) per share for the Three and Six Months Ended March 31, 2012 and 2011, (in thousands, except share information):

	Three Months Ended March 31,	
	2012	2011
<b>Numerator:</b>		
Net income (loss) attributable to common shareholders	\$ (3,431)	\$ (10,131)
Net income (loss) attributable to restricted shareholders		
Net income (loss)	\$ (3,431)	\$ (10,131)
<b>Denominator:</b>		
Weighted average common shares outstanding basic	14,638,678	14,481,005
Effect of dilutive stock options and non-vested restricted stock		
Weighted average common and common equivalent shares outstanding diluted	14,638,678	14,481,005
Basic loss per share	\$ (0.23)	\$ (0.70)
Diluted loss per share	\$ (0.23)	\$ (0.70)
	Six Months Ended March 31,	
	2012	2011
<b>Numerator:</b>		
Net income (loss) attributable to common shareholders	\$ (7,154)	\$ (14,430)
Net income (loss) attributable to restricted shareholders		



Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Net income (loss)	\$ (7,154)	\$ (14,430)
<b>Denominator:</b>		
Weighted average common shares outstanding basic	14,603,693	14,463,996
Effect of dilutive stock options and non-vested restricted stock		
Weighted average common and common equivalent shares outstanding diluted	14,603,693	14,463,996
Basic loss per share	\$ (0.49)	\$ (1.00)
Diluted loss per share	\$ (0.49)	\$ (1.00)

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)**

For the three months and six months ended March 31, 2012 and 2011, 20,000 and 158,500 stock options, respectively, were excluded from the computation of fully diluted earnings per share because the exercise prices of the options were greater than the average price of our common stock. For the three months and six months ended March 31, 2012 and 2011, 352,360 and 419,600 shares, respectively, of restricted stock were excluded from the computation of fully diluted earnings per share because we reported a loss from continuing operations.

**6. OPERATING SEGMENTS**

We manage and measure performance of our business in three distinct operating segments: Communications, Residential and Commercial & Industrial. These segments are reflective of how the Company's Chief Operating Decision Maker ( CODM ) reviews operating results for the purposes of allocating resources and assessing performance. The Company's CODM is its Chief Executive Officer. The Communications segment consists of low voltage installation, design, planning and maintenance for mission critical infrastructure such as data centers. The Residential segment consists of electrical installation, replacement and renovation services in single-family, condominium, townhouse and low-rise multifamily housing units. The Commercial & Industrial segment provides a broad range of electrical design, construction, renovation, engineering and maintenance services to the commercial and industrial markets.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. We evaluate performance based on income from operations of the respective business units prior to the allocation of Corporate office expenses. Transactions between segments are eliminated in consolidation. Our Corporate office provides general and administrative as well as support services to our three operating segments. Management allocates costs to segments for selling, general and administrative expenses and depreciation expense.

Segment information for the three and six months ended March 31, 2012 and 2011 is as follows:

	Three Months Ended March 31, 2012				
	Communications	Residential	Commercial & Industrial	Corporate	Total
Revenues	\$ 29,024	\$ 29,628	\$ 54,155	\$	\$ 112,807
Cost of services	25,244	25,097	49,882	(2)	100,221
Gross profit	3,780	4,531	4,273	2	12,586
Selling, general and administrative	2,863	4,061	3,727	4,571	15,222
Corporate allocations	474	472	1,423	(2,369)	
Loss (gain) on sale of assets		3	(90)		(87)
Restructuring charge			236	28	264
Income (loss) from operations	\$ 443	\$ (5)	\$ (1,023)	\$ (2,228)	\$ (2,813)
<b>Other data:</b>					
Depreciation and amortization expense	\$ 75	\$ 90	\$ 69	\$ 303	\$ 537
Total assets	\$ 18,502	\$ 27,318	\$ 67,087	\$ 46,272	\$ 159,179

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)**

	Three Months Ended March 31, 2011 as Restated				
	Communications	Residential	Commercial & Industrial	Corporate	Total
Revenues	\$ 23,368	\$ 26,310	\$ 68,648	\$	\$ 118,326
Cost of services	20,944	22,714	69,260	81	112,999
Gross profit	2,424	3,596	(612)	(81)	5,327
Selling, general and administrative	1,723	3,936	1,550	6,863	14,072
Corporate allocations	586	572	2,287	(3,445)	
(Gain) Loss on sale of assets		(48)	(7)	(32)	(87)
Income (loss) from operations	\$ 115	\$ (864)	\$ (4,442)	\$ (3,467)	\$ (8,658)
Other data:					
Depreciation and amortization expense	\$ 22	\$ 84	\$ 158	\$ 1,297	\$ 1,561
Total assets	\$ 19,957	\$ 21,878	\$ 86,853	\$ 62,980	\$ 191,668

	Six Months Ended March 31, 2012				
	Communications	Residential	Commercial & Industrial	Corporate	Total
Revenues	\$ 55,126	\$ 58,900	\$ 114,075	\$	\$ 228,101
Cost of services	48,007	49,721	106,870	8	204,606
Gross profit	7,119	9,179	7,205	(8)	23,495
Selling, general and administrative	5,385	8,003	6,808	8,400	28,596
Corporate allocations	949	943	2,846	(4,738)	
Loss (gain) on sale of assets	11	7	(88)		(70)
Restructuring charge			818	46	864
Income (loss) from operations	\$ 774	\$ 226	\$ (3,179)	\$ (3,716)	\$ (5,895)
Other data:					
Depreciation and amortization expense	\$ 140	\$ 172	\$ 157	\$ 590	\$ 1,059
Total assets	\$ 18,502	\$ 27,318	\$ 67,087	\$ 46,272	\$ 159,179

	Six Months Ended March 31, 2011 As Restated				
	Communications	Residential	Commercial & Industrial	Corporate	Total
Revenues	\$ 43,290	\$ 52,354	\$ 132,493	\$	\$ 228,137
Cost of services	37,660	44,222	129,789	81	211,752
Gross profit	5,630	8,132	2,704	(81)	16,385
Selling, general and administrative	3,481	8,131	6,846	14,266	32,724
Corporate allocations	1,136	1,160	4,433	(6,729)	
Loss (gain) on sale of assets		(70)	(49)	(3,146)	(3,265)

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Income (loss) from operations	\$ 1,013	\$ (1,089)	\$ (8,526)	\$ (4,472)	\$ (13,074)
Other data:					
Depreciation and amortization expense	\$ 48	\$ 183	\$ 393	\$ 2,844	\$ 3,468
Total assets	\$ 19,957	\$ 21,878	\$ 86,853	\$ 62,980	\$ 191,668

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)****7. STOCKHOLDERS EQUITY**

The 2006 Equity Incentive Plan became effective on May 12, 2006 (as amended, the 2006 Equity Incentive Plan). The 2006 Equity Incentive Plan provides for grants of stock options as well as grants of stock, including restricted stock. We have approximately 1.0 million shares of common stock authorized for issuance under the 2006 Equity Incentive Plan.

On May 12, 2008, 10,555 shares of outstanding common stock that were reserved for issuance upon exchange of previously issued shares pursuant to our Plan were cancelled.

*Treasury Stock*

During the six months ended March 31, 2012, we repurchased 34,578 common shares from our employees to satisfy minimum tax withholding requirements upon the vesting of restricted stock issued under the 2006 Equity Incentive Plan, and 27,242 unvested shares were forfeited by former employees and returned to treasury stock. We issued 100,000 shares out of treasury stock under our share-based compensation programs.

During the six months ended March 31, 2011, we repurchased 18,846 common shares from our employees to satisfy minimum tax withholding requirements upon the vesting of restricted stock issued under the 2006 Equity Incentive Plan and 63,077 unvested shares were forfeited by former employees and returned to treasury stock. We issued 204,000 shares out of treasury stock under our share-based compensation programs.

*Restricted Stock*

Restricted Stock Awards:

Fiscal Year	Shares Granted	Weighted Average Fair Value at Date of Grant	Vested	Forfeitures	Shares Outstanding	Expense recognized through March 31, 2012
2006	384,850	\$ 24.78	258,347	126,503		\$ 6,402
2006	25,000	\$ 17.36	25,000			\$ 434
2007	20,000	\$ 25.08	20,000			\$ 502
2007	4,000	\$ 26.48	4,000			\$ 106
2008	101,650	\$ 19.17	85,750	15,900		\$ 1,779
2009	185,100	\$ 8.71	146,400	38,700		\$ 1,344
2010	225,486	\$ 3.64	59,347	77,439	88,700	\$ 450
2011	320,000	\$ 3.39	87,579	68,761	163,660	\$ 319
2012	100,000	\$ 2.00			100,000	\$ 33

During the six months ended March 31, 2012 and 2011, we recognized \$276 and \$436 respectively, in compensation expense related to these restricted stock awards. At March 31, 2012, the unamortized compensation cost related to outstanding unvested restricted stock was \$749. We expect to recognize \$261 of this unamortized compensation expense during the remaining six months of our 2012 fiscal year and \$488 thereafter. A summary of restricted stock awards for the years ended September 30, 2012, 2011 and 2010 is provided in the table below:

	Years Ended September 30,		
	2012	2011	2010
Unvested at beginning of year	376,200	352,086	230,716
Granted	100,000	320,000	225,486

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Vested	(96,598)	(165,628)	(66,116)
Forfeited	(27,242)	(130,258)	(38,000)
Unvested at end of year	352,360	376,200	352,086

**Table of Contents**

**INTEGRATED ELECTRICAL SERVICES, INC.**

**Notes to Consolidated Financial Statements**

**(All Amounts in Thousands Except Share Amounts)**

All the restricted shares granted under the 2006 Equity Incentive Plan (vested or unvested) participate in dividends issued to common shareholders, if any.

*Phantom Stock Units*

We granted 24,632 shares of performance-based phantom stock units ( PSUs ) to the members of the Board of Directors in 2011. These PSU s will be paid via unrestricted stock grants to each director upon his departure from the Board of Directors.

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)***Stock Options*

We utilized a binomial option pricing model to measure the fair value of stock options granted. Our determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, our expected stock price volatility over the term of the awards, the risk-free rate of return, and actual and projected employee stock option exercise behaviors. The expected life of stock options is not considered under the binomial option pricing model that we utilize. The assumptions used in the fair value method calculation for the years ended September 30, 2012, 2011 and 2010 are disclosed in the following table:

	Years Ended March 31,		
	2012	2011	2010
Weighted average value per option granted during the period	\$ N/A	2.05	\$ N/A
Dividends (1)	\$ N/A		\$ N/A
Stock price volatility (2)	N/A	69.9%	N/A
Risk-free rate of return	N/A	1.9%	N/A
Option term	N/A	10.0 years	N/A
Expected life	N/A	6.0 years	N/A
Forfeiture rate (3)	N/A	0.0%	N/A

(1) We do not currently pay dividends on our common stock.

(2) Based upon the Company's historical volatility.

(3) The forfeiture rate for these options was assumed on the date of grant to be zero based on the limited number of employees who have been awarded stock options.

Stock-based compensation expense recognized during the period is based on the value of the portion of the share-based payment awards that is ultimately expected to vest during the period. As stock-based compensation expense recognized in the Consolidated Statements of Operations is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. We estimate our forfeitures at the time of grant and revise, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

The following table summarizes activity under our stock option plans.

	Shares	Weighted Average Exercise Price
Outstanding, September 30, 2008	161,000	\$ 26.66
Options granted	7,500	17.09
Exercised		
Forfeited and Cancelled	(10,000)	41.61
Outstanding, September 30, 2009	158,500	\$ 18.66
Options granted		
Exercised		
Forfeited and Cancelled		



Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Outstanding, September 30, 2010	158,500	\$	18.66
Options granted	20,000		3.24
Exercised			
Forfeited and Cancelled	(158,500)		18.66
Outstanding, September 30, 2011	20,000	\$	3.24
Options granted			
Exercised			
Forfeited and Cancelled			
Outstanding, March 31, 2012	20,000	\$	3.24

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)**

The following table summarizes options outstanding and exercisable at March 31, 2012:

Range of Exercise Prices	Outstanding as of March 31, 2012	Remaining Contractual Life in Years	Weighted-Average Exercise Price	Exercisable as of March 31, 2012	Weighted-Average Exercise Price
\$3.24	20,000	9.30	\$3.24		\$3.24
	20,000	9.30	\$3.24		\$3.24

All of our outstanding options vest over a three-year period at a rate of one-third per year upon the annual anniversary date of the grant and expire ten years from the grant date if they are not exercised. Upon exercise of stock options, it is our policy to first issue shares from treasury stock, then to issue new shares. Unexercised stock options expire by July 2021.

**8. SECURITIES AND EQUITY INVESTMENTS***Investment in EnerTech Capital Partners II L.P.*

Our investment in EnerTech was approximately 2% of the overall ownership in EnerTech at March 31, 2012 and September 30, 2011. As such, we accounted for this investment using the cost method of accounting.

EnerTech's investment portfolio periodically results in unrealized losses reflecting a possible, other-than-temporary impairment of our investment. If the facts arise that lead us to determine that any unrealized losses are not temporary, we would write-down our investment in EnerTech through a charge to other expense in the period of such determination. The carrying value of our investment in EnerTech at March 31, 2012 and September 30, 2011 was \$1,003 and \$1,003, respectively, and is currently recorded as a component of Other Non-Current Assets in our Consolidated Balance Sheets. The following table presents the reconciliation of the carrying value and unrealized gains (losses) to the fair value of the investment in EnerTech as of March 31, 2012 and September 30, 2011:

	March 31, 2012	September 30, 2011
Carrying value	\$ 1,003	\$ 1,003
Unrealized gains (losses)	94	
Fair value	\$ 1,097	\$ 1,003

On December 31, 2011, EnerTech's general partner, with the consent of the fund's investors, extended the fund through December 31, 2012. The fund will terminate on this date unless extended by the fund's valuation committee. The fund may be extended for another one-year period through December 31, 2013 with the consent of the fund's valuation committee.

**9. EMPLOYEE BENEFIT PLANS***401(k) Plan*

## Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

In November 1998, we established the Integrated Electrical Services, Inc. 401(k) Retirement Savings Plan (the 401(k) Plan ). All full-time IES employees are eligible to participate on the first day of the month subsequent to completing thirty days of service and attaining age twenty-one. Participants become vested in our matching contributions following three years of service.

---

**Table of Contents**

**INTEGRATED ELECTRICAL SERVICES, INC.**

**Notes to Consolidated Financial Statements**

**(All Amounts in Thousands Except Share Amounts)**

On February 13, 2009, we suspended company matching cash contributions to employee's contributions due to the significant impact the economic recession has had on the Company's financial performance. We made no contributions to the 401(k) plan for the three months ended March 31, 2012 and 2011, respectively.

*Executive Deferred Compensation Plan*

Under the Executive Deferred Compensation Plan certain employees are permitted to defer a portion (up to 75%) of their base salary and/or bonus for a Plan Year. The Compensation Committee of the Board of Directors may, in its sole discretion, credit one or more participants with an employer deferral (contribution) in such amount as the Committee may choose (Employer Contribution). The Employer Contribution, if any, may be a fixed dollar amount, a fixed percentage of the participant's compensation, base salary, or bonus, or a matching amount with respect to all or part of the participant's elective deferrals for such plan year, and/or any combination of the foregoing as the Committee may choose.

On February 13, 2009, we suspended Company matching cash contributions to employee's contributions due to the significant impact the economic recession has had on the Company's financial performance. We made no contributions to the Executive Deferred Compensation Plan for the three months ended March 31, 2012 and 2011 respectively.

*Post Retirement Benefit Plans*

Certain individuals at one of the Company's locations are entitled to receive fixed annual payments that reach a maximum amount, as specified in the related agreements, for a ten year period following retirement or, in some cases, the attainment of 62 years of age. We recognize the unfunded status of the plan as part of current liabilities and non-current liabilities in our Consolidated Balance Sheet. Benefits vest 50% after ten years of service, which increases by 10% per annum until benefits are fully vested after 15 years of service. We had an unfunded benefit liability of \$746 and \$597 recorded as of March 31, 2012 and 2011 respectively.

**10. FAIR VALUE MEASUREMENTS**

*Fair Value Measurement Accounting*

This disclosure relates to the activity for assets and liabilities measured at fair value on a recurring basis, including transfers of assets and liabilities between Level 1 and Level 2 of the fair value hierarchy and the separate presentation of purchases, sales, issuances and settlements of assets and liabilities within Level 3 of the fair value hierarchy. In addition, we provide enhanced disclosure of the valuation techniques and inputs used in the fair value measurements within Level 2 and Level 3 when applicable.

Fair value is considered the price to sell an asset, or transfer a liability, between market participants on the measurement date. Fair value measurements assume that the asset or liability is (1) exchanged in an orderly manner, (2) the exchange is in the principal market for that asset or liability, and (3) the market participants are independent, knowledgeable, able and willing to transact an exchange. Fair value accounting and reporting establishes a framework for measuring fair value by creating a hierarchy for observable independent market inputs and unobservable market assumptions and expands disclosures about fair value measurements. Considerable judgment is required to interpret the market data used to develop fair value estimates. As such, the estimates presented herein are not necessarily indicative of the amounts that could be realized in a current exchange. The use of different market assumptions and/or estimation methods could have a material effect on the estimated fair value.

Financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2012 are summarized in the following table by the type of inputs applicable to the fair value measurements:

**Table of Contents****INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)**

	Total Fair Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable (Level 3)
Money market accounts	\$ 8,817	\$ 8,817		
Executive Savings Plan assets	548	548		
Executive Savings Plan liabilities	(541)	(541)		
Total	\$ 8,824	\$ 8,824		

Below is a description of the inputs used to value the assets summarized in the preceding table:

Level 1 Inputs represent unadjusted quoted prices for identical assets exchanged in active markets.

Level 2 Inputs include directly or indirectly observable inputs other than Level 1 inputs such as quoted prices for similar assets exchanged in active or inactive markets; quoted prices for identical assets exchanged in inactive markets; and other inputs that are considered in fair value determinations of the assets.

Level 3 Inputs include unobservable inputs used in the measurement of assets. Management is required to use its own assumptions regarding unobservable inputs because there is little, if any, market activity in the assets or related observable inputs that can be corroborated at the measurement date.

**11. COMMITMENTS AND CONTINGENCIES***Legal Matters*

From time to time we are a party to various claims, lawsuits and other legal proceedings that arise in the ordinary course of business. We maintain various insurance coverage to minimize financial risk associated with these proceedings. None of these proceedings, separately or in the aggregate, are expected to have a material adverse effect on our financial position, results of operations or cash flows. With respect to all such proceedings, we record reserves when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. We expense routine legal costs related to these proceedings as they are incurred.

The following is a discussion of our significant legal matters:

Ward Transformer Site

One of our subsidiaries has been identified as one of more than 200 potentially responsible parties (PRPs) with respect to the clean-up of an electric transformer resale and reconditioning facility, known as the Ward Transformer Site, located in Raleigh, North Carolina. The facility built, repaired, reconditioned and sold electric transformers from approximately 1964 to 2005. We did not own or operate the facility but a corporation that we acquired in July 1999 is believed to have sent transformers to the facility during the 1990 s. During the course of its operation, the facility was contaminated by Polychlorinated Biphenyls (PCBs), which also have been found to have migrated off the site.

Four PRPs have commenced clean-up of on-site contaminated soils under an Emergency Removal Action pursuant to a settlement agreement and Administrative Order on Consent entered into between the four PRPs and the U.S. Environmental Protection Agency (EPA) in September 2005. We are not a party to that settlement agreement or Order on Consent. In April 2009, two of these PRPs, Carolina Power and Light Company and Consolidation Coal Company, filed suit against us and most of the other PRPs in the U.S. District Court for the Eastern District of North Carolina (Western Division) to contribute to the cost of the clean-up. In addition to the on-site clean-up, the EPA has selected

## Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

approximately 50 PRPs to which it sent a Special Notice Letter in late 2008 to organize the clean-up of soils off site and address contamination of groundwater and other miscellaneous off-site issues. We were not a recipient of that letter.

Based on our investigation to date, there is evidence to support our defense that our subsidiary contributed no PCB contamination to the site. In addition, we have tendered a demand for indemnification to the former owner of the acquired corporation that may have transacted business with the facility. As of March 31, 2012, we have not recorded a reserve for this matter, as we believe the likelihood of our responsibility for damages is not probable and a potential range of exposure is not estimable.

**Table of Contents**

**INTEGRATED ELECTRICAL SERVICES, INC.**

**Notes to Consolidated Financial Statements**

**(All Amounts in Thousands Except Share Amounts)**

*Risk Management*

We retain the risk for workers' compensation, employer's liability, automobile liability, general liability and employee group health claims, resulting from uninsured deductibles per accident or occurrence which are subject to annual aggregate limits. Our general liability program provides coverage for bodily injury and property damage. Losses up to the deductible amounts are accrued based upon our known claims incurred and an estimate of claims incurred but not reported. As a result, many of our claims are effectively self-insured. Many claims against our insurance are in the form of litigation. At March 31, 2012, we had \$7,207 accrued for insurance liabilities. We are also subject to construction defect liabilities, primarily within our Residential segment. As of March 31, 2012, we had reserved \$402 for these claims.

Some of the underwriters of our casualty insurance program require us to post letters of credit as collateral. This is common in the insurance industry. To date, we have not had a situation where an underwriter has had reasonable cause to effect payment under a letter of credit. At March 31, 2012, \$8,182 of our outstanding letters of credit were utilized to collateralize our insurance program.

*Surety*

Many customers, particularly in connection with new construction, require us to post performance and payment bonds issued by a surety. Those bonds provide a guarantee to the customer that we will perform under the terms of our contract and that we will pay our subcontractors and vendors. If we fail to perform under the terms of our contract or to pay subcontractors and vendors, the customer may demand that the surety make payments or provide services under the bond. We must reimburse the sureties for any expenses or outlays they incur on our behalf. To date, we have not been required to make any reimbursements to our sureties for bond-related costs.

As is common in the surety industry, sureties issue bonds on a project-by-project basis and can decline to issue bonds at any time. We believe that our relationships with our sureties will allow us to provide surety bonds as they are required. However, current market conditions, as well as changes in our sureties' assessment of our operating and financial risk, could cause our sureties to decline to issue bonds for our work. If our sureties decline to issue bonds for our work, our alternatives would include posting other forms of collateral for project performance, such as letters of credit or cash, seeking bonding capacity from other sureties, or engaging in more projects that do not require surety bonds. In addition, if we are awarded a project for which a surety bond is required but we are unable to obtain a surety bond, the result can be a claim for damages by the customer for the costs of replacing us with another contractor.

As of March 31, 2012, the estimated cost to complete our bonded projects was approximately \$75,430. We evaluate our bonding requirements on a regular basis, including the terms offered by our sureties. On May 7, 2010 we entered into a new surety agreement. We believe the bonding capacity presently provided by our current sureties is adequate for our current operations and will be adequate for our operations for the foreseeable future. As of March 31, 2012, we had outstanding \$3,959 to collateralize our obligations to certain of our previous sureties (as is included in Other Non-Current Assets in our Consolidated Balance Sheet). Posting letters of credit in favor of our sureties reduces the borrowing availability under our Revolving Credit Facility.

*Other Commitments and Contingencies*

Some of our customers and vendors require us to post letters of credit as a means of guaranteeing performance under our contracts and ensuring payment by us to subcontractors and vendors. If our customer has reasonable cause to effect payment under a letter of credit, we would be required to reimburse our creditor for the letter of credit. At March 31, 2012, \$630 of our outstanding letters of credit was to collateralize our vendors.

On January 9, 2012, we entered into a settlement agreement with regard to \$2,000 of collateral held by a surety who previously issued construction payment and performance bonds for us. The agreement called for a total settlement of \$2,200 to be paid in monthly installments through February 2013. In the event of default, we are entitled to file and execute upon an agreed judgment in our favor in the amount of \$2,450. To date, we have received payments of \$175; however, the payment due on April 30, 2012 has not been received as of the filing of this Form 10-Q. We are currently negotiating revised payment terms with the surety and have not filed the agreed judgment. Collection of this debt is

## Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

deemed probable, but there is a risk of loss ranging from \$0 to \$1,825, the recorded value as of the filing of this Form 10-Q. Conversely, there is potential for additional other income of \$450 under the terms of the agreed judgment offset by associated legal fees. To date, we have made no adjustment to the outstanding receivable balance, which was \$1,975 as of March 31, 2012, and, in any event, intend to aggressively pursue full payment. In the event we are unsuccessful in



**Table of Contents**

**INTEGRATED ELECTRICAL SERVICES, INC.**

**Notes to Consolidated Financial Statements**

**(All Amounts in Thousands Except Share Amounts)**

negotiating revised payment terms acceptable to us or the surety otherwise fails to make payment to us, we intend to file the agreed judgment in the amount of \$2,450, less payments made to the date of such filing. The amount of the agreed judgment is subject to interest at the rate of 5.0% per annum.

Between October 2004 and September 2005, we sold all or substantially all of the assets of certain of our wholly-owned subsidiaries. As these sales were assets sales, rather than stock sales, we may be required to fulfill obligations that were assigned or sold to others, if the purchaser is unwilling or unable to perform the transferred liabilities. If this were to occur, we would seek reimbursement from the purchasers. These potential liabilities will continue to diminish over time. To date, we have not been required to perform on any projects sold under this divestiture program.

From time to time, we may enter into firm purchase commitments for materials such as copper or aluminum wire which we expect to use in the ordinary course of business. These commitments are typically for terms less than one year and require us to buy minimum quantities of materials at specific intervals at a fixed price over the term. As of March 31, 2012, we had no such open purchase commitments.

**12. RESTATEMENT**

*Restatement*

The September 30, 2011 consolidated financial statements included in our Original Form 10-K filed on December 20, 2011 contained errors primarily related to the understatement of our vacation accrual that should have been recorded at September 30, 2008 and in each subsequent annual and interim period to September 30, 2011. Additionally, for all restated periods we recorded other immaterial adjustments. These adjustments included, but were not limited to, recording billing, payroll and other accruals, and the associated revenue impacts, in the proper accounting period. Accordingly, the September 30, 2011 consolidated financial statements, and all quarterly periods therein, were restated to properly record these transactions and other immaterial adjustments. Refer to our amended form 10-K/A for a more detailed explanation. In addition, we have restated the Statement of Cash Flows and segment information for the three months and six months ended March 31, 2011 to correct for these errors in these financial statements.

## **Table of Contents**

### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our audited consolidated financial statements, the related notes, and management's discussion and analysis included in our annual report on Form 10-K/A for the year ended September 30, 2011. This discussion contains forward-looking statements and involves numerous risks and uncertainties, including, but not limited to the risk factors discussed in the Risk Factors section of our annual report on Form 10-K/A for the year ended September 30, 2011, and in the Disclosures Regarding Forward-Looking Statements, and elsewhere in this quarterly report on form 10-Q. Actual results may differ materially from those contained in any forward-looking statements.

All dollar values reported in this section are reported in thousands of dollars unless otherwise specified.

#### **Critical Accounting Policies**

Our discussion and analysis of our financial condition and results of operations are based on our condensed consolidated financial statements, which have been prepared in accordance with GAAP. Preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses.

We have identified the accounting principles that we believe are most critical to our reported financial status by considering accounting policies that involve the most complex or subjective decisions or assessments. These accounting policies are those related to revenue recognition, the assessment of goodwill impairment, our allowance for doubtful accounts receivable, the recording of our self-insurance liabilities and our estimation of the valuation allowance for deferred tax assets. These accounting policies, as well as others, are described in Part 2. Item 8. Financial Statements and Supplementary Data Note 2, Summary of Significant Accounting Policies in our annual report on Form 10-K/A for the year ended September 30, 2011.

#### **SALE OF FACILITIES**

##### *Sale of Non-Strategic Manufacturing Facility*

On November 30, 2010, a subsidiary of the Company sold substantially all the assets and certain liabilities of a non-strategic manufacturing facility engaged in manufacturing and selling fabricated metal buildings housing electrical equipment, such as switchgears, motor starters and control systems, to Siemens Energy, Inc. As part of this transaction, Siemens Energy, Inc. also acquired certain real property where the fabrication facilities are located from another subsidiary of the Company. The purchase price of \$10,086 was adjusted to reflect working capital variances. The transaction was completed on December 10, 2010 at which time we recognized a gain of \$6,763.

##### *Sale of Non-Core Electrical Distribution Facility*

On February 28, 2011, Key Electrical Supply, Inc., a wholly owned subsidiary of the Company, sold substantially all the assets and certain liabilities of a non-core electrical distribution facility engaged in distributing wiring, lighting, electrical distribution, power control and generators for residential and commercial applications to Elliot Electric Supply, Inc. The purchase price of \$6,676 was adjusted to reflect working capital variances. The loss on this transaction was immaterial.

##### *Seasonality and Quarterly Fluctuations*

Results of operations from our Residential construction segment are subject to seasonal fluctuations, depending on weather trends, with typically higher revenues generated during spring and summer and lower revenues generated during fall and winter. The Communications and Commercial & Industrial segments of our business are less subject to seasonal trends, as work in these segments generally is performed inside structures protected from the weather. Our service and maintenance business is generally not affected by seasonality. In addition, the construction industry has historically been highly cyclical. Our volume of business may be adversely affected by declines in construction projects resulting from adverse regional or national economic conditions. Quarterly results may also be materially affected by the timing of new construction projects. Accordingly, operating results for any fiscal period are not necessarily indicative of results that may be achieved for any subsequent fiscal period.

**Table of Contents***The 2011 Restructuring Plan*

In the second quarter of our 2011 fiscal year, we began a new restructuring program (the 2011 Restructuring Plan ) that was designed to consolidate operations within our Commercial & Industrial business. Pursuant to the 2011 Restructuring Plan we will either sell or close certain underperforming facilities within our Commercial & Industrial operations. The 2011 Restructuring Plan is a key element of our commitment to return the Company to profitability.

The facilities directly affected by the 2011 Restructuring Plan are in several locations throughout the country, including Arizona, Florida, Iowa, Massachusetts, Louisiana, Nevada and Texas. These facilities were selected due to current business prospects and the extended time frame needed to return the facilities to a profitable position. We expect that closure costs could range from \$4,500 to \$5,500 in the aggregate. Closure costs associated with the 2011 Restructuring Plan include equipment and facility lease termination expenses, incremental management consulting expenses and severance costs for employees. As part of our restructuring charges for the six months ended March 31, 2012 within our Commercial & Industrial segment we recognized \$35 in severance costs, \$764 in consulting services, and \$65 in costs related to lease terminations. The Company is in the process of winding down these facilities. As the Company concludes the wind-down and closure process for each of these facilities, their respective results of operations will be reclassified and presented within future statements of operations as Discontinued Operations. US GAAP does not permit an earlier reclassification.

At March 31, 2012, the estimated costs to complete the 14 projects remaining at these facilities totaled approximately \$3,372; of which all but approximately \$392 has been subcontracted to other electrical contractors. Historically, the wind-down operations negatively impacted liquidity due to their underperformance. For fiscal year ended September 30, 2010, the last reporting period prior to the impact of winding-down, these facilities experienced revenue of \$62,968, selling general & administrative expenses of \$9,590, and an operating loss of \$9,536. For fiscal year ended September 30, 2011 these wind down facilities experienced revenue of \$43,736, selling general and administrative expenses of \$5,019 and an operating loss of \$18,084. Included within the 2011 selling general and administrative expenses is a \$2,850 settlement of an outstanding receivable, written off in a prior period. Excluding this settlement during the quarter ended March 31, 2011, operating loss for these wind-down facilities was \$20,934. In many cases, the losses increased as these facilities experienced cost associated with the wind-down. These costs include, subcontracting previously self-performed work, difficulties in retaining experienced staff, charges associated with facility lease termination, employee severance and retention agreements and professional fees.

To date, we have completed approximately 90% of the backlog of these facilities that existed at the adoption of the restructuring plan. As a result, revenues and selling general & administrative expenses have been substantially reduced. For the six months ended March 31, 2012, these wind-down facilities experienced revenues of \$6,217, selling general & administrative expenses of \$502 and an operating loss of \$3,196. The operating loss for the six months ended March 31, 2012 is being negatively impacted by the operational difficulties associated with the wind-down as detailed above. Additionally, to date we have recognized the majority of the expected severance, retention and lease termination charges.

The completion of the wind-down of these facilities will eliminate the revenues, as well as the associated operating losses and negative liquidity impact. The majority of costs associated with these facilities are directly related to their distinct operations. As such, the majority of the costs will be eliminated upon the completion of the wind-down process. The go-forward operations will benefit from the elimination of negative financial impact of these underperforming operations.

The following table presents the results of operations for the 2011 Restructuring Plan for the three months ended March 31, 2012:

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011 (Restated)
Revenues	\$ 3,095	\$ 11,991
Gross profit (loss)	(570)	(1,395)
Selling, general, & administrative expenses	341	(1,421)
Restructuring	236	
Loss / (gain) from sale of assets	(62)	(1)
Income (loss) from operations	\$ (1,085)	\$ 27

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Other data:			
Working capital	\$	3,752	\$ 19,141
Total assets:	\$	6,529	\$ 24,374

**Table of Contents****THREE MONTHS ENDED MARCH 31, 2012 COMPARED TO THREE MONTHS ENDED MARCH 31, 2011****Results of Operations**

We report our operating results across three operating segments: Communications, Residential and Commercial & Industrial. Expenses associated with our Corporate office are classified as a fourth segment. The following table presents selected historical results of operations of IES and subsidiaries.

	Three Months Ended March 31, 2012		Three Months Ended March 31, 2011 Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Revenues	\$ 112,807	100.0%	\$ 118,326	100.0%
Cost of services	100,221	88.8%	112,999	95.5%
Gross profit	12,586	11.2%	5,327	4.5%
Selling, general and administrative expenses	15,222	13.5%	14,072	11.9%
Gain on sale of assets	(87)	(0.1)%	(87)	(0.1)%
Restructuring charges	264	0.2%		%
Loss from operations	(2,813)	(2.4)%	(8,658)	(7.3)%
Interest and other expense, net	536	0.5%	544	0.5%
Loss from operations before income taxes	(3,349)	(2.9)%	(9,202)	(7.8)%
Provision (benefit) for income taxes	82	0.1%	929	0.8%
Net loss	\$ (3,431)	(3.0)%	\$ (10,131)	(8.6)%

**Revenues**

	Three Months Ended March 31, 2012		Three Months Ended March 31, 2011 Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Communications	\$ 29,024	25.7%	\$ 23,368	19.7%
Residential	29,628	26.3%	26,310	22.2%
Commercial & Industrial	54,155	48.0%	68,648	58.1%
Total Consolidated	\$ 112,807	100.0%	\$ 118,326	100.0%

Consolidated revenues for the three months ended March 31, 2012 were \$5,519 less than the three months ended March 31, 2011, a decrease of 4.7%.

Our Communications segment revenues increased \$5,656 during the three months ended March 31, 2012, a 24.2% increase compared to the three months ended March 31, 2011. We recognized revenues of \$5,305 that can be attributed to the commencement of work on a significant project from a long term customer during the first quarter 2012. The markets we serve have expanded rapidly as the current and expected demand for information and data storage has increased. We have a long history of serving our customers in such mission critical environments, resulting in our increased revenue as these markets continue to expand.

## Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

Our Residential segment revenues increased \$3,318 during the three months ended March 31, 2012, an increase of 12.6% as compared to the three months ended March 31, 2011. Approximately \$3,324 of the revenues during the three months ended March 31, 2011 were attributable to the non-core electrical distribution facility that was sold in February 2011. Excluding

**Table of Contents**

the revenues from the divested facility, our Residential segment showed an increase, quarter over quarter, of \$6,642. The increase is due primarily to an increase in our single-family revenues of approximately \$3,300. While the strongest growth was seen in our Texas markets, which represents approximately 75% of our single-family sales, we experienced similar growth as a percentage increase in our other markets as well. Additionally, our Residential segment entered into the solar installation market in late 2011, concentrated primarily in California. Solar installation revenue was approximately \$2,400. Multi-family revenues increased approximately \$1,100, attributable to an influx of private financing options over HUD/FHA backed financing, and increased apartment occupancy rates creating a demand for the construction of apartment units.

Our Commercial & Industrial segment revenues decreased \$14,493 during the three months ended March 31, 2012, a decrease of 21.1% compared to the three months ended March 31, 2011 primarily due to a decrease in revenues associated with the Company's wind-down facilities described in the 2011 Restructuring Plan. Revenues associated with the wind-down facilities described in the 2011 Restructuring Plan totaled \$3,135, a decrease of \$8,856 when compared to the three months ended March 31, 2011. Excluding the revenues associated with the wind-down facilities, revenues decreased \$5,897. We experienced a decline in revenues in our Oregon and Nebraska facilities of approximately \$2,000 and \$1,800, respectively, due to the completion of large projects in both locations. Additionally, we are in the process of winding down our Baltimore facility and, as such, have experienced a reduction in revenues of approximately \$1,400.

**Gross Profit**

	Three Months Ended March 31,		2011	
	2012		Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Communications	\$ 3,780	13.0%	\$ 2,424	10.4%
Residential	4,531	15.3%	3,596	13.8%
Commercial & Industrial	4,273	7.9%	(612)	-1.0%
Corporate	2	0.0%	(81)	-0.1%
<b>Total Consolidated</b>	<b>\$ 12,586</b>	<b>11.2%</b>	<b>\$ 5,326</b>	<b>4.5%</b>

Our consolidated gross profit percentage increased to 11.2% during the three months ended March 31, 2012, as compared to 4.5% during the three months ended March 31, 2011.

Our Communications segment gross profit increased \$1,356 during the three months ended March 31, 2012 as compared to the three months ended March 31, 2011. The increase in gross profit was driven by increased revenues coupled with an increase in gross margin. Gross profit was negatively impacted by the Baltimore office, which had a negative gross profit of \$276 and \$246 during the three months ended March 31, 2012, and March 31, 2011, respectively. The Baltimore location was selected for closure based upon current business performance and the extended time frame needed to return the operation to profitability.

Our Residential segment gross profit increased \$935 during the three months ended March 31, 2012, as compared to the three months ended March 31, 2011. Gross margin in the Residential segment increased to 15.3% during the three months ended March 31, 2012. Single family operations comprised the largest increase in gross profit at \$1,100, attributed to the stability in the price of copper wire as well as an overall increase in revenue volume. Additionally, an increase of approximately \$200 of the gross profit increase can be attributed to our entrance into the solar installation market. The remaining increase in gross profit results from decreased insurance claim development costs, offset by reduced margins in the multi-family operations due to increased competition and job specific difficulties encountered in the three months ended March 31, 2012.

Our Commercial & Industrial segment gross profit increased \$4,885 during the three months ended March 31, 2012, as compared to the three months ended March 31, 2011. The negative gross margins associated with the wind-down operations described in the Company's 2011 Restructuring Plan resulted in \$537 of negative gross profit during the three months ended March 31, 2012, compared to a negative gross profit of \$1,395 during the three months ended March 31, 2011. The negative gross margins recorded for the wind-down operations described in the Company's 2011 Restructuring Plan are





**Table of Contents**

primarily due to higher costs associated with either subcontracting or assigning certain contracts to other electrical subcontractors together with the extensive operating difficulties relating to labor productivity following the notice of the potential sale or closure of these facilities. The Baltimore facility, within Commercial & Industrial segment, had a negative gross profit of \$235 during the three months ended March 31, 2012, an increase of \$12, as compared to the three months ended March 31, 2011. The Baltimore location was selected for closure based upon current business performance and the extended time frame needed to return the operation to profitability. Excluding the gross profit associated with the wind-down facilities, gross profit increased \$4,060. During the three months ended March 31, 2011, we experienced losses on contracts in our Colorado and Nebraska facilities, totaling approximately \$2,600. Additionally, we benefited from improved performance in Oregon and Virginia facilities during the three months ended March 31, 2012, that totaled approximately \$1,400.

**Selling, General and Administrative Expenses**

	Three Months Ended March 31,		2011	
	2012		Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Communications	\$ 3,337	11.5%	\$ 2,309	9.9%
Residential	4,533	15.3%	4,508	17.1%
Commercial & Industrial	5,150	9.5%	3,837	5.6%
Corporate	2,202		3,418	
<b>Total Consolidated</b>	<b>\$ 15,222</b>	<b>13.5%</b>	<b>\$ 14,072</b>	<b>11.9%</b>

Selling, general and administrative expenses include costs not directly associated with performing work for our customers. These costs consist primarily of compensation and benefits related to corporate and division management, occupancy and utilities, training, professional services, information technology costs, consulting fees, travel and certain types of depreciation and amortization. We allocate certain corporate selling, general and administrative costs across our segments as we believe this more accurately reflects the costs associated with operating each segment.

During the three months ended March 31, 2012, our selling, general and administrative expenses were \$15,222, an increase of \$1,150, or 8.2%, as compared to the three months ended March 31, 2011. Included in the three months ended March 31, 2011 is a recovery of \$2,850 settlement of an outstanding receivable, written off in a prior period. Excluding this, the selling, general and administrative expenses decreased \$1,700, and as a percent of revenue to 13.5% in 2012 from 14.3% in 2011.

Our Communications segment experienced an increase of \$1,028 in selling, general and administrative expenses during the three months ended March 31, 2012 compared to the three months ended March 31, 2011. Selling, general and administrative expenses as a percentage of revenues in the Communications segment increased to 11.5% of segment revenue during the three months ended March 31, 2012. The increase in selling, general and administrative expenses is primarily due to higher expenses associated with our expansion of facilities in Southern California. Additionally, bad debt expenses increased due primarily to the wind-down operations of our Baltimore facility.

Our Residential segment experienced an increase of \$25 in selling, general and administrative expenses during the three months ended March 31, 2012 compared to the three months ended March 31, 2011. Approximately \$899 of the selling, general and administrative expenses included in the three months ended March 31, 2011 is attributable to the non-core electrical distribution facility that was sold in February 2011. Removing this from the comparison, the actual change, period over period, was an increase of \$924. Selling, general and administrative expenses as a percentage of revenues in the Residential segment declined to 15.3% of segment revenue during the three months ended March 31, 2012. The increase in selling, general and administrative expenses is attributable to approximately \$400 in employee incentives and approximately \$200 in expenses to enter the solar installation market.

Our Commercial & Industrial segment experienced an increase of \$1,313 in selling, general and administrative expenses during the three months ended March 31, 2012 compared to the three months ended March 31, 2011. Selling, general and administrative expenses as a percentage of revenues in the Commercial & Industrial segment increased to 9.5% of segment revenue during the three months ended March 31, 2012. The selling, general and administrative expenses associated with the



**Table of Contents**

wind-down operations described in the Company's 2011 Restructuring Plan were \$316 during the three months ended March 31, 2012, compared to \$1,429, during the three months ended March 31, 2011, net of a \$2,850 settlement of an outstanding receivable, written off in a prior period. The selling, general and administrative expenses recorded for the wind-down operations described in the Company's 2011 Restructuring Plan are primarily due to professional fees and lease termination expenses. The Baltimore facility within the Commercial & Industrial segment had selling, general and administrative expenses of \$291 during the three months ended March 31, 2012, a decrease of \$177, as compared to the three months ended March 31, 2011. The Baltimore location was selected for closure based upon current business performance and the extended time frame needed to return the operation to profitability. Excluding the selling general and administrative expenses associated with the wind-down facilities, selling general and administrative expenses decreased \$1,360, primarily due to the consolidation of redundant support functions within the Louisiana and Virginia facilities.

Our Corporate segment experienced a decrease of \$1,216 in selling, general and administrative expenses during the three months ended March 31, 2012 compared to the three months ended March 31, 2011. This decrease is primarily attributable to a significant reduction in our corporate office operations, including a decrease in headcount and related employment expenses, decreased professional fees and depreciation.

**Restructuring Charges**

The following table presents the elements of costs incurred for the 2011 Restructuring Plan.

	Three Months Ended March 31,	
	2012	2011
	(In thousands)	
Severance compensation	\$ (34)	\$
Consulting and other charges	281	
Lease termination costs	17	
Total restructuring charges	\$ 264	\$

**Interest and Other Expense, net**

	Three Months Ended March 31,	
	2012	2011
	(In thousands)	
Interest expense	\$ 459	\$ 491
Deferred financing charges	84	84
Total interest expense	543	575
Interest income	(8)	(24)
Other (income) expense, net	1	(7)
Total interest and other expense, net	\$ 536	\$ 544

During the three months ended March 31, 2012, we incurred interest expense of \$459 primarily comprised of the Tontine Term Loan and the Insurance Financing Agreements (as defined in Working Capital), an average letter of credit balance of \$8,812 under the Revolving Credit Facility (as defined in Working Capital) and an average unused line of credit balance of \$31,188. This compares to interest expense of \$491 for the three months ended March 31, 2011, on a debt balance primarily comprised of the Tontine Term Loan, an average letter of credit balance of \$13,087 under the Revolving Credit Facility and an average unused line of credit balance of \$46,913.

For the three months ended March 31, 2012 and 2011, we earned interest income of \$8 and \$24, respectively, on the average Cash and Cash Equivalents balances of \$17,500 and \$32,846, respectively.

**Provision for Income Taxes**

On May 12, 2006, we had a change in ownership as defined in Internal Revenue Code Section 382. As such, our net operating loss utilization after the change date will be subject to Section 382 limitation for federal income taxes and some state income taxes. We have provided valuation allowance on all net operating losses where it is determined it is more likely than not that the net operating loss will expire without being utilized.

**Table of Contents**

The provision for income taxes decreased from \$929 for the three months ended March 31, 2011 to \$82 for the three months ended March 31, 2012. The decrease in expense for the three months ended March 31, 2012 is attributable to a decrease in loss from operations before income taxes.

**SIX MONTHS ENDED MARCH 31, 2012, COMPARED TO SIX MONTHS ENDED MARCH 31, 2011****Results of Operations**

We report our operating results across three operating segments: Communications, Residential and Commercial & Industrial. Expenses associated with our Corporate office are classified as a fourth segment. The following table presents selected historical results of operations of IES and subsidiaries.

	Six Months Ended March 31,		2011	
	2012		Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Revenues	\$ 228,101	100.0%	\$ 228,137	100.0%
Cost of services	204,606	89.7%	211,752	92.8%
Gross profit	23,495	10.3%	16,385	7.2%
Selling, general and administrative expenses	28,596	12.5%	32,724	14.3%
Gain on sale of assets	(70)	%	(6,816)	(3.0)%
Asset impairment		%	3,551	1.6%
Restructuring charges	864	0.4%		%
Loss from operations	(5,895)	(2.6)%	(13,074)	(5.7)%
Interest and other expense, net	1,009	0.4%	1,103	0.5%
Loss from operations before income taxes	(6,904)	(3.0)%	(14,177)	(6.2)%
Provision (benefit) for income taxes	250	0.1%	253	0.1%
Net loss	\$ (7,154)	(3.1)%	\$ (14,430)	(6.3)%

	Six months ended March 31,		2011	
	2012		Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Communications	\$ 55,126	24.2%	\$ 43,290	19.0%
Residential	58,900	25.8%	52,354	22.9%
Commercial & Industrial	114,075	50.0%	132,493	58.1%
Total Consolidated	\$ 228,101	100.0%	\$ 228,137	100.0%

Consolidated revenues for the six months ended March 31, 2012 were \$36 less than the six months ended March 31, 2011, an decrease of 0.0%.

Our Communications segment revenues increased \$11,836 during the six months ended March 31, 2012, a 27.3% increase compared to the six months ended March 31, 2011. We recognized revenues of \$5,443 that can be attributed to commencing work on a significant project during the first quarter 2012. This is indicative of the expanding market for network infrastructure. The markets we serve have expanded rapidly as the current and expected demand for information and data storage has increased. We have a long history of serving our customers in such mission

critical environments, resulting in our increased revenue as these markets continue to expand.

**Table of Contents**

Our Residential segment revenues increased \$6,546 during the six months ended March 31, 2012, an increase of 12.5% as compared to the six months ended March 31, 2011. Approximately \$8,271 of the revenue during the six months ended March 31, 2011 is attributable to the non-core electrical distribution facility that was sold in February 2011. Removing this revenue from the comparison, our Residential segment showed an increase period over period of \$14,817. The increase is due primarily to an increase in our single-family revenues of approximately \$7,000. While the strongest growth was seen in our Texas markets, which represents approximately 75% of our single-family sales, we experienced similar growth as a percentage increase in our other markets as well. Additionally, our Residential segment entered into the solar installation market in late 2011, concentrated primarily in California. Solar installation revenue was approximately \$3,800. Multi-family revenues increased approximately \$4,600, attributable to an influx of private financing options over HUD/FHA backed financing, and increased apartment occupancy rates, creating a demand for the construction of apartment units.

Revenues in our Commercial & Industrial segment decreased \$18,418 during the six months ended March 31, 2012, a decrease of 13.9% as compared to the six months ended March 31, 2011, primarily due to a decrease in revenues associated with the Company's wind-down facilities described in the 2011 Restructuring Plan. Revenues associated with the wind-down facilities described in the 2011 Restructuring Plan totaled \$6,218, a decrease of \$19,393 when compared to the six months ended March 31, 2011. Excluding the revenues associated with the wind-down facilities, revenues increased \$1,015. We are in the process of winding down our Baltimore facility, and as such have experienced a reduction in revenues of approximately \$1,159. Revenues from the remaining Commercial & Industrial locations remained relatively flat.

**Gross Profit**

	Six Months Ended March 31,		2011	
	2012		Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Communications	\$ 7,119	12.9%	\$ 5,630	13.0%
Residential	9,179	15.6%	8,132	15.5%
Commercial & Industrial	7,205	6.3%	2,704	2.0%
Corporate	(8)	0.0%	(81)	-0.1%
Total Consolidated	\$ 23,495	10.3%	\$ 16,385	7.2%

Our consolidated gross profit percentage increased to 10.3% during the six months ended March 31, 2012, as compared to 7.2% during the six months ended March 31, 2012.

Our Communications segment gross profit increased \$1,489 during the six months ended March 31, 2012, as compared to the six months ended March 31, 2011. The increase in gross profit is attributed to more efficient execution on projects, an increase in higher margin service work and a reduction in overhead costs from the consolidation of administrative functions to one location.

Our Residential segment gross profit increased \$1,047 during the six months ended March 31, 2012, as compared to the six months ended March 31, 2011. Gross margin percentage in the Residential segment increased to 15.6% during the six months ended March 31, 2012. Single family operations comprised the largest increase in gross profit at \$2,300, attributed to the stability in the price of copper wire as well as an overall increase in revenue volume. The increase in gross profit from single family operations was offset by a negative gross margin of approximately \$50 attributed to our entrance into the solar installation market. The remaining increase in gross profit resulted from decreased insurance claim development costs, offset by reduced margins in the multi-family operations due to increased competition and job specific difficulties encountered in the six months ended March 31, 2012.

Our Commercial & Industrial segment gross profit increased \$4,504 during the six months ended March 31, 2012, as compared to the six months ended March 31, 2011. The negative gross margins associated with the wind-down operations described in the Company's 2011 Restructuring Plan resulted in \$1,928 of negative gross profit during the six months ended

**Table of Contents**

March 31, 2012 compared to a negative gross profit of \$1,311 during the six months ended March 31, 2011. The negative gross margins recorded for the wind-down operations described in the Company's 2011 Restructuring Plan are primarily due to higher costs associated with either subcontracting or assigning certain contracts to other electrical subcontractors together with the extensive operating difficulties relating to labor productivity following the notice of the potential sale or closure of these facilities. The Baltimore facility within Commercial & Industrial had a negative gross profit of \$919 during the six months ended March 31, 2012, an increase in negative gross profit of \$894, as compared to the six months ended March 31, 2011. The Baltimore location was selected for closure based upon current business performance and the extended time frame needed to return the operation to profitability. Excluding the gross profit associated with the wind-down facilities, gross profit increased \$5,150. During the six months ended March 31, 2011, we experienced losses on contracts in Colorado and Nebraska facilities totaling approximately \$4,100. These losses were not repeated during the six months ended March 31, 2012.

**Selling, General & Administrative Expenses**

	Six Months Ended March 31,		2011	
	2012		Restated	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Communications	\$ 6,334	11.5%	\$ 4,617	10.7%
Residential	8,946	15.2%	12,564	24.0%
Commercial & Industrial	9,654	8.5%	8,006	6.0%
Corporate	3,662		7,537	
<b>Total Consolidated</b>	<b>\$ 28,596</b>	<b>12.5%</b>	<b>\$ 32,724</b>	<b>14.3%</b>

Selling, general and administrative expenses include costs not directly associated with performing work for our customers. These costs consist primarily of compensation and benefits related to corporate and division management, occupancy and utilities, training, professional services, information technology costs, consulting fees, travel and certain types of depreciation and amortization.

During the six months ended March 31, 2012, our selling, general and administrative expenses were \$28,596, a decrease of \$4,128, or 12.6%, as compared to the six months ended March 31, 2011. Included in the six months ended March 31, 2011 is a recovery of \$2,850 settlement of an outstanding receivable, written off in a prior period in our Commercial & Industrial segment. Excluding this, the selling, general and administrative expenses decreased \$6,978.

Our Communications segment experienced an increase of \$1,171 in selling, general and administrative expenses during the six months ended March 31, 2012 compared to the six months ended March 31, 2011. Selling, general and administrative expenses as a percentage of revenues in the Communications segment increased to 11.5% of segment revenue during the six months ended March 31, 2012. The increase in selling, general and administrative expenses is primarily due to higher expenses associated with our expansion of facilities in Southern California, including litigation expenses. Additionally, bad debt expenses increased due primarily to the wind down operations of our Baltimore facility.

Our Residential segment experienced a decrease of \$3,618 in selling, general and administrative expenses during the six months ended March 31, 2012 compared to the six months ended March 31, 2011. Selling, general and administrative expenses as a percentage of revenues in the Residential segment declined to 15.2% of segment revenue during the six months ended March 31, 2012. Approximately \$1,993 of the selling, general and administrative expenses included in the six months ended March 31, 2011 is attributable to the non-core electrical distribution facility that was sold in February 2011. Removing this from the comparison, the actual change period over period was an increase of \$1,625. The increase in selling, general and administrative expenses is attributable to approximately \$900 in employee incentives, additional compensation expense of \$200, and approximately \$300 in expenses to enter the solar installation market.

Our Commercial & Industrial segment experienced an increase of \$1,648 in selling, general and administrative expenses during the six months ended March 31, 2012 compared to the six months ended March 31, 2011. Selling, general and administrative expenses as a percentage of revenues in the Commercial & Industrial segment increased to 8.5% of segment



**Table of Contents**

revenue during the six months ended March 31, 2011. The selling, general and administrative expenses associated with the wind-down operations described in the Company's 2011 Restructuring Plan were \$502 during the six months ended March 31, 2012, compared to \$3,059, during the six months ended March 31, 2011, net of a \$2,850 settlement of an outstanding receivable, written off in a prior period. The selling, general and administrative expenses recorded for the wind-down operations described in the Company's 2011 Restructuring Plan are primarily due to professional fees and lease termination expenses. The Baltimore facility within Commercial & Industrial had selling general and administrative expenses of \$570 during the six months ended 2012, a decrease of \$347, as compared to the six months ended March 31, 2011. The Baltimore location was selected for closure based upon current business performance and the extended time frame needed to return the operation to profitability. Excluding the selling general and administrative expenses associated with the wind-down facilities, selling general and administrative expenses increased \$1,355, primarily due to increased incentive compensation.

Our Corporate segment experienced a decrease of \$3,875 in selling, general and administrative expenses during the six months ended March 31, 2012 compared to the six months ended March 31, 2011. This decrease is primarily attributable to a reduction in our corporate office operations, including a decrease in headcount and related employment expenses, and decreased depreciation. Additionally, there were several severance agreements in 2011 totaling \$562 compared to \$428 in 2012.

**Restructuring Charges**

In conjunction with our 2011 Restructuring Plan we recognized the following costs during the six months ended March 31, 2012 and March 31, 2011:

	Six Months Ended March 31,	
	2012	2011
	(In thousands)	
Severance compensation	\$ 35	\$
Consulting and other charges	727	
Lease termination costs	102	
 Total restructuring charges	 \$ 864	 \$

**Interest and Other Expense, net**

	Six Months Ended March 31,	
	2012	2011
	(In thousands)	
Interest expense	\$ 913	\$ 1,006
Deferred financing charges	175	169
 Total interest expense	 1,088	 1,175
 Interest income	 (15)	 (49)
Other (income) expense, net	(65)	(24)
 Total interest and other expense, net	 \$ 1,008	 \$ 1,102

During the six months ended March 31, 2012, we incurred interest expense of \$1,088 on an average debt balance of \$10,000 primarily comprised of the Tontine Term Loan (as defined in Working Capital) and the Insurance Financing Agreements (as defined in Working Capital), an average letter of credit balance of \$8,796 under the Revolving Credit Facility (as defined in Working Capital) and an average unused line of credit balance of \$39,356. This compares to interest expense of \$1,175 for the six months ended March 31, 2011, on an average debt balance of \$10,000 primarily comprised of the Tontine Term Loan and the Insurance Financing Agreements, an average letter of credit balance of \$14,508 under the Revolving Credit Facility and an average unused line of credit balance of \$45,487.

Edgar Filing: INTEGRATED ELECTRICAL SERVICES INC - Form 10-Q

For the six months ended March 31, 2012 and 2011, we earned interest income of \$65 and \$24 respectively, on the average Cash and Cash Equivalents balances of \$19,590 and \$32,384, respectively.

## **Table of Contents**

### **Provision for Income Taxes**

On May 12, 2006, we had a change in ownership as defined in Internal Revenue Code Section 382. As such, our net operating loss utilization after the change date will be subject to Section 382 limitation for federal income taxes and some state income taxes. We have provided valuation allowance on all net operating losses where it is determined it is more likely than not that the net operating loss will expire without being utilized.

The provision for income taxes for the six months ended March 31, 2011 and March 31, 2012 was \$250.

### **Liquidity and Capital Resources**

As of March 31, 2012, we had cash and cash equivalents of \$17,766, working capital of \$56,649 and \$22,009 of available capacity under our Revolving Credit Facility. We anticipate that the combination of cash on hand, cash flows and available capacity under our Revolving Credit Facility will provide sufficient cash to enable us to meet our working capital needs, debt service requirements and capital expenditures for property and equipment through the next twelve months. Our ability to generate cash flow is dependent on many factors, including demand for our services, the availability of projects at margins acceptable to us, the ultimate collectability of our receivables, and our ability to borrow on our amended Revolving Credit Facility, if needed. We were not required to test our covenants under our Revolving Credit Facility in the period as our Total Liquidity was greater than the minimum under our Revolving Credit Facility. Had we been required to test our covenants, we would have failed at March 31, 2012.

We continue to closely monitor the financial markets and general national and global economic conditions. To date, we have experienced no loss or lack of access to our invested cash or cash equivalents; however, we can provide no assurances that access to our invested cash and cash equivalents will not be impacted in the future by adverse conditions in the financial markets.

#### *Operating Activities*

Our cash flow from operations is not only influenced by cyclical demand for our services, operating margins and the type of services we provide, but can also be influenced by working capital needs such as the timing of our receivable collections. Working capital needs are generally lower during our fiscal first and second quarters due to the seasonality that we experience in many regions of the country.

Operating activities used net cash of \$7,799 during the six months ended March 31, 2012, as compared to \$11,444 of net cash used in the six months ended March 31, 2011. The decrease in the use of cash from operating activities in the six months ended March 31, 2012 is due primarily to a decrease in the net loss of \$7,276, a decrease in working capital usage of \$2,691 and a decrease of depreciation expense of \$2,360, offset by the \$2,850 recovery and \$6,811 gain on sale of assets in 2011.

#### *Investing Activities*

In the six months ended March 31, 2012, net cash used from investing activities was \$978 as compared to \$15,682 of net cash provided by investing activities in the six months ended March 31, 2011. Investing activities in the six months ended March 31, 2012 included \$998 used for capital expenditures, and an \$8,812 increase to restricted cash required by our credit facility. Investing activities in the six months ended March 31, 2011 included \$16,287 from the sale of facilities, partially offset by \$755 used for capital expenditures.

#### *Financing Activities*

Financing activities used net cash of \$9,034 in the six months ended March 31, 2012 compared to usage of \$455 used in the six months ended March 31, 2011. Financing activities included \$128 and \$390 used for repayments of debt in the six months ended March 31, 2012 and March 31, 2011, respectively.

#### *Surety*

Many customers, particularly in connection with new construction, require us to post performance and payment bonds issued by a surety. These bonds provide a guarantee to the customer that we will perform under the terms of our contract and that we will pay our subcontractors and vendors. If we fail to perform under the terms of our contract or to pay subcontractors and vendors, the customer may demand that the surety make payments or provide services under the bond. We must reimburse the sureties for any expenses or outlays they incur on our behalf. To date, we have not been required to make any reimbursements to our sureties for bond-related costs.



**Table of Contents**

As is common in the surety industry, sureties issue bonds on a project-by-project basis and can decline to issue bonds at any time. We believe that our relationships with our sureties will allow us to provide surety bonds as they are required. However, current market conditions, as well as changes in our sureties' assessment of our operating and financial risk, could cause our sureties to decline to issue bonds for our work. If our sureties decline to issue bonds for our work, our alternatives would include posting other forms of collateral for project performance, such as letters of credit or cash, seeking bonding capacity from other sureties, or engaging in more projects that do not require surety bonds. In addition, if we are awarded a project for which a surety bond is required but we are unable to obtain a surety bond, the result could be a claim for damages by the customer for the costs of replacing us with another contractor.

As of March 31, 2012, the estimated cost to complete our bonded projects was approximately \$75,430. We believe the bonding capacity presently provided by our sureties is adequate for our current operations and will be adequate for our operations for the foreseeable future. As of March 31, 2012, we utilized \$3,986 of cash (as is included in Other Non-Current Assets in our Consolidated Balance Sheet) as collateral for certain of our previous bonding programs.

*Bonding Capacity*

At March 31, 2012, we had adequate surety bonding capacity under our surety agreements. Our ability to access this bonding capacity is at the sole discretion of our sureties. As of March 31, 2012, the expected cumulative cost to complete for projects covered by our sureties was \$75,430. We believe we have adequate remaining available bonding capacity to meet our current needs, subject to the sole discretion of our sureties. For additional information, please refer to Note 11 *Commitments and Contingencies - Surety* of this form 10-Q.

*The Revolving Credit Facility*

On May 12, 2006, we entered into a Loan and Security Agreement (the *Loan and Security Agreement*), for a revolving credit facility (the *Revolving Credit Facility*) with Bank of America, N.A. and certain other lenders. On May 7, 2008, we renegotiated the terms of our Revolving Credit Facility and entered into an amended agreement with the same financial institutions. On April 30, 2010, we renegotiated the terms of, and entered into an amendment to, the Loan and Security Agreement, pursuant to which the maturity date was extended to May 12, 2012. In connection with the amendment, we incurred an amendment fee of \$0.2 million.

On December 15, 2011, we renegotiated the terms of, and entered into an amendment to, the Loan and Security Agreement without incurring termination charges. Under the terms of the amended Revolving Credit Facility, the size of the facility was reduced to \$40,000 and the maturity date was extended to November 12, 2012. Further, we were required to cash collateralize all of our letters of credit issued by the banks. The cash collateral is added to the borrowing base calculation at 100% throughout the term of the agreement. The Revolving Credit Facility requires that we maintain a fixed charge coverage ratio of not less than 1.0:1.0 at any time that our aggregate amount of unrestricted cash on hand plus availability is less than \$25,000 and, thereafter, until such time as our aggregate amount of unrestricted cash on hand plus availability has been at least \$25,000 for a period of 60 consecutive days. Additionally, if there are any loans outstanding on or after the April 30, 2012, the Company's EBITDA for the period from October 1, 2011 through March 31, 2012, may not exceed a negative EBITDA threshold of \$2,500 and we will be required to have a cumulative fixed charge coverage ratio of at least 1.0:1.0 at all times beginning April 1, 2012 to maintain any borrowings under the agreement. The measurement period for this additional test for borrowings begins with the monthly operating results for April 2012 and adds the monthly operating results for each month thereafter to determine the cumulative test during such time as revolving loans are outstanding. Failure to meet this performance test will result in an immediate event of default. The amended agreement also calls for cost of borrowings of 4.0% over LIBOR per annum. Cost for letters of credit are the same as borrowings and also include a 25 basis point fronting fee. All other terms and conditions remain unchanged. In connection with the amendment, we incurred an amendment fee of \$0.1 million which, together with unamortized balance of the prior amendment is being amortized using the straight line method through November 12, 2012.

On May 11, 2012, we renegotiated the terms of, and entered into an amendment to, the Loan and Security Agreement without incurring termination charges. Under the terms of the amended Revolving Credit Facility, we are subject to covenant that requires we maintain a fixed coverage ratio of not less than 1.0:1.0 at any time that our aggregate amount of unrestricted cash on hand plus availability is less than \$30,000 and, thereafter, until such time as our aggregate amount of unrestricted cash on hand plus availability has been at least \$30,000 for a period of 60 consecutive days. Additionally, if there are any loans outstanding on or after March 31, 2012, April 30, 2012 and May 31, 2012, the Company's EBITDA may not exceed a negative EBITDA threshold established for each month within this period. The negative EBITDA threshold is measured from October 1, 2011 until the months ended March 31, 2012, April 30, 2012 and May 31, 2012. The negative EBITDA threshold for March 31, 2012, April 30, 2012 and May 31, 2012 is \$4,700, \$4,850 and \$4,725, respectively. To extent we

---

## **Table of Contents**

exceed the negative thresholds for March 31, 2012 April 30, 2012 and May 31, 2012 the Company will prohibited form borrowing until such time we do not exceed the negative threshold in a subsequent month. As of June 30, 2012, the Company's negative EBITDA threshold for the period from October 1, 2011 through June 30, 2012, may not exceed \$4,475 and we will be required to have a cumulative fixed charge coverage ratio of at least 1.0:1.0 at all times beginning July 31, 2012 to maintain any borrowings under the agreement. The measurement period for this additional test for borrowings begins with the monthly operating results for July 1, 2012 and adds the monthly operating results for each month thereafter to determine the cumulative test during such time as revolving loans are outstanding. Failure to meet this performance test will result in an immediate event of default. The negative EBITDA threshold excludes any gain or loss related to a surety settlement described in Note 11 *Commitments and Contingencies*.

The Revolving Credit Facility is guaranteed by our subsidiaries and secured by first priority liens on substantially all of our subsidiaries' existing and future acquired assets, exclusive of collateral provided to our surety providers. The Revolving Credit Facility contains customary affirmative, negative and financial covenants. The Revolving Credit Facility also restricts us from paying cash dividends and places limitations on our ability to repurchase our common stock.

Borrowings under the Revolving Credit Facility may not exceed a borrowing base that is determined monthly by our lenders based on available collateral, primarily certain accounts receivables and cash collateral supporting our letters of credit. None of our inventories qualified for borrowing availability after we sold the inventory attributable to our Key Electrical Supply company in February 2011. Under the terms of the Revolving Credit Facility in effect as of March 31, 2012, interest for loans and letter of credit fees is based on our Total Liquidity, which is calculated for any given period as the sum of average daily availability for such period plus average daily unrestricted cash on hand for such period as follows:

At March 31, 2012, we had \$22,009 available to us under the Revolving Credit Facility with no outstanding borrowings. We had \$8,812 in outstanding letters of credit fully collateralized with restricted cash.

As of March 31, 2012, we were subject to the financial covenant under the Revolving Credit Facility requiring that we maintain a fixed charge coverage ratio of not less than 1.0:1.0 at any time that our aggregate amount of unrestricted cash on hand plus availability is less than \$25.0 million and, thereafter, until such time as our aggregate amount of unrestricted cash on hand plus availability has been at least \$25.0 million for a period of 60 consecutive days. As of March 31, 2012, our Total Liquidity was in excess of \$25.0 million; had our Total Liquidity been less than \$25.0 million at March 31, 2012, we would not have met the required 1.0:1.0 fixed charge coverage ratio test.

### ***The Tontine Term Loan***

On December 12, 2007, we entered into a \$25.0 million senior subordinated loan agreement (the "Tontine Term Loan") with Tontine Capital Partners, L.P., a related party. The Tontine Term Loan bears interest at 11.0% per annum and is due on May 15, 2013. Interest is payable quarterly in cash or in-kind at our option. Any interest paid in-kind will bear interest at 11.0% in addition to the loan principal. On April 30, 2010, we prepaid \$15.0 million of principal on the Tontine Term Loan. On May 1, 2010, Tontine assigned the Tontine Term Loan to TCP Overseas Master Fund II, L.P. We may repay the Tontine Term Loan at any time prior to the maturity date at par, plus accrued interest without penalty. The Tontine Term Loan is subordinated to our Revolving Credit Facility. The Tontine Term Loan is an unsecured obligation of the Company and its subsidiary borrowers. The Tontine Term Loan contains no financial covenants or restrictions on dividends or distributions to stockholders.

### **Controlling Shareholder**

On October 3, 2011, the Company entered into an amended and restated letter agreement with James M. Lindstrom, to memorialize Mr. Lindstrom's appointment, effective October 3, 2011, as Chief Executive Officer and President of the Company. Mr. Lindstrom previously served in such capacities on an interim basis since June 2011 and has served as Chairman of the Company's Board of Directors since February 2011. Mr. Lindstrom was an employee of Tontine from 2006 until October 2011. In his capacity as Chief Executive Officer and President, Mr. Lindstrom has the ability to affect the composition of the Company's management and influence the business operations of the Company or extraordinary transactions outside the normal course of the Company's business.

On July 21, 2011, Tontine filed an amended Schedule 13D indicating its ownership level of 57.4% of the Company's outstanding common stock. Although Tontine has not indicated any plans to alter its ownership level, should Tontine reconsider its investment plans and sell its controlling interest in the Company, a change in ownership would occur. A change in ownership, as defined by Internal Revenue Code Section 382, could reduce the availability of net operating losses for federal and state income tax purposes. Furthermore, a change in control would trigger the change of control provisions in a



**Table of Contents**

number of our material agreements, including our Revolving Credit Facility, bonding agreements with our sureties and employment contracts with certain officers and employees of the Company. On April 30, 2010, we prepaid \$15,000 of the original \$25,000 principal outstanding on the Tontine Term Loan; accordingly \$10,000 remains outstanding under the Tontine Term Loan.

**Off-Balance Sheet Arrangements and Contractual Obligations**

As is common in our industry, we have entered into certain off-balance sheet arrangements that expose us to increased risk. Our significant off-balance sheet transactions include commitments associated with non-cancelable operating leases, letter of credit obligations, firm commitments for materials and surety guarantees.

We enter into non-cancelable operating leases for many of our vehicle and equipment needs. These leases allow us to retain our cash because we do not own the vehicles or equipment and we pay a monthly lease rental fee. At the end of the lease, we have no further obligation to the lessor. We may cancel or terminate a lease before the end of its term. Typically, we would be liable to the lessor for various lease cancellation or termination costs and the difference between the fair market value of the leased asset and the implied book value of the leased asset as calculated in accordance with the lease agreement.

Some of our customers and vendors require us to post letters of credit as a means of guaranteeing performance under our contracts and ensuring payment by us to subcontractors and vendors. If our customer has reasonable cause to effect payment under a letter of credit, we would be required to reimburse our creditor for the letter of credit. At March 31, 2012, \$630 of our outstanding letters of credit were utilized to collateralize our customers and vendors.

Some of the underwriters of our casualty insurance program require us to post letters of credit as collateral, as is common in the insurance industry. To date, we have not had a situation where an underwriter has had reasonable cause to effect payment under a letter of credit. At March 31, 2012, \$8,182 of our outstanding letters of credit were utilized to collateralize our insurance programs.

From time to time, we may enter into firm purchase commitments for materials such as copper wire and aluminum wire, among others, which we expect to use in the ordinary course of business. These commitments are typically for terms less than one year and require us to buy minimum quantities of materials at specified intervals at a fixed price over the term. As of March 31, 2012, we did not have any open purchase commitments.

Many of our customers require us to post performance and payment bonds issued by a surety. Those bonds guarantee the customer that we will perform under the terms of a contract and that we will pay subcontractors and vendors. In the event that we fail to perform under a contract or pay subcontractors and vendors, the customer may demand the surety to pay or perform under our bond. Our relationship with our sureties is such that we will indemnify the sureties for any expenses they incur in connection with any of the bonds they issue on our behalf. To date, we have not incurred any costs to indemnify our sureties for expenses they incurred on our behalf.

As of March 31, 2012, our future contractual obligations due by September 30 of each of the following fiscal years include (in thousands) (1):

	Less than 1 Year	1 to 3 Years	3 to 5 Years	More than 5 Years	Total
Long-term debt obligations	\$ 1,367	\$ 10,000	\$	\$	\$ 11,367
Operating lease obligations	\$ 4,575	\$ 5,897	\$ 590	\$ 967	\$ 12,029
Capital lease obligations	\$ 233	\$ 161	\$	\$	\$ 394
Total	\$ 6,175	\$ 16,058	\$ 590	\$ 967	\$ 23,790

(1) The tabular amounts exclude the interest obligations that will be created if the debt and capital lease obligations are outstanding for the periods presented.



**Table of Contents**

Our other commitments expire by September 30 of each of the following fiscal years (in thousands):

	FYE Sept 30, 2012	FYE Sept 30, 2013	FYE Sept 30, 2014	Thereafter	Total
Standby letters of credit	\$ 5,216	\$ 3,596	\$	\$	\$ 8,812
Other commitments	\$	\$	\$	\$	\$
<b>Total</b>	<b>\$ 5,216</b>	<b>\$ 3,596</b>	<b>\$</b>	<b>\$</b>	<b>\$ 8,812</b>

**Outlook**

We anticipate that the combination of cash on hand, cash flows and available capacity under our Revolving Credit Facility will provide sufficient cash to enable us to meet our working capital needs, debt service requirements and capital expenditures for property and equipment through the next twelve months. We expect that our capital expenditures will range from \$1.5 to \$2.0 million for the fiscal year ending on September 30, 2012. Our ability to generate cash flow is dependent on our successful finalization of our restructuring efforts and many other factors, including demand for our products and services, the availability of projects at margins acceptable to us, the ultimate collectability of our receivables and our ability to borrow on our amended Revolving Credit Facility. For additional information see *Disclosure Regarding Forward-Looking Statements* in Part I of this Form 10-Q.

**Table of Contents****Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Management is actively involved in monitoring exposure to market risk and continues to develop and utilize appropriate risk management techniques. Our exposure to significant market risks includes fluctuations in commodity prices for copper, aluminum, steel and fuel. Commodity price risks may have an impact on our results of operations due to the fixed price nature of many of our contracts. We are also exposed to interest rate risk with respect to our outstanding debt obligations on the Revolving Credit Facility. For additional information see *Disclosure Regarding Forward-Looking Statements* in Part I of this Form 10-Q.

**Commodity Risk**

Our exposure to significant market risks includes fluctuations in commodity prices for copper, aluminum, steel and fuel. Commodity price risks may have an impact on our results of operations due to fixed nature of many of our contracts. During 2011 and 2010, commodity prices were volatile, and we experienced overall increases in prices of copper, aluminum, steel and fuel. Over the long-term, we expect to be able to pass along a portion of these costs to our customers, as market conditions in the construction industry will allow.

**Interest Rate Risk**

We are also exposed to interest rate risk, with respect to our outstanding revolving debt obligations as well as our letters of credit.

The following table presents principal or notional amounts and related interest rates by fiscal year of maturity for our debt obligations at March 31, 2012 (Dollar amounts in thousands):

	2012	2013	2014	2015	2016	Thereafter	Total
<b>Debt Obligations - Fixed Rate:</b>							
Tontine Term Loan (11%)	\$	\$ 10,000	\$	\$	\$	\$	\$ 10,000
Capital Lease (22%)	\$ 158	\$ 317	\$ 26				501
<b>Fair Value of Debt:</b>							
Fixed Rate	\$ 146	\$ 10,708	\$ 19	\$	\$	\$	\$ 10,873

**Item 4. Controls and Procedures****Disclosure controls and procedures**

In connection with the restatements discussed in the explanatory note and in Notes 17 and 18 of our financial statements in our Form 10-K/A, under the direction of our Chief Executive Officer and Chief Financial Officer, we reevaluated our disclosure controls and procedures. We identified two material weaknesses in our internal control over financial reporting with respect to our inter-departmental communications processes at our Corporate office and within our Commercial & Industrial segment. Specifically, the Company's policies, procedures and personnel resources responsible for both our vacation accrual and certain other expenses, including software amortization, were not effective. Solely as a result of these material weaknesses, we concluded that our disclosure controls and procedures were not effective as of December 31, 2011.

During the first and second quarters of our 2012 fiscal year, we improved our inter-departmental communications at our Corporate office and Commercial & Industrial segment. We additionally implemented staffing changes, which we believe remediated each material weakness. In connection with the filing of our Form 10-K/A under the direction of our Chief Executive Officer and Chief Financial Officer, we have evaluated our disclosure controls and procedures as currently in effect, including the remedial actions discussed above, and we have concluded that, as of the March 30, 2012 filing of our December 31, 2011 Form 10-Q, our disclosure controls and procedures were effective.

**Changes in Internal Control over Financial Reporting**

As mentioned above, there were two material weaknesses that we identified. The first relates to a control deficiency at our corporate office that resulted in the inadequate reporting of certain software amortization expense. The corporate office failed to provide adequate managerial oversight, did not perform a timely review of the useful lives of its assets and did not engage in adequate inter-department communications between the IT and finance departments. The deficiency was identified by corporate management as of September 30, 2011, resulting in material revision of software amortization expense among



---

**Table of Contents**

the quarterly periods of fiscal 2011. The second material weakness identified relates to a control deficiency at our Commercial & Industrial segment that resulted in the under accrual of vacation expense. The vacation accrual for salaried employees within this segment was understated due to inadequate inter-department communications between the human resources and finance departments. This deficiency impacted our vacation accrual balance for all annual and interim periods from September 30, 2008 through 2011. The deficiency was identified by corporate management during the close process within our first quarter of fiscal year 2012, resulting in the restatement of our September 30, 2011 Form 10-K.

*Remediation of Material Weakness*

Management believes it has remediated the material weakness related to the review of the useful lives of its assets. The remediation included enhanced inter-department communication, additional internal financial review and a specific review of all material software currently capitalized and amortized during the company's financial close process.

Management believes it has remediated the material weakness related to the required vacation accrual. The remediation included updating the accrual process at the Commercial & Industrial segment to include the previously absent employees as of the first quarter in fiscal year 2012 and enhanced inter-departmental communication as well as the hiring of an additional resource in the finance department within our Commercial & Industrial segment.

As of the March 30, 2012 filing of the December 31, 2011 form 10-Q we believe the steps identified above have remediated the identified material weaknesses. Apart from the completion of this remediation process, there have been no changes in our internal control over financial reporting that occurred during the quarter ended March 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**ITEM 1. Legal Proceedings**

For further information regarding legal proceedings, see Note 11, *Commitments and Contingencies - Legal Matters* to the Consolidated Financial Statements, which is incorporated herein by reference.

**Item 1A. Risk Factors**

Except as set forth below, there have been no material changes to the risk factors disclosed under Item 1A - Risk Factors in our annual report on form 10-K /A for the year ended September 30, 2011.

***Availability of net operating losses may be reduced by a change in ownership.***

A change in ownership, as defined by Internal Revenue Code Section 382, could reduce the availability of net operating losses for federal and state income tax purposes. Should Tontine be considered under Internal Revenue Code Section 382 to sell or exchange all or a portion of its position in IES, a change in ownership could occur. In addition, a change in ownership could occur resulting from the purchase of common stock by an existing or a new 5% shareholder as defined by Internal Revenue Code Section 382. Due to the complex factual determinations involved with the determination of a change in ownership under Internal Revenue Code Section 382 and the regulations promulgated thereunder, it is possible for such a change in ownership to occur without our knowledge. Currently, we have approximately \$286.5 million of federal net operating losses that are available to use to offset taxable income, exclusive of net operating losses from the amortization of additional tax goodwill. In addition, we have approximately \$12.6 million of net operating loss not currently available due to the limitation imposed by Internal Revenue Code Section 382, exclusive of net operating losses from the amortization of additional tax goodwill, and will be available to offset taxable income in future periods. Should a change in ownership occur, all net operating losses incurred prior to the change in ownership would be subject to limitation imposed by Internal Revenue Code Section 382 and this would substantially reduce the amount of net operating losses currently available to offset taxable income. In addition, the net operating losses for federal and state purposes have not been reviewed by the Internal Revenue Service or any other taxing authorities. Should the Internal Revenue Service or any other taxing authority successfully challenge the amount or the availability of net operating losses, the potential benefit of the net operating losses could be substantially reduced.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.



---

**Table of Contents**

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. (Removed and Reserved)**

**Item 5. Other Information**

None.

**Item 6. Exhibits**

3.1	Second Amended and Restated Certificate of Incorporation of Integrated Electrical Services, Inc. (Incorporated by reference to Exhibit 4.1 to the Company's registration statement on Form S-8 filed on May 12, 2006)
3.2	Bylaws of Integrated Electrical Services, Inc. (Incorporated by reference to Exhibit 4.2 to the Company's registration statement on Form S-8, filed on May 12, 2006)
*10.1	Sublease Agreement between Tontine Associates, LLC and IES Shared Services, Inc, dated March 29, 2012
*10.2	Amendment to Loan and Security Agreement, dated May 11, 2012
*31.1	Rule 13a-14(a)/15d-14(a) Certification of James M. Lindstrom, Chief Executive Officer(1)
*31.2	Rule 13a-14(a)/15d-14(a) Certification of Robert W. Lewey, Chief Financial Officer(1)
*32.1	Section 1350 Certification of James M. Lindstrom, Chief Executive Officer(1)
*32.2	Section 1350 Certification of Robert W. Lewey, Chief Financial Officer(1)
**101.INS	XBRL Instance Document
**101.SCH	XBRL Schema Document
**101.LAB	XBRL Label Linkbase Document
**101.PRE	XBRL Presentation Linkbase Document
**101.DEF	XBRL Definition Linkbase Document
**101.CAL	XBRL Calculated Linkbase Document

\* Filed herewith.

\*\* Furnished herewith.

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, who has signed this report on behalf of the registrant and as the principal financial officer of the registrant.

**INTEGRATED ELECTRICAL SERVICES, INC.**

Date: May 14, 2012

By: /s/ ROBERT W. LEWEY  
**Robert W. Lewey**  
**Senior Vice President and Chief Financial Officer**