

ENGLOBAL CORP
Form 10-Q
November 19, 2012

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 September 29, 2012

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

Commission File No. 001-14217

ENGlobal Corporation
(Exact name of registrant as specified in its charter)

Nevada
(State or other jurisdiction of
incorporation or organization)

88-0322261
(I.R.S Employer Identification No.)

654 N. Sam Houston Parkway E., Suite 400, Houston, TX
(Address of principal executive offices)

77060-5914
(Zip code)

(281) 878-1000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shortened period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

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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	<input type="checkbox"/>	Accelerated Filer	<input type="checkbox"/>
Non-Accelerated Filer (Do not check if a smaller reporting company)	<input type="checkbox"/>	Smaller Reporting Company	<input checked="" type="checkbox"/>

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

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the close of business on November 14, 2012.

\$0.001 Par Value Common Stock	26,964,339 shares
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QUARTERLY REPORT ON FORM 10-Q
FOR THE PERIOD ENDED SEPTEMBER 29, 2012

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PART I. - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ENGlobal Corporation
Condensed Consolidated Statements of Operations and Comprehensive Loss
(Unaudited)

For the Three Months Ended For the Nine Months Ended
September 29, September September 29, September 30,
2012 30, 2011 2012 2011
(amounts in thousands, except loss per share data)

Operating revenues	\$57,482	\$60,482	\$ 175,805	\$ 162,961
Operating costs	54,212	53,706	162,455	145,767
Gross profit	3,270	6,776	13,350	17,194
Selling, general and administrative expenses	6,162	6,682	19,301	18,716
Goodwill impairment	14,568	—	14,568	—
Operating income (loss)	(17,460)	94	(20,519)	(1,522)
Other income (expense):				
Other income (expense), net	(98)	(8)	(100)	(68)
Interest expense, net	(643)	(303)	(1,320)	(711)
Loss from continuing operations before income taxes	(18,201)	(217)	(21,939)	(2,301)
Provision (benefit) for federal and state income taxes				
	412	138	5,606	(460)
Loss from continuing operations	(18,613)	(355)	(27,545)	(1,841)
Loss from discontinued operations, net of taxes	(3,717)	(918)	(4,779)	(1,263)
Net loss	(22,330)	(1,273)	\$(32,324)	(3,104)
Other comprehensive income (expense)				
Foreign currency translation adjustment	—	—	(1)	—
Comprehensive loss	\$(22,330)	\$(1,273)	\$(32,325)	\$(3,104)
Loss per common share – basic and diluted:				
Net loss from continuing operations	\$(0.69)	\$(0.01)	\$(1.02)	\$(0.07)
Net loss from discontinued operations	\$(0.14)	\$(0.04)	\$(0.18)	\$(0.05)
Net loss	\$(0.83)	\$(0.05)	\$(1.20)	\$(0.12)
Weighted average shares used in computing loss per common share – basic and diluted				
	26,964	26,620	26,882	26,585

See accompanying notes to unaudited interim condensed consolidated financial statements.

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ENGlobal Corporation
Condensed Consolidated Balance Sheets
(Unaudited)

ASSETS	September 29, 2012	December 31, 2011
	(amounts in thousands, except share amounts)	
Current Assets:		
Cash and cash equivalents	\$634	\$26
Restricted cash	6,134	2,275
Trade receivables, net of allowances of \$2,299 and \$1,792	46,949	44,159
Prepaid expenses and other current assets	504	846
Notes receivable	514	514
Costs and estimated earnings in excess of billings on uncompleted contracts	7,632	6,790
Assets held for sale	13,813	19,054
Federal and state income taxes receivable	389	79
Deferred tax asset	—	3,989
Total Current Assets	76,569	77,732
Property and equipment, net	3,241	3,260
Goodwill	2,805	17,373
Other intangible assets, net	2,097	2,835
Long-term trade and notes receivable, net of current portion and allowances	899	899
Deferred tax asset, non-current	—	1,206
Other assets	882	874
Total Assets	\$86,493	\$104,179
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$9,247	\$8,316
Accrued compensation and benefits	13,328	10,400
Current portion of debt	29,406	16,602
Deferred rent	606	635
Billings in excess of costs and estimated earnings on uncompleted contracts	3,986	4,421
Liabilities held for sale	2,862	4,058
Other current liabilities	706	1,247
Total Current Liabilities	60,141	45,679
Commitments and Contingencies (Note 11)		
Stockholders' Equity:		
Common stock - \$0.001 par value; 75,000,000 shares authorized; 26,964,339 and 26,882,518 shares outstanding and 27,945,438 and 27,803,617 shares issued at September 29, 2012 and December 31, 2011, respectively	28	28
Additional paid-in capital	38,258	38,081
Retained earnings (deficit)	(9,502)	22,822
Treasury stock - 981,099 shares at September 29, 2012 and December 31, 2011	(2,362)	(2,362)
Accumulated other comprehensive loss	(70)	(69)
Total Stockholders' Equity	26,352	58,500

Total Liabilities and Stockholders' Equity	\$86,493	\$104,179
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See accompanying notes to unaudited interim condensed consolidated financial statements.

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ENGlobal Corporation
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	For the Nine Months Ended	
	September 29, 2012	September 30, 2011
	(amounts in thousands)	
Cash Flows from Operating Activities:		
Net loss	\$(32,324)	\$(3,104)
Adjustments to reconcile net loss to cash provided by (used in) operating activities:		
Depreciation and amortization	1,452	2,730
Share-based compensation expense	177	307
Deferred income tax expense (benefit)	6,166	(1,047)
Impairment of goodwill	16,965	—
(Gain) loss on disposal of property, plant and equipment	47	(18)
Changes in current assets and liabilities, net of acquisitions:		
Trade accounts and other receivables	(1,467)	(3,300)
Costs and estimated earnings in excess of billings on uncompleted contracts	(704)	(1,693)
Prepaid expenses and other assets	16	482
Accounts payable	770	(210)
Accrued compensation and benefits	3,986	4,289
Billings in excess of costs and estimated earnings on uncompleted contracts	(520)	1,163
Other liabilities	(2,578)	1,876
Income taxes receivable	(264)	(425)
Net cash provided by (used in) operating activities	\$(8,278)	\$1,050
Cash Flows from Investing Activities:		
Property and equipment acquired	(228)	(452)
Restricted cash	(3,859)	—
Proceeds from sale of other assets	170	65
Net cash used in investing activities	\$(3,917)	\$(387)
Cash Flows from Financing Activities:		
Borrowings on line of credit	149,872	118,947
Payments on line of credit	(136,818)	(116,358)
Repayments under capital lease	—	(51)
Other long-term debt repayments	(250)	(941)
Net cash provided by financing activities	\$12,804	\$1,597
Effect of Exchange Rate Changes on Cash	(1)	—
Net change in cash	608	2,260
Cash and cash equivalents, at beginning of period	26	49
Cash and cash equivalents, at end of period	\$634	\$2,309

See accompanying notes to unaudited interim condensed consolidated financial statements.

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Notes to Unaudited Interim Condensed Consolidated Financial Statements

NOTE 1 – BASIS OF PRESENTATION AND CRITICAL ACCOUNTING POLICIES

The condensed consolidated financial statements of ENGlobal Corporation (which may be referred to as "ENGlobal", "the Company," "we," "us," or "our") are prepared in accordance with accounting principles generally accepted in the United States of America. The Company consolidates all of its subsidiaries' financial results, and significant inter-company accounts and transactions have been eliminated in the consolidation.

The condensed consolidated financial statements of the Company included herein are unaudited for the three and nine-month periods ended September 29, 2012 and September 30, 2011, have been prepared from the books and records of the Company pursuant to the rules and regulations of the Securities and Exchange Commission, and in the case of the condensed balance sheet as of December 31, 2011, have been derived from the audited financial statements of the Company. These financial statements reflect all adjustments (consisting of normal recurring adjustments), which are, in the opinion of management, necessary to fairly present the results for the periods presented. Certain information and note disclosures, normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted pursuant to rules and regulations of the Securities and Exchange Commission. These condensed consolidated financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2011, included in the Company's Annual Report on Form 10-K, as amended, filed with the Securities and Exchange Commission. The Company has assessed subsequent events through the date of filing of these condensed consolidated financial statements with the Securities and Exchange Commission and believes that the disclosures made herein are adequate to make the information presented herein not misleading. Certain reclassifications have been made to the 2011 condensed consolidated financial statements to conform the presentation to report discontinued operations. Refer to Note 3.

On January 1, 2012, we changed from a traditional month-end calendar close cycle to a 4-4-5 calendar close methodology. Under this new methodology, each quarter (formerly comprised of 3 calendar months) is comprised of 13 weeks, which includes two 4-week months and one 5-week month. This change in accounting periods has not had a material effect on the comparability to prior periods.

NOTE 2 – LIQUIDITY

The Company has been operating under difficult circumstances in 2012. For the nine-month period ended September 29, 2012, the Company reported a net loss of approximately \$32.3 million that included a non-cash charge of approximately \$16.9 million relating to a goodwill impairment (see Note 4) and a non-cash charge of approximately \$6.2 million relating to a valuation allowance established in connection with the Company's deferred tax assets (see Note 9). During 2012, our net borrowings under our revolving credit facilities have increased approximately \$13.0 million to fund our operations. Due to challenging market conditions, our revenues and profitability have declined during 2012. As a result, we have failed to comply with several financial covenants under our credit facilities resulting in defaults (see Note 7). Although we have sold assets and reduced personnel in an attempt to improve our liquidity position, we cannot assure you that we will be successful in obtaining the cure or waiver of the defaults under the respective credit facilities. If we fail to obtain the cure or waiver of the defaults under the facilities after any forbearance period, the lenders may exercise any and all rights and remedies available to them under their respective agreements, including demanding immediate repayment of all amounts then outstanding or initiating foreclosure or insolvency proceedings. In such event and if we are unable to obtain alternative financing, our business will be materially and adversely affected, and we may be forced to sharply curtail or cease our operations. In addition, based on current conditions, it is probable that our independent registered public accounting firm will include an explanatory paragraph with respect to our ability to continue as a going concern in its report on our financial statements for the

year ending December 31, 2012.

NOTE 3 - DISCONTINUED OPERATIONS

During the third quarter of 2011, as part of its strategic evaluation of operations, the Company determined that the expected future profitability of the Electrical Services group was not sufficient to support maintaining it as a viable business and that it did not fit within the future strategic plan due to its operational differences. As a result, effective July 1, 2011, the Company initiated a plan to sell the operations of its Electrical Services group. These assets and their related operations have been classified as discontinued operations and accordingly, are presented as discontinued operations in the Company's re-casted consolidated financial statements. The net assets and liabilities related to the discontinued operations are shown on the Condensed Consolidated Balance Sheet as "Assets held for sale" and "Liabilities held for sale," respectively. The results of the discontinued operations are shown on the Condensed Consolidated Statements of Operations as "Loss from discontinued operations, net of taxes".