

INTEGRATED ELECTRICAL SERVICES INC
Form 10-Q
February 10, 2014
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 December 31, 2013

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.

(Exact name of registrant as specified in its charter)

Delaware **76-0542208**
(State or other jurisdiction of **(I.R.S. Employer**
incorporation or organization) **Identification No.)**
5433 Westheimer Road, Suite 500, 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

On February 10, 2014, there were 17,918,254 shares of common stock outstanding.

Table of Contents

INTEGRATED ELECTRICAL SERVICES, INC. AND SUBSIDIARIES

INDEX

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
Item 1. Consolidated Financial Statements	
<u>Consolidated Balance Sheets as of December 31, 2013 and September 30, 2013</u>	5
<u>Consolidated Statements of Comprehensive Income for the Three Months Ended December 31, 2013 and 2012</u>	6
<u>Consolidated Statements of Cash Flows for the Three Months Ended December 31, 2013 and 2012</u>	7
<u>Notes to Consolidated Financial Statements</u>	8
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	30
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	40
<u>Item 4. Controls and Procedures</u>	40
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings.</u>	40
<u>Item 1A. Risk Factors.</u>	41
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	42
<u>Item 3. Defaults Upon Senior Securities</u>	42
<u>Item 4. Mine Safety Disclosures</u>	42
<u>Item 5. Other Information</u>	42
<u>Item 6. Exhibits</u>	42
<u>Signatures</u>	44
<u>Exhibit 31.1</u>	
<u>Exhibit 31.2</u>	
<u>Exhibit 32.1</u>	
<u>Exhibit 32.2</u>	

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. In some cases, you can identify forward-looking statements by terminology such as "may", "will", "could", "should", "expect", "plan", "project", "intend", "anticipate", "believe", "seek", "estimate", "predict", "potential", "put" or other similar terms or other comparable terminology. 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:

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

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 our severance plan or financing and surety arrangements;

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

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

difficulty in fulfilling the covenant terms of our credit facilities;

competition in our respective industries, 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 projects;

the inability to achieve, or difficulties and delays in achieving, potential benefits of the acquisition of MISCOR Group, Ltd;

challenges integrating other new businesses into the Company or new types of work, products or processes into our segments;

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

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 projects;

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

additional closures or sales of facilities could result in significant future charges and a significant disruption of our operations;

inaccurate estimates used when entering into fixed-priced contracts;

the cost and availability of qualified labor;

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;

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

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

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;

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

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

Table of Contents

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

loss of key personnel and effective transition of new management;

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

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 effect of litigation, claims and contingencies, including warranty losses, damages or other latent defect claims in excess of our existing reserves and accruals;

warranty losses or other unexpected liabilities stemming from former segments 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;

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

the ability of IES to enter into, and the terms of, future contracts;

the inability to carry out plans and strategies as expected;

future capital expenditures and refurbishment, repair and upgrade costs; and delays in and costs of refurbishment, repair and upgrade projects; and

liabilities under laws and regulations protecting the environment.

You should understand that the foregoing, as well as other risk factors discussed in this document, as well as the other risk factors discussed in Part I, Item 1A of our Annual Report on Form 10-K/A for the fiscal year ended September 30, 2013, 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 any information, including information concerning our controlling shareholder, net operating losses, restructuring efforts, borrowing availability, cash position, pro forma financial statements 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.

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

	December 31, 2013	September 30, 2013
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 17,253	\$ 20,757
Accounts receivable:		
Trade, net of allowance of \$945 and \$980, respectively	66,530	73,540
Retainage	16,498	17,473
Inventories	16,652	20,147
Costs and estimated earnings in excess of billings on uncompleted contracts	7,559	8,336
Prepaid expenses and other current assets	6,603	3,772
Total current assets	131,095	144,025
LONG-TERM RECEIVABLES, net of allowance	28	35
PROPERTY AND EQUIPMENT	10,141	10,414
GOODWILL	13,924	13,924
INTANGIBLE ASSETS	3,978	4,138
OTHER NON-CURRENT ASSETS	6,056	6,716
Total assets	\$ 165,222	\$ 179,252
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Current maturities of long-term debt	\$ 3,529	\$ 3,562
Accounts payable and accrued expenses	61,633	74,320
Billings in excess of costs and estimated earnings on uncompleted contracts	20,099	20,676
Total current liabilities	85,261	98,558
LONG-TERM DEBT, net of current maturities	9,333	10,210
LONG-TERM DEFERRED TAX LIABILITY	905	905
OTHER NON-CURRENT LIABILITIES	7,078	7,093
Total liabilities	102,577	116,766
STOCKHOLDERS EQUITY:		
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, none issued and outstanding		
	182	182

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

Common stock, \$0.01 par value, 100,000,000 shares authorized; 18,203,379 and 18,203,379 shares issued and 17,918,254 and 17,944,322 outstanding, respectively		
Treasury stock, at cost, 285,125 and 259,057 shares, respectively	(2,427)	(2,332)
Additional paid-in capital	174,649	174,514
Accumulated other comprehensive income	12	17
Retained deficit	(109,771)	(109,895)
Total stockholders' equity	62,645	62,486
Total liabilities and stockholders' equity	\$ 165,222	\$ 179,252

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

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

	Three Months Ended December 31,	
	2013	2012
Revenues	\$ 120,079	\$ 127,264
Cost of services	101,963	109,284
Gross profit	18,116	17,980
Selling, general and administrative expenses	17,572	14,922
Gain on sale of assets	(41)	(19)
Income from operations	585	3,077
Interest and other (income) expense:		
Interest expense	518	607
Interest income	(1)	(12)
Other (income) expense, net	(196)	1,734
Interest and other expense, net	321	2,329
Income from continuing operations before income taxes	264	748
Provision (benefit) for income taxes	(1)	115
Net income from continuing operations	\$ 265	\$ 633
Discontinued operations (Note 17)		
Loss from discontinued operations	(141)	(138)
Benefit for income taxes		(15)
Net loss from discontinued operations	(141)	(123)
Net income	\$ 124	\$ 510
Unrealized gain on interest hedge, net of tax	12	
Comprehensive income	\$ 136	\$ 510
Earnings (loss) per share:		
Continuing operations	\$ 0.02	\$ 0.04
Discontinued operations	\$ (0.01)	\$ (0.01)
Basic	\$ 0.01	\$ 0.03
Diluted earnings (loss) per share:		

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

Continuing operations	\$	0.02	\$	0.04
Discontinued operations	\$	(0.01)	\$	(0.01)
Diluted	\$	0.01	\$	0.03
Shares used in the computation of earnings (loss) per share				
Basic		17,817,254		14,801,903
Diluted		17,898,832		14,919,189

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)**

	Three Months Ended December 31,	
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 124	\$ 510
Adjustments to reconcile net loss to net cash provided by operating activities:		
Bad debt expense	45	(138)
Deferred financing cost amortization	127	209
Depreciation and amortization	617	539
Loss (gain) on sale of assets	56	14
Non-cash compensation expense	200	492
Changes in operating assets and liabilities		
Accounts receivable	7,050	3,378
Inventories	3,495	2,107
Costs and estimated earnings in excess of billings	777	149
Prepaid expenses and other current assets	(1,915)	(4,257)
Other non-current assets	510	199
Accounts payable and accrued expenses	(12,684)	2,426
Billings in excess of costs and estimated earnings	(577)	(2,325)
Other non-current liabilities	(24)	(11)
Net cash (used in) provided by operating activities	(2,199)	3,292
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(267)	(369)
Net cash used in investing activities	(267)	(369)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayments of debt	(877)	(24)
Purchase of treasury stock	(161)	(346)
Change in restricted cash		(409)
Net cash used in financing activities	(1,038)	(779)
NET INCREASE (DECREASE) IN CASH EQUIVALENTS	(3,504)	2,144
CASH AND CASH EQUIVALENTS, beginning of period	20,757	18,729
CASH AND CASH EQUIVALENTS, end of period	\$ 17,253	\$ 20,873

	2013	2012
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	\$ 264	\$ 419
Cash paid for income taxes	\$ 95	\$ 62

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. is a holding company that owns and manages operating subsidiaries in business activities across a variety of end markets. Our operations are currently organized into four principal business segments, based upon the nature of our current 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 for commercial and industrial projects nationwide.

Infrastructure Solutions - Provider of industrial and rail services, and electrical and mechanical solutions to domestic and international customers. (This segment was created in connection with the acquisition of MISCOR Group, Ltd. (MISCOR))

The words IES , the Company , we , our , and us refer to Integrated Electrical Services, Inc. and, except as otherwise specified herein, to our wholly-owned subsidiaries.

Our Communications segment is a leading provider of network infrastructure products and services. Services offered include the design, installation and maintenance of network infrastructure for numerous industry groups. We provide design and installation of audio/visual, telephone, fire, wireless and intrusion alarm systems as well as design/build, service and maintenance of data network systems. We perform services across the United States from our ten offices, headquartered in Tempe, Arizona.

Our Residential segment provides electrical installation services for single-family housing and multi-family apartment complexes and CATV cabling installations for residential and light commercial applications. In addition to our core electrical construction work, the Residential segment provides services for the installation of residential solar power, smart meters, electric car charging stations and stand-by generators, both for new construction and existing residences. The segment is comprised of 24 locations, with headquarters in Houston, Texas. Residential locations geographically cover Texas, the Sun-Belt, and the Western and Mid-Atlantic regions of the United States, including Hawaii.

Our Commercial & Industrial segment offers a broad range of electrical design, construction, renovation, engineering and maintenance services to the commercial and industrial markets. The Commercial & Industrial segment consists of 18 locations, headquartered in Houston, Texas. Locations geographically cover Texas, Nebraska, Colorado, Oregon and the Mid-Atlantic region. Services include the design of electrical systems within a building or complex, procurement and installation of wiring and connection to power sources, end-use equipment and fixtures, as well as contract maintenance. We focus on projects that require special expertise, such as design-and-build projects that utilize the capabilities of our in-house experts, or projects which require specific market expertise, such as transmission and distribution and power generation facilities. We also provide service, maintenance and renovation and upgrade work, which tends to be either recurring or have lower sensitivity to economic cycles, or both. We provide services for a variety of projects, including: high-rise residential and office buildings, power plants, manufacturing facilities, data centers, chemical plants, refineries, wind farms, solar facilities, municipal infrastructure and health care facilities, and residential developments. Our utility services consist of overhead and underground installation and maintenance of electrical and other utilities transmission and distribution networks, installation and splicing of high-voltage transmission and distribution lines, substation construction and substation and right-of-way maintenance. Our maintenance services generally provide recurring revenues that are typically less affected by levels of construction activity.

Our Infrastructure Solutions segment provides maintenance and repair services to several industries, including electric motor repair and rebuilding for the steel, railroad, marine, petrochemical, pulp and paper, wind energy, mining, automotive and power generation industries. Infrastructure Solutions repairs and manufactures industrial lifting magnets for the steel and scrap industries, provides locomotive maintenance, remanufacturing, and repair services to the rail industry, and manufactures and rebuilds power assemblies, engine parts, and other components for large diesel engines. Infrastructure Solutions is made up of nine total locations, which includes our Infrastructure Solutions headquarters in Ohio. These segment locations geographically cover Alabama, Indiana, Ohio, West Virginia, Maryland and California.

Table of Contents

INTEGRATED ELECTRICAL SERVICES, INC.

Notes to Consolidated Financial Statements

(All Amounts in Thousands Except Share Amounts)

Related Party Transactions

On December 12, 2007, we entered into the Tontine Term Loan, with Tontine, which the Company terminated and prepaid in full in the second quarter of fiscal 2013. See Note 4, Debt *The Tontine Term Loan*, for further discussion.

On March 29, 2012, we entered into a sublease agreement with Tontine Associates, LLC, an affiliate of Tontine Capital Partners, L.P. (together with its affiliates Tontine), 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. The lease has terms at market rates and payments by the Company are at a rate consistent with that paid by Tontine Associates, LLC to its landlord. See also Note 2, Controlling Shareholder, for further discussion.

Basis of Financial Statement Preparation

The accompanying unaudited condensed consolidated financial statements include the accounts of IES and its wholly-owned subsidiaries, and have been prepared in accordance with the instructions to interim financial reporting as prescribed by the SEC. These interim financial statements do not include all disclosures required by accounting principles generally accepted in the United States of America, and should be read in the context of the consolidated financial statements and notes thereto filed with the Securities and Exchange Commission (the SEC) in our Annual Report on Form 10-K for the year ended September 30, 2013. In the opinion of management, the unaudited condensed consolidated financial statements contained in this report include all known accruals and adjustments necessary for a fair statement of the results of operations for the periods reported herein. All such adjustments are of a normal recurring nature.

Fair Value of Financial Instruments

Our financial instruments consist of cash and cash equivalents, accounts receivable, notes receivable, investments, accounts payable, a loan agreement, and an interest rate swap agreement. We believe that the carrying value of financial instruments, with the exception of our cost method investment in EnerTech, in the accompanying Consolidated Balance Sheets, approximates their fair value due to their short-term nature.

We estimate the fair value of our investment in EnerTech Capital Partners II L.P. (EnerTech) (Level 3) using quoted market prices for underlying publicly traded securities, and estimated enterprise values determined using cash flow projections and market multiples of the underlying non-public companies. For additional information on our investment in EnerTech, please refer to Note 9, *Securities and Equity Investments* .

For a detailed discussion of financial assets and liabilities measured at fair value on a recurring basis, please refer to Note 11, Fair Value Measurements in the Notes to these Consolidated Financial Statements.

Goodwill

Goodwill attributable to each reporting unit is tested for impairment by comparing the fair value of each reporting unit with its carrying value. Fair value is determined using discounted cash flows. These impairment tests are required to be performed at least annually. Significant estimates used in the methodologies include estimates of future cash flows, future short-term and long-term growth rates, and weighted average cost of capital for each of the reportable units. On an ongoing basis (absent any impairment indicators), we perform an impairment test annually using a measurement date of September 30.

Intangible Assets

Intangible assets with definite lives are amortized over their estimated useful lives based on expected economic benefit with no residual value. Customer relationships are amortized assuming gradual attrition. Intangible assets with indefinite lives are not subject to amortization. We perform a test for impairment annually, or more frequently when indicators of impairment are present.

Table of Contents

INTEGRATED ELECTRICAL SERVICES, INC.

Notes to Consolidated Financial Statements

(All Amounts in Thousands Except Share Amounts)

Use of Estimates

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 segments, realizability of deferred tax assets, unrecognized tax benefits and self-insured claims liabilities and related reserves.

Inventories

Inventories generally consist of raw materials, work in process, finished goods, and parts and supplies held for use in the ordinary course of business. Inventory is valued at the lower of cost or market generally using the historical average cost or first-in, first-out (FIFO) method. When circumstances dictate, we write down inventory to its estimated realizable value based on assumptions about future demand, market conditions, plans for disposal, and physical condition of the product. Where shipping and handling costs to receive materials are borne by us, these charges are included in inventory and charged to cost of services upon use in our projects or the providing of services.

Cash and Cash Equivalents

We consider all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Comprehensive Income

Comprehensive income includes all changes in equity during a period except those resulting from investments by and distributions to stockholders.

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, Commercial & Industrial, and Infrastructure Solutions 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. Results for our Infrastructure Solutions segment may be affected by the timing of scheduled outages at our customers' facilities. Accordingly, operating results for any fiscal period are not necessarily indicative of results that may be achieved for any subsequent fiscal period.

New Accounting Pronouncements

In February 2013, the FASB issued accounting guidance related to the reporting of amounts reclassified out of accumulated other comprehensive income. This guidance sets forth new disclosure requirements for items reclassified from accumulated other comprehensive income by requiring disclosures for both the changes in accumulated other comprehensive income by component and where the significant items reclassified from accumulated other comprehensive income are classified in the Statements of Consolidated Comprehensive Income. See Note 7, Other Comprehensive Income, for further discussion.

Table of Contents

INTEGRATED ELECTRICAL SERVICES, INC.

Notes to Consolidated Financial Statements

(All Amounts in Thousands Except Share Amounts)

2. CONTROLLING SHAREHOLDER

At December 31, 2013, Tontine Capital Partners, L.P. together with its affiliates (collectively "Tontine") was the controlling shareholder of the Company's common stock. Accordingly, Tontine has the ability to exercise significant control over our affairs, including the election of directors and any action requiring the approval of shareholders.

While Tontine is subject to restrictions under federal securities laws on sales of its shares as an affiliate, pursuant to a Registration Rights Agreement between Tontine and the Company, Tontine delivered a request to the Company for registration of all of its shares of IES common stock, and on February 21, 2013, the Company filed a shelf registration statement to register Tontine's shares (as amended, the "Shelf Registration Statement"). The Shelf Registration Statement was declared effective by the SEC on June 18, 2013. As long as the Shelf Registration Statement remains effective, Tontine has the ability to resell any or all of its shares from time to time in one or more offerings, as described in the Shelf Registration Statement and in any prospectus supplement filed in connection with an offering pursuant to the Shelf Registration Statement.

Should Tontine sell or otherwise dispose of all or a portion of its position in IES, a change in ownership could occur. A change in ownership, as defined by Internal Revenue Code Section 382, could reduce the availability of net operating losses ("NOLs") for federal and state income tax purposes. On January 28, 2013, the Company implemented a tax benefit protection plan (the "NOL Rights Plan") that is designed to deter an acquisition of the Company's stock in excess of a threshold amount that could trigger a change of control within the meaning of Internal Revenue Code Section 382. For additional information on the NOL Rights Plan, please see our Current Report on Form 8-K, filed with the SEC on January 28, 2013. There can be no assurance that the NOL Rights Plan will be effective in deterring a change of control or protecting the NOLs. Furthermore, a change in control would trigger the change of control provisions in a number of our material agreements, including our credit facility, bonding agreements with our sureties and certain employment contracts with certain officers and employees of the Company.

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 began the closure of certain underperforming facilities within our Commercial & Industrial operations. The 2011 Restructuring Plan was a key element of our commitment to return the Company to profitability.

The facilities directly affected by the 2011 Restructuring Plan were in several locations throughout the country, including Arizona, Florida, Iowa, Massachusetts, Louisiana, Nevada and Texas. These facilities were selected due to business prospects at that time and the extended time frame needed to return the facilities to a profitable position. Closure costs associated with the 2011 Restructuring Plan included equipment and facility lease termination expenses, incremental management consulting expenses and severance costs for employees. The Company has completed the

wind down of these facilities with minimal completion remaining. As part of our restructuring charges reported within discontinued operations for our Commercial & Industrial segment we recognized zero and \$(4) in severance charges; zero and \$47 in consulting services; and zero in costs related to lease terminations for the three months ended December 31, 2013 and 2012, respectively. Charges related to the 2011 Restructuring Plan in our fiscal year ended 2014 are expected to be immaterial.

The 2011 Restructuring Plan pertains only to our Commercial & Industrial segment. The following table summarizes the activities related to our restructuring activities by component:

	Severance Charges	Lease Termination & Other Charges	Total
Restructuring liability at September 30, 2013	\$ 115	\$ 160	\$ 275
Cash payments made	(58)	(19)	(77)
Restructuring liability at December 31, 2013	\$ 57	\$ 141	\$ 198

Table of Contents**INTEGRATED ELECTRICAL SERVICES, INC.****Notes to Consolidated Financial Statements****(All Amounts in Thousands Except Share Amounts)****4. DEBT***Debt consists of the following:*

	December 31, 2013	September 30, 2013
Wells Fargo Term Loan, paid in installments thru Aug 9, 2016	\$ 12,833	\$ 13,708
Capital leases and other	29	64
Total debt	12,862	13,772
Less Short-term debt and current maturities of long-term debt	(3,529)	(3,562)
Total long-term debt	\$ 9,333	\$ 10,210

Future payments on debt as of December 31, 2013 are as follows:

	Capital Leases and Other	Term Debt	Total
2014	\$ 27	\$ 2,625	\$ 2,652
2015	2	3,500	3,502
2016		6,708	6,708
Total	\$ 29	\$ 12,833	\$ 12,862

For the three months ended December 31, 2013 and 2012, we incurred interest expense of \$518 and \$607, respectively.

The 2012 Revolving Credit Facility

On August 9, 2012, we entered into a Credit and Security Agreement (the *Credit Agreement*), for a \$30,000 revolving credit facility (the *2012 Credit Facility*) with Wells Fargo Bank, National Association (*Wells Fargo*) with a maturity date of August 9, 2015, unless earlier terminated. We have entered into two amendments to the 2012 Credit Facility. On February 12, 2013, we entered into an amendment of our 2012 Credit Facility (the *Amendment*), to extend the term to August 9, 2016, add IES Renewable Energy, LLC as a borrower, and provide for a term loan (the *Wells Fargo*

Term Loan). On September 13, 2013, we entered into an amendment of the 2012 Credit Facility (the Second Amendment), which amended the Wells Fargo Term Loan, removed the requirement to cash collateralize our outstanding letters of credit, and added IES Subsidiary Holdings Inc., Magnetech Industrial Services, Inc., and HK Engine Components, LLC, as borrowers.

The 2012 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 2012 Credit Facility also restricts us from paying cash dividends and places limitations on our ability to repurchase our common stock.

The 2012 Credit Facility contains customary affirmative, negative and financial covenants. The 2012 Credit Facility requires that we maintain a fixed charge coverage ratio of not less than 1.0:1.0 at any time that our Liquidity (defined as the aggregate amount of unrestricted cash and cash equivalents on hand plus Excess Availability (as defined in the Credit Facility)) or Excess Availability fall

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

below stipulated levels. The Second Amendment provided for tiered thresholds. Through December 31, 2013, our Liquidity could not fall below \$15,000. Thereafter, our Liquidity must not fall below \$20,000. Additionally, our Excess Availability must not fall below \$5,000. As of December 31, 2013, our Liquidity was in excess of \$15,000 and Excess Availability was in excess of \$5,000; had we not met these thresholds at December 31, 2013, we would not have met the required 1.0:1.0 fixed charge coverage ratio test.

Borrowings under the 2012 Credit Facility may not exceed a borrowing base that is determined monthly by our lenders based on available collateral, primarily certain accounts receivables, inventories and personal property and equipment. Under the terms of the 2012 Credit Facility, amounts outstanding bear interest at a per annum rate equal to a Daily Three Month LIBOR (as defined in the Credit Agreement), plus an interest rate margin, which is determined quarterly, based on the following thresholds:

Level	Thresholds	Interest Rate Margin
I	Liquidity £ \$20,000 at any time during the period; or Excess Availability £ \$7,500 at any time during the period; or Fixed charge coverage ratio < 1.0:1.0	4.00 percentage points
II	Liquidity > \$20,000 at all times during the period; and Liquidity £ \$30,000 at any time during the period; and Excess Availability \$7,500; and Fixed charge coverage ratio ³ 1.0:1.0	3.50 percentage points
III	Liquidity > \$30,000 at all times during the period; and Excess Availability > \$7,500; and Fixed charge coverage ratio ³ 1.0:1.0	3.00 percentage points

In addition, we are charged monthly in arrears for (1) an unused commitment fee of 0.50% per annum, (2) a collateral monitoring fee ranging from \$1 to \$2, based on the then-applicable interest rate margin, (3) a letter of credit fee based on the then-applicable interest rate margin and (4) certain other fees and charges as specified in the Credit Agreement.

At December 31, 2013, we had \$5,811 available to us under the 2012 Credit Facility, \$6,660 in outstanding letters of credit with Wells Fargo and no outstanding borrowings.

The Second Amendment to the 2012 Credit Facility increased our total Term Loan by \$10,147 to \$13,708 at September 30, 2013. The Wells Fargo Term Loan is payable in equal monthly installments of \$292 through August 9, 2016, with the residual unpaid principal balance due on that date. The Second Amendment also extended the term and reduced the annual interest rate to 5% plus 3 Month LIBOR, through September 13, 2014. Following that time, the Wells Fargo Term Loan amounts outstanding bear interest at a per annum rate equal to a Daily Three Month LIBOR plus an interest rate margin, which is determined quarterly, based on the following thresholds:

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

Level	Thresholds	Interest Rate Margin
I	Liquidity £ \$20,000 at any time during the period; or Excess Availability £ \$7,500 at any time during the period; or Fixed charge coverage ratio < 1.0:1.0	5.00 percentage points
II	Liquidity > \$20,000 at all times during the period; and Liquidity £ \$30,000 at any time during the period; and Excess Availability \$7,500; and Fixed charge coverage ratio ³ 1.0:1.0	4.50 percentage points
III	Liquidity > \$30,000 at all times during the period; and Excess Availability > \$7,500; and Fixed charge coverage ratio ³ 1.0:1.0	4.00 percentage points

The Tontine Term Loan

On December 12, 2007, we entered into the Tontine Term Loan, a \$25,000 senior subordinated loan agreement, with Tontine, which the Company terminated and prepaid in full in the second quarter of fiscal 2013, as further described below.

The Tontine Term Loan bore interest at 11.0% per annum and was due on May 15, 2013. Interest was payable quarterly in cash or in-kind at our option. Any interest paid in-kind would bear interest at 11.0% in addition to the loan principal. The Tontine Term Loan was subordinated to the 2012 Credit Facility. The Tontine Term Loan was an unsecured obligation of the Company and its subsidiary borrowers and contained no financial covenants or restrictions on dividends or distributions to stockholders. The Tontine Term Loan was amended on August 9, 2012 in connection with the Company entering into the 2012 Credit Facility. The amendment did not materially impact the Company's obligations under the Tontine Term Loan.

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 Tontine Capital Overseas Master Fund II, L.P, also a related party. Pursuant to its terms, we were permitted to repay the Tontine Term Loan at any time prior to the maturity date at par, plus accrued interest without penalty within the restrictions of the 2012 Credit Facility. On February 13, 2013, we repaid the remaining \$10,000 of principal on the Tontine Term Loan, plus accrued interest, with existing cash on hand and proceeds from the Wells Fargo Term Loan.

Capital Lease

The Company leases certain equipment under agreements, which are classified as capital leases and included in property, plant and equipment. Amortization of this equipment for the three months ended December 31, 2013 and 2012 was \$22 and \$ 46, respectively, and is included in depreciation expense in the accompanying statements of comprehensive income.

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. If the effect is dilutive, participating securities are included in the computation of basic earnings per share. Our participating securities 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.

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

The following table reconciles the components of the basic and diluted earnings (loss) per share for the three months ended December 31, 2013 and 2012:

	Three Months Ended December 31,	
	2013	2012
Numerator:		
Net earnings from continuing operations attributable to common shareholders	\$ 264	\$ 623
Net earnings from continuing operations attributable to restricted shareholders	1	10
Net earnings from continuing operations	\$ 265	\$ 633
Net loss from discontinued operations attributable to common shareholders	\$ (141)	\$ (123)
Net loss from discontinued operations	\$ (141)	\$ (123)
Net earnings attributable to common shareholders	\$ 123	\$ 500
Net earnings attributable to restricted shareholders	1	10
Net earnings	\$ 124	\$ 510
Denominator:		
Weighted average common shares outstanding basic	17,817,254	14,801,903
Effect of dilutive stock options and non-vested restricted stock	81,578	117,286
Weighted average common and common equivalent shares outstanding diluted	17,898,832	14,919,189
Basic earnings (loss) per share:		
Basic earnings per share from continuing operations	\$ 0.02	\$ 0.04
	\$ (0.01)	\$ (0.01)

Basic loss per share from discontinued operations

Basic earnings per share	\$	0.01	\$	0.03
Diluted earnings (loss) per share:				
Diluted earnings per share from continuing operations	\$	0.02	\$	0.04
Diluted loss per share from discontinued operations	\$	(0.01)	\$	(0.01)
Diluted earnings per share	\$	0.01	\$	0.03

For the three months ended December 31, 2013 and 2012, 150,000 and zero 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.

6. OPERATING SEGMENTS

We manage and measure performance of our business in four distinct operating segments: Communications, Residential, Commercial & Industrial, and Infrastructure Solutions. 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. For a description of our operating segments, please refer to Note 1, *Business Description of the Business*

The accounting policies of the segments are the same as those described in the summary of significant accounting policies in Note 1, *Business* . 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 four operating segments. Management allocates costs between segments for selling, general and administrative expenses and depreciation expense.

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

Segment information for the three months ended December 31, 2013 and 2012 is as follows:

	Three Months Ended December 31, 2013					
	Communication	Residential	Industrial	Solutions	Corporate	Total
Revenues	\$ 24,591	\$ 41,212	\$ 41,230	\$ 13,046	\$	\$ 120,079
Cost of services	20,659	33,794	37,316	10,194		101,963
Gross profit	3,932	7,418	3,914	2,852		18,116
Selling, general and administrative	2,982	6,481	3,480	2,387	2,242	17,572
Loss (gain) on sale of assets		(40)	(4)	3		(41)
Income (loss) from operations	\$ 950	\$ 977	\$ 438	\$ 462	\$ (2,242)	\$ 585
Other data:						
Depreciation and amortization expense	\$ 100	\$ 123	\$ 67	\$ 242	\$ 85	\$ 617
Capital expenditures	7	5	55	54	115	236
Total assets	\$ 22,006	\$ 34,670	\$ 46,372	\$ 27,817	\$ 34,357	\$ 165,222

	Three Months Ended December 31, 2012					
	Communication	Residential	Industrial	Solutions	Corporate	Total
Revenues	\$ 40,119	\$ 36,005	\$ 51,140	\$	\$	\$ 127,264
Cost of services	32,887	29,899	46,498			109,284
Gross profit	7,232	6,106	4,642			17,980
Selling, general and administrative	3,558	5,228	3,736		2,400	14,922
Loss (gain) on sale of assets	1	(9)	(11)			(19)
Income (loss) from operations	\$ 3,673	\$ 887	\$ 917	\$	\$ (2,400)	\$ 3,077
Other data:						
Depreciation and amortization expense	\$ 87	\$ 95	\$ 57	\$	\$ 300	\$ 539
Capital expenditures	41	26	13			80
Total assets	\$ 34,072	\$ 31,914	\$ 54,436	\$	\$ 44,736	\$ 165,158

7. OTHER COMPREHENSIVE INCOME

For the three months ended December 31, 2013, changes in other comprehensive income by component, net of tax, are detailed below, and represent net gains (losses) on our cash flow hedge.

Balance at September 30, 2013	\$ 17
Other comprehensive income before reclassifications	1
Amounts reclassified from accumulated other comprehensive income	(6)
Balance at at December 31, 2013	\$ 12

Amounts reclassified from accumulated other comprehensive income, net of tax, were reported in interest expense in our consolidated statements of comprehensive income.

8. 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.

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

During the three months ended December 31, 2013, we repurchased 33,568 common shares from our employees to satisfy minimum tax withholding requirements upon the vesting of restricted stock issued under the 2006 Equity Incentive Plan. We issued 7,500 shares out of treasury stock under our share-based compensation programs for restricted shares granted.

Restricted Stock

Restricted Stock Awards:

Fiscal Year	Shares Granted	Weighted Average Fair Value at Date of Grant	Shares Vested	Shares Forfeited	Shares Outstanding	Expense recognized through December 31, 2013
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	147,456	78,030		495
2011	320,000	3.39	240,129	73,205	6,666	816
2012	107,500	2.07	69,167		38,333	160
2013	12,500	5.00	4,167		8,333	24
2014	7,500	4.60			7,500	1

During the three months ended December 31, 2013 and 2012, we recognized \$104 and \$91, respectively, in compensation expense related to these restricted stock awards. At December 31, 2013, the unamortized compensation cost related to outstanding unvested restricted stock was \$147. We expect to recognize \$93 of this unamortized compensation expense during the remaining nine months of our 2014 fiscal year and \$54 thereafter. A summary of restricted stock awards for the years ended September 30, 2013 and 2012 and the three months ended December 31, 2013 is provided in the table below:

Three Months Ended December 31,	Years Ended September 30,
2013	2013
	2012

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

Unvested at beginning of year	159,246	257,826	376,200
Granted	7,500	12,500	107,500
Vested	(105,914)	(111,080)	(192,973)
Forfeited			(32,901)
Unvested at end of period	60,832	159,246	257,826

Phantom Stock Units

Phantom stock units (PSUs) are primarily granted to the members of the Board of Directors as part of their overall compensation. These PSUs are paid via unrestricted stock grants to each director upon their departure from the Board of Directors. We record compensation expense for the full value of the grant on the date of grant. For the three months ended December 31, 2013 and 2012, we recognized \$36 and \$36 in compensation expense related to these grants.

From time to time, PSUs are granted to employees. These PSUs are paid via unrestricted stock grants to each employee upon the satisfaction of the grant terms. We record compensation expense for the PSUs granted to employees over the grant vesting period. For the three months ended December 31, 2013 and 2012, we recognized zero and \$363 in compensation expense related to these grants.

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. No options were granted in the three month period ended December 31, 2013. The assumptions used in the fair value method calculation for the years ended 2013 and 2012 are disclosed in the following table:

	Years Ended September 30,	
	2013	2012
Weighted average value per option granted during the period	\$ 3.43	N/A
Dividends (1)	\$	N/A
Stock price volatility (2)	66.6%	N/A
Risk-free rate of return	0.9%	N/A
Option term	10.0 years	N/A
Expected life	6.0 years	N/A
Forfeiture rate (3)	10.0%	N/A

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

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

(3) Based upon the company's historical data.

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. Stock-based compensation expense recognized in the Consolidated Statements of Comprehensive Income is based on awards ultimately expected to vest. 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.

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

	Shares	Weighted Average Exercise Price
Outstanding, September 30, 2011	20,000	\$ 3.24
Options granted		
Exercised		
Forfeited and Cancelled		
Outstanding, September 30, 2012	20,000	\$ 3.24
Options granted	150,000	5.76
Exercised		
Forfeited and Cancelled		
Outstanding, September 30, 2013	170,000	\$ 5.46
Options granted		
Exercised		
Forfeited and Cancelled		
Outstanding, December 31, 2013	170,000	\$ 5.46

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 December 31, 2013:

Exercise Prices	Outstanding as of	Remaining	Exercisable as of		
	December 31, 2013	Contractual Life Years	Weighted-Average Exercise Price	December 31, 2013	Weighted-Average Exercise Price
\$3.24	20,000	7.55	\$ 3.24	13,333	\$ 3.24
\$5.76	150,000	9.33	\$ 5.76		\$
	170,000		\$ 5.46	13,333	\$ 3.24

Our 2011 options vest over a three year period at a rate of one-third per year upon the annual anniversary date of the grant. Our 2013 options cliff vest at the end of a two year period ending at the anniversary date of the grant. All options 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 share. Unexercised stock options expire July 2021 and May 2023.

During the three months ended December 31, 2013 and 2012, we recognized \$62 and \$3, respectively, in compensation expense related to our stock option awards. At December 31, 2013, the unamortized compensation cost related to outstanding unvested stock options was \$317. We expect to recognize \$182 of this unamortized compensation expense during the remaining nine months of our 2014 fiscal year and \$135 thereafter.

The intrinsic value of stock options outstanding and exercisable was \$33 and \$31 at December 31, 2013 and 2012, respectively. The intrinsic value is calculated as the difference between the fair value as of the end of the period and the exercise price of the stock options.

9. SECURITIES AND EQUITY INVESTMENTS*Investment in EnerTech*

In April 2000, we committed to invest up to \$5,000 in EnerTech. As of September 30, 2009, we fulfilled our \$5,000 investment under this commitment. As our investment is 2.21% of the overall ownership in EnerTech at December 31, 2013 and September 30, 2013, we account for this investment using the cost method of accounting. EnerTech's investment portfolio from time to time results in unrealized losses reflecting a possible, other-than-temporary, impairment of our investment. The carrying value of our investment in EnerTech at December 31, 2013 and September 30, 2013 was \$919.

The following table presents the reconciliation of the carrying value and unrealized gains to the fair value of the investment in EnerTech as of December 31, 2013 and September 30, 2013:

	December 31, 2013	September 30, 2013
Carrying value	\$ 919	\$ 919
Unrealized gains	129	138
Fair value	\$ 1,048	\$ 1,057

At each reporting date, the Company performs evaluations of impairment for this investment to determine if any unrealized losses are other-than-temporary. This evaluation considers a number of factors including, but not limited to, the length of time and extent to which the fair value has been less than cost, the financial condition and near term prospects of the issuer and management's ability and intent to hold the securities until fair value recovers. The assessment of the ability and intent to hold these securities to recovery focuses on liquidity needs, asset and liability management objectives and securities portfolio objectives. Based on the results of this evaluation, we believe the unrealized gain at December 31, 2013 indicated our investment was not impaired.

On December 31, 2013, EnerTech's general partner, with the consent of the fund's investors, extended the fund through December 31, 2014. 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, 2015 with the consent of the fund's valuation committee.

Table of Contents

INTEGRATED ELECTRICAL SERVICES, INC.

Notes to Consolidated Financial Statements

(All Amounts in Thousands Except Share Amounts)

10. EMPLOYEE BENEFIT PLANS

401(k) Plan

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 sixty days of service and attaining age twenty-one. Participants become vested in our matching contributions following three years of service. After suspending Company matching under the 401(k) Plan in February 2009, we reinstated the employee match in March of 2013. We recognized \$65, and zero, respectively in matching expenses as of December 31, 2013 and 2012.

Infrastructure Solutions has two 401(k) plans. The first provides for employees covered by collective bargaining agreements and has no provision for employer contributions. The second provides for employees outside collective bargaining agreements and has a provision for employer contributions. We recognized \$19 in matching expense during the three months ended December 31, 2013.

Executive Savings Plan

Under the Executive Deferred Compensation Plan adopted on July 1, 2004 (the Executive Savings 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.

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 a non-current liability 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 \$844 and \$833 recorded as of December 31, 2013 and 2012, respectively.

Multiemployer Pension Plan

Infrastructure Solutions participates in a multiemployer direct benefit pension plan for employees covered under our collective bargaining agreement. We do not administer the plan. We do not significantly participate in this plan. As of December 31, 2012, this plan was funded at 84.9%.

11. FAIR VALUE MEASUREMENTS

Fair Value Measurement Accounting

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.

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

We estimate the fair value of our interest rate swap agreement with Wells Fargo to be \$12 at December 31, 2013, using Level 2 inputs, including an estimated market valuation from Wells Fargo Bank. For additional information, please see Note 15, Derivative Instruments.

We estimate the fair value of the contingent consideration related to the acquisition of certain assets from the Acro Group to be \$30 at December 31, 2013, using Level 3 inputs, including a discounted revenue projection. The fair value of this contingent liability will vary depending on actual revenues earned. For additional information, please see Note 16, Business Combinations Acquisition of Certain Assets from the Acro Group.

We estimate the fair value of our unfavorable MISCOR leases to be \$(461), using Level 2 inputs, including estimated market valuation including market rates from comparable properties. For additional information, please see Note 16, Business Combinations Acquisition of MISCOR.

Financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2013, are summarized in the following table by the type of inputs applicable to the fair value measurements:

	Total Fair Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable (Level 3)
Executive savings plan assets	\$ 619	\$ 619	\$	\$
Executive savings plan liabilities	(506)	(506)		
Interest rate swap agreement	12		12	
Contingent consideration agreement	(30)			(30)
Unfavorable acquired leases	(461)		(461)	
Total	\$ (366)	\$ 113	\$ (449)	\$ (30)

The table below presents a reconciliation of the fair value of our contingent consideration obligation, which uses significant unobservable inputs (Level 3).

Fair Value at September 30, 2013	Contingent Consideration Agreement
	\$ 95

Issuances	
Settlements	
Adjustments to Fair Value	(65)
Fair Value at December 31, 2013	\$ 30

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.

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

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.

12. INVENTORY

Inventories consist of the following components:

	December 31, 2013	September 30, 2013
Raw materials	\$ 2,611	\$ 2,389
Work in process	3,180	3,519
Finished goods	1,368	1,545
Parts and supplies	9,493	12,694
Total inventories	\$ 16,652	\$ 20,147

13. INTANGIBLE ASSETS

Intangible assets consist of the following:

	December 31, 2013			
	Estimated Useful Lives (in Years)	Gross Carrying Amount	Accumulated Amortization	Net
Trademarks/trade names	Indefinite	\$ 1,200	\$	\$ 1,200
Technical library	20	400	6	394
Customer relationships	6.3	2,100	134	1,966
Order backlog	0.4	350	350	
Covenants not to compete	3.0	140	39	101
Developed technology	4.0	400	83	317
Total		\$ 4,590	\$ 612	\$ 3,978

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

Amortization of intangible assets was \$134 for the three months ended December 31, 2013. Our future amortization expense for years ended September 30, is as follows:

Year Ended September 30,	
January 1 - September 30, 2014	\$ 339
2015	499
2016	471
2017	398
2018	358
Thereafter	713
Total	\$ 2,778

Table of Contents

INTEGRATED ELECTRICAL SERVICES, INC.

Notes to Consolidated Financial Statements

(All Amounts in Thousands Except Share Amounts)

14. 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 coverages 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, due to Polychlorinated Biphenyls (PCBs) contamination on and off the site. The subsidiary, which we acquired in January 1999, is believed to have sent transformers to the facility during the 1990s. Based on our investigation to date, there is evidence to support our defense that our subsidiary contributed no PCB contamination to the site.

In April 2009, two 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. The plaintiffs were two of four PRPs that 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 addition to the on-site clean-up, the EPA has selected 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. On January 8, 2013, the EPA held a meeting with those PRPs as well as others that were not recipients of the letter to discuss potential settlement of its costs associated with the site. The Company was invited to attend this meeting and asked to confirm whether it would participate in settlement discussions, which the Company confirmed. The Company intends to present to the EPA the evidence developed in litigation to support the argument that the Company did not contribute PCB contamination to the site. The Company has tendered a demand for indemnification to the former owner of the acquired corporation that may have transacted business with the facility. As of December 31, 2013, 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.

Hamilton Wage and Hour

The Company is a defendant in three wage-and-hour suits seeking class action certification that were filed between August 29, 2012 and June 24, 2013, in the U.S. District Court for the Eastern District of Texas. Each of these cases is among several others filed by Plaintiffs' attorney against contractors working in the Port Arthur, Texas Motiva plant on various projects over the last few years. The claims are based on alleged failure to compensate for time spent bussing to and from the plant, donning safety wear and other activities. It does not appear the Company will face significant exposure for any unpaid wages. In a separate earlier case based on the same allegations, a federal district court ruled that the time spent traveling on the busses is not compensable. On January 11, 2013, the U.S. Court of Appeals for the Fifth Circuit upheld the district court's ruling finding no liability for wages for time spent bussing into the facility, and on October 8, 2013, the U.S. Supreme Court declined to review plaintiffs' appeal of the Fifth Circuit dismissal of their claims for compensation for time spent bussing to the facility, effectively reducing the Company's risk of liability on this issue in its cases. Our investigation indicates that all claims for time spent on other activities either were inapplicable to the Company's employees or took place during times for which the Company's employees were compensated. We have filed responsive pleadings and, following initial discovery, are positioning the cases to obtain a dismissal of all claims. As of December 31, 2013, 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, as well as pollution coverage, 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 December 31, 2013, we had \$4,873 accrued for insurance liabilities. We are also subject to construction defect liabilities, primarily within our Residential segment. As of December 31, 2013, we had \$432 reserved 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 December 31, 2013, \$6,347 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 December 31, 2013, the estimated cost to complete our bonded projects was approximately \$55,195. We evaluate our bonding requirements on a regular basis, including the terms offered by our sureties. 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 December 31, 2013, we had cash totaling \$500 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 2012 Credit

Facility.

On May 7, 2013, the Company and certain of its current and future subsidiaries and affiliates entered into a new agreement of indemnity (the Surety Agreement) with certain entities affiliated with Suremerica Surety Underwriting Services, LLC (Suremerica). Pursuant to the Surety Agreement, we have agreed to assign to Suremerica, among other things, as collateral to secure our obligations under the Surety Agreement, our rights, title and interest in, and all accounts receivable and related proceeds arising pursuant to, any contract bonded by Suremerica on our behalf. Further, under the Surety Agreement, we have also agreed that, upon written demand, we will deposit with Suremerica, as additional collateral, an amount determined by Suremerica to be sufficient to discharge any claim made against Suremerica on a bond issued on our behalf.

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 December 31, 2013, \$313 of our outstanding letters of credit were to collateralize our vendors.

Table of Contents

INTEGRATED ELECTRICAL SERVICES, INC.

Notes to Consolidated Financial Statements

(All Amounts in Thousands Except Share Amounts)

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, and based on subsequent payment defaults, was amended to provide for additional collateral and a total settlement amount of \$2,025 (\$2,200 less the \$175 already received) to be paid in monthly installments beginning September 30, 2012 through July 2014 with an interest rate of 12%. Following a subsequent amendment to postpone or modify payment dates, on January 2, 2013, the Company tendered a notice of default to the surety and its coal mining operations, which had been pledged as additional collateral. Given the surety's failure to make the payments due on December 31, 2012, and January 31, 2013, and its continued attempts to restructure the underlying settlement agreement, the Company concluded the collection of the receivable was not probable as of December 31, 2012, and recorded a reserve in the amount \$1,725 for the first quarter of fiscal 2013, bringing the receivable's net carrying value to zero. The charge was recorded as other expense within our Consolidated Statements of Comprehensive Income and the reserve was recorded within our current assets within the Consolidated Balance Sheet.

On March 8, 2013, the Company issued a notice of acceleration of the promissory notes signed by the two mining companies, and subsequently filed suit to enforce the acceleration and to domesticate the agreed judgment against the surety and its owner in Virginia. Following these actions, the surety entered into an amended agreement with the Company which provided for payment of \$300, which was received on June 24, 2013, and additional monthly installments with final payment due June 30, 2014. As of the filing of this report on Form 10-Q, the Company had received installment payments totaling \$550. The defendants have defaulted on payments due in November 2013, December 2013 and January 2014. The defendants have indicated that they are pursuing financing and expect to become current on all payments due in the near term. In the meantime, the Company expects to reinstate legal actions targeted at recovering the full amount due. The extent of recovery of the remaining balance, if any, cannot be determined. However, the possibility of a partial or full recovery exists, particularly if the defendants are successful in obtaining financing. We have classified the \$550 received as of December 31, 2013 as other income within our Consolidated Statements of Comprehensive Income. Any subsequent recovery will be included in other income.

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 December 31, 2013, we had no such open purchase commitments.

15. DERIVATIVE INSTRUMENTS

On March 1, 2013, we entered into an interest rate swap agreement with Wells Fargo Bank, N.A. in conjunction with our Wells Fargo Term Loan to hedge interest rate risk. Borrowings under the Wells Fargo Term Loan bore interest at a per annum rate equal to Daily Three Month LIBOR plus an applicable margin. Our interest rate swap agreement bears interest of 1.00% less the per annum rate equal to Daily Three Month LIBOR, thus mitigating the interest rate risk associated with the Daily Three Month LIBOR and ensuring a fixed rate for hedged borrowings under the Wells Fargo Term Loan.

Our derivative instrument is held at fair value on our consolidated balance sheet. Related cash flows are recorded as operating activities on the consolidated statement of cash flows. Gains and losses related to this derivative instrument are recognized within other comprehensive income. As of December 31, 2013, the interest rate swap agreement was 100% effective, as interest for both the Wells Fargo Term Loan and interest rate swap agreement were calculated utilizing the Daily Three Month LIBOR rate on the same principal basis.

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

The following table presents the gross fair value of our interest rate swap derivative, and the line items where it appears on our consolidated balance sheet:

	December 31, 2013	September 30, 2013
Assets		
Prepaid expenses and other current assets	\$ 12	\$ 17
Stockholder's equity	\$ 12	\$ 17
Accumulated other comprehensive income		

16. BUSINESS COMBINATION*Acquisition of Certain Assets from the Acro Group*

On February 8, 2013, IES Renewable Energy, LLC (IES Renewable), an indirect wholly-owned subsidiary of the Company, entered into an Asset Purchase Agreement with a group of entities operating under the name of the Acro Group: Residential Renewable Technologies, Inc., Energy Efficiency Solar, Inc. and Lonestar Renewable Technologies Acquisition Corp. (collectively, the Acro Group). Pursuant to the terms of the Asset Purchase Agreement, the Company agreed to acquire certain assets in connection with the Acro Group's turn-key residential solar integration business (the Acquired Assets). The Acquired Assets include, but are not limited to, assets relating to the Acro Group's solar installation sales and marketing platform and the backlog of contracts entered into by the Acro Group with residential solar customers, which provide for the payment of sales and marketing fees in connection with the sale, installation and third-party financing of residential solar equipment. The transaction closed on February 15, 2013 (the Closing Date).

Following consummation of the transaction, IES Residential, Inc. (IES Residential), a wholly-owned subsidiary of the Company, began offering full-service residential solar integration services, including design, procurement, permitting, installation, financing services through third parties and warranty services for residential customers. IES Residential had previously provided solar installation subcontracting services to the Acro Group, and as of February 8, 2013, was owed \$3,800 for subcontracting services provided up to that date (such balance, as of the day prior to the Closing Date, the Accounts Receivable Balance).

Total consideration received by the Acro Group for the Acquired Assets consisted of (i) IES Residential's release of the Accounts Receivable Balance, (ii) payment by IES Renewable to the Acro Group of a percentage of future gross revenue generated from the Acquired Assets in an amount not to exceed \$2,000 over the 12-month period beginning the first full month following the Closing Date, subject to certain reductions as described in the Asset Purchase Agreement, and (iii) \$828 representing amounts paid by IES Residential, to the Acro Group to fund certain of its operating expenses between January 4, 2013 and the Closing Date.

Purchase price and fair value of assets acquired and liabilities assumed

The Company accounted for the transaction under the acquisition method of accounting, which requires recording assets and liabilities at fair value (Level 3). These Level 3 fair value assessments were measured based on a third party valuation, utilizing methodologies including discounted cash flow, replacement cost, and excess earnings. The total purchase price was allocated to the tangible assets and separately identifiable intangible assets acquired and liabilities assumed based on their fair values on the Closing Date.

The valuations were derived based on assumptions made by management. While management believes that its assumptions underlying the valuations are reasonable, different estimates and assumptions could result in different values being assigned to individual assets acquired and liabilities assumed. The fair value of assets acquired and liabilities assumed on the Closing Date is as follows:

IES receivable from the Acro Group as of December 31, 2012 (a)	\$ 2,263
IES deferred cost recorded in connection with transactions with Acro Group between January 1, 2013 and February 15, 2013	1,042
Cash purchase consideration	828
Fair value of contingent consideration (b)	665
Total consideration transferred	\$ 4,798

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

- (a) As of the Closing Date, IES had a receivable from the Acro Group from past transactions between the two companies. This receivable was forgiven by IES as a portion of the consideration paid to acquire the Acro Group assets and liabilities.
- (b) The contingent consideration is based on a formula of the Acro Group's revenue for the first 12 months after February 15, 2013, with a maximum and minimum amount payable by IES.

Total estimate of consideration expected to be transferred	4,798
Fair value of assets acquired and liabilities assumed:	
Trade receivables	\$ 317
Prepaid commissions	46
Inventory	16
Property and equipment	40
Order backlog	350
Covenant not-to-compete	140
Developed technology	400
Vacation payable	(26)
Customer incentive payable	(70)
Deferred revenue	(600)
Goodwill: (c)	\$ 4,185

- (c) The goodwill is attributable to the workforce of the acquired business and other intangibles that do not qualify for separate recognition.

Acquisition of MISCOR

On September 13, 2013 we completed the acquisition of 100% of the voting equity interests of MISCOR Group, Ltd. (MISCOR), a provider of maintenance and repair services including engine parts and components to the industrial and rail services. MISCOR operates in locations in Indiana, Alabama, Ohio, West Virginia, Maryland, and California. Following the consummation of the transaction, MISCOR represents the sole component of our Infrastructure Solutions segment.

Total consideration received by MISCOR shareholders consisted of 2,795,577 shares of IES common stock valued at \$11,853, combined with cash totaling \$4,364.

Purchase price and fair value of assets acquired and liabilities assumed

The Company accounted for the transaction under the acquisition method of accounting, which requires recording assets and liabilities at fair value (Level 3). These Level 3 fair value assessments were measured based on a third party valuation, utilizing methodologies including discounted cash flow, replacement cost, and excess earnings, which are subject to finalization. The total estimated purchase price was allocated to the tangible assets and separately identifiable intangible assets acquired and liabilities assumed based on their preliminary estimated fair values on September 13, 2013.

The valuations derived from estimated fair value assessments and assumptions used by management are preliminary pending finalization of certain intangible asset valuations. While management believes that its preliminary estimates and assumptions underlying the valuations are reasonable, different estimates and assumptions could result in different values being assigned to individual assets acquired and liabilities assumed. This may result in adjustments to the preliminary amounts recorded and goodwill, which could be material. The preliminary valuation of the assets acquired and liabilities assumed as of September 13, 2013 is as follows:

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

IES Common Shares (2,795,577)	\$ 11,853
Cash purchase consideration	4,364
Total consideration transferred	\$ 16,217
Total estimate of consideration expected to be transferred	\$ 16,217
Fair value of assets acquired and liabilities assumed:	
Trade receivables	\$ 4,925
Prepays	532
Inventory	7,530
Property and equipment	5,355
Customer relationships	2,100
Technical library	400
Trade names	1,200
Other assets	552
Trade payables	(4,143)
Accrued liabilities	(2,016)
Term loan	(5,511)
Goodwill: (a)	\$ 5,293

- (a) Although this goodwill is not deductible for tax purposes, we acquired tax basis of \$10.0 million in goodwill and intangible assets recognized by MISCOR prior to our purchase agreement with them. The deferred tax asset associated with the basis is fully offset by a corresponding valuation allowance. No value was assigned in the purchase price allocation above to the original intangible assets recognized by MISCOR prior to our purchase agreement.

Unaudited Pro Forma Information 2013 Acquisitions

The following unaudited supplemental pro forma results of operations include the results of each MISCOR and the assets acquired from the Acro Group acquired during the year ended September 30, 2013, described above as if each had been consolidated as of October 1, 2011, and have been provided for illustrative purposes only and do not purport to be indicative of the actual results that would have been achieved by the combined companies for the periods presented or that may be achieved by the combined companies in the future. Future results may vary significantly from the results reflected in the following pro forma financial information because of future events and transactions, as well as other factors, many of which are beyond IES's control.

The unaudited pro forma financial information reflects certain adjustments related to the acquisition, such as the recording of incremental depreciation expense in connection with fair value adjustments to property and equipment,

incremental amortization expense in connection with recording acquired identifiable intangible assets at fair value, and the elimination of the impact of historical transactions between IES and the Acro Group that would have been treated as intercompany transactions had the companies been consolidated. The unaudited pro forma financial information also includes the effect of certain non-recurring items as of October 1, 2011 such as \$3,034 in acquisition related costs incurred during the year ended September 30, 2013. The unaudited pro forma financial statements include these acquisition related costs as if they had been incurred on October 1, 2011.

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

The supplemental pro forma results of operations for the years ended September 30, 2013 and 2012, as if the assets of Acro Group had been acquired and the acquisition of MISCOR had been completed on October 1, 2011, are as follows:

	Unaudited	
	Three Months Ended	Three Months Ended
	December 31,	December 31,
	2013	2012
Revenues	\$ 120,079	\$ 142,002
Net income from continuing operations	\$ 265	\$ 729

17. DISCONTINUED OPERATIONS

In 2011, we initiated the closure of all or portions of our Commercial & Industrial and Communications facilities in Arizona, Florida, Iowa, Louisiana, Maryland, Massachusetts, Nevada and Texas. These facilities were a key aspect of our commitment to return the Company to profitability and selected based on their current business prospects and the extended time frame needed to return the facilities to a profitable position. From the time of identification through December 31, 2013, we have sub-leased or terminated our lease contracts for leased facilities. We have satisfied substantially all of our contracts through either the subcontracting or self-performance. We have completed the wind down of these facilities as of December 31, 2013. Results from operations of these facilities for the three months ended December 31, 2013 and 2012 are presented in our Consolidated Statements of Comprehensive Income as discontinued operations.

The components of the results of discontinued operations for these facilities are as follows:

	Three Months Ended December 31,	
	2013	2012
Revenues	\$ 58	\$ 516
Cost of services	117	450
Gross profit	(59)	66
Selling, general and administrative	82	161
Restructuring charge		43
Loss from discontinued operations	(141)	(138)
(Benefit) provision for income taxes		(15)

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

Net loss from discontinued operations \$ (141) \$ (123)

Included in the Consolidated Balance Sheets at December 31, 2013 and September 30, 2013 are the following major classes of assets and liabilities associated with discontinued operations:

	December 31, 2013	September 30, 2013
Assets of discontinued operations:		
Current	\$ 714	\$ 1,123
Liabilities of discontinued operations:		
Current	\$ 636	\$ 889

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

The following discussion and analysis should be read in conjunction with our Consolidated Financial Statements and the notes thereto, set forth in Item 8, *Financial Statements and Supplementary Data* of our Annual Report on Form 10-K/A for the year ended September 30, 2013. For additional information, see *Disclosure Regarding Forward Looking Statements* in Part I of our Annual Report on Form 10-K/A for the year ended September 30, 2013.

OVERVIEW**Executive Overview**

Please refer to *Item 1. Business* of our Annual Report on Form 10-K/A for the year ended September 30, 2013 for a discussion of the Company's services and corporate strategy. Integrated Electrical Services, Inc., a Delaware corporation, is a holding company that owns and manages diverse operating subsidiaries, comprised of providers of industrial products and infrastructure services to a variety of end markets. Our operations are currently organized into four principal business segments: Communications, Residential, Commercial & Industrial, and Infrastructure Solutions.

RESULTS OF OPERATIONS

We report our operating results across our four operating segments: Communications, Residential, Commercial & Industrial and Infrastructure Solutions. Expenses associated with our Corporate office are classified as a fifth segment. The following table presents selected historical results of operations of IES. The Infrastructure Solutions segment was added in connection with the acquisition of MISCOR on September 13, 2013.

	Three Months Ended December 31,			
	2013		2012	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Revenues	\$ 120,079	100.0%	\$ 127,264	100.0%
Cost of services	101,963	84.9%	109,284	85.9%
Gross profit	18,116	15.1%	17,980	14.1%
Selling, general and administrative expenses	17,572	14.6%	14,922	11.7%
Gain on sale of assets	(41)	0.0%	(19)	0.0%
Net income from operations	585	0.5%	3,077	2.4%
Interest and other (income) expense, net	321	0.3%	2,329	1.8%
Income from operations before income taxes	264	0.2%	748	0.6%
Provision (benefit) for income taxes	(1)	0.0%	115	0.1%
Net income from continuing operations	265	0.2%	633	0.5%
Net loss from discontinued operations	(141)	(0.1)%	(138)	(0.1)%
(Benefit) provision for income taxes		0.0%	(15)	0.0%

Net loss from discontinued operations	(141)	(0.1)%	(123)	(0.1)%
Net income	\$ 124	0.1%	\$ 510	0.4%

Consolidated revenues for the three months ended December 31, 2013 were \$7.2 million lower than for the three months ended December 31, 2012, a decrease of 5.6%. Revenues decreased at our Communications and Commercial & Industrial segments. These decreases were partly offset by growth within our Residential segment. Additionally, Infrastructure Solutions contributed \$13.0 million in revenues for the three months ended December 31, 2013.

Table of Contents

Our overall gross profit percentage increased to 15.1% during the three months ended December 31, 2013 as compared to 14.1% during the three months ended December 31, 2012. However, the gross profit percentage for our existing businesses, excluding the Infrastructure Services business acquired in September 2013, was comparable with prior year, at 14.0%. Improved gross profit percentages at our Residential and Commercial & Industrial segments largely offset compressed margins at our Communications segment. Our new Infrastructure Solutions business drove the overall increase in gross profit percentage, as it contributed gross profit of \$2.8 million at a 21.2% margin, which included the impact of \$0.4 million of additional cost associated with the sale of inventory that was written up to fair value in purchase accounting upon the acquisition of MISCOR in September of 2013.

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, segment and branch management (including incentive-based compensation), 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 December 31, 2013, our selling, general and administrative expenses were \$17.6 million, an increase of \$2.7 million, or 17.8%, as compared to the three months ended December 31, 2012. The addition of our Infrastructure Solutions business contributed \$2.2 million of the additional cost. The remaining increase primarily resulted from higher personnel and incentive costs directly attributable to increased activity and profitability at our Residential segment, partly offset by lower cost at our Commercial & Industrial segment.

Communications

	Three Months Ended December 31,			
	2013		2012	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Revenue	\$ 24,591	100.0%	\$ 40,119	100.0%
Gross Profit	3,932	16.0%	7,232	18.0%
Selling, general and administrative expenses	2,982	12.1%	3,558	8.9%

Revenue. Our Communications segment revenues decreased by \$15.5 million during the three months ended December 31, 2013, a 38.7% decrease compared to the three months ended December 31, 2012. The decrease is primarily the result of the completion of certain high-tech manufacturing projects performed in the three months ended December 31, 2012, which did not recur in the same period in 2013, as well as the decision of a large customer to procure its own materials to be used in our work, rather than sourcing those materials through us. Revenues from high-tech manufacturing projects were \$3.3 million during the three months ended December 31, 2013, compared to \$11.6 million during the three months ended December 31, 2012. Revenues attributable to data centers were \$7.8 million for the three months ended December 31, 2013 compared to \$13.8 million for the three months ended December 31, 2012.

Gross Profit. Our Communications segment's gross profit during the three months ended December 31, 2013 decreased \$3.3 million, or 45.6%, as compared to the three months ended December 31, 2012. Gross profit as a percentage of revenue decreased 2.0% to 16.0% for the three months ended December 31, 2013, due primarily to the completion of certain high-tech manufacturing projects which were ongoing in the three months ended December 31, 2012, but did not recur in the same period in 2013.

Selling, General and Administrative Expenses. Our Communications segment's selling, general and administrative expenses decreased \$0.6 million, or 16.2%, during the three months ended December 31, 2013 compared to the three months ended December 31, 2012 as a result of decreased incentive compensation associated with lower profitability. Selling, general and administrative expenses as a percentage of revenues in the Communication segment increased 3.2% to 12.1% of segment revenue during the three months ended December 31, 2013 compared to the three months ended December 31, 2012. Although costs were reduced, cost as a percentage of revenue still increased, as revenue declined sharply, and certain of our fixed costs were not reduced.

Table of Contents**Residential**

	Three Months Ended December 31,			
	2013		2012	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Revenue	\$ 41,212	100.0%	\$ 36,005	100.0%
Gross Profit	7,418	18.0%	6,106	17.0%
Selling, general and administrative expenses	6,481	15.7%	5,228	14.5%

Revenue. Our Residential segment revenues increased by \$5.2 million during the three months ended December 31, 2013, an increase of 14.5% as compared to the three months ended December 31, 2012. Revenues for our multi-family construction increased by \$2.3 million during the three months ended December 31, 2013, as overall market conditions have continued to improve. Multi-family construction projects were primarily driven by increased demand for rental housing throughout the regions in which we operate. Single-family construction revenues increased by \$2.6 million, primarily in Texas, where the economy has experienced continued growth and population expansion. Revenue was impacted to a lesser degree by decreases in solar installations and increases in cable and service activity.

Gross Profit. During the three months ended December 31, 2013, our Residential segment experienced a \$1.3 million, or 21.5%, increase in gross profit as compared to the three months ended December 31, 2012. Gross profit increased due to higher volume of both single-family and multi-family projects, offset by lower volume and reduced gross margin percentage in solar projects. Gross margin percentage increased within single-family and multi-family, as demand has increased and copper prices have become more stable. The increased gross profit percentages for both single-family and multi-family were partly offset by higher group medical and other insurance costs.

Selling, General and Administrative Expenses. Our Residential segment experienced a \$1.3 million, or 24.0%, increase in selling, general and administrative expenses during the three months ended December 31, 2013 compared to the three months ended December 31, 2012. Selling, general and administrative expenses as a percentage of revenues in the Residential segment increased 1.2% to 15.7% of segment revenue during the three months ended December 31, 2013. This increase is attributable primarily to the scaling of operations, including increased incentives in both single-family and multi-family divisions during the three months ended December 31, 2013, and was impacted to a lesser degree by administrative expenses for our solar business, which increased subsequent to the February 2013 acquisition of certain assets of the Acro Group. As incentive compensation is based on cash flow, in addition to earnings, expense for the quarter ended December 31, 2013 was higher because of increased earnings as well as the benefit of the timing of working capital changes.

Commercial & Industrial

	Three Months Ended December 31,			
	2013		2012	
	\$	%	\$	%
	(Dollars in thousands, Percentage of revenues)			
Revenue	\$ 41,230	100.0%	\$ 51,140	100.0%
Gross Profit	3,914	9.5%	4,642	9.1%
Selling, general and administrative expenses	3,480	8.4%	3,736	7.3%

Revenue. Revenues in our Commercial & Industrial segment decreased \$9.9 million during the three months ended December 31, 2013, a decrease of 19.4% compared to the three months ended December 31, 2012. Our Commercial & Industrial segment is impacted not only by industry construction trends, but also specific industry and local economic trends. Impacts from these trends on our revenues may be delayed due to the long lead time of our projects. During the three months ended December 31, 2013, our revenue decrease was the result of large commercial projects for which we recognized substantial revenue in the three months ended December 31, 2012, but which are now complete or nearing completion.

Table of Contents

Gross Profit. Our Commercial & Industrial segment's gross profit during the three months ended December 31, 2013 decreased by \$0.7 million, or 15.7%, as compared to the three months ended December 31, 2012. Commercial & Industrial's gross margin percentage increased 0.4% to 9.5% during the three months ended December 31, 2013, primarily as a result of increased productivity. While we have experienced some reprieve in project bid margins on new work, particularly in our industrial branches, the competitive market that has existed during the prolonged recession has continued to constrain significant increases in project bid margins in most commercial markets.

Selling, General and Administrative Expenses. Our Commercial & Industrial segment's selling, general and administrative expenses during the three months ended December 31, 2013 decreased by \$0.3 million, or 6.8%, compared to the three months ended December 31, 2012 as a result of lower compensation expense in connection with lower earnings, as well as a reduction in legal costs. However, selling, general and administrative expenses as a percentage of revenues in the Commercial & Industrial segment increased by 1.1% during the three months ended December 31, 2013. Despite the reduction in cost, cost as a percentage of revenue still increased as revenues declined sharply, and certain fixed costs were not reduced.

Infrastructure Solutions

	Three Months Ended December 31, 2013	
	\$	%
	(Dollars in thousands, Percentage of revenues)	
Revenue	\$ 13,046	100.0%
Gross Profit	2,852	21.9%
Selling, general and administrative expenses	2,387	18.3%

The Infrastructure Solutions segment was added in connection with the acquisition of MISCOR on September 13, 2013. Therefore, our consolidated results of operations do not include results for this segment for the quarter ended December 31, 2012.

Restructuring Charges

In the second quarter of our 2011 fiscal year, we began the 2011 Restructuring Plan that was designed to consolidate operations within our Commercial & Industrial business. Pursuant to the 2011 Restructuring Plan, we planned to either sell or close certain underperforming facilities within our Commercial & Industrial operations. The 2011 Restructuring Plan was a key element of our commitment to return the Company to profitability. The results of operations related to the 2011 Restructuring Plan are included in the net loss from discontinued operations within our Consolidated Statements of Comprehensive Income for the three months ended December 31, 2013 and 2012.

The facilities directly affected by the 2011 Restructuring Plan were in several locations throughout the country, including Arizona, Florida, Iowa, Louisiana, Massachusetts, Nevada and Texas. These facilities were selected due to their business prospects at that time and the extended time frame needed to return the facilities to a profitable position.

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

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

	Three Months Ended December 31,	
	2013	2012
	(In thousands)	
Severance compensation	\$	\$ (62)
Consulting and other charges		1,099
Lease termination costs		133
Total restructuring charges	\$	\$ 1,170

Table of Contents**Interest and Other Expense, net**

	Three Months Ended December 31,	
	2013	2012
	(In thousands)	
Interest expense	\$ 391	\$ 472
Deferred financing charges	127	135
Total interest expense	518	607
Interest income	(1)	(12)
Other (income) expense, net	(197)	1,734
Total interest and other expense, net	\$ 320	\$ 2,329

Interest Expense

During the three months ended December 31, 2013, we incurred interest expense of \$0.5 million primarily comprised of interest expense from the Wells Fargo Term Loan, an average letter of credit balance of \$6.6 million under the 2012 Credit Facility and an average unused line of credit balance of \$23.4 million. This compares to interest expense of \$0.6 million for the three months ended December 31, 2012, on a debt balance primarily comprised of the Tontine Term Loan, an average letter of credit balance of \$8.5 million under the 2006 Credit Facility and an average unused line of credit balance of \$21.5 million.

Interest Income

For the three months ended December 31, 2013 and 2012 we earned interest income of \$1 thousand and \$12 thousand on the average Cash and Cash Equivalents balances of \$16.2 million and \$19.0 million, respectively.

Other (Income) Expense

During the three months ended December 31, 2012, we fully reserved for an outstanding receivable for a settlement agreement with a former surety. The surety has failed to make payments in accordance with the settlement agreement, and has proposed a modified payment structure to satisfy the debt. The Company concluded that collectability was not probable as of December 31, 2012, and has recorded a reserve for the entire balance of \$1.7 million. The reserve was recorded as other expense within our Consolidated Statements of Comprehensive Income. For the three months ended December 31, 2013, we recovered \$0.1 million of this settlement. The recovery was recorded as other income within our Consolidated Statements of Comprehensive Income. Please refer to Note 14, Commitments and Contingencies in the Notes to the Consolidated Financial Statements set forth in Part I, Item 1 of this Quarterly Report on Form 10-Q for additional information.

PROVISION FOR INCOME TAXES

Our provision for income taxes decreased from \$115 thousand for the three months ended December 31, 2012 to a benefit of \$1 thousand for the three months ended December 31, 2013. The decrease is attributable to a decrease in the projected effective tax rate and a reduction in state income tax expense attributable to a previous period.

WORKING CAPITAL

During the three months ended December 31, 2013, working capital increased by \$0.3 million from September 30, 2013, reflecting a \$12.9 million decrease in current assets and a \$13.3 million decrease in current liabilities during the period.

During the three months ended December 31, 2013, our current assets decreased by \$12.9 million, or 9.0%, to \$131.1 million, as compared to \$144.0 million as of September 30, 2013. Cash and cash equivalents decreased by \$3.5 million during the three months ended December 31, 2013 as compared to September 30, 2013. The current trade accounts receivables, net, decreased by \$7.0 million at December 31, 2013, as compared to September 30, 2013. Days sales outstanding (DSOs) decreased to 54 as of December 31, 2013 from 59 as of September 30, 2013. The improvement was driven predominantly by increased collection efforts. While the rate of collections may vary, our secured position, resulting from our ability to secure liens against our customers' overdue receivables, reasonably assures that collection will occur eventually to the extent that our security retains value. Inventory decreased \$3.5 million during the three months ended December 31, 2013 compared to September 30, 2013, due primarily to the timing of materials usage on certain of our Commercial & Industrial jobs.

Table of Contents

During the three months ended December 31, 2013, our total current liabilities decreased by \$13.3 million to \$85.3 million, compared to \$98.6 million as of September 30, 2013. During the three months ended December 31, 2013, accounts payable and accrued expenses decreased \$12.7 million. Billings in excess of costs decreased by \$0.6 million during the three months ended December 31, 2013 compared to September 30, 2013. Finally, current maturities of long-term debt increased by \$0.0 million during the three months ended December 31, 2013.

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.

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 December 31, 2013, the estimated cost to complete our bonded projects was approximately \$55.2 million. 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 December 31, 2013, we utilized \$0.5 million of cash (as is included in *Other Non-Current Assets* in our Consolidated Balance Sheet) as collateral for certain of our previous bonding programs.

The 2012 Revolving Credit Facility

On August 9, 2012, we entered into a Credit and Security Agreement (the *Credit Agreement*), for a \$30.0 million revolving credit facility (the *2012 Credit Facility*) with Wells Fargo Bank, National Association (*Wells Fargo*) with a maturity date of August 9, 2015, unless earlier terminated. We have subsequently entered into two amendments to the 2012 Credit Facility. On February 12, 2013, we entered into an amendment of our 2012 Credit Facility (the *Amendment*), extending the terms to August 9, 2016, adding IES Renewable Energy, LLC as a borrower, and providing for a term loan (the *Wells Fargo Term Loan*). On September 13, 2013, we entered into an amendment of the 2012 Credit Facility (the *Second Amendment*) in connection with the acquisition of MISCOR, increased our total Wells Fargo Term Loan by \$10.2 million to \$13.7 million, removed the requirement to cash collateralize our outstanding letters of credit, and added IES Subsidiary Holdings Inc., Magnetech Industrial Services, Inc., and HK Engine Components LLC, as borrowers.

The 2012 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 2012 Credit Facility also restricts us from paying cash dividends and places limitations on our ability to repurchase our common stock.

The 2012 Credit Facility contains customary affirmative, negative and financial covenants. The 2012 Credit Facility requires that we maintain a fixed charge coverage ratio of not less than 1.0:1.0 at any time that our Liquidity (the aggregate amount of unrestricted cash and cash equivalents on hand plus Excess Availability) or Excess Availability fall below the level stipulated within the 2012 Credit Facility, the First Amendment, and Second Amendment. The Second Amendment provided for tiered thresholds. Through December 31, 2013, our Liquidity could not fall below \$15.0 million. Thereafter, our Liquidity must not fall below \$20.0 million. Our Excess Availability must not fall below \$4.0 million through September 30, 2013. This minimum threshold increases by \$0.3 million monthly through December 31, 2013, at which time and thereafter, our Excess Availability must not fall below \$5.0 million. As of December 31, 2013, our Liquidity was in excess of \$15.0 million and Excess Availability was in excess of \$4.0 million; had we not met these thresholds at December 31, 2013, we would not have met the required 1.0:1.0 fixed charge coverage ratio test.

Table of Contents

Borrowings under the 2012 Credit Facility may not exceed a borrowing base that is determined monthly by our lenders based on available collateral, primarily certain accounts receivables, inventories and personal property and equipment. Under the terms of the 2012 Credit Facility, amounts outstanding bear interest at a per annum rate equal to a Daily Three Month LIBOR (as defined in the Credit Agreement), plus an interest rate margin, which is determined quarterly.

In addition, we are charged monthly in arrears for (1) an unused commitment fee of 0.50% per annum, (2) a collateral monitoring fee ranging from \$1 thousand to \$2 thousand, based on the then-applicable interest rate margin, (3) a letter of credit fee based on the then-applicable interest rate margin and (4) certain other fees and charges as specified in the Credit Agreement.

At December 31, 2013, we had \$5.8 million available to us under the 2012 Credit Facility, \$6.7 million in outstanding letters of credit with Wells Fargo and no outstanding borrowings.

The Second Amendment to the 2012 Credit Facility increased our total Wells Fargo Term Loan by \$10.2 million to \$13.7 million. The Wells Fargo Term Loan is payable in equal monthly installments of \$0.3 million through August 9, 2016, with the residual unpaid principal balance due on that date. The Second Amendment also extended the terms, and reduced the annual interest rate to 5% plus 3 Month LIBOR, through September 13, 2014. Following that time, the Wells Fargo Term Loan amounts outstanding bear interest at a per annum rate equal to a Daily Three Month LIBOR plus an interest rate margin, which is determined quarterly.

The Tontine Term Loan

On December 12, 2007, we entered into the Tontine Term Loan, a \$25 million senior subordinated loan agreement, with Tontine, which the Company terminated and prepaid in full subsequent to the first quarter of fiscal 2013, as further described below.

The Tontine Term Loan bore interest at 11.0% per annum and was due on May 15, 2013. Interest was payable quarterly in cash or in-kind at our option. Any interest paid in-kind would bear interest at 11.0% in addition to the loan principal. The Tontine Term Loan was subordinated to the 2012 Credit Facility. The Tontine Term Loan was an unsecured obligation of the Company and its subsidiary borrowers and contained no financial covenants or restrictions on dividends or distributions to stockholders. The Tontine Term Loan was amended on August 9, 2012 in connection with the Company entering into the 2012 Credit Facility. The amendment did not materially impact the Company's obligations under the Tontine Term Loan.

On April 30, 2010, we prepaid \$15 million of principal on the Tontine Term Loan. On May 1, 2010, Tontine assigned the Tontine Term Loan to Tontine Capital Overseas Master Fund II, L.P, also a related party. Pursuant to its terms, we were permitted to repay the Tontine Term Loan at any time prior to the maturity date at par, plus accrued interest without penalty within the restrictions of the 2012 Credit Facility. On February 13, 2013, we repaid the remaining \$10 million of principal on the Tontine Term Loan, plus accrued interest, with existing cash on hand and proceeds from the Wells Fargo Term Loan.

Capital Lease

The Company leases certain equipment under agreements, which are classified as capital leases and included in property, plant and equipment. We recognized amortization expense of \$22 thousand and \$46 thousand during the three months ended December 31, 2013 and 2012, respectively. These amounts are included in depreciation expense in the accompanying statements of comprehensive income.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2013, we had cash and cash equivalents of \$17.3 million, working capital of \$45.8 million, and \$6.7 million of letters of credit outstanding under our 2012 Credit Facility. We anticipate that the combination of cash on hand, cash flows and available capacity under our 2012 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 2012 Credit Facility, if needed. We were not required to test our covenants under our 2012 Credit Facility during the period. Had we been required to test our covenants, we would have failed at December 31, 2013.

Table of Contents

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 cyclicity, 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 \$2.2 million during the three months ended December 31, 2013, as compared to \$3.3 million of net cash provided in the three months ended December 31, 2012. We used substantially more cash to reduce our accounts payable and accrued expenses in three months ended December 31, 2013 as compared to three months ended December 31, 2012.

Investing Activities

In the three months ended December 31, 2013, net cash used in investing activities was \$0.3 million as compared to \$0.4 million in the three months ended December 31, 2012. Expenditures in both periods relate to the purchase of property and equipment.

Financing Activities

Financing activities used net cash of \$1.0 million in the three months ended December 31, 2013 compared to \$0.8 million used in the three months ended December 31, 2012. Financing activities for the three months ended December 31, 2013 included \$0.9 million in payments on our Wells Fargo Term Loan and \$0.1 million for the repurchase of common stock to satisfy payroll tax obligations. Financing activities in the three months ended December 31, 2012 included an increase of \$0.4 million in restricted cash to satisfy the requirements of our 2012 Credit Facility. This requirement was removed in 2013, reducing the restricted cash balance to zero. Financing activities in the three months ended December 31, 2012 also included \$0.4 million for the repurchase of common stock to satisfy payroll tax obligations.

Bonding Capacity

At December 31, 2013, we had adequate surety bonding capacity under our surety agreements. Our ability to access this bonding capacity is at the sole discretion of our surety providers. As of December 31, 2013, the expected cumulative cost to complete for projects covered by our surety providers was \$49.2 million. We believe we have adequate remaining available bonding capacity to meet our current needs, subject to the sole discretion of our surety providers. For additional information, please refer to Note 14, *Commitments and Contingencies - Surety* in the notes to our Consolidated Financial Statements.

CONTROLLING SHAREHOLDER

On September 13, 2013, Tontine filed an amended Schedule 13D indicating its ownership level of 58% of the Company's outstanding common stock. While Tontine is subject to restrictions under federal securities laws on sales of its shares as an affiliate, on February 20, 2013, pursuant to a Registration Rights Agreement, Tontine delivered a

request to the Company for registration of all of its shares of IES common stock, and on February 21, 2013, the Company filed a shelf registration statement (as amended, the Shelf Registration Statement) to register Tontine s shares. The Shelf Registration Statement was declared effective by the SEC on June 18, 2013. As long as the Shelf Registration Statement remains effective, Tontine will have the ability to resell any or all of its shares from time to time in one or more offerings, as described in the Shelf Registration Statement and in any prospectus supplement filed in connection with an offering pursuant to the Shelf Registration Statement.

Should Tontine sell, exchange, or otherwise dispose of all or a portion of its position in IES, a change in ownership could 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. As of December 31, 2013 we have approximately \$466 million of federal NOLs that are available to use to offset taxable income, inclusive of NOLs from the amortization of additional tax goodwill. As of December 31, 2013 we had approximately \$315 million of federal NOLs that are available to use to offset taxable income, exclusive of NOLs from the amortization of additional tax goodwill. On January 28, 2013, the Company implemented a tax benefit protection plan (the NOL Rights Plan) that was designed to deter an acquisition of the Company s stock in excess of a threshold amount that could trigger a change of control within the meaning of Internal Revenue Code Section 382. The NOL Rights Plan was filed as an Exhibit to our Current Report on Form 8-K filed with the SEC on January 28, 2013 and any description thereof is qualified in its entirety by the

Table of Contents

terms of the NOL Rights Plan. There can be no assurance that the NOL Rights Plan will be effective in deterring a change of control or protecting or realizing the NOLs. Furthermore, a change in control would trigger the change of control provisions in a number of our material agreements, including our 2012 Credit Facility, bonding agreements with our sureties and our executive severance plan.

On April 30, 2010, we prepaid \$15.0 million of the original \$25.0 million principal outstanding on the Tontine Term Loan; accordingly at September 30, 2012, \$10.0 million remained outstanding under the Tontine Term Loan, which was scheduled to mature on May 15, 2013. On February 13, 2013, we repaid the remaining \$10.0 million of principal on the Tontine Term Loan, plus accrued interest, with existing cash on hand and proceeds from the Wells Fargo Term Loan. Pursuant to its terms, we were permitted to repay the Tontine Term Loan at any time prior to the maturity date at par, plus accrued interest without penalty within the restrictions of the 2012 Credit Facility.

On September 13, 2013, the Company completed the acquisition of MISCOR. As of July 24, 2013, Tontine beneficially owned 49.9% of the issued and outstanding shares of MISCOR common stock. Given Tontine's significant holdings in both the Company and MISCOR, only the disinterested members of the IES Board of Directors voted on, and unanimously approved, the Merger Agreement. In addition, MISCOR established a special committee of independent directors that voted on and approved the Merger Agreement and recommended approval of the Merger Agreement by the MISCOR full board of directors. After receiving approval from the special committee, the disinterested members of the MISCOR board of directors unanimously approved the Merger Agreement. In connection with the merger, Tontine elected to receive stock consideration in exchange for 100% of its shares of MISCOR common stock tendered pursuant to the merger, such that, according to its amended Schedule 13D filed on September 13, 2013, its ownership of IES common stock increased from approximately 56.7% immediately prior to the merger to approximately 58.0% immediately following the merger.

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 thousand. The lease has terms at market rates and payments by the Company are at a rate consistent with that paid by Tontine Associates, LLC to its landlord.

James M. Lindstrom has served as Chief Executive Officer and President of the Company since October 3, 2011. 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.

David B. Gendell has served as a member of the Company's Board of Directors since February 2012. Mr. Gendell, who is the brother of Jeffrey Gendell, the founder and managing member of Tontine, is also an employee of Tontine.

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 when 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 December 31, 2013, \$0.3 million of our outstanding letters of credit were 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 December 31, 2013, \$6.3 million of our outstanding letters of credit were to collateralize our insurance programs.

Table of Contents

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 December 31, 2013, 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 December 31, 2013, 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	\$ 2,625	\$ 10,208	\$	\$	\$ 12,833
Operating lease obligations	4,060	6,736	1,956	278	13,030
Capital lease obligations	27	1,780			1,807
Total	\$ 6,712	\$ 18,724	\$ 1,956	\$ 278	\$ 27,670

(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.

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

	2014	2015	2016	Thereafter	Total
Standby letters of credit	\$ 6,660	\$	\$	\$	\$ 6,660
Other commitments					
Total	\$ 6,660	\$	\$	\$	\$ 6,660

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 2012 Credit Facility and the Wells Fargo Term Loan. For additional information see *Disclosure Regarding Forward-Looking Statements* in Part I of this Quarterly Report on 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. 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 subject to interest rate risk on our floating interest rate borrowings. Floating rate debt, where the interest rate fluctuates periodically, exposes us to short-term changes in market interest rates.

While all of the long-term debt outstanding under our 2012 Credit Facility is structured on floating interest rate terms, approximately 77% of our long-term debt outstanding as of December 31, 2013 was effectively subject to fully floating interest rate terms after giving effect to our interest rate hedging arrangement. A one percentage point increase in the interest rates on our long-term debt outstanding under our 2012 Credit Facility as of December 31, 2013 would cause a \$0.1 million pre-tax annual increase in interest expense.

Item 4. Controls and Procedures

Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting that occurred during the three months ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Disclosure Controls and Procedures

In accordance with Exchange Act Rule 13a-15 and 15d-15, we carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2013 to provide reasonable assurance that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Our disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

PART II. OTHER INFORMATION

Item 1. *Legal Proceedings*

For further information regarding legal proceedings, see Note 14, *Commitments and Contingencies - Legal Matters* in the notes to our Consolidated Financial Statements, which is incorporated herein by reference.

Table of Contents

Item 1A. Risk Factors

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, 2013.

Table of Contents

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

None.

Item 3. *Defaults Upon Senior Securities*

None.

Item 4. *Mine Safety Disclosures*

None.

Item 5. *Other Information*

None.

Item 6. *Exhibits and Financial Statement Schedules*

(a) Financial Statements and Supplementary Data, Financial Statement Schedules and Exhibits
See Index to Financial Statements under Item 8, *Financial Statements and Supplementary Data* of this Form 10-Q.

(b) Exhibits

**Exhibit
No.**

Description

- | | |
|-----|---|
| 2.1 | Agreement and Plan of Merger effective as of March 13, 2013, by and among Integrated Electrical Services, Inc., IES Subsidiary Holdings, Inc. and MISCOR Group, Ltd. (Attached as part of Annex A to the joint proxy statement/prospectus that is part of this Registration Statement) (the schedules and annexes have been omitted pursuant to Item 601(b)(2) of Regulation S-K) |
| 2.2 | First Amendment to Agreement and Plan of Merger, dated as of July 10, 2013, by and among Integrated Electrical Services, Inc., IES Subsidiary Holdings, Inc. and MISCOR Group, Ltd. (Attached as part of Annex A to the joint proxy statement/prospectus that is part of this Registration Statement) |
| 2.3 | Asset Purchase Agreement, dated February 8, 2013, by and among IES Renewable Energy, LLC, Residential Renewable Energy Technologies, Inc., Energy Efficiency Solar, Inc., and Lonestar Renewable Technologies Acquisition Corp. (Incorporated by reference to Exhibit 2.1 to the Company's Quarterly Report on Form 10-Q filed on February 14, 2013) (the schedules and annexes have been omitted pursuant to Item 601(b)(2) of Regulation S-K) |
| 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 Certificate of Designations of Series A Junior Participating Preferred Stock (Incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on January 28, 2013)

Table of Contents

3.3	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)
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)
(1)101.INS	XBRL Instance Document
(1)101.SCH	XBRL Schema Document
(1)101.LAB	XBRL Label Linkbase Document
(1)101.PRE	XBRL Presentation Linkbase Document
(1)101.DEF	XBRL Definition Linkbase Document
(1)101.CAL	XBRL Calculation Linkbase Document

(1) Filed 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 on February 10, 2014.

INTEGRATED ELECTRICAL SERVICES, INC.

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