GULF ISLAND FABRICATION INC
Form 10-Q
July 29, 2014
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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 June 30, 2014

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 001-34279

GULF ISLAND FABRICATION, INC.

(Exact name of registrant as specified in its charter)

LOUISIANA	**72-1147390**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

16225 PARK TEN PLACE, SUITE 280

HOUSTON, TEXAS	**77084**
(Address of principal executive offices)	**(Zip Code)**

(713) 714-6100

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x 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 x 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 definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer x
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 x

The number of shares of the registrant s common stock, no par value per share, outstanding as of July 29, 2014 was 14,504,978.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

GULF ISLAND FABRICATION, INC.

CONSOLIDATED BALANCE SHEETS

	June 30, 2014 (Unaudited)	December 31, 2013 (Note 1)
	(in thousands)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 31,367	$ 36,569
Contracts receivable, net	64,476	98,579
Contract retainage	117	111
Costs and estimated earnings in excess of billings on uncompleted contracts	17,564	24,727
Prepaid expenses and other	4,116	4,862
Inventory	10,787	11,329
Deferred tax assets	3,695	9,927
Income tax receivable	1,559	1,365
Assets held for sale	13,527	14,527
Total current assets	147,208	201,996
Property, plant and equipment, net	231,930	223,555
Other assets	676	683
Total assets	$ 379,814	$ 426,234
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 32,623	$ 66,054
Billings in excess of costs and estimated earnings on uncompleted contracts	19,561	35,006
Accrued employee costs	7,281	7,516
Accrued expenses	3,107	3,699
Total current liabilities	62,572	112,275
Deferred tax liabilities	36,211	38,397
Total liabilities	98,783	150,672
Shareholders equity:		
Preferred stock, no par value, 5,000,000 shares authorized, no shares issued and outstanding		
	10,067	10,012

Common stock, no par value, 20,000,000 shares authorized, 14,504,978 issued and oustanding at June 30, 2014 and 14,493,748 at December 31, 2013, respectively		
Additional paid-in capital	93,625	93,125
Retained earnings	177,339	172,425
Total shareholders equity	281,031	275,562
Total liabilities and shareholders equity	$ 379,814	$ 426,234

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

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GULF ISLAND FABRICATION, INC.

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Revenue	$ 129,169	$ 154,575	$ 263,859	$ 304,997
Cost of revenue	118,847	144,898	244,764	288,616
Gross profit	10,322	9,677	19,095	16,381
General and administrative expenses	3,873	2,853	7,246	5,208
Operating income	6,449	6,824	11,849	11,173
Other income (expense):				
Interest expense	(25)	(60)	(49)	(124)
Interest income	2		5	1
Other income (expense)	8	(43)	(96)	(43)
	(15)	(103)	(140)	(166)
Income before income taxes	6,434	6,721	11,709	11,007
Income taxes	2,124	2,442	3,864	3,941
Net income	$ 4,310	$ 4,279	$ 7,845	$ 7,066
Per share data:				
Basic earnings per share common shareholders	$ 0.30	$ 0.30	$ 0.54	$ 0.49
Diluted earnings per share common shareholders	$ 0.30	$ 0.30	$ 0.54	$ 0.49
Weighted-average shares	14,500	14,457	14,498	14,456
Effect of dilutive securities: employee stock options		3		3
Adjusted weighted-average shares	14,500	14,460	14,498	14,459
Cash dividend declared per common share	$ 0.10	$ 0.10	$ 0.20	$ 0.20

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

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GULF ISLAND FABRICATION, INC.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY (UNAUDITED)

	Common Stock		Additional Paid-In	Retained	Total Shareholders
	Shares	Amount	Capital	Earnings	Equity
		(in thousands, except share data)			
Balance at January 1, 2014	14,493,748	$ 10,012	$ 93,125	$ 172,425	$ 275,562
Net income				7,845	7,845
Vesting of restricted stock	11,230	(9)	(88)		(97)
Compensation expense restricted stock		64	588		652
Dividends on common stock				(2,931)	(2,931)
Balance at June 30, 2014	14,504,978	$ 10,067	$ 93,625	$ 177,339	$ 281,031

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

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GULF ISLAND FABRICATION, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six Months Ended June 30,	
	2014	2013
	(in thousands)	
Cash flows from operating activities:		
Net income	$ 7,845	$ 7,066
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	12,958	12,376
Loss on sale of asset	85	
Deferred income taxes	4,046	4,323
Compensation expense restricted stock	652	341
Changes in operating assets and liabilities:		
Contracts receivable and retainage	34,097	(29,263)
Costs and estimated earnings in excess of billings on uncompleted contracts	7,163	(10,565)
Prepaid expenses and other assets	746	(2,091)
Inventory	542	(110)
Accounts payable	(33,431)	18,415
Billings in excess of costs and estimated earnings on uncompleted contracts	(15,445)	14,385
Accrued employee costs	(334)	2,173
Accrued expenses	(592)	(2,040)
Current income taxes	(194)	170
Net cash provided by operating activities	18,138	15,180
Cash flows from investing activities:		
Capital expenditures, net	(21,334)	(7,431)
Proceeds on the sale of equipment	925	
Net cash used in investing activities	(20,409)	(7,431)
Cash flows from financing activities:		
Borrowings against line of credit	22,000	26,000
Payments on line of credit	(22,000)	(26,000)
Payments of dividends on common stock	(2,931)	(2,919)
Net cash used in financing activities	(2,931)	(2,919)
Net change in cash and cash equivalents	(5,202)	4,830
Cash and cash equivalents at beginning of period	36,569	24,888
Cash and cash equivalents at end of period	$ 31,367	$ 29,718

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

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GULF ISLAND FABRICATION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

FOR THE THREE MONTH AND SIX-MONTH

PERIODS ENDED JUNE 30, 2014 AND 2013

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Gulf Island Fabrication, Inc., together with its subsidiaries (the Company , we or our), is a leading fabricator of offshore drilling and production platforms and other specialized structures. The Company s principal corporate office is located in Houston, Texas and its fabrication facilities are location in Houma, Louisiana and San Patricio County, Texas. The Company s principal markets are concentrated in the offshore regions and along the coast of the Gulf of Mexico. The consolidated financial statements include the accounts of Gulf Island Fabrication, Inc. and its majority owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Gulf Island Fabrication, Inc. (Gulf Island, we, our or the Company) serves as a holding company and conducts all o its operations through its subsidiaries, which include Gulf Island, L.L.C. (Gulf Island) and Gulf Marine Fabricators, L.P. (Gulf Marine) both of which perform fabrication of offshore drilling and production platforms and other specialized structures used in the development and production of oil and gas reserves Gulf Island Marine Fabricators, L.L.C. (Gulf Island Marine), which performs marine fabrication and construction services), Dolphin Services, L.L.C. (Dolphin Services), which performs offshore and onshore fabrication and construction services, Dolphin Steel Sales, L.L.C. (Dolphin Steel Sales), which sells steel plate and other steel products and Gulf Island Resources, L.L.C. (Gulf Island Resources), which hires laborers with similar rates and terms as those provided by contract labor service companies.

Structures and equipment fabricated by us include: jackets and deck sections of fixed production platforms; hull, tendon, and/or deck sections of floating production platforms (such as TLPs , SPARs , FPSOs and MinDOCs); piles wellhead protectors; subsea templates; various production, compressor and utility modules; offshore living quarters; towboats, offshore support vessels, dry docks, liftboats, tanks and barges. The Company also provides offshore interconnect pipe hook-up, inshore marine construction, manufacture and repair of pressure vessels, heavy lifts such as ship integration and TLP module integration, loading and offloading of jack-up drilling rigs, semi-submersible drilling rigs, TLPs, SPARs or other similar cargo, onshore and offshore scaffolding, piping insulation services, and steel warehousing and sales. For definitions of certain technical terms contained in this Form 10-Q, see the Glossary of Certain Technical Terms contained in our Annual Report on Form 10-K for the year ended December 31, 2013.

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information, the instructions to Form 10-Q, and Article 10 of Regulation S-X. Accordingly, the consolidated financial statements do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Cash flows from operating activities for accrued contract losses and prepaid subcontractor costs in the consolidated statement of cash flows for the six-month period ended June 30, 2013 has been reclassified to conform to the June 30, 2014 presentation. Operating results for the three and six-month periods ended June 30, 2014 are not necessarily indicative of the results that may be expected for the year ended December 31, 2014.

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The balance sheet at December 31, 2013 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements.

For further information, refer to the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2013.

NOTE 2 CONTRACTS RECEIVABLE AND RETAINAGE

The principal customers of the Company include major and large independent oil and gas companies, marine companies, and their contractors. Of our contracts receivable balance at June 30, 2014, $45.2 million, or 70.1%, is with three customers. The significant projects for these three customers consist of a deepwater hull for one customer, two separate projects with fabrication and installation of offshore skids for a second customer, and jackets, piles, and topsides for a deepwater Gulf of Mexico project for a third customer.

At June 30, 2014, the Company s contracts receivable balance included a reserve for bad debt in the amount of $0.9 million, recorded in the third quarter 2013 in connection with a vessel upgrade and outfitting project.

NOTE 3 ASSETS HELD FOR SALE

On July 13, 2012, we received notice from our customer, Bluewater Industries, requesting (i) a slowdown of work on ATP Oil & Gas (UK) Limited s Cheviot project, and (ii) an amendment to the scheduled payment terms under the original contract. On August 16, 2012, we entered into a binding agreement with Bluewater, an engineering consulting firm engaged by ATP UK to oversee the fabrication of the Cheviot project, to amend and restate the original contract and suspend the project. We also entered into a security agreement with Bluewater pursuant to which Bluewater granted us a security interest in certain of its equipment.

As of December 31, 2012, $56.8 million had been billed on the Cheviot project and the outstanding balance was approximately $31.3 million. We recorded a $14.5 million reserve on the balance as of December 31, 2012. All installments under the agreement were paid through February 28, 2013; however the remaining balance of $30.9 million was not paid on or before March 31, 2013, triggering a default by our customer. As of April 1, 2013, the agreement terminated and we initiated action to enforce our rights under the security agreement.

As of June 30, 2013, the carrying amount of assets and liabilities relating to the project was reclassified as held for sale in our consolidated balance sheet, resulting in a non-cash change in contract receivables, billings in excess of cost and estimated earnings on uncompleted contracts, and assets held for sale. There was no additional loss recorded in connection with the non-cash reclassification.

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Assets held for sale are required to be measured at the lower of their carrying amount or fair value less cost to sell. Management determined fair value with the assistance of third party valuation specialists, assuming the sale of the underlying assets individually or in the aggregate to a willing market participant, including normal ownership risks assumed by the purchaser, and the sale of certain components at scrap value. We estimated fair value relying primarily on the cost approach and applied the market approach where comparable sales transaction information was readily available. The cost approach is based on current replacement or reproduction costs of the subject assets less depreciation attributable to physical, functional, and economic factors. The market approach involves gathering data on sales and offerings of similar assets in order to value the subject assets. This approach also includes an assumption for the measurement of the loss in value from physical, functional, and economic factors. The fair value of assets held for sale represent Level 3 fair value measurements (as defined by GAAP), based primarily on the limited availability of market pricing information for either identical or similar items. As of June 30, 2014, management estimates that the fair value of these assets held for sale was $13.5 million.

During the first quarter, 2014, we entered into an agreement with the manufacturer of certain equipment, representing approximately 50% of the fair value of assets held for sale, whereby the manufacturer agreed to assist with restoration and marketing efforts, in return for a percentage of the sale proceeds.

To date, we have not sold, licensed, or leased any of the equipment subject to the security agreement; however, we continue to actively market the equipment, and believe that the fair value of the assets is recoverable through the eventual disposition of project deliverables and the enforcement of our security interest in Bluewater s equipment. However, the ultimate amount we are able to recover for these assets is dependent upon various factors such as our ability to enforce our security interest over all of the deliverables and equipment, as well as market interest in the project deliverables and equipment, which may change in the future. The timing of any sales we are able to consummate and the price we are able to obtain may result in a revision to the recorded fair value amount of any remaining assets held for sale.

NOTE 4 LINE OF CREDIT

The Company has a credit agreement with Whitney Bank and JPMorgan Chase Bank, N.A. (as amended, the Credit Agreement) that provides the Company with an $80 million revolving credit facility (the Credit Facility). The Credit Agreement also allows the Company to use up to the full amount of the available borrowing base for letters of credit and matures on December 31, 2014. We intend to renew the Credit Facility prior to its expiration.

The Credit Facility is secured by substantially all of our assets other than real property located in the state of Louisiana. Amounts borrowed under the Credit Facility bear interest, at our option, at either the prime lending rate established by JPMorgan Chase Bank, N.A. or LIBOR plus 1.5 percent. We pay a fee on a quarterly basis of one-fourth of one percent per annum on the weighted-average unused portion of the Credit Facility.

At June 30, 2014, no amounts were outstanding under the Credit Facility, and we had outstanding letters of credit totaling $47.8 million, reducing the unused portion of our revolving credit facility to $32.2 million. We are required to maintain certain financial covenants, including a minimum current ratio of 1.25 to 1, a net worth minimum requirement of $250.3 million, debt to net worth ratio of 0.5 to 1, and earnings before interest, taxes, depreciation and amortization (EBITDA) to interest expense ratio of 4.0 to 1. As of June 30, 2014, we were in compliance with all covenants.

NOTE 5 CONTRACT COSTS

We define pass-through costs as material, freight, equipment rental, and sub-contractor services included in the direct costs of revenue associated with projects.

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The Company uses the percentage-of-completion accounting method for fabrication contracts. Revenue from fixed-price or unit rate contracts is recognized on the percentage-of-completion method, computed by the efforts-expended method which measures the percentage of labor hours incurred to date as compared to estimated total labor hours to complete each contract. This progress percentage is applied to our estimate of total anticipated gross profit for each contract to determine gross profit earned to date. Revenue recognized in a period for a contract is the amount of gross profit recognized for that period plus pass-through costs incurred on the contract during the period. Consequently, pass-through costs are included in revenue but have no impact in the determination of gross profit for a particular period.

Pass-through costs as a percentage of revenue were 50.9% and 53.1% for the three-month periods ended June 30, 2014 and 2013, respectively. Pass-through costs as a percentage of revenue were 50.1% and 54.7% for the six-month periods ended June 30, 2014 and 2013, respectively.