MCGRATH RENTCORP
Form 10-Q
July 30, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2015

Commission file number 0-13292

McGRATH RENTCORP

(Exact name of registrant as specified in its Charter)

California	94-2579843
(State or other jurisdiction	(I.R.S. Employer
of incorporation or organization)	Identification No.)

5700 Las Positas Road, Livermore, CA 94551-7800

(Address of principal executive offices)

Registrant's telephone number: (925) 606-9200

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 definition of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one).

Large accelerated filer x	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 x

As of July 29, 2015, 25,814,394 shares of Registrant’s Common Stock were outstanding.

FORWARD LOOKING STATEMENTS

Statements contained in this Quarterly Report on Form 10-Q (this "Form 10-Q") which are not historical facts are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. All statements, other than statements of historical facts, regarding McGrath RentCorp's (the "Company's") business strategy, future operations, financial position, estimated revenues or losses, projected costs, prospects, plans and objectives are forward-looking statements. These forward-looking statements appear in a number of places and can be identified by the use of forward-looking terminology such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "future," "intend," "hopes" or "certain" or the negative of these terms or other variations or comparable terminology.

Management cautions that forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties that could cause our actual results to differ materially from those projected in such forward-looking statements. Further, our future business, financial condition and results of operations could differ materially from those anticipated by such forward-looking statements and are subject to risks and uncertainties as set forth under "Risk Factors" in this form 10-Q.

Forward-looking statements are made only as of the date of this Form 10-Q and are based on management's reasonable assumptions, however these assumptions can be wrong or affected by known or unknown risks and uncertainties. No forward-looking statement can be guaranteed and subsequent facts or circumstances may contradict, obviate, undermine or otherwise fail to support or substantiate such statements. Readers should not place undue reliance on these forward-looking statements and are cautioned that any such forward-looking statements are not guarantees of future performance. Except as otherwise required by law, we are under no duty to update any of the forward-looking statements after the date of this Form 10-Q to conform such statements to actual results or to changes in our expectations.

Part I - Financial Information

Item 1. Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders

McGrath RentCorp

We have reviewed the accompanying condensed consolidated balance sheet of McGrath RentCorp and subsidiaries (the "Company") as of June 30, 2015, and the related condensed consolidated statements of income and comprehensive income for the three-month and six-month periods ended June 30, 2015 and 2014, and cash flows for the six-month periods ended June 30, 2015 and 2014. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the condensed consolidated interim financial statements referred to above for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of December 31, 2014, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for the year then ended (not presented herein); and we expressed an unqualified opinion on those consolidated financial statements in our report dated February 26, 2015. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2014, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Grant Thornton LLP

San Jose, California

July 30, 2015

McGRATH RENTCORP

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

(in thousands, except per share amounts)	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Six Months Ended June 30, 2015	Six Months Ended June 30, 2014
Revenues				
Rental	$67,305	$65,809	$132,807	$128,239
Rental related services	17,227	15,146	32,594	28,658
Rental operations	84,532	80,955	165,401	156,897
Sales	10,968	14,170	19,755	25,208
Other	526	620	1,058	1,200
Total revenues	96,026	95,745	186,214	183,305
Costs and Expenses				
Direct costs of rental operations:				
Depreciation of rental equipment	19,016	17,924	37,698	35,821
Rental related services	12,901	11,366	24,800	21,673
Other	16,226	15,188	31,437	28,738
Total direct costs of rental operations	48,143	44,478	93,935	86,232
Costs of sales	6,965	9,188	12,274	16,356
Total costs of revenues	55,108	53,666	106,209	102,588
Gross profit	40,918	42,079	80,005	80,717
Selling and administrative expenses	24,453	23,840	49,665	47,251
Income from operations	16,465	18,239	30,340	33,466
Other income (expense):				
Interest expense	(2,347)	(2,335)	(4,738)	(4,538)
Gain on sale of property, plant and equipment	—	812	—	812
Foreign currency exchange gain (loss)	(85)	78	(253)	(10)
Income before provision for income taxes	14,033	16,794	25,349	29,730
Provision for income taxes	5,543	6,589	10,013	11,654
Net income	$8,490	$10,205	$15,336	$18,076
Earnings per share:				
Basic	$0.33	$0.39	$0.59	$0.70
Diluted	$0.32	$0.39	$0.58	$0.69
Shares used in per share calculation:				
Basic	26,142	25,912	26,117	25,851
Diluted	26,273	26,220	26,272	26,223
Cash dividends declared per share	$0.250	$0.245	$0.500	$0.490

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

McGRATH RENTCORP

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
(in thousands)	2015	2014	2015	2014
Net income	$8,490	$10,205	$15,336	$18,076
Other comprehensive income (loss):				
Foreign currency translation adjustment	6	(11)	89	23
Tax benefit (provision)	—	2	(16)	(4)
Comprehensive income	$8,496	$10,196	$15,409	$18,095

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

McGrath RentCorp

CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited)

(in thousands)	June 30, 2015	December 31, 2014
Assets		
Cash	$739	$1,167
Accounts receivable, net of allowance for doubtful accounts of $2,047 in 2015 and $2,038 in 2014	93,974	101,294
Rental equipment, at cost:		
Relocatable modular buildings	699,781	664,340
Electronic test equipment	269,668	261,995
Liquid and solid containment tanks and boxes	307,795	303,303
	1,277,244	1,229,638
Less accumulated depreciation	(420,755)	(403,888)
Rental equipment, net	856,489	825,750
Property, plant and equipment, net	110,422	108,628
Prepaid expenses and other assets	33,417	41,424
Intangible assets, net	9,901	10,336
Goodwill	27,808	27,808
Total assets	$1,132,750	$1,116,407
Liabilities and Shareholders' Equity		
Liabilities:		
Notes payable	$337,177	$322,478
Accounts payable and accrued liabilities	76,636	71,357
Deferred income	29,726	29,139
Deferred income taxes, net	262,388	268,902
Total liabilities	705,927	691,876
Shareholders’ equity:		
Common stock, no par value - Authorized 40,000 shares		
Issued and outstanding - 26,106 shares as of June 30, 2015 and 26,051 shares as of December 31, 2014	109,232	106,469
Retained earnings	317,620	318,164
Accumulated other comprehensive loss	(29)	(102)
Total shareholders’ equity	426,823	424,531
Total liabilities and shareholders’ equity	$1,132,750	$1,116,407

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

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McGrath RentCorp

CONDENSED Consolidated Statements of Cash Flows

(unaudited)

(in thousands)	Six Months Ended June 30, 2015	2014
Cash Flows from Operating Activities :		
Net income	$15,336	$18,076
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	42,171	39,982
Provision for doubtful accounts	690	1,014
Share-based compensation	1,953	1,984
Gain on sale of used rental equipment	(5,565)	(6,444)
Gain on sale of property, plant and equipment	—	(812)
Foreign currency exchange loss	253	10
Change in:		
Accounts receivable	6,630	(2,448)
Prepaid expenses and other assets	8,007	(2,287)
Accounts payable and accrued liabilities	1,715	2,236
Deferred income	587	2,080
Deferred income taxes	(6,514)	1,781
Net cash provided by operating activities	65,263	55,172
Cash Flows from Investing Activities:		
Purchase of rental equipment	(71,237)	(68,105)
Purchase of property, plant and equipment	(5,832)	(6,101)
Proceeds from sale of used rental equipment	11,815	13,757
Proceeds from sale of property, plant and equipment	—	2,501
Net cash used in investing activities	(65,254)	(57,948)
Cash Flows from Financing Activities:		
Net borrowing (repayments) under bank lines of credit	34,699	(3,003)
Borrowing under Series B senior notes	—	40,000
Principal payment on Series A senior notes	(20,000)	(20,000)
Proceeds from the exercise of stock options	1,458	302
Excess tax benefit from exercise and disqualifying disposition of stock options	313	1,173
Taxes paid related to net share settlement of stock awards	(584)	(3,378)
Repurchase of common stock	(3,132)	—
Payment of dividends	(13,176)	(12,833)
Net cash provided by (used in) financing activities	(422)	2,261
Effect of exchange rate changes on cash	(15)	26
Net decrease in cash	(428)	(489)
Cash balance, beginning of period	1,167	1,630
Cash balance, end of period	$739	$1,141

Supplemental Disclosure of Cash Flow Information:		
Interest paid, during the period	$4,896	$4,198
Net income taxes paid, during the period	$1,490	$8,526
Dividends accrued during the period, not yet paid	$6,588	$6,425
Rental equipment acquisitions, not yet paid	$8,390	$12,033

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

McGRATH RENTCORP

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2015

NOTE 1. CONDENSED CONSOLIDATED FINANCIAL INFORMATION

The condensed consolidated financial statements for the three and six months ended June 30, 2015 and 2014 have not been audited, but in the opinion of management, all adjustments (consisting of normal recurring accruals, consolidating and eliminating entries) necessary for the fair presentation of the consolidated financial position, results of operations and cash flows of McGrath RentCorp (the “Company”) have been made. The accompanying unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). Certain information and note disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted pursuant to those rules and regulations. The consolidated results for the six months ended June 30, 2015 should not be considered as necessarily indicative of the consolidated results for the entire fiscal year. These condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company’s latest Annual Report on Form 10-K filed with the SEC on February 26, 2015 for the year ended December 31, 2014 (the “2014 Annual Report”).

NOTE 2. NEW ACCOUNTING PRONOUNCEMENTS

In April 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2015-03, Imputation of Interest (Subtopic 835-30). The amendments in this update require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with the presentation of debt discounts. The Company does not expect the adoption of this accounting guidance to have a significant impact on its consolidated financial statements.

NOTE 3. EARNINGS PER SHARE

Basic earnings per share (“EPS”) is computed as net income divided by the weighted-average number of shares of common stock outstanding for the period. Diluted EPS is computed assuming conversion of all potentially dilutive securities including the dilutive effect of stock options, unvested restricted stock awards and other potentially dilutive securities. The table below presents the weighted-average number of shares of common stock used to calculate basic and diluted earnings per share:

(in thousands)	Three Months Ended June 30, 2015	2014	Six Months Ended June 30, 2015	2014
Weighted-average number of shares of common stock for calculating basic earnings per share	26,142	25,912	26,117	25,851
Effect of potentially dilutive securities from equity-based compensation	131	308	155	372
Weighted-average number of shares of common stock for calculating diluted earnings per share	26,273	26,220	26,272	26,223

The following securities were not included in the computation of diluted earnings per share as their effect would have been anti-dilutive:

(in thousands)	Three Months Ended June 30, 2015	2014	Six Months Ended June 30, 2015	2014
Options to purchase shares of common stock	650	15	215	9

In May 2008, the Company's Board of Directors authorized the Company to repurchase an aggregate of 2,000,000 shares of the Company's outstanding common stock. The Company has in the past made purchases of shares of its common stock from time to time in over-the-counter market (NASDAQ) transactions and/or through privately negotiated, large block transactions. Furthermore, in March 2015, pursuant to authorization from the Company's Board of Directors, the Company entered into a share repurchase plan, in accordance with Rule 10b5-1 of the Securities Exchange Act of 1934, for the repurchase of up to 987,790 shares of the Company's common stock. All shares repurchased by the Company are canceled and returned to the status of authorized but unissued shares of common stock. The following table presents share repurchase activities during the three and six month ended June 30, 2015 and 2014.

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
(in thousands, except per share amounts)	2015	2014	2015	2014
Number of shares repurchased	89	—	102	—
Aggregate purchase price	$2,754	—	$3,132	—
Average price per repurchased shares	$30.79	—	$30.81	—

As of June 30, 2015, 1,898,347 shares remain authorized for repurchase.

NOTE 4. INTANGIBLE ASSETS

Intangible assets consist of the following:

	Estimated useful life	June 30,	December 31,
(dollar amounts in thousands)	in years	2015	2014
Trade name	Indefinite	$5,700	$ 5,700
Customer relationships	11	9,611	9,611
		15,311	15,311
Less accumulated amortization		(5,410)	(4,975)
		$9,901	$ 10,336

The Company assesses potential impairment of its goodwill and intangible assets when there is evidence that events or circumstances have occurred that would indicate the recovery of an asset's carrying value is unlikely. The Company also assesses potential impairment of its goodwill and intangible assets on an annual basis regardless of whether there is evidence of impairment. If indicators of impairment were to be present in intangible assets used in operations and future discounted cash flows were not expected to be sufficient to recover the assets' carrying amount, an impairment loss would be charged to expense in the period identified. The amount of an impairment loss that would be recognized is the excess of the asset's carrying value over its fair value. Factors the Company considers important, which may cause impairment include, among others, significant changes in the manner of use of the acquired asset, negative industry or economic trends, and significant underperformance relative to historical or projected operating results.

The Company typically conducts its annual impairment analysis in the fourth quarter of its fiscal year. The impairment analysis did not result in an impairment charge for the fiscal year ended December 31, 2014. Determining the fair value of a reporting unit is judgmental and involves the use of significant estimates and assumptions. The Company based its fair value estimates on assumptions that it believes are reasonable but are uncertain and subject to changes in market conditions.

Intangible assets with finite useful lives are amortized over their respective useful lives. Based on the carrying values at June 30, 2015 and assuming no subsequent impairment of the underlying assets, the amortization expense is expected to be $0.4 million for the remainder of fiscal year 2015 and $0.8 million in each of the fiscal years 2016 through 2020.

NOTE 5. SEGMENT REPORTING

The Company's four reportable segments are (1) its modular building rental division ("Mobile Modular"); (2) its electronic test equipment rental division ("TRS-RenTelco"); (3) its containment solutions for the storage of hazardous and non-hazardous liquids and solids division ("Adler Tanks"); and (4) its classroom manufacturing division selling modular buildings used primarily as classrooms in California ("Enviroplex"). The operations of each of these segments are described in Part I – Item 1, "Business," and the accounting policies of the segments are described in "Note 2 – Significant Accounting Policies" in the Company's annual report on Form 10-K for the year ended December 31, 2014. Management focuses on several key measures to evaluate and assess each segment's performance, including rental revenue growth, gross profit, income from operations and income before provision for income taxes. Excluding interest expense, allocations of revenue and expense not directly associated with one of these segments are generally allocated to Mobile Modular, TRS-RenTelco and Adler Tanks based on their pro-rata share of direct revenues. Interest expense is allocated among Mobile Modular, TRS-RenTelco and Adler Tanks based on their pro-rata share of average rental equipment at cost, intangible assets, accounts receivable, deferred income and customer security deposits. The Company does not report total assets by business segment. Summarized financial information for the six months ended June 30, 2015 and 2014 for the Company's reportable segments is shown in the following table:

(dollar amounts in thousands)	Mobile Modular	TRS-RenTelco	Adler Tanks	Enviroplex [1]	Consolidated
Six Months Ended June 30,					
2015					
Rental revenues	$54,088	$44,000	$34,719	$ —	$ 132,807
Rental related services revenues	19,591	1,450	11,553	—	32,594
Sales and other revenues	7,325	10,545	742	2,201	20,813
Total revenues	81,004	55,995	47,014	2,201	186,214
Depreciation of rental equipment	9,280	20,477	7,941	—	37,698
Gross profit	32,266	22,751	24,380	608	80,005
Selling and administrative expenses	22,642	11,611	13,819	1,593	49,665
Income (loss) from operations	9,624	11,140	10,561	(985)	30,340
Interest (expense) income allocation	(2,481)	(1,053)	(1,297)	93	(4,738)
Income (loss) before provision for income taxes	7,143	9,834	9,264	(892)	25,349
Rental equipment acquisitions	38,691	30,077	5,919	—	74,687
Accounts receivable, net (period end)	46,913	23,547	20,310	3,204	93,974
Rental equipment, at cost (period end)	699,781	269,668	307,795	—	1,277,244
Rental equipment, net book value (period end)	501,071	112,275	243,143	—	856,489
Utilization (period end) [2]	74.3 %	60.3 %	61.7 %		
Average utilization [2]	74.3 %	59.8 %	60.9 %		
2014					
Rental revenues	$44,212	$48,184	$35,843	$ —	$ 128,239
Rental related services revenues	15,328	1,617	11,713	—	28,658
Sales and other revenues	11,415	11,977	769	2,247	26,408
Total revenues	70,955	61,778	48,325	2,247	183,305
Depreciation of rental equipment	7,842	20,539	7,440	—	35,821
Gross profit	25,774	28,138	26,060	745	80,717
Selling and administrative expenses	19,830	12,004	13,836	1,581	47,251
Income (loss) from operations	5,944	16,134	12,224	(836)	33,466
Interest (expense) income allocation	(2,290)	(1,053)	(1,284)	89	(4,538)
Gain on sale of property, plant and equipment	341	276	195	—	812
Income (loss) before provision for income taxes	3,995	15,347	11,135	(747)	29,730
Rental equipment acquisitions	38,177	18,387	15,092	—	71,656
Accounts receivable, net (period end)	42,947	22,500	21,057	2,580	89,084
Rental equipment, at cost (period end)	626,457	259,907	298,248	—	1,184,612
Rental equipment, net book value (period end)	443,086	103,816	248,630	—	795,532
Utilization (period end) [2]	71.6 %	62.2 %	61.5 %		
Average utilization [2]	70.2 %	58.3 %	61.8 %		

1. Gross Enviroplex sales revenues were $2,208 and $3,323 for the six months ended June 30, 2015 and 2014, respectively, which includes inter-segment sales to Mobile Modular of $7 and $1,076, respectively, which have been eliminated in consolidation.
2. Utilization is calculated each month by dividing the cost of rental equipment on rent by the total cost of rental equipment excluding accessory equipment and for Mobile Modular and Adler Tanks excluding new equipment inventory. The Average Utilization for the period is calculated using the average costs of rental equipment.

No single customer accounted for more than 10% of total revenues for the six months ended June 30, 2015 and 2014. Revenues from foreign country customers accounted for 6% of the Company's total revenues for the same periods.

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

This Form 10-Q, including the following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), contains forward-looking statements under federal securities laws. Forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties. Our actual results could differ materially from those indicated by forward-looking statements as a result of various factors. These factors include, but are not limited to, those set forth under this Item, those discussed in Part II—Item 1A, "Risk Factors" and elsewhere in this Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the SEC on February 26, 2015 (the "2014 Annual Report") and those that may be identified from time to time in our reports and registration statements filed with the SEC.

This discussion should be read in conjunction with the Condensed Consolidated Financial Statements and related Notes included in Part I—Item 1 of this Form 10-Q and the Consolidated Financial Statements and related Notes and the Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our 2014 Annual Report. In preparing the following MD&A, we presume that readers have access to and have read the MD&A in our 2014 Annual Report, pursuant to Instruction 2 to paragraph (b) of Item 303 of Regulation S-K. We undertake no duty to update any of these forward-looking statements after the date of filing of this Form 10-Q to conform such forward-looking statements to actual results or revised expectations, except as otherwise required by law.

General

The Company, incorporated in 1979, is a leading rental provider of relocatable modular buildings for classroom and office space, electronic test equipment for general purpose and communications needs, and liquid and solid containment tanks and boxes. The Company's primary emphasis is on equipment rentals. The Company is comprised of four business segments: (1) its modular building rental division ("Mobile Modular"); (2) its electronic test equipment rental division ("TRS-RenTelco"); (3) its containment solutions for the storage of hazardous and non-hazardous liquids and solids division ("Adler Tanks"); and (4) its classroom manufacturing division selling modular buildings used primarily as classrooms in California ("Enviroplex").

The Mobile Modular segment includes the results of operations of Mobile Modular Portable Storage, which represented 6% of the Company's total revenues in the six months ended June 30, 2015. Mobile Modular Portable Storage commenced operations in 2008 and offers portable storage units and high security portable office units for rent, lease and purchase.

In the six months ended June 30, 2015, Mobile Modular, TRS-RenTelco, Adler Tanks and Enviroplex contributed 28%, 39%, 37% and negative 4% of the Company's income before provision for income taxes (the equivalent of "pretax income"), respectively, compared to 13%, 52%, 38% and negative 3% for the same period in 2014. Although managed as a separate business unit, Enviroplex's revenues, pretax income contribution and total assets are not significant relative to the Company's consolidated financial position. Accordingly, we have not presented a separate discussion of Enviroplex's results of operations in this MD&A.

The Company generates its revenues primarily from the rental of its equipment on operating leases and from sales of equipment occurring in the normal course of business. The Company requires significant capital outlay to purchase its rental inventory and recovers its investment through rental and sales revenues. Rental revenues and certain other service revenues negotiated as part of lease agreements with customers and related costs are recognized on a straight-line basis over the terms of the leases. Sales revenues and related costs are recognized upon delivery and installation of the equipment to customers. Sales revenues are less predictable and can fluctuate from quarter to quarter and year to year depending on customer demands and requirements. Generally, rental revenues recover the equipment's capitalized cost in a short period of time relative to the equipment's potential rental life and when sold, sale proceeds usually recover a high percentage of its capitalized cost.

The Company's modular revenues (consisting of revenues from Mobile Modular, Mobile Modular Portable Storage and Enviroplex) are derived from rentals and sales to education and commercial customers, with a majority of revenues generated by education customers. Modular revenues are primarily affected by demand for classrooms, which in turn is affected by shifting and fluctuating school populations, the levels of state funding to public schools, the need for temporary classroom space during reconstruction of older schools and changes in policies regarding class size. As a result of any reduced funding, lower expenditures by these schools may result in certain planned programs to increase the number of classrooms, such as those that the Company provides, to be postponed or terminated. However, reduced expenditures may also result in schools reducing their long-term facility construction projects in favor of using the Company's modular classroom solutions. At this time, the Company can provide no assurances as to whether public schools will either reduce or increase their demand for the Company's modular classrooms as a result of fluctuations in state funding of public schools. Looking forward, the Company believes that any interruption in the passage of facility bonds or contraction of class size reduction programs by public schools may have a material adverse effect on both rental and sales revenues of the Company. (For more information, see "Item 1. Business – Relocatable Modular Buildings – Classroom Rentals and Sales to Public Schools (K-12)" in the Company's 2014 Annual Report and "Item 1A. Risk Factors – Significant reductions of, or delays in, funding to public schools have caused the demand and pricing for our modular classroom units to decline, which has in the past caused, and may cause in the future, a reduction in our revenues and profitability" in Part II – Other Information of this Form 10-Q.)

Revenues of TRS-RenTelco are derived from the rental and sale of general purpose and communications test equipment to a broad range of companies, from Fortune 500 to middle and smaller market companies primarily in the electronics, communications, aerospace and defense industries. Electronic test equipment revenues are primarily affected by the business activity within these industries related to research and development, manufacturing, and communication infrastructure installation and maintenance.

Revenues of Adler Tanks are derived from the rental and sale of fixed axle tanks ("tanks") and vacuum containers, dewatering containers and roll-off containers (collectively referred to as "boxes"). These tanks and boxes are rented to a broad range of industries and applications including oil and gas exploration and field services, refinery, chemical and industrial plant maintenance, environmental remediation and field services, infrastructure building construction, marine services, pipeline construction and maintenance, tank terminals services, wastewater treatment, and waste management and landfill services for the containment of hazardous and non-hazardous liquids and solids. The liquid and solid containment tanks and boxes rental business was acquired through the acquisition of Adler Tank Rentals, LLC on December 11, 2008.

The Company's rental operations include rental and rental related service revenues which comprised approximately 89% and 86% of consolidated revenues in the six months ended June 30, 2015 and 2014, respectively. Of the total rental operations revenues for the six months ended June 30, 2015, Mobile Modular, TRS-RenTelco and Adler Tanks comprised 45%, 27% and 28%, respectively, compared to 38%, 32% and 30%, respectively, in the same period of 2014. The Company's direct costs of rental operations include depreciation of rental equipment, rental related service costs, impairment of rental equipment (if any), and other direct costs of rental operations, which include direct labor, supplies, repairs, insurance, property taxes, license fees, cost of sub-rentals and amortization of certain lease costs.

The Company's Mobile Modular, TRS-RenTelco and Adler Tanks business segments sell modular units, electronic test equipment and liquid and solid containment tanks and boxes, respectively, which are either new or previously rented. In addition, Enviroplex sells new modular buildings used primarily as classrooms in California. For the six months ended June 30, 2015 and 2014, sales and other revenues of modular, electronic test equipment and liquid and solid containment tanks and boxes comprised approximately 11% and 14%, respectively, of the Company's consolidated revenues. Of the total sales and other revenues for the six months ended June 30, 2015 and 2014, Mobile Modular and Enviroplex together comprised 46% and 52%, respectively, and TRS-RenTelco comprised 51% and 45%, respectively. Adler Tanks sales and other revenues for the six months ended June 30, 2015 and 2014 were 3% of the Company's total sales and other revenues. The Company's cost of sales includes the carrying value of the equipment sold and the direct costs associated with the equipment sold, such as delivery, installation, modifications and related site work.

Selling and administrative expenses primarily include personnel and benefit costs, which include share-based compensation, depreciation and amortization, bad debt expense, advertising costs, and professional service fees. The Company believes that sharing of common facilities, financing, senior management, and operating and accounting systems by all of the Company's operations results in an efficient use of overhead. Historically, the Company's operating margins have been impacted favorably to the extent its costs and expenses are leveraged over a large installed customer base. However, there can be no assurance as to the Company's ability to maintain a large installed customer base or ability to sustain its historical operating margins.

Adjusted EBITDA

To supplement the Company's financial data presented on a basis consistent with accounting principles generally accepted in the United States of America ("GAAP"), the Company presents "Adjusted EBITDA", which is defined by the Company as net income before interest expense, provision for income taxes, depreciation, amortization, and share-based compensation. The Company presents Adjusted EBITDA as a financial measure as management believes it provides useful information to investors regarding the Company's liquidity and financial condition and because management, as well as the Company's lenders, use this measure in evaluating the performance of the Company.

Management uses Adjusted EBITDA as a supplement to GAAP measures to further evaluate period-to-period operating performance, compliance with financial covenants in the Company's revolving lines of credit and senior notes and the Company's ability to meet future capital expenditure and working capital requirements. Management believes the exclusion of non-cash charges, including share-based compensation, is useful in measuring the Company's cash available for operations and performance of the Company. Because management finds Adjusted EBITDA useful, the Company believes its investors will also find Adjusted EBITDA useful in evaluating the Company's performance.

Adjusted EBITDA should not be considered in isolation or as a substitute for net income, cash flows, or other consolidated income or cash flow data prepared in accordance with GAAP or as a measure of the Company's profitability or liquidity. Adjusted EBITDA is not in accordance with or an alternative for GAAP, and may be different from non–GAAP measures used by other companies. Unlike EBITDA, which may be used by other companies or investors, Adjusted EBITDA does not include share-based compensation charges. The Company believes that Adjusted EBITDA is of limited use in that it does not reflect all of the amounts associated with the Company's results of operations as determined in accordance with GAAP and does not accurately reflect real cash flow. In addition, other companies may not use Adjusted EBITDA or may use other non-GAAP measures, limiting the usefulness of Adjusted EBITDA for purposes of comparison. The Company's presentation of Adjusted EBITDA should not be construed as an inference that the Company will not incur expenses that are the same as or similar to the adjustments in this presentation. Therefore, Adjusted EBITDA should only be used to evaluate the Company's results of operations in conjunction with the corresponding GAAP measures. The Company compensates for the limitations of Adjusted EBITDA by relying upon GAAP results to gain a complete picture of the Company's performance. Because Adjusted EBITDA is a non-GAAP financial measure, as defined by the SEC, the Company includes in the tables below reconciliations of Adjusted EBITDA to the most directly comparable financial measures calculated and presented in accordance with GAAP.

Reconciliation of Net Income to Adjusted EBITDA

	Three Months Ended		Six Months Ended		Twelve Months Ended	
(dollar amounts in thousands)	June 30, 2015	2014	June 30, 2015	2014	June 30, 2015	2014
Net income	$8,490	$10,205	$15,336	$18,076	$42,969	$42,410
Provision for income taxes	5,543	6,589	10,013	11,654	29,211	27,340
Interest	2,347	2,335	4,738	4,538	9,480	8,865
Depreciation and amortization	21,265	20,050	42,171	39,982	83,314	79,186
EBITDA	37,645	39,179	72,258	74,250	164,974	157,801
Share-based compensation	1,022	1,029	1,953	1,984	3,823	3,409
Adjusted EBITDA [1]	$38,667	$40,208	$74,211	$76,234	$168,797	$161,210
Adjusted EBITDA margin [2]	40 %	42 %	40 %	42 %	41 %	42 %

Reconciliation of Adjusted EBITDA to Net Cash Provided by Operating Activities

	Three Months Ended		Six Months Ended		Twelve Months Ended	
(dollar amounts in thousands)	June 30, 2015	2014	June 30, 2015	2014	June 30, 2015	2014
Adjusted EBITDA [1]	$38,667	$40,208	$74,211	$76,234	$168,797	$161,210
Interest paid	(2,888)	(3,041)	(4,896)	(4,198)	(9,772)	(8,680)
Net income taxes paid	(1,174)	(8,187)	(1,490)	(8,526)	(15,239)	(12,821)
Gain on sale of used rental equipment	(2,696)	(3,944)	(5,565)	(6,444)	(14,489)	(13,279)
Gain on sale of property, plant and equipment	—	(812)	—	(812)	—	(812)
Foreign currency exchange (gain) loss	65	(78)	253	10	574	4
Change in certain assets and liabilities:						
Accounts receivable, net	(4,613)	(6,013)	7,320	(1,434)	(4,890)	(1,798)
Prepaid expenses and other assets	1,870	(4,874)	8,007	(2,287)	(3,358)	(2,330)
Accounts payable and other liabilities	1,032	(534)	(13,164)	549	7,811	934
Deferred income	367	4,395	587	2,080	3,643	147

Net cash provided by operating activities	$30,630	$17,120	$65,263	$55,172	$133,077	$122,575

1. Adjusted EBITDA is defined as net income before interest expense, provision for income taxes, depreciation, amortization, and share-based compensation.
2. Adjusted EBITDA Margin is calculated as Adjusted EBITDA divided by total revenues for the period.

Adjusted EBITDA is a component of two restrictive financial covenants for the Company's unsecured Amended Credit Facility, and Series A Senior Notes and Series B Senior Notes (both as defined and more fully described under the heading "Liquidity and Capital Resources" in this MD&A). These instruments contain financial covenants requiring the Company to not:

- Permit the Consolidated Fixed Charge Coverage Ratio (as defined in the Amended Credit Facility and the Note Purchase Agreement (as defined and more fully described under the heading "Liquidity and Capital Resources" in this MD&A)) of Adjusted EBITDA (as defined in the Amended Credit Facility and the Note Purchase Agreement) to fixed charges as of the end of any fiscal quarter to be less than 2.50 to 1. At June 30, 2015, the actual ratio was 3.95 to 1.
- Permit the Consolidated Leverage Ratio of funded debt (as defined in the Amended Credit Facility and the Note Purchase Agreement) to Adjusted EBITDA at any time during any period of four consecutive quarters to be greater than 2.75 to 1. At June 30, 2015, the actual ratio was 2.00 to 1.

At June 30, 2015, the Company was in compliance with each of the aforementioned covenants. There are no anticipated trends that the Company is aware of that would indicate non-compliance with these covenants, although, significant deterioration in our financial performance could impact the Company's ability to comply with these covenants.

Recent Developments

On June 10, 2015, the Company announced that the Board of Directors declared a quarterly cash dividend of $0.25 per common share for the quarter ended June 30, 2015, an increase of 2% over the prior year's comparable quarter.

Results of Operations

Three Months Ended June 30, 2015 Compared to

Three Months Ended June 30, 2014

Overview

Consolidated revenues for the three months ended June 30, 2015 increased less than 1% to $96.0 million, from $95.7 million for the same period in 2014. Consolidated net income for the three months ended June 30, 2015 decreased 17% to $8.5 million, from $10.2 million for the same period in 2014. Earnings per diluted share for the three months ended June 30, 2015 decreased 18% to $0.32 from $0.39 for the same period in 2014.

For the three months ended June 30, 2015, on a consolidated basis:

- Gross profit decreased 3%, to $40.9 million from $42.1 million for the same period in 2014. TRS-RenTelco's gross profit decreased $3.6 million, or 24%, primarily due to lower gross profit on rental and sales revenues. Adler Tanks' gross profit decreased $1.2 million, or 9%, due to lower gross profit on rental, rental related services and sales revenues. Enviroplex's gross profit increased $0.2 million, primarily due to higher sales revenues. Mobile Modular's gross profit increased $3.5 million, or 27%, due to higher gross profit on rental and rental related revenues, partly offset by lower gross profit on sales revenues.
- Selling and administrative expenses increased 3% to $24.5 million from $23.8 million in the same period in 2014, primarily due to increased employee headcount, salaries and benefit costs.
- Interest expense was flat at $2.3 million compared to the same period in 2014, as 11% higher average debt levels of the Company was offset by 9% lower net average interest rates of 2.82% in 2015 compared to 3.10% in 2014.
- In 2014, other non-operating income included the Company's sale of an excess property in June 2014 for net proceeds of $2.5 million resulting in a gain on sale of $0.8 million, which was allocated to Mobile Modular, TRS-RenTelco and Adler Tanks based on their pro-rata share of direct revenues. This property was previously used as one of the Company's branch sales and inventory centers prior to the TRS acquisition in 2004. Since 2004, the property had not been used in support of rental operations. There were no sales of excess properties in 2015.
- Pre-tax income contribution by Mobile Modular, TRS-RenTelco and Adler Tanks was 29%, 38% and 34%, respectively, compared to 13%, 53% and 37%, respectively, for the comparable 2014 period. These results are discussed on a segment basis below. Enviroplex pre-tax income contribution was a negative 1% in 2015 compared to a negative 3% in 2014.
- Adjusted EBITDA decreased $1.5 million, or 4%, to $38.7 million, compared to $40.2 million in 2014.

Mobile Modular

For the three months ended June 30, 2015, Mobile Modular's total revenues increased $4.8 million, or 13%, to $42.1 million compared to the same period in 2014, primarily due to higher rental and rental related services revenues, partly offset by lower sales revenues. The revenue increase, together with higher gross margin on rental, rental related services and sales revenues, partly offset by higher selling and administrative expenses, resulted in a 90% increase in pre-tax income to $4.0 million for the three months ended June 30, 2015, from $2.1 million for the same period in 2014.

The following table summarizes quarterly results for each revenue and gross profit category, income from operations, pre-tax income and other selected information.

Mobile Modular – Three Months Ended 6/30/15 compared to Three Months Ended 6/30/14 (Unaudited)

(dollar amounts in thousands)	Three Months Ended June 30, 2015	2014	Increase (Decrease) $	%
Revenues				
Rental	$27,680	$22,679	$5,001	22 %
Rental related services	10,488	8,011	2,477	31 %
Rental operations	38,168	30,690	7,478	24 %
Sales	3,831	6,489	(2,658)	-41 %
Other	121	136	(15)	-11 %
Total revenues	42,120	37,315	4,805	13 %
Costs and Expenses				
Direct costs of rental operations:				
Depreciation of rental equipment	4,719	4,011	708	18 %
Rental related services	7,388	5,768	1,620	28 %
Other	10,740	9,441	1,299	14 %
Total direct costs of rental operations	22,847	19,220	3,627	19 %
Costs of sales	2,711	5,025	(2,314)	-46 %
Total costs of revenues	25,558	24,245	1,313	5 %
Gross Profit				
Rental	12,221	9,227	2,994	32 %
Rental related services	3,100	2,243	857	38 %
Rental operations	15,321	11,470	3,851	34 %
Sales	1,120	1,464	(344)	-23 %
Other	121	136	(15)	-11 %
Total gross profit	16,562	13,070	3,492	27 %
Selling and administrative expenses	11,286	10,090	1,196	12 %
Income from operations	5,276	2,980	2,296	77 %
Interest expense allocation	(1,228)	(1,187)	41	3 %
Gain on sale of property, plant and equipment	—	341	(341)	-100%
Pre-tax income	$4,048	$2,134	$1,914	90 %
Other Information				
Average rental equipment [1]	$655,479	$585,468	$70,011	12 %
Average rental equipment on rent	$487,706	$411,333	$76,373	19 %
Average monthly total yield [2]	1.41 %	1.29 %		9 %

Average utilization [3]	74.4	%	70.3	%		6	%
Average monthly rental rate [4]	1.89	%	1.84	%		3	%
Period end rental equipment [1]	$668,176		$594,988		$73,188	12	%
Period end utilization [3]	74.3	%	71.6	%		4	%

1. Average and Period end rental equipment represents the cost of rental equipment excluding new equipment inventory and accessory equipment.
2. Average monthly total yield is calculated by dividing the averages of monthly rental revenues by the cost of rental equipment, for the period.
3. Period end utilization is calculated by dividing the cost of rental equipment on rent by the total cost of rental equipment excluding new equipment inventory and accessory equipment. Average utilization for the period is calculated using the average month end costs of rental equipment.
4. Average monthly rental rate is calculated by dividing the averages of monthly rental revenues by the cost of rental equipment on rent, for the period.

Mobile Modular's gross profit for the three months ended June 30, 2015 increased 27%, to $16.6 million from $13.1 million for the same period in 2014. For the three months ended June 30, 2015 compared to the same period in 2014:

- Gross Profit on Rental Revenues – Rental revenues increased $5.0 million, or 22%, primarily due to 19% higher average rental equipment on rent and 3% higher average monthly rental rates in 2015 as compared to 2014. As a percentage of rental revenues, depreciation was 17% in 2015 compared to 18% in 2014, and other direct costs were 39% in 2015 compared to 42% in 2014, which resulted in gross margin percentages of 44% in 2015 compared 41% in 2014. The higher rental revenues, together with higher rental margins resulted in gross profit on rental revenues increasing $3.0 million, or 32%, to $12.2 million in 2015.
- Gross Profit on Rental Related Services – Rental related services revenues increased $2.5 million, or 31%, compared to 2014. Most of these service revenues are negotiated with the initial modular building lease and are recognized on a straight-line basis with the associated costs over the initial term of the lease. The increase in rental related services revenues was primarily attributable to higher amortization of delivery and return delivery and dismantle revenues and higher delivery and return delivery revenues at Mobile Modular Portable Storage. The higher revenues, together with higher gross margin percentage of 30% in 2015 compared to 28% in 2014, resulted in rental related services gross profit increasing $0.9 million to $3.1 million in 2015.
- Gross Profit on Sales – Sales revenues decreased $2.7 million, or 41%, compared to 2014, primarily due to lower new equipment sales. Lower sales revenues, partly offset by higher gross margin percentage of 29% in 2015 compared with 23% in 2014, resulted in gross profit on sales decreasing $0.3 million, or 23%, to $1.1 million. Sales occur routinely as a normal part of Mobile Modular's rental business; however, these sales and related gross margins can fluctuate from quarter to quarter and year to year depending on customer requirements, equipment availability and funding.

For the three months ended June 30, 2015, selling and administrative expenses increased 12%, to $11.3 million from $10.1 million in the same period in 2014, primarily due to increased employee headcount, salaries and benefit costs and higher allocated corporate expenses.

TRS-RenTelco

For the three months ended June 30, 2015, TRS-RenTelco's total revenues decreased $4.2 million, or 13%, to $27.9 million compared to the same period in 2014, primarily due to lower rental and sales revenues. Pre-tax income decreased 40% to $5.3 million for the three months ended June 30, 2015 from $8.9 million for the same period in 2014, primarily due to lower gross profit on rental and sales revenues, partly offset by lower selling and administrative expenses.

The following table summarizes quarterly results for each revenue and gross profit category, income from operations, pre-tax income and other selected information.

TRS-RenTelco – Three Months Ended 6/30/15 compared to Three Months Ended 6/30/14 (Unaudited)

(dollar amounts in thousands)	Three Months Ended June 30, 2015	2014	Increase (Decrease) $	%
Revenues				
Rental	$21,889	$24,424	$(2,535)	-10%
Rental related services	794	895	(101)	-11%
Rental operations	22,683	25,319	(2,636)	-10%
Sales	4,832	6,374	(1,542)	-24%
Other	386	444	(58)	-13%
Total revenues	27,901	32,137		