TEAM INC
Form 10-Q
April 08, 2013
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 10-Q

**(Mark One)**

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
**For the quarterly period ended February 28, 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 001-08604**

# TEAM, INC.

**(Exact Name of Registrant as Specified in Its Charter)**

| | |
|---|---|
| **Delaware** | **74-1765729** |
| **(State or Other Jurisdiction of Incorporation or Organization)** | **(I.R.S. Employer Identification No.)** |

| | |
|---|---|
| **13131 Dairy Ashford, Suite 600, Sugar Land, Texas** | **77478** |
| **(Address of Principal Executive Offices)** | **(Zip Code)** |

**(281) 331-6154**

**(Registrant s Telephone Number, Including Area Code)**

**200 Hermann Drive, Alvin, Texas 77511**

**(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)**

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 þ 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 þ 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. (Check one):

| | | | |
|---|---|---|---|
| Large accelerated filer | ¨ | Accelerated filer | þ |
| Non-accelerated filer | ¨ | Smaller reporting company | ¨ |
| (Do not check if a 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 þ

The Registrant had 20,587,808 shares of common stock, par value $0.30, outstanding and 89,569 shares of treasury stock as of April 1, 2013.

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**PART I FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**

**TEAM, INC. AND SUBSIDIARIES**

**CONSOLIDATED CONDENSED BALANCE SHEETS**

**(in thousands, except share and per share data)**

| | February 28, 2013 (unaudited) | May 31, 2012 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 36,422 | $ 22,477 |
| Receivables, net of allowance of $5,352 and $4,405 | 154,974 | 157,625 |
| Inventory | 26,811 | 24,986 |
| Prepaid income taxes | 4,588 | |
| Deferred income taxes | 4,660 | 5,157 |
| Prepaid expenses and other current assets | 6,643 | 8,430 |
| Total current assets | 234,098 | 218,675 |
| Property, plant and equipment, net | 72,503 | 62,041 |
| Assets held for sale | 5,757 | 5,830 |
| Intangible assets, net of accumulated amortization of $8,118 and $5,658 | 26,899 | 18,508 |
| Goodwill | 104,787 | 95,002 |
| Other assets, net | 2,834 | 3,081 |
| Deferred income taxes | 259 | 651 |
| Total assets | $ 447,137 | $ 403,788 |
| **LIABILITIES AND EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 15,805 | $ 18,427 |
| Other accrued liabilities | 37,935 | 38,492 |
| Income taxes payable | 1,396 | 4,737 |
| Deferred income taxes | 107 | |
| Total current liabilities | 55,243 | 61,656 |
| Deferred income taxes | 15,563 | 11,259 |
| Long-term debt | 89,063 | 85,872 |
| Other long-term liabilities | 6,661 | |
| Total liabilities | 166,530 | 158,787 |
| Commitments and contingencies | | |
| Equity: | | |
| Preferred stock, 500,000 shares authorized, none issued | | |
| Common stock, par value $0.30 per share, 30,000,000 shares authorized; 20,586,397 and 19,954,996 shares issued | 6,175 | 5,985 |
| Additional paid-in capital | 98,357 | 85,801 |
| Retained earnings | 173,011 | 152,049 |

| | | |
|---|---|---|
| Accumulated other comprehensive income (loss) | (878) | (2,587) |
| Treasury stock at cost, 89,569 and 89,569 shares | (1,344) | (1,344) |
| Total Team shareholders equity | 275,321 | 239,904 |
| Non-controlling interest | 5,286 | 5,097 |
| Total equity | 280,607 | 245,001 |
| Total liabilities and equity | $ 447,137 | $ 403,788 |

See accompanying notes to unaudited consolidated condensed financial statements.

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**TEAM, INC. AND SUBSIDIARIES**

**UNAUDITED CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS**

**(in thousands, except per share data)**

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | February 28, 2013 | February 29, 2012 | February 28, 2013 | February 29, 2012 |
| Revenues | $ 150,975 | $ 136,523 | $ 513,115 | $ 435,889 |
| Operating expenses | 112,084 | 99,920 | 362,224 | 304,393 |
| Gross margin | 38,891 | 36,603 | 150,891 | 131,496 |
| Selling, general and administrative expenses | 38,278 | 33,210 | 115,280 | 100,116 |
| Earnings (loss) from unconsolidated affiliates | (4) | 63 | 862 | 911 |
| Operating income | 609 | 3,456 | 36,473 | 32,291 |
| Interest expense, net | 743 | 619 | 2,019 | 1,769 |
| Foreign currency loss (gain) | 729 | (90) | 917 | 74 |
| Earnings (loss) before income taxes | (863) | 2,927 | 33,537 | 30,448 |
| Less: Provision for income taxes | (319) | 946 | 12,409 | 11,266 |
| Net income (loss) | (544) | 1,981 | 21,128 | 19,182 |
| Less: Income (loss) attributable to non-controlling interest | (9) | (30) | 166 | 35 |
| Net income (loss) available to Team shareholders | $ (535) | $ 2,011 | $ 20,962 | $ 19,147 |
| Net income (loss) per share: Basic | $ (0.03) | $ 0.10 | $ 1.04 | $ 0.98 |
| Net income (loss) per share: Diluted | $ (0.03) | $ 0.10 | $ 0.99 | $ 0.93 |

See accompanying notes to unaudited consolidated condensed financial statements.

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**TEAM, INC. AND SUBSIDIARIES**

**UNAUDITED CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME**

**(in thousands)**

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | February 28, 2013 | February 29, 2012 | February 28, 2013 | February 29, 2012 |
| Net income (loss) | $ (544) | $ 1,981 | $ 21,128 | $ 19,182 |
| Foreign currency translation adjustment | (1,985) | 3,293 | 2,305 | (3,037) |
| Foreign currency hedge | (143) | (117) | (791) | 1,164 |
| Tax provision attributable to other comprehensive income | 594 | (754) | 218 | 41 |
| Total comprehensive income (loss) | (2,078) | 4,403 | 22,860 | 17,350 |
| Less: Total comprehensive income (loss) attributable to non-controlling interest | (14) | 2 | 189 | 33 |
| Total comprehensive income (loss) available to Team shareholders | $ (2,064) | $ 4,401 | $ 22,671 | $ 17,317 |

See accompanying notes to unaudited consolidated condensed financial statements.

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**TEAM, INC. AND SUBSIDIARIES**

**UNAUDITED CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS**

**(in thousands)**

| | Nine Months Ended February 28, 2013 | Nine Months Ended February 29, 2012 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 21,128 | $ 19,182 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Earnings from unconsolidated affiliates | (862) | (911) |
| Depreciation and amortization | 14,454 | 12,913 |
| Amortization of deferred loan costs | 167 | 228 |
| Foreign currency loss | 917 | 74 |
| Deferred income taxes | 5,475 | 2,135 |
| Write-down of fixed assets | 73 | |
| Non-cash compensation cost | 3,022 | 3,518 |
| (Increase) decrease: | | |
| Receivables | 6,675 | 7,554 |
| Inventory | (1,675) | (2,170) |
| Prepaid expenses and other current assets | 2,596 | 2,056 |
| Increase (decrease): | | |
| Accounts payable | (3,528) | (7,150) |
| Other accrued liabilities | (2,796) | (229) |
| Income taxes | (7,430) | (4,572) |
| Net cash provided by operating activities | 38,216 | 32,628 |
| Cash flows from investing activities: | | |
| Capital expenditures | (18,803) | (15,825) |
| Business acquisitions, net of cash acquired | (18,589) | (19,351) |
| Proceeds from sale of assets | 15 | 220 |
| Distributions from joint venture | 1,000 | 800 |
| Decrease in other assets, net | 55 | 13 |
| Net cash used in investing activities | (36,322) | (34,143) |
| Cash flows from financing activities: | | |
| Borrowings under revolving credit agreement, net | 2,400 | 13,710 |
| Payments related to term and auto notes | | (236) |
| Debt issuance costs | | (799) |
| Corporate tax effect from share-based payment arrangements | 3,002 | 1,195 |
| Issuance of common stock from share-based payment arrangements | 8,242 | 2,227 |
| Payments related to withholding tax for share-based payment arrangements | (1,517) | (853) |
| Net cash provided by financing activities | 12,127 | 15,244 |
| Effect of exchange rate changes on cash | (76) | (347) |
| Net increase in cash and cash equivalents | 13,945 | 13,382 |
| Cash and cash equivalents at beginning of period | 22,477 | 14,078 |
| Cash and cash equivalents at end of period | $ 36,422 | $ 27,460 |

See accompanying notes to unaudited consolidated condensed financial statements.

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**TEAM, INC. AND SUBSIDIARIES**

**NOTES TO UNAUDITED CONSOLIDATED CONDENSED**

**FINANCIAL STATEMENTS**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES**

***Introduction.*** Unless otherwise indicated, the terms Team, Inc., Team, the Company, we, our and us are used in this report to refer to Team, Inc., to one or more of our consolidated subsidiaries or to all of them taken as a whole. We are incorporated in the State of Delaware and our company website can be found at *www.teamindustrialservices.com*. Our corporate headquarters is located at 13131 Dairy Ashford, Suite 600, Sugar Land, Texas, 77478 and our telephone number is (281) 331-6154. Prior to January 3, 2012 our stock was traded on the NASDAQ Global Select Market ( NASDAQ ) under the symbol TISI . Beginning January 3, 2012 our stock is now traded on the New York Stock Exchange ( NYSE ) under the same symbol. Our fiscal year ends on May 31 of each calendar year.

We are a leading provider of specialty maintenance and inspection services required in maintaining high temperature and high pressure piping systems and vessels that are utilized extensively in heavy industries. We offer an array of complementary services including:

- Inspection and Assessment
- Field Heat Treating
- Leak Repair
- Fugitive Emissions Control
- Hot Tapping
- Field Machining
- Technical Bolting
- Field Valve Repair
- Heat Exchanger and Maintenance
- Isolation Test Plugging
- Pipeline Integrity Management

We offer these services in over 125 locations throughout the world. Our industrial services are available 24 hours a day, 7 days a week, 365 days a year. We market our services to companies in a diverse array of heavy industries which include the petrochemical, refining, power, pipeline, steel, pulp and paper industries, as well as municipalities, shipbuilding, original equipment manufacturers ( OEMs ), distributors, and some of the world s largest engineering and construction firms. Our services are also provided across a broad geographic reach.

***Basis for presentation.*** These interim financial statements are unaudited, but in the opinion of our management, reflect all adjustments, consisting of normal recurring adjustments necessary for a fair presentation of results for such periods. The consolidated condensed balance sheet at May 31, 2012 is derived from the May 31, 2012 audited consolidated financial statements. The results of operations for any interim period are not necessarily indicative of results for the full year. These financial statements should be read in conjunction with the financial statements and notes thereto contained in our annual report on Form 10-K for the fiscal year ended May 31, 2012.

***Consolidation.*** The consolidated financial statements include the accounts of Team, Inc. and our majority-owned subsidiaries where we have control over operating and financial policies. Investments in affiliates in which we have the ability to exert significant influence over operating and financial policies, but where we do not control the operating and financial policies, are accounted for using the equity method. All material intercompany accounts and transactions have been eliminated in consolidation.

***Use of estimates.*** Our accounting policies conform to Generally Accepted Accounting Principles in the U.S. ( GAAP ). Our most significant accounting policies are described below. The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and judgments that affect our reported financial position and results of operations. We review significant estimates and judgments affecting our consolidated financial statements on a recurring basis and record the effect of any necessary adjustments prior to their publication. Estimates and judgments are based on information available at the time such estimates and judgments are made. Adjustments made with respect to the use of these estimates and judgments often relate to information not previously available. Uncertainties with respect to such estimates and judgments are inherent in the preparation of financial statements. Estimates and judgments are used in, among other things, (1) aspects of revenue recognition, (2) valuation of tangible and intangible assets and subsequent assessments for possible impairment, (3) the fair value of the non-controlling interest in subsidiaries that are not wholly-owned, (4) estimating various factors used to accrue liabilities for workers compensation, auto, medical and general liability, (5) establishing an allowance for uncollectible accounts receivable, (6) estimating the useful lives of our assets and (7) assessing future tax exposure and the realization of tax assets.

***Fair value of financial instruments.*** Our financial instruments consist primarily of cash, cash equivalents, accounts receivable, accounts payable and debt obligations. The carrying amount of cash, cash equivalents, trade accounts receivable and trade accounts payable are representative of their respective fair values due to the short-term maturity of these instruments. The fair value of our banking facility is representative of the carrying value based upon the variable terms and management s opinion that the current rates available to us with the same maturity and security structure are equivalent to that of the banking facility.

***Cash and cash equivalents.*** Cash and cash equivalents consist of all demand deposits and funds invested in highly liquid short-term investments with original maturities of three months or less.

***Inventory.*** Inventory is stated at the lower of cost (first-in, first-out method) or market. Inventory includes material, labor and certain fixed overhead costs.

***Property, plant and equipment.*** Property, plant and equipment are stated at cost less accumulated depreciation and amortization. Leasehold improvements are amortized over the shorter of their respective useful life or the lease term. Depreciation and amortization of assets are computed by the straight-line method over the following estimated useful lives of the assets:

| Classification | Useful Life |
|---|---|
| Buildings | 20-40 years |
| Leasehold improvements | 2-15 years |
| Machinery and equipment | 2-12 years |
| Furniture and fixtures | 2-10 years |
| Computers and computer software | 2-5 years |
| Automobiles | 2-5 years |

***Goodwill, intangible assets, and non-controlling interest.*** Goodwill represents the excess of costs over fair value of assets of businesses acquired. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but are instead tested for impairment at least annually in accordance with the provisions of the Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) 350, *Intangibles Goodwill and Other* ( ASC 350 ). Intangible assets with estimated useful lives are amortized over their respective estimated useful lives to their estimated residual values and reviewed for impairment in accordance with ASC 350.

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We operate in only one segment the industrial services segment (see Note 14). Within the industrial services segment, we are organized as two divisions. Our TCM division provides the services of inspection and assessment and field heat treating. Our TMS division provides the services of leak repair, fugitive emissions, hot tapping, field machining, technical bolting, field valve repair and other mechanical services. Each division has goodwill relating to past acquisitions and we assess goodwill for impairment at the TCM and TMS divisional level. Our annual goodwill impairment test is conducted as of May 31 of each year, which is our fiscal year end. Conducting the impairment test as of May 31 of each fiscal year aligns with our annual budget process which is typically completed during the fourth quarter of each year. In addition, performing our annual goodwill impairment test as of this date allows for a thorough consideration of the valuations of our business units subsequent to the completion of our annual budget process but prior to our financial year end reporting date.

On May 31, 2012, we adopted Accounting Standards Update ( ASU ) 2011-08, *Testing Goodwill for Impairment* ( ASU 2011-08 ), which requires reporting entities to assess relevant events and circumstances in evaluating whether it is more likely than not that the fair value of a reporting unit is less than the carrying amount of goodwill. If, after assessing the totality of events and circumstances, an entity determines that it is more likely than not that the fair value of a reporting unit is greater than the carrying amount, then the first and second steps of the goodwill impairment test described in ASC 350 are not necessary. We evaluated considerations under ASU 2011-08 such as macroeconomic effects on our business, industry and market considerations, cost factors that could have a negative effect on cash flows or earnings, overall financial performance, entity-specific events, events affecting reporting units, and any realization of a sustained decrease in the price of our stock. After consideration of the aforementioned events and circumstances, we concluded that it was more likely than not that the fair value of a reporting unit was greater than the carrying amount of goodwill. Accordingly, we did not perform the two-step process described in ASC 350 for our fiscal year 2012 annual test.

There was $104.8 million and $95.0 million of goodwill at February 28, 2013 and May 31, 2012, respectively. A summary of goodwill is as follows (in thousands):

| | Nine Months Ended February 28, 2013 (unaudited) | | |
|---|---|---|---|
| | **TCM Division** | **TMS Division** | **Total** |
| Balance at May 31, 2012 | $ 75,131 | $ 19,871 | $ 95,002 |
| Acquisition and purchase price adjustments | 9,950 | (1,222) | 8,728 |
| Foreign currency adjustments | 492 | 565 | 1,057 |
| Balance at February 28, 2013 | $ 85,573 | $ 19,214 | $ 104,787 |

***Income taxes.*** We follow the guidance of the ASC 740, *Income Taxes* ( ASC 740 ), which requires that we use the asset and liability method of accounting for deferred income taxes and provide deferred income taxes for all significant temporary differences. As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax payable and related tax expense together with assessing temporary differences resulting from differing treatment of certain items, such as depreciation, for tax and accounting purposes. These differences can result in deferred tax assets and liabilities, which are included within our consolidated balance sheets. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe that it is more likely than not (a likelihood of more than 50%) that some portion or all of the deferred tax assets will not be realized, we must establish a valuation allowance. We consider all available evidence to determine whether, based on the weight of the evidence, a valuation allowance is needed. Evidence used includes information about our current financial position and our results of operations for the current and preceding years, as well as all currently available information about future years, including our anticipated future performance, the reversal of deferred tax liabilities, share-based compensation and tax planning strategies.

***Workers compensation, auto, medical and general liability accruals.*** In accordance with ASC 450, *Contingencies* ( ASC 450 ), we record a loss contingency when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. We review our loss contingencies on an ongoing basis to ensure that we have appropriate reserves recorded on our balance sheet. These reserves are based on historical experience with claims incurred but not received, estimates and judgments made by management, applicable insurance coverage for litigation matters, and are adjusted as circumstances warrant. For workers compensation, our self-insured retention is $1 million and our automobile liability self-insured retention is currently $500,000 per occurrence. For general liability claims we have an effective self-insured retention of $3 million per occurrence. For medical claims, our self-insured retention is $150,000 per individual claimant determined on an annual basis. For environmental liability claims, our self-insured retention is $500,000 per occurrence. We maintain insurance for claims that exceed such self-retention limits. The insurance is subject to terms, conditions, limitations and exclusions that may not fully compensate us for all losses. Our estimates and judgments could change based on new information, changes in laws or regulations, changes in management s plans or intentions, or the outcome of legal proceedings, settlements or other factors. If different estimates and judgments were applied with respect to these matters, it is likely that reserves would be recorded for different amounts.

***Revenue recognition.*** We determine our revenue recognition guidelines for our operations based on guidance provided in applicable accounting standards and positions adopted by the FASB or the Securities and Exchange Commission (the SEC ). Most of our projects are short-term in nature and we predominantly derive revenues by providing a variety of industrial services on a time and material basis. For all of these services, our revenues are recognized when services are rendered or when product is shipped to the job site and risk of ownership passes to the customer. However, due to various contractual terms with our customers, at the end of any reporting period, there may be earned but unbilled revenue that is accrued to properly match revenues with related costs. The amount of earned but unbilled revenue included in accounts receivable was $20.6 million at February 28, 2013 and May 31, 2012.

***Allowance for doubtful accounts.*** In the ordinary course of business, a percentage of our accounts receivable are not collected due to billing disputes, customer bankruptcies, dissatisfaction with the services we performed and other various reasons. We establish an allowance to account for those accounts receivable that will eventually be deemed uncollectible. The allowance for doubtful accounts is based on a combination of our historical experience and management s review of long outstanding accounts receivable.

***Concentration of credit risk.*** No single customer accounts for more than 10% of consolidated revenues.

***Earnings per share.*** Basic earnings per share is computed by dividing net income available to Team shareholders by the weighted-average number of shares of common stock outstanding during the year. Diluted earnings per share is computed by dividing net income available to Team shareholders, less income or loss for the period attributable to the non-controlling interest, by the sum of, (1) the weighted-average number of shares of common stock, net of treasury stock, outstanding during the period, (2) the dilutive effect of the assumed exercise of share-based compensation using the treasury stock method and (3) the dilutive effect of the assumed conversion of our non-controlling interest to our common stock (see Note 2).

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Amounts used in basic and diluted earnings per share, for the three and nine months ended February 28, 2013 and February 29, 2012, are as follows (in thousands):

| | Three Months Ended (unaudited) | | Nine Months Ended (unaudited) | |
|---|---|---|---|---|
| | February 28, 2013 | February 29, 2012 | February 28, 2013 | February 29, 2012 |
| Weighted-average number of basic shares outstanding | 20,387 | 19,733 | 20,104 | 19,610 |
| Stock options, stock units and performance awards | 753 | 792 | 770 | 757 |
| Assumed conversion of non-controlling interest | 171 | 203 | 204 | 233 |
| Total shares and dilutive securities | 21,311 | 20,728 | 21,078 | 20,600 |

There were zero and 578,000 options to purchase shares of common stock outstanding during the three month periods ended, February 28, 2013 and February 29, 2012, respectively, excluded from the computation of diluted earnings per share because the options exercise prices were greater than the average market price of common shares during the periods. There were 1,000 and 643,000 options to purchase shares of common stock outstanding during the nine month periods ended February 28, 2013 and February 29, 2012, respectively, excluded from the computation of diluted earnings per share because the options exercise prices were greater than the average market price of common shares during the periods.

***Foreign currency.*** For subsidiaries whose functional currency is not the U.S. Dollar, assets and liabilities are translated at period ending rates of exchange and revenues and expenses are translated at period average exchange rates. Translation adjustments for the asset and liability accounts are included as a separate component of accumulated other comprehensive income (loss) in shareholders equity. Foreign currency transaction gains and losses are included in our statement of income. Effective December 1, 2009, we began to account for Venezuela as a highly-inflationary economy and the effect of all subsequent currency fluctuations between the Bolivar and the U.S. Dollar are recorded in our statement of income (see Note 16).

***Accounting Principles Not Yet Adopted***

***ASU 2011-11.*** In December 2011, an update was issued related to new disclosures on offsetting assets and liabilities of financial and derivative instruments. The amendments require the disclosure of gross asset and liability amounts, amounts offset on the balance sheet and amounts subject to the offsetting requirements, but not offset on the balance sheet. This standard does not amend the existing guidance on when it is appropriate to offset. The standard update is effective for annual periods beginning after January 1, 2013. We do not expect the adoption of this standard to have a material impact on our results of operations, financial position or cash flows.

***Newly Adopted Accounting Principles***

***ASU 2011-08***. In September 2011, the FASB issued ASU 2011-08. ASU 2011-08 amends ASC 350 to permit an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount of goodwill as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. If, after assessment of qualitative factors, an entity determines that it is more likely than not that the fair value of a reporting unit is greater than the carrying amount, then the first and second steps of the goodwill impairment test described in ASC 350 are not necessary. ASU 2011-08 is effective for annual and interim impairment tests performed for fiscal years beginning after December 15, 2011 with early adoption permitted. This update was early adopted by Team on May 31, 2012. The adoption of this pronouncement did not have any impact on our results of operations, financial position or cash flows.

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***ASU 2011-05.*** In June 2011, the FASB issued an update to existing guidance on the presentation of comprehensive income. This update requires the presentation of the components of net income and other comprehensive income either in a single continuous statement or in two separate but consecutive statements. In addition, companies are also required to present reclassification adjustments for items that are reclassified from other comprehensive income to net income on the face of the financial statements. In December 2011, the FASB issued an accounting update to defer the effective date for presentation of reclassification of items out of accumulated other comprehensive income to net income. These updates are effective for fiscal years and interim periods beginning after December 15, 2011 with early adoption permitted. This update was adopted by Team on June 1, 2012. The adoption of this pronouncement did not have a material effect on our results of operations, financial position or cash flows.

***ASU 2011-04.*** In May 2011, an update regarding fair value measurement was issued to conform the definition of fair value and common requirements for measurement of and disclosure about fair value under U.S. GAAP and International Financial Reporting Standards. The standard also clarifies the application of existing fair value measurement requirements and expands the disclosure requirements for fair value measurements that are estimated using significant unobservable Level 3 inputs. The standard update is effective for interim and annual periods beginning after December 15, 2011. The adoption of this standard did not have a material impact on our results of operations, financial position or cash flows.

**2. ACQUISITIONS**

In August 2012, Team s subsidiary, Quest Integrity Group ( Quest ), acquired a specialty remote digital video inspection company based in New Zealand for approximately $3.0 million. Based upon the substantially completed purchase price allocation, we have recorded $0.7 million in fixed assets, $1.1 million in intangible assets classified as customer relationships, $0.3 million in intangible assets classified as non-compete agreements and $0.9 million in goodwill. In September 2012, Team also acquired the common stock of TCI Services, Inc. ( TCI ) for approximately $24.1 million of which $16.5 million was cash paid and $7.6 million was deferred payments. TCI is a company based in Oklahoma specializing in the inspection and repair of above ground storage tanks. Based upon the substantially completed purchase price allocation associated with the acquisition of TCI, we have recorded $4.1 million in net working capital, $2.6 million in fixed assets, $6.7 million in intangible assets classified as customer relationships, $1.1 million in intangible assets classified as trade name, $9.6 million in goodwill, $1.0 million in other current liabilities and $6.6 million in other long-term liabilities. The $1.0 million in other current liabilities and $6.6 million in other long-term liabilities represent future consideration to be paid of which $3.0 million is an estimate of contingent payments to be made based upon the future performance criteria of TCI. The combined unaudited annual revenues for both acquired businesses are approximately $24 million in their most recently completed fiscal years and the total consideration for both was approximately $27 million, subject to adjustments for working capital true-ups and the future performance of the businesses. As a result of the two business acquisitions, we expect to be able to deduct $6.7 million of the goodwill recognized for tax purposes.

In fiscal year 2012, we completed two small acquisitions for a total of $19.4 million which were recorded as $1.2 million in net working capital, $3.0 million in fixed assets, $7.5 million in intangible assets classified as customer relationships and $7.7 million in goodwill. Both acquisitions were financed through borrowings on our banking credit facility. We performed purchase price allocations based on our most current assessments of fair value of the assets acquired and the liabilities assumed. We completed a final valuation report of intangibles and goodwill associated with these transactions during the first half of fiscal year 2013. The final purchase price allocation associated with both of these transactions did not result in material adjustments and, accordingly, no retrospective adjustments were made in the accompanying 2012 financial statements.

On November 3, 2010, we purchased Quest, a privately held advanced inspection services and engineering assessment company. We effectively purchased 95% of Quest and expect to purchase the remaining 5% in fiscal year 2015 for a purchase consideration based upon the future financial performance of Quest as defined in the purchase agreement. Future consideration would be payable in unregistered shares of our common stock for an

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aggregate value of no less than $2.4 million, provided the aggregate value of the consideration does not exceed 20% of our outstanding common stock. Our valuation of the remaining 5% equity of Quest at the date of acquisition was $4.9 million, which is reflected in the equity section of the Consolidated Balance Sheet as Non-controlling interest.

Information regarding the change in carrying value of the non-controlling interest is set forth below (in thousands):

| | |
|---|---|
| Fair value of non-controlling interest at November 3, 2010 | $ 4,917 |
| Income attributable to non-controlling interest | 362 |
| Other comprehensive income attributable to non-controlling interest | 7 |
| Carrying value of non-controlling interest at February 28, 2013 | $ 5,286 |

**3. RECEIVABLES**

A summary of accounts receivable as of February 28, 2013 and May 31, 2012 is as follows (in thousands):

| | February 28, 2013 (unaudited) | May 31, 2012 |
|---|---|---|
| Trade accounts receivable | $ 139,757 | $ 141,469 |
| Unbilled revenues | 20,569 | 20,561 |
| Allowance for doubtful accounts | (5,352) | (4,405) |
| Total | $ 154,974 | $ 157,625 |

**4. INVENTORY**

A summary of inventory as of February 28, 2013 and May 31, 2012 is as follows (in thousands):

| | February 28, 2013 (unaudited) | May 31, 2012 |
|---|---|---|
| Raw materials | $ 3,253 | $ 3,529 |
| Work in progress | 948 | 937 |
| Finished goods | 22,610 | 20,520 |
| Total | $ 26,811 | $ 24,986 |

**5. PROPERTY, PLANT AND EQUIPMENT**

A summary of property, plant and equipment as of February 28, 2013 and May 31, 2012 is as follows (in thousands):

| | February 28, 2013 (unaudited) | May 31, 2012 |
|---|---|---|
| Land | $ 3,112 | $ 1,285 |
| Buildings and leasehold improvements | 18,017 | 15,095 |
| Machinery and equipment | 133,738 | 121,533 |
| Furniture and fixtures | 2,668 | 2,246 |

| | | |
|---|---|---|
| Computers and computer software | 8,600 | 7,980 |
| Automobiles | 3,856 | 2,624 |
| Construction in progress | 4,848 | 1,912 |
| Total | 174,839 | 152,675 |
| Accumulated depreciation and amortization | (102,336) | (90,634) |
| Property, plant and equipment, net | $ 72,503 | $ 62,041 |

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### 6. ASSETS HELD FOR SALE

Assets held for sale of $5.8 million pertains to two parcels of land in or around Houston. The largest parcel is 50 acres purchased in October 2007 on which we had previously planned to construct future facilities in Pearland, Texas. During the fourth quarter of fiscal year 2012, we decided not to proceed with construction of the future facilities at this location and recognized a $1.7 million asset write-down of pre-construction building costs and capitalized interest. The properties are being actively marketed using the services of a broker.

### 7. INTANGIBLE ASSETS

A summary of intangible assets as of February 28, 2013 and May 31, 2012 is as follows (in thousands):

| | February 28, 2013 (unaudited) | | | May 31, 2012 | | |
|---|---|---|---|---|---|---|
| | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
| Customer relationships | $ 21,462 | $ (3,559) | $ 17,903 | $ 12,198 | $ (1,973) | $ 10,225 |
| Non-compete agreements | 3,719 | (3,164) | 555 | 3,136 | (2,844) | 292 |
| Trade names | 4,075 | (362) | 3,713 | 2,962 | (207) | 2,755 |
| Technology | 5,112 | (1,033) | 4,079 | 5,112 | (634) | 4,478 |
| Licenses | 649 | | 649 | 758 | | 758 |
| Total | $ 35,017 | $ (8,118) | $ 26,899 | $ 24,166 | $ (5,658) | $ 18,508 |

Amortization expense for the three months ended February 28, 2013 and February 29, 2012 was $0.8 million and $0.9 million, respectively. Amortization expense for the nine months ended February 28, 2013 and February 29, 2012 was $2.5 million and $2.0 million, respectively.

### 8. OTHER ACCRUED LIABILITIES

A summary of other accrued liabilities as of February 28, 2013 and May 31, 2012 is as follows (in thousands):

| | February 28, 2013 (unaudited) | May 31, 2012 |
|---|---|---|
| Payroll and other compensation expenses | $ 23,942 | $ 27,871 |
| Insurance accruals | 4,925 | 4,388 |
| Property, sales and other non-income related taxes | 1,508 | 1,966 |
| Other | 7,560 | 4,267 |
| Total | $ 37,935 | $ 38,492 |

### 9. LONG-TERM DEBT, DERIVATIVES AND LETTERS OF CREDIT

In July 2011, we renewed our banking credit facility (the Credit Facility ) with our banking syndicate. The Credit Facility has borrowing capacity of up to $150 million in multiple currencies, bears interest based on a variable Eurodollar rate option (LIBOR plus 1.75% margin at February 28, 2013) with the margin based on financial covenants set forth in the Credit Facility, and matures in July 2016. In connection with the renewal of the Credit Facility, we capitalized $0.8 million of associated debt issuance costs which are amortized over the life of the Credit Facility. At February 28, 2013, we were in compliance with all financial covenants of the Credit Facility. All debt is long term.

ASC 815, *Derivatives and Hedging* ( ASC 815 ) established accounting and reporting standards requiring that derivative instruments be recorded at fair value and included in the balance sheet as assets or liabilities. The

accounting for changes in the fair value of a derivative instrument depends on the intended use of the derivative and the resulting designation, which is established at the inception date of a derivative. Special accounting for derivatives qualifying as fair value hedges allows derivatives gains and losses to offset related results on the hedged item in the statement of income. For derivative instruments designated as cash flow hedges, changes in fair value, to the extent the hedge is effective, are recognized in other comprehensive income until the hedged item is recognized in earnings. Hedge effectiveness is measured at least quarterly based on the relative cumulative changes in fair value between the derivative contract and the hedged item over time. Credit risks related to derivatives include the possibility that the counter-party will not fulfill the terms of the contract. We considered counter-party credit risk to our derivative contracts when valuing our derivative instruments.

The amounts recognized in other comprehensive income, and reclassified into income, for the three and nine months ended February 28, 2013 and February 29, 2012 are as follows (in thousands):

| | Gain (Loss) Recognized in Other Comprehensive Income Three Months Ended (unaudited) | | Gain (Loss) Reclassified from Other Comprehensive Income to Earnings Three Months Ended (unaudited) | | Gain (Loss) Recognized in Other Comprehensive Income Nine Months Ended (unaudited) | | Gain (Loss) Reclassified from Other Comprehensive Income to Earnings Nine Months Ended (unaudited) | |
|---|---|---|---|---|---|---|---|---|
| | February 28, 2013 | February 29, 2012 | February 28, 2013 | February 29, 2012 | February 28, 2013 | February 29, 2012 | February 28, 2013 | February 29, 2012 |
| Euro denominated long-term debt | $ (143) | $ (117) | $ | $ | $ (791) | $ 1,164 | $ | $ |
| Total | $ (143) | $ (117) | $ | $ | $ (791) | $ 1,164 | $ | $ |

Our borrowing of 12.3 million under the Credit Facility serves as an economic hedge of our net investment in our European operations as fluctuations in the fair value of the borrowing attributable to the U.S. Dollar/Euro spot rate will offset translation gains or losses attributable to our investment in our European operations. At February 28, 2013, the 12.3 million borrowing had a U.S. Dollar value of $16.1 million.

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. Any ineffectiveness related to our hedges was not material for any of the periods presented.

The following table presents the fair value totals and balance sheet classification for derivatives designated as hedges under ASC 815 (in thousands):

| | February 28, 2013 (unaudited) | | | May 31, 2012 | | |
|---|---|---|---|---|---|---|
| | Classification | Balance Sheet Location | Fair Value | Classification | Balance Sheet Location | Fair Value |
| Euro denominated long-term debt | Liability | Long-term debt | $ 1,887 | Liability | Long-term debt | $ 2,678 |
| Total | | | $ 1,887 | | | $ 2,678 |

In order to secure our insurance programs we are required to post letters of credit generally issued by a bank as collateral. A letter of credit commits the issuer to remit specified amounts to the holder, if the holder demonstrates that we failed to meet our obligations under the letter of credit. If this were to occur, we would be obligated to reimburse the issuer for any payments the issuer was required to remit to the holder of the letter of credit. We were contingently liable for outstanding stand-by letters of credit totaling $15.3 million at

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February 28, 2013 and $13.5 million at May 31, 2012. Outstanding letters of credit reduce amounts available under our Credit Facility and are considered as having been funded for purposes of calculating our financial covenants under the Credit Facility.

**10. FAIR VALUE MEASUREMENTS**

As defined in ASC 820, *Fair Value Measurements and Disclosures* ( ASC 820 ), fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We utilize market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable. We primarily apply the market approach for recurring fair value measurements and endeavor to utilize the best information available. Accordingly, we utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The use of unobservable inputs is intended to allow for fair value determinations in situations in which there is little, if any, market activity for the asset or liability at the measurement date. We are able to classify fair value balances based on the observability of those inputs. ASC 820 establishes a fair value hierarchy such that Level 1 measurements include unadjusted quoted market prices for identical assets or liabilities in an active market, Level 2 measurements include quoted market prices for identical assets or liabilities in an active market which have been adjusted for items such as effects of restrictions for transferability and those that are not quoted but are observable through corroboration with observable market data, including quoted market prices for similar assets, and Level 3 measurements include those that are unobservable and of a highly subjective measure.

The following table sets forth, by level within the fair value hierarchy, our financial assets and liabilities that are accounted for at fair value on a recurring basis as of February 28, 2013. As required by ASC 820, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement (in thousands):

| | February 28, 2013 (unaudited) | | | |
|---|---|---|---|---|
| | Quoted Prices in Active Markets for Identical Items (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
| Euro denominated long-term debt | $ | $ 1,887 | $ | $ 1,887 |
| Net liabilities | $ | $ 1,887 | $ | $ 1,887 |

**11. SHARE-BASED COMPENSATION**

We have adopted stock incentive plans and other arrangements pursuant to which our Board of Directors (the Board ) may grant stock options, restricted stock, stock units, stock appreciation rights, common stock or performance awards to officers, directors and key employees. At February 28, 2013, there were approximately 1.4 million stock options, restricted stock units and performance awards outstanding to officers, directors and key employees. The exercise price, terms and other conditions applicable to each form of share-based compensation under our plans is generally determined by the Compensation Committee of our Board at the time of grant and may vary.

Our share-based payments consist primarily of stock options, stock units, common stock and performance awards. The governance of our share-based compensation does not directly limit the number of future awards. There are 7,020,000 shares cumulatively authorized to be issued under our stock incentive plans. Shares issued in connection with our share-based compensation are issued out of authorized but unissued common stock. Compensation expense related to share-based compensation totaled $3.0 million and $3.5 million for the nine months ended February 28, 2013 and February 29, 2012, respectively. The tax benefit related to share-based compensation was $3.0 million and $1.2 million for the nine months ended February 28, 2013 and February 29, 2012, respectively. At February 28, 2013, $8.7 million of unrecognized compensation expense related to share-based compensation is expected to be recognized over a remaining weighted-average period of 2.9 years.

We determine the fair value of each stock option at the grant date using a Black-Scholes model and recognize the resulting expense of our stock option awards over the period during which an employee is required to provide services in exchange for the awards, usually the vesting period. There was no compensation expense related to stock options for the nine months ended February 28, 2013. Compensation expense related to stock options was $0.8 million for the nine months ended February 29, 2012. Our options typically vest in equal annual installments over a four year service period. Expense related to an option grant is recognized on a straight line basis over the specified vesting period for those options. Stock options generally have a ten year term. Transactions involving our stock options during the nine months ended February 28, 2013 and February 29, 2012 are summarized below:

| | Nine months Ended February 28, 2013 (unaudited) | | Nine Months Ended February 29, 2012 (unaudited) | |
|---|---|---|---|---|
| | No. of Options (in thousands) | Weighted Average Exercise Price | No. of Options (in thousands) | Weighted Average Exercise Price |
| Shares under option, beginning of period | 1,562 | $ 18.95 | 1,856 | $ 17.81 |
| Changes during the period: | | | | |
| Granted | | $ | | $ |
| Exercised | (508) | $ 16.23 | (217) | $ 10.27 |
| Cancelled | | $ | (2) | $ 30.33 |
| Expired | | $ | (10) | $ 30.33 |
| Shares under option, end of period | 1,054 | $ 20.25 | 1,627 | $ 18.73 |
| Exercisable at end of period | 1,054 | $ 20.25 | 1,623 | $ 18.70 |

Options exercisable at February 28, 2013 had a weighted-average remaining contractual life of 3.7 years. For total options outstanding at February 28, 2013, the range of exercise prices and remaining contractual lives are as follows (unaudited):

| Range of Prices | No. of Options (in thousands) | Weighted Average Exercise Price | Weighted Average Remaining Life (in years) |
|---|---|---|---|
| $6.42 to $9.62 | 122 | $ 8.92 | 2.2 |
| $9.63 to $12.82 | 157 | $ 11.10 | 2.9 |
| $12.83 to $16.03 | 308 | $ 14.56 | 3.3 |
| $16.04 to $32.05 | 467 | $ 30.05 | 4.6 |
| | 1,054 | $ 20.25 | 3.7 |

Stock units are settled with common stock upon vesting unless it is not legally feasible to issue shares, in which case the value of the award is settled in cash. We determine the fair value of each stock unit based on the market price on the date of grant. Stock units generally vest in annual installments over four years and the expense associated with the units is recognized over the same vesting period. We also grant common stock to our directors which typically vest immediately. Compensation expense related to stock units and director stock grants totaled $2.6 million and $2.3 million for the nine months ended February 28, 2013 and February 29, 2012, respectively.

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Transactions involving our stock units and director stock grants during the nine months ended February 28, 2013 and February 29, 2012 are summarized below:

| | Nine Months Ended February 28, 2013 (unaudited) | | Nine Months Ended February 29, 2012 (unaudited) | |
|---|---|---|---|---|
| | No. of Stock Units (in thousands) | Weighted Average Fair Value | No. of Stock Units (in thousands) | Weighted Average Fair Value |
| Stock and stock units, beginning of period | 342 | $ 21.73 | 310 | $ 19.80 |
| Changes during the period: | | | | |
| Granted | 141 | $ 32.81 | 159 | $ 24.78 |
| Vested and settled | (142) | $ 22.54 | (119) | $ 20.80 |
| Cancelled | (8) | $ 22.40 | (5) | $ 21.19 |
| Stock and stock units, end of period | 333 | $ 26.07 | 345 | $ 21.73 |

Performance awards are settled with common stock upon vesting unless it is not legally feasible to issue shares, in which case the value of the award is settled in cash. We determine the fair value of each performance award based on the market price on the date of grant. Performance awards granted to our Chairman of our Board vest over the longer of four years or the achievement of performance goals based upon our future results of operations. Compensation expense related to performance awards totaled $0.4 million for the nine months ended February 28, 2013 and February 29, 2012. Transactions involving our performance awards during the nine months ended February 28, 2013 and February 29, 2012 are summarized below:

| | Nine Months Ended February 28, 2013 (unaudited) | | Nine Months Ended February 29, 2012 (unaudited) | |
|---|---|---|---|---|
| | No. of Performance Awards (in thousands) | Weighted Average Fair Value | No. of Performance Awards (in thousands) | Weighted Average Fair Value |
| Performance awards, beginning of period | 65 | $ 21.86 | 61 | $ 20.33 |
| Changes during the period: | | | | |
| Granted | 19 | $ 32.89 | 24 | $ 25.16 |
| Vested and settled | (27) | $ 22.04 | (20) | $ 21.14 |
| Cancelled | | $ | | $ |
| Performance awards, end of period | 57 | $ 25.45 | 65 | $ 21.86 |

**12. OTHER COMPREHENSIVE INCOME**

A summary of other comprehensive income included within shareholders equity as of February 28, 2013 and May 31, 2012 is as follows (in thousands):

| | February 28, 2013 (unaudited) | May 31, 2012 |
|---|---|---|
| Foreign currency translation adjustments | $ (2,311) | $ (4,593) |
| Foreign currency hedge | 1,887 | 2,678 |
| Tax provision on other comprehensive income | (454) | (672) |

| | | | | |
|---|---|---|---|---|
| Total | $ | (878) | $ | (2,587) |

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The following table represents the related tax effects allocated to each component of other comprehensive income (in thousands):

| | Nine Months Ended February 28, 2013 (unaudited) | | | Nine Months Ended February 29, 2012 (unaudited) | | |
|---|---|---|---|---|---|---|
| | **Gross Amount** | **Tax Effect** | **Net Amount** | **Gross Amount** | **Tax Effect** | **Net Amount** |
| Foreign currency translation adjustments | $ 2,305 | $ (91) | $ 2,214 | $ (3,037) | $ 494 | $ (2,543) |
| Foreign currency hedge | (791) | 309 | (482) | 1,164 | (453) | 711 |