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INTEGRATED ELECTRICAL SERVICES INC
Form 8-K
May 12, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 8-K

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

Date of Report: May 12, 2003

Commission File No. 001-13783

INTEGRATED ELECTRICAL SERVICES, INC.

(Exact name of registrant as specified in its charter)

Delaware 76-0542208
(State or other jurisdiction of (I.R.S. Employer Identification No.)
incorporation or organization)

1800 West Loop South
Suite 500
Houston, Texas 77027-3233
(Address of principal executive offices) (zip code)

Registrant's telephone number, including area code: (713) 860-1500

ITEM 5. OTHER EVENTS

Integrated Electrical Services, Inc., a Delaware corporation (the "Company") is the largest provider of electrical contracting services in the United States, providing a broad range of services including designing, building and maintaining electrical, low voltage and utilities systems for the commercial and industrial, residential, low voltage and service and maintenance markets.

On February 27, 2003, the Company consummated the acquisition of the assets of Encompass Electrical Technologies - Rocky Mountains, Inc. d/b/a Riviera Electric, Inc. ("Riviera"). Riviera performs electrical contracting services primarily in Denver, Colorado, and has locations throughout the state.

In connection with the acquisition of Riviera and to comply with the disclosure requirements of the Securities and Exchange Commission regarding the financial statements of the business acquired, the Company is filing this Current Report containing the following audited and unaudited pro forma financial statements.

- (a) Financial Statements of Business Acquired
See Pages 3 through 18
- (b) Pro Forma Financial Statements
See Pages 19 through 22

ITEM 7. FINANCIAL STATEMENTS, PRO FORMA FINANCIAL INFORMATION
AND EXHIBITS

(A) FINANCIAL STATEMENTS OF BUSINESS ACQUIRED

INDEPENDENT AUDITOR'S REPORT

Integrated Electrical Services, Inc.
Houston, Texas

We have audited the accompanying balance sheets of Encompass Electrical Technologies - Rocky Mountains, Inc. d/b/a Riviera Electric, Inc. (a Colorado corporation) as of December 31, 2002 and 2001, and the related statements of operations, changes in stockholder's equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 2 to the financial statements, the Company sold substantially all of its operating assets on February 27, 2003. As a result, the company has changed its basis of accounting from the going concern basis to the liquidation basis of accounting as of December 31, 2002.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Encompass Electrical Technologies - Rocky Mountains, Inc. d/b/a Riviera Electric, Inc. as of December 31, 2002 and 2001, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

BROCKMANN, ARMOUR & CO. LLC
Denver, Colorado
May 5, 2003

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ENCOMPASS ELECTRICAL TECHNOLOGIES, - ROCKY MOUNTAINS, INC.
d/b/a RIVIERA ELECTRIC, INC.
BALANCE SHEETS

ASSETS

| | December 31, | |
|---|---------------|---------------|
| | 2002 | 2001 |
| Current assets: | | |
| Cash and cash equivalents | \$ -- | \$ -- |
| Accounts receivable, net of allowance for doubtful Accounts of \$400,000 and \$260,000, respectively - | | |
| Uncompleted contracts | 12,558,266 | 7,926,119 |
| Completed contracts | 291,989 | 193,585 |
| Service | 3,865,597 | 3,933,046 |
| Retainage | 3,790,382 | 3,351,061 |
| Employee and other | 11,966 | 20,380 |
| Provision for loss on disposal of assets | (6,846,940) | -- |
| Costs and estimated earnings in excess of billings on uncompleted contracts | 541,042 | 468,762 |
| Unbilled work-in-process | 179,258 | 512,162 |
| Deferred tax asset, current | -- | 282,000 |
| Other current assets | 113,998 | 54,714 |
| | 14,505,558 | 16,741,829 |
| Property and equipment, net of accumulated depreciation and amortization | 964,848 | 1,200,930 |
| Other assets: | | |
| Goodwill, net of impairment reserve totaling \$23,106,875 as of December 31, 2002 and net of accumulated amortization totaling \$1,732,661 as of December 31, 2001, respectively | -- | 21,374,214 |
| Due from parent company, net of impairment reserve totaling \$8,818,913 and \$0, respectively | -- | 10,505,838 |
| Other assets | 228,142 | 239,236 |
| | 228,142 | 32,119,288 |
| Total assets | \$ 15,698,548 | \$ 50,062,047 |

See independent auditor's report and notes to financial statements.

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ENCOMPASS ELECTRICAL TECHNOLOGIES, - ROCKY MOUNTAINS, INC.
d/b/a RIVIERA ELECTRIC, INC.
BALANCE SHEETS (continued)

LIABILITIES

| | December 31, | |
|---|---------------|---------------|
| | 2002 | 2001 |
| | ----- | ----- |
| Current liabilities: | | |
| Checks written in excess of cash balance | \$ 448,718 | \$ 136,085 |
| Accounts payable - | | |
| Trade | 4,907,551 | 4,377,880 |
| Retainage | 231,069 | 68,606 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | 1,513,458 | 1,485,293 |
| Accrued liabilities - | | |
| Salaries, wages and bonuses | 3,030,182 | 3,065,523 |
| Payroll tax, withholdings and other | 790,685 | 726,509 |
| Compensated absences | 562,994 | 495,770 |
| Pension and profit-sharing contributions | 63,498 | 182,515 |
| Reserve for health insurance claims and other | 439,393 | 246,385 |
| | ----- | ----- |
| Total current liabilities | 11,987,548 | 10,784,566 |
| Deferred tax liability, non-current | 96,000 | 100,000 |
| | | |
| STOCKHOLDER'S EQUITY | | |
| Common stock, no par value, 1,000 shares authorized, 100 shares issued and outstanding | 26,291,479 | 26,291,479 |
| Retained earnings (accumulated deficit) | (22,676,479) | 12,886,002 |
| | ----- | ----- |
| Total stockholder's equity | 3,615,000 | 39,177,481 |
| | ----- | ----- |
| Total Liabilities and Stockholders' Equity | \$ 15,698,548 | \$ 50,062,047 |
| | ===== | ===== |

See independent auditor's report and notes to financial statements.

ENCOMPASS ELECTRICAL TECHNOLOGIES, - ROCKY MOUNTAINS, INC.
d/b/a RIVIERA ELECTRIC, INC.
STATEMENTS OF OPERATIONS

December 31,
2002 2001

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| | | |
|---|-----------------|---------------|
| | ----- | ----- |
| Revenue: | | |
| Contracts | \$ 64,626,413 | \$ 59,305,363 |
| Service | 19,442,135 | 22,989,745 |
| | ----- | ----- |
| | 84,068,548 | 82,295,108 |
| Cost of revenue: | | |
| Contracts | 52,160,400 | 45,311,726 |
| Service | 16,909,203 | 18,905,761 |
| | ----- | ----- |
| | 69,069,603 | 64,217,487 |
| Gross profit | 14,998,945 | 18,077,621 |
| General and administrative expenses | 11,959,415 | 11,955,519 |
| Provision for loss on disposal of assets | 6,846,940 | -- |
| Impairment of amounts due from parent company | 8,818,913 | -- |
| | ----- | ----- |
| Income (loss) from operations | (12,626,323) | 6,122,102 |
| Other income (expense): | | |
| Interest income | 3,963 | 21,749 |
| Gain (loss) on disposal of property and equipment | 10,161 | (151,157) |
| Other income | 104,096 | 345,748 |
| | ----- | ----- |
| | 118,220 | 216,340 |
| Income (loss) before income tax provision and cumulative effect of change in accounting principle | (12,508,103) | 6,338,442 |
| Income tax provision: | | |
| Current | 1,402,164 | 2,561,768 |
| Deferred | 278,000 | 34,000 |
| | ----- | ----- |
| | 1,680,164 | 2,595,768 |
| Income (loss) before cumulative effect of change in accounting principle | (14,188,267) | 3,742,674 |
| Cumulative effect of change in accounting principle, | 21,374,214 | -- |
| net of tax | ----- | ----- |
| Net income (loss) | \$ (35,562,481) | \$ 3,742,674 |
| | ===== | ===== |

See independent auditor's report and notes to financial statements.

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ENCOMPASS ELECTRICAL TECHNOLOGIES, - ROCKY MOUNTAINS, INC.
d/b/a RIVIERA ELECTRIC, INC.
STATEMENT OF CHANGES IN STOCKHOLDER'S EQUITY
YEARS ENDED DECEMBER 31, 2002 AND 2001

| | Common Stock | | Retained earnings (accumulated (deficit)) | Total |
|---|-------------------------------------|---------------|---|---------------|
| | Shares issued and outstanding | Amount | | |
| Balance, January 1, 2001 | 100 | \$ 18,355,324 | \$ 6,178,958 | \$ 24,534,282 |
| Increase attributable to merger of affiliate company | -- | 7,936,155 | 2,964,370 | 10,900,525 |
| Net income | -- | -- | 3,742,674 | 3,742,674 |
| Balance, December 31, 2001 | 100 | 26,291,479 | 12,886,002 | 39,177,481 |
| Net loss | -- | -- | (35,562,481) | (35,562,481) |
| Balance, December 31, 2002 | 100 | \$ 26,291,479 | \$ (22,676,479) | \$ 3,615,000 |

See independent auditor's report and notes to financial statements.

7

ENCOMPASS ELECTRICAL TECHNOLOGIES, - ROCKY MOUNTAINS, INC.
d/b/a RIVIERA ELECTRIC, INC.
STATEMENT OF CASH FLOWS

| | December 31, | |
|---|-----------------|--------------|
| | 2002 | 2001 |
| Cash flows from operating activities: | | |
| Net income (loss) | \$ (35,562,481) | \$ 3,742,674 |
| Adjustments to reconcile net income (loss) to net cash Provided (used) by operating activities - | | |
| Depreciation and amortization | 348,465 | 906,000 |
| Provision for allowance for doubtful accounts | 140,000 | (232,419) |
| (Gain) loss on disposal of property and equipment | (10,161) | 151,157 |
| Cumulative effect of change in accounting principle | 21,374,214 | -- |
| Impairment of amounts due from parent company | 8,818,913 | -- |
| Provision for loss on disposal of assets | 6,846,940 | -- |

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| | | |
|--|-------------|-------------|
| Deferred income tax provision | 278,000 | 34,000 |
| (Increase) decrease in - | | |
| Accounts receivable | (5,234,009) | 5,614,417 |
| Costs and estimated earnings in excess of billings on uncompleted contracts | (72,280) | (275,262) |
| Unbilled work-in-progress | 332,904 | (168,457) |
| Other current assets | (48,190) | 41,313 |
| Increase (decrease) in - | | |
| Checks written in excess of cash balance | 312,633 | 507,608 |
| Accounts payable | 692,134 | 27,248 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | 28,165 | (2,918,251) |
| Accrued liabilities | 170,050 | 1,240,412 |
| | ----- | ----- |
| Net cash provided (used) by operating activities | (1,584,703) | 8,670,440 |
| Cash flows from investing activities: | | |
| Release of restricted cash | -- | 111,543 |
| Proceeds from disposal of property and equipment | 12,031 | 40,573 |
| Purchase of property and equipment | (114,253) | (394,000) |
| | ----- | ----- |
| Net cash used by investing activities | (102,222) | (241,884) |
| Cash flows from financing activities: | | |
| Net advances from / (advances to) parent company | 1,686,925 | (8,428,556) |
| | ----- | ----- |
| Net cash provided (used) by financing activities | 1,686,925 | (8,428,556) |
| | ----- | ----- |
| Net increase in cash and cash equivalents | -- | -- |
| Cash and cash equivalents, beginning of year | -- | -- |
| | ----- | ----- |
| Cash and cash equivalents, end of year | \$ -- | \$ -- |
| | ===== | ===== |

See independent auditor's report and notes to financial statements.

Encompass Electrical Technologies - Rocky Mountains, Inc.
d/b/a Riviera Electric, Inc.

NOTES TO FINANCIAL STATEMENTS

1. Organization and description of business:

Encompass Electrical Technologies - Rocky Mountains, Inc. d/b/a Riviera Electric, Inc. (the Company), a wholly owned subsidiary of Encompass Services Corporation (ESC), is a construction and servicing company specializing in building and maintaining electrical systems in the State of Colorado. The Company performs work primarily in the industrial, commercial and municipal markets.

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The Company was incorporated on February 12, 1998, as CCC3 Acquisition Co., a wholly owned subsidiary of Consolidated Capital Corporation (CCC), in the State of Colorado. On February 27, 1998, CCC merged with Riviera Electric Construction Co., where CCC was the surviving corporation, and in March 1998 took the trade name Riviera Electric, Inc. On September 15, 1998, CCC changed its name to Building One Services Corporation (Building One). On February 22, 2000, Building One merged with Group Maintenance America Corp and changed its name to Encompass Services Corporation. On March 21, 2001, the Company changed its name to Encompass Electrical Technologies - Rocky Mountains, Inc., d/b/a Riviera Electric, Inc.

The Company's long-term construction contracts are primarily comprised of fixed-price contracts and cost-plus-a-fee contracts subject to a guaranteed maximum price. The Company's service contracts are primarily comprised of fixed-price and time and material contracts. One customer comprised 17% of contract revenues and two customers comprised 37% of contract revenues during the years ended December 31, 2002 and 2001, respectively.

2. Summary of significant accounting policies:

Liquidation basis of accounting

As discussed further in Note 14 to the financial statements, on February 27, 2003, the Company sold substantially all of its operating assets and contracts to IES ENC, Inc., a wholly owned subsidiary of Integrated Electrical Services, Inc. As a result, the Company has changed its basis of accounting from the going concern basis to the liquidation basis of accounting as of December 31, 2002. In conjunction with this change in the Company's basis of accounting, the Company has recognized a provision for loss on disposal of assets totaling \$6,846,940 to reflect the Company's net assets at a value approximating the net proceeds received from the sale of the Company.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

9

Operating cycle

The length of the Company's contracts typically last six months, but occasionally exceed one year. In accordance with normal construction industry practice, the Company includes in current assets and current liabilities certain amounts relating to construction contracts, which may be realizable and payable over a period in excess of one year.

Accounting for construction contracts and service revenue

Revenues from long-term construction contracts are recognized on the percentage-of-completion method, measured by the percentage of total costs incurred to date to estimated total costs for each contract. This method is used because management considers expected costs to be the best available measure of progress on these contracts.

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Revenues from cost-plus-fee contracts are recognized on the basis of costs incurred during the period plus the fee earned. Contract costs include all direct job costs and those indirect costs related to contract performance, such as indirect labor, payroll taxes and benefits, supplies, insurance, vehicle expenses, equipment repairs, and depreciation. General and administrative costs are charged to expense as incurred.

The asset, "Costs and estimated earnings in excess of billings on uncompleted contracts", represents revenue recognized in excess of billings. The liability, "Billings in excess of costs and estimated earnings on uncompleted contracts", represents billings in excess of revenue recognized.

Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined. Changes in job performance, job conditions, and estimated profitability, including those arising from final contract settlements, may result in revisions to costs and income and are recognized in the period in which the revisions are determined. Profit incentives are included in revenues when their realization is reasonably assured. An amount equal to contract costs attributable to claims is included in revenues when realization is probable and the amount can be reliably estimated.

Revenues from service work are recognized on the accrual method, measured by amounts billed and unbilled work-in-process, which is comprised of billable hours at stated contractual billing rates plus reimbursable expenses at stated contractual mark-up rates.

Concentrations of risk

Financial instruments that potentially subject the Company to credit risk consist principally of cash and cash equivalents and accounts receivable.

Accounts receivable are concentrated with customers located throughout Colorado. At December 31, 2002 and 2001, two and three customers comprised approximately 30% and 43%, respectively of outstanding accounts receivable. To reduce the credit risk associated with accounts receivable, the Company routinely files liens and analyzes the credit worthiness of its customers and reviews the funding mechanisms of municipal projects to protect the Company's interests.

10

Cash and cash equivalents

The Company includes cash equivalents under the caption cash and cash equivalents. Cash equivalents include money market funds and other highly liquid financial instruments with an initial maturity of less than three months. Checks written in excess of cash balance represents outstanding checks exceeding the Company's bank balances.

Accounts receivable

Accounts receivable from long-term construction contracts are based on contract prices. Accounts receivable from service work are based on contract prices, and consist primarily of groups of small-balance homogeneous accounts, which are collectively evaluated for impairment.

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The Company provides an allowance for doubtful accounts based upon a review of outstanding receivables, historical collection information, and existing economic conditions. Contract and service receivables are due 30 days after the date of the invoice. Retentions receivable are due 30 days after completion of the project and acceptance by the owner. Receivables past due more than 180 days are considered delinquent. Delinquent receivables may be reserved or written-off based on individual credit evaluation and specific circumstances of each customer. As of December 31, 2002 and 2001, the Company had \$400,000 and \$260,000, respectively, reserved as allowance for doubtful accounts.

Property and equipment

Property and equipment is stated at cost. Repairs and maintenance of a routine nature are charged to expense as incurred, while those that improve or extend the life of existing assets are capitalized. When items of property and equipment are sold or retired, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is included in income. Depreciation is provided on a straight-line basis over the estimated useful lives of the respective assets. Vehicles, office furniture and equipment and machinery and equipment are depreciated between 3 and 7 years. Leasehold improvements are depreciated between 5 and 7 years.

Realization of long-lived assets

In accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", the Company evaluates the recoverability of property and equipment or other assets, if facts and circumstances indicate that any of those assets might be impaired. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying amount to determine if an impairment of such property has occurred. The effect of any impairment would be to expense the difference between the fair value of such property and its carrying value. To date, the Company has not recorded any such impairment.

11

Fair value of financial instruments

The Company's financial instruments include cash and cash equivalents, accounts receivable, amounts due from parent company and accounts payable. The fair values of these financial instruments approximates their carrying amounts based on their subsequent liquidation as a result of the sale of the Company.

Advertising

Advertising costs are charged to expense as incurred and are included in general and administrative expenses. Advertising expense totaled \$154,945 and \$92,300 for the years ended December 31, 2002 and 2001, respectively.

Income taxes

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The current provision for income taxes represents estimated income taxes currently due. Deferred tax assets and liabilities are recorded for the estimated future tax effects of temporary differences between the tax basis of assets and liabilities and amounts reported in the balance sheets. The overall change in deferred tax assets and liabilities for the period measures the deferred tax provision for the period. Effects of changes in enacted tax laws on deferred tax assets and liabilities are reflected as adjustments to tax expense in the period of enactment.

3. Goodwill

Effective January 1, 2002, the Company adopted Statement of Accounting Standards (SFAS), No. 142, "Goodwill and Other Intangible Assets," which establishes new accounting and reporting requirements for goodwill and other intangible assets. Under SFAS No. 142, all goodwill amortization ceased effective January 1, 2002. Goodwill attributable to each of the Company's reporting units was tested for impairment by comparing the fair value of each reporting unit with its carrying value. Fair value was determined using discounted cash flows, market multiples and market capitalization as of January 1, 2002. Significant estimates used in the methodologies include estimates of future cash flows, future short-term and long-term growth rates, weighted average cost of capital and estimates of market multiples for each of the reportable units. These impairment tests are required to be performed at adoption of SFAS No. 142 and at least annually thereafter or upon divestiture of a reporting unit. The Company determined its investment in goodwill had become impaired and recorded an impairment charge of \$21,374,214. Under SFAS No. 142, the impairment adjustment recognized at adoption of the new rules was reflected as a cumulative effect of change in accounting principle in the Company's statements of operations. Impairment adjustments recognized after adoption, if any, generally are required to be recognized as operating expenses.

The audited results of operations presented below for the year ended December 31, 2002 and adjusted results of operations for the year December 31, 2001 reflect the operations of the Company had the Company adopted the non-amortization provisions of SFAS No. 142 effective January 1, 2001:

12

| | 2002 | 2001 |
|--|----------------|--------------|
| | ----- | ----- |
| Reported net income (loss) | \$(35,562,481) | \$ 3,742,674 |
| Add: Cumulative effect of a change in accounting principle, net of tax | 21,374,214 | -- |
| Add: Goodwill amortization, net of tax | -- | 527,538 |
| | ----- | ----- |
| Adjusted net income (loss) | \$(14,188,267) | \$ 4,270,212 |
| | ===== | ===== |

4. Property and equipment

| | | Accumulated | Net Book |
|--------------------|------|--------------|----------|
| December 31, 2002: | Cost | Depreciation | Value |
| | | | |

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| | | | |
|--------------------------------|-------------|-------------|------------|
| Vehicles | \$ 203,169 | \$ 137,145 | \$ 66,024 |
| Office furniture and equipment | 961,296 | 623,132 | 338,164 |
| Machinery and equipment | 474,761 | 269,533 | 205,228 |
| Leasehold improvements | 478,245 | 122,813 | 355,432 |
| | ----- | ----- | ----- |
| | \$2,117,471 | \$1,152,623 | \$ 964,848 |
| | ===== | ===== | ===== |

December 31, 2001:

| | | | |
|--------------------------------|-------------|------------|-------------|
| Vehicles | \$ 209,871 | \$ 102,304 | \$ 107,567 |
| Office furniture and equipment | 848,595 | 443,195 | 405,400 |
| Machinery and equipment | 474,761 | 197,268 | 277,493 |
| Leasehold improvements | 471,486 | 61,016 | 410,470 |
| | ----- | ----- | ----- |
| | \$2,004,713 | \$ 803,783 | \$1,200,930 |
| | ===== | ===== | ===== |

Depreciation expense on property and equipment totaled \$348,465 and \$378,462 for the years ended December 31, 2002 and 2001, respectively. Depreciation expense allocated to cost of contract revenue for the years ended December 31, 2002 and 2001, totaled \$111,938 and \$122,098, respectively.

5. Income taxes

The Company accounts for income taxes under the provisions of Statement of Financial Accounting Standards (SFAS) No. 109, "Accounting for Income Taxes", which establishes accounting and reporting standards for recognizing the tax effects of differences between the tax basis of assets and liabilities and their reported amounts in the financial statements.

The Company has an informal tax sharing agreement with ESC under which the Company incurs income tax expense (benefit) for taxes computed as if the Company were a separate entity. The Company recognizes an asset or liability to ESC in the amount of current income taxes and records deferred taxes calculated pursuant to the rules of SFAS No. 109.

During the years ended December 31, 2002 and 2001, the Company provided for income tax expense at a combined Federal and state rate of 37.5%. A reconciliation between the reported provision for income taxes and the expected amounts computed by applying the

statutory Federal income tax rate of 34% to earnings before income taxes is as follows for the years ended December 31, 2002 and 2001:

| | | |
|--|----------------|--------------|
| | 2002 | 2001 |
| | ----- | ----- |
| Expected tax expense (benefit) | \$ (4,252,755) | \$ 2,155,070 |
| State income taxes, net of federal benefit | (579,125) | 293,470 |
| Permanent differences and other | 6,512,044 | 147,228 |
| | ----- | ----- |
| Total provision for income taxes | \$ 1,680,164 | \$ 2,595,768 |

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Permanent differences are primarily attributable to the non-deductibility of the provision for loss on disposal of assets and impairment of amounts due from ESC.

The provision for income taxes for the years ended December 31, 2002 and 2001 consists of the following:

| | 2002 | 2001 |
|----------|-------------|-------------|
| | ----- | ----- |
| Current | \$1,402,164 | \$2,561,768 |
| Deferred | 278,000 | 34,000 |
| | ----- | ----- |
| | \$1,680,164 | \$2,595,768 |
| | ===== | ===== |

The deferred income tax (expense) for the years ended December 31, 2002 and 2001, results from the following:

| | 2002 | 2001 |
|--|--------------|-------------|
| | ----- | ----- |
| Differences between financial and tax reporting: | | |
| Allowance for doubtful accounts | \$ 52,500 | \$ (87,157) |
| Accrued compensated absences | 25,209 | 62,484 |
| Accrued reserve for health insurance claims | 74,473 | 63,294 |
| Contracts less than 10% complete | 66,966 | (37,135) |
| Provision for loss on disposal of assets | 2,567,603 | -- |
| Depreciation | 4,173 | (36,562) |
| Increase in valuation allowance | (3,068,000) | -- |
| Other | (924) | 1,076 |
| | ----- | ----- |
| | \$ (278,000) | \$ (34,000) |
| | ===== | ===== |

The net deferred tax asset (liability) consists of the following as of December 31:

| | 2002 | 2001 |
|-------------|-------------|------------|
| | ----- | ----- |
| Current | \$ -- | \$ 282,000 |
| Non-current | (96,000) | (100,000) |
| | ----- | ----- |
| | \$ (96,000) | \$ 182,000 |
| | ===== | ===== |

Following are the components of the net deferred tax assets (liabilities) as of December 31:

| | 2002 | 2001 |
|----------------------|-------|-------|
| | ----- | ----- |
| Deferred tax assets: | | |

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| | | |
|--|-------------|------------|
| Allowance for doubtful accounts | \$ 150,000 | \$ 97,500 |
| Accrued compensated absences | 211,123 | 185,914 |
| Accrued reserve for health insurance claims | 137,768 | 63,295 |
| Provision for loss on disposal of assets | 2,567,603 | -- |
| Other | 1,506 | 3,053 |
| | ----- | ----- |
| | 3,068,000 | 349,762 |
| Less valuation allowance | (3,068,000) | -- |
| | ----- | ----- |
| Total deferred tax asset | -- | 349,762 |
| Deferred tax liabilities | | |
| Contracts less than 10% complete | -- | (66,966) |
| Depreciation | (96,000) | (100,796) |
| | ----- | ----- |
| Total deferred tax liabilities | (96,000) | (167,762) |
| | ----- | ----- |
| Net deferred tax assets (liabilities) | \$ (96,000) | \$ 182,000 |
| | ===== | ===== |

A valuation allowance has been provided at December 31, 2002, as the benefits of the deferred tax asset will accrue to the benefit of ESC upon their recognition, the benefit of which is not anticipated to be reimbursed to the Company.

6. Contracts in progress

| | Year ended December 31, | |
|--|-------------------------|----------------|
| | 2002 | 2001 |
| | ----- | ----- |
| Total contracts | \$ 86,574,545 | \$ 101,775,147 |
| Estimated costs: | | |
| Costs to date | 53,084,473 | 42,588,617 |
| Costs to complete | 16,525,986 | 37,085,987 |
| | ----- | ----- |
| Total estimated costs | 69,610,459 | 79,674,604 |
| | ----- | ----- |
| Estimated gross profit | \$ 16,964,086 | \$ 22,100,543 |
| | ===== | ===== |
| Amount billed to date | \$ 67,042,598 | \$ 55,152,521 |
| Cost and estimated earnings in excess of billings on uncompleted contracts | 541,042 | 468,762 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | (1,513,458) | (1,485,293) |
| | ----- | ----- |
| Contract revenue earned | 66,070,182 | 54,135,990 |
| Costs to date | 53,084,473 | 42,588,617 |
| | ----- | ----- |
| Gross profit earned | \$ 12,985,709 | \$ 11,547,373 |
| | ===== | ===== |

7. Backlog

The following is a reconciliation of backlog representing unearned contract revenue on signed contracts:

| | December 31, | |
|------------------------------|---------------|---------------|
| | 2002 | 2001 |
| Balance, January 1, | \$ 47,639,157 | \$ 36,408,843 |
| New contracts | 33,719,896 | 63,310,660 |
| Contract adjustments | 3,771,723 | 7,225,017 |
| | 85,130,776 | 106,944,520 |
| Less contract revenue earned | (64,626,413) | (59,305,363) |
| Balance, December 31, | \$ 20,504,363 | \$ 47,639,157 |

8. Operating leases

The Company leases certain vehicles under master lease agreements originated by ESC on behalf of the Company and office equipment, storage, job site housing and office facilities under various operating lease agreements with initial terms ranging from 30 to 84 months that expire through March 2008. Future minimum lease payments under operating lease arrangements as of December 31, 2002 are as follows:

| | Year ending December 31, |
|------------|-----------------------------|
| 2003 | \$1,569,570 |
| 2004 | 1,313,521 |
| 2005 | 1,182,819 |
| 2006 | 795,431 |
| 2007 | 649,083 |
| Thereafter | 41,790 |
| | \$5,552,214 |

Rent expense under such operating lease arrangements for the years ended December 31, 2002 and 2001 totaled \$1,598,198 and \$1,499,789, respectively, which is included in general and administrative expense and costs of contract revenue.

9. Profit Sharing Plan / 401(k) plan

ESC maintains a group profit sharing/401(k) plan covering all full-time employees who have been employed by the Company for more than three months. Under the plan, employees may make before-tax contributions ranging from 0% to 15%, subject to certain other limitations. Employer contributions are made at a rate of 50% of pre-tax earnings, up to a maximum of 6% of eligible earnings. Employees are fully vested in their individual

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contributions immediately and fully vested in Company contributions after one year of employment. For plan years ended December 31, 2002 and 2001, matching contributions to the group plan made by the Company totaled \$494,636 and \$493,138, respectively.

16

10. Related party transactions

The Company subcontracted to other divisions of ESC as well as provided electrical services for other divisions of ESC. ESC also provided group health, general liability, worker's compensation and casualty insurance, a group 401(k) plan and surety bonds for its divisions. The following is a list of related party transactions with ESC and other divisions of ESC as of or for the years ended December 31:

| | 2002 | 2001 |
|---|------------|------------|
| | ----- | ----- |
| Accounts receivable | \$ 526,376 | \$ 490,709 |
| Retention receivable | 112,854 | 2,580 |
| Accounts payable | 940,900 | 7,499 |
| Retention payable | 158,716 | 876 |
| Management fees paid to ESC | 3,023,609 | 2,752,334 |
| Insurance premiums paid to ESC | 1,862,811 | 1,558,536 |
| 401 (k) remittances | 2,091,140 | 2,082,950 |
| Surety bonds | 80,497 | 158,453 |
| Intercompany revenues earned | 3,069,121 | 2,350,918 |
| Intercompany subcontract costs incurred | 2,160,493 | 106,112 |

As of December 31, 2002, the Company has impaired the net intercompany balance due from ESC totaling \$8,818,913 as ESC is in Chapter 11 reorganization and this amount was not satisfied as a result of the sale of substantially all of the operating assets of the Company (see Note 14).

11. Merger

Effective March 22, 2001, the Company and Zwart, Inc. d/b/a Mountain View Electric (MVE), a wholly owned subsidiary of ESC, entered into a merger agreement to combine the operations of the two companies. Subsequent to the merger, the Company dissolved MVE.

12. Partial self-insurance plan

ESC provides a group health insurance plan providing medical benefits to eligible employees of the Company under a partially self-insured plan (the "Plan"). Under the Plan, the Company pays for all claims less than \$75,000 per year, per plan member, with a third-party insurance carrier providing for "stop loss" insurance on claims in excess of this amount. The Plan is administered by a third-party administrator. The Company reserves amounts each month for estimated claims incurred but not reported (payable by the Company) based on administrator provided estimates. Reserves as of December 31, 2002 and 2001 total \$367,000 and \$135,000, which are included on the accompanying balance sheets under the caption "Reserve for health insurance claims and other". Claims and administrative fees paid during the years ended December 31, 2002 and 2001 totaled \$3,000,047 and \$3,104,801, respectively.

17

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13. Cash flows

During the year ended December 31, 2001, the Company had non-cash operating, investing and financing activities resulting from its merger with MVE on March 22, 2001 as follows:

| | |
|--|-------------|
| Net cash received in merger | \$ 139,515 |
| Accounts receivable and other current assets | 2,398,486 |
| Receivable from ESC | 1,249,736 |
| Cost and estimated earnings in excess of billings on uncompleted contracts | 75,495 |
| Unbilled work-in-process | 65,786 |
| Property and equipment, net of accumulated depreciation totaling \$63,167 | 122,470 |
| Goodwill, net of accumulated amortization totaling \$304,806 | 8,211,495 |
| Accounts payable | (480,894) |
| Accrued liabilities | (203,107) |
| Billings in excess of costs and estimated earnings on uncompleted contracts | (678,457) |
| Common stock | (7,936,155) |
| Retained earnings | (2,964,370) |

14. Subsequent event

On February 27, 2003, the Company sold all of its operating assets and contracts to IES ENC, Inc., a wholly owned subsidiary of Integrated Electrical Services, Inc., for \$3,850,000 less a final purchase price adjustment of approximately \$235,000, for a net total of approximately \$3,615,000 plus assumed liabilities.

15. Commitments and contingencies

The Company engages in cost-plus-a-fee contracts subject to guaranteed maximum price provisions. These contracts have specific definitions for cost and are subject to audit provisions by the owners or general contractors. No determination has been made as to the impact, if any, an audit of the underlying costs would have on the Company's financial position or results of operations. Currently, none of the Company's contracts are under audit.

The Company is occasionally engaged in legal matters, which arise in the ordinary course of business. Management intends to vigorously defend such matters. Management does not believe that the disputes will have a material adverse impact on the results of operations or financial position of the Company.

The Company had pledged its operating assets as of December 31, 2002 and 2001 and was a guarantor of various debt obligations of ESC.

(B) PRO FORMA FINANCIAL INFORMATION

INTEGRATED ELECTRICAL SERVICES, INC.

UNAUDITED PRO FORMA FINANCIAL STATEMENTS

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BASIS OF PRESENTATION

The unaudited pro forma statements of operations for the year ended September 30, 2002, presents the statement of operations data to give effect to the acquisition by Integrated Electrical Services, Inc. ("IES"), of Riviera Electric, Inc. as if it had occurred on October 1, 2001. The unaudited pro forma statements of operations for the six months ended March 31, 2003, presents the statement of operations data to give effect to the acquisition by Integrated Electrical Services, Inc., of Riviera Electric, Inc. (the "Company") as if it had occurred on October 1, 2002.

IES has analyzed the savings that it expects to realize from reductions in administrative bonuses on plans that will not continue and management charges and has reflected these savings in the unaudited pro forma statements of operations.

Certain pro forma adjustments are based on preliminary estimates, available information and certain assumptions that IES management deems appropriate and may be revised as additional information becomes available. The pro forma financial data do not purport to represent what IES's combined results of operations would actually have been if such transactions in fact had occurred on this date and are not necessarily representative of IES's combined financial position or results of operations for any future period. Since the acquired entity was not under common control or management prior to its acquisition by IES, historical combined results may not be comparable to, or indicative of, future performance. The unaudited pro forma combined financial statements should be read in conjunction with the historical consolidated financial statements and notes thereto included in the company's Annual Report for the year ended September 30, 2002 filed on Form 10-K. See also "Risk Factors" included elsewhere therein.

19

INTEGRATED ELECTRICAL SERVICES, INC., AND SUBSIDIARIES UNAUDITED PRO FORMA STATEMENT OF OPERATIONS FOR THE YEAR ENDED SEPTEMBER 30, 2002 (IN THOUSANDS)

| | IES and Subsidiaries | Riviera Electric, Inc. | Pro Forma Adjustments | |
|--|-------------------------|---------------------------|--------------------------|--------|
| | ----- | ----- | ----- | |
| REVENUES..... | \$ 1,475,430 | \$ 84,069 | \$ - | |
| COST OF SERVICES..... | 1,253,844 | 69,070 | - | |
| | ----- | ----- | ----- | |
| Gross profit..... | 221,586 | 14,999 | - | |
| SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES..... | 174,184 | 11,959 | (4,117) | (a, b) |
| RESTRUCTURING CHARGES..... | 5,556 | - | - | |
| PROVISION FOR LOSS ON DISPOSAL OF ASSETS IMPAIRMENT OF AMOUNTS DUE FROM PARENT... | - | 6,847 | (6,847) | (c) |
| | - | 8,819 | (8,819) | (d) |
| | ----- | ----- | ----- | |
| Income (loss) from operations..... | 41,846 | (12,626) | 19,783 | |
| OTHER INCOME (EXPENSE): | | | | |

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| | | | |
|--|--------------|-------------|-----------|
| Interest expense..... | (26,702) | 4 | - |
| Other, net..... | 964 | 114 | - |
| | ----- | ----- | ----- |
| Interest and other expense, net..... | (25,738) | 118 | - |
| INCOME (LOSS) BEFORE INCOME TAXES AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE..... | 16,108 | (12,508) | 19,783 |
| PROVISION FOR INCOME TAXES..... | 6,175 | 1,680 | 1,147 |
| CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET OF TAX..... | 283,284 | 21,374 | - |
| | ----- | ----- | ----- |
| NET INCOME (LOSS)..... | \$ (273,351) | \$ (35,562) | \$ 18,636 |
| | ===== | ===== | ===== |
| BASIC EARNINGS (LOSS) PER SHARE: | | | |
| Basic earnings per share before cumulative effect of change in accounting principle..... | | | |
| | \$ 0.25 | | |
| | ===== | | |
| Cumulative effect of change in accounting principle..... | | | |
| | \$ (7.11) | | |
| | ===== | | |
| Basic earnings (loss) per share..... | \$ (6.86) | | |
| | ===== | | |
| DILUTED EARNINGS (LOSS) PER SHARE: | | | |
| Diluted earnings per share before cumulative effect of change in accounting principle..... | | | |
| | \$ 0.25 | | |
| | ===== | | |
| Cumulative effect of change in accounting principle..... | | | |
| | \$ (7.11) | | |
| | ===== | | |
| Diluted earnings (loss) per share..... | \$ (6.86) | | |
| | ===== | | |
| SHARES USED IN THE COMPUTATION OF EARNINGS (LOSS) PER SHARE: | | | |
| Basic..... | 39,847,591 | | |
| | ===== | | |
| Diluted..... | 39,847,591 | | |
| | ===== | | |

See note to unaudited pro forma financial statements.

21

INTEGRATED ELECTRICAL SERVICES, INC., AND SUBSIDIARIES
UNAUDITED PRO FORMA STATEMENT OF OPERATIONS
FOR THE SIX MONTHS ENDED MARCH 31, 2003
(IN THOUSANDS)

| | IES and Subsidiaries | Riviera Electric, Inc. | Pro Forma Adjustments |
|-----------------------|-------------------------|---------------------------|--------------------------|
| | ----- | ----- | ----- |
| REVENUES..... | \$ 691,712 | \$ 27,896 | \$ - |
| COST OF SERVICES..... | 591,251 | 23,580 | - |
| | ----- | ----- | ----- |

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| | | | | |
|---|------------|-------------|-----------|-------|
| Gross profit..... | 100,461 | 4,316 | - | |
| SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES..... | 76,079 | 4,344 | (1,140) | (a,b) |
| PROVISION FOR LOSS ON DISPOSAL OF ASSETS..... | - | 6,847 | (6,847) | (c) |
| IMPAIRMENT OF AMOUNT DUE | - | 8,819 | (8,819) | (d) |
| | ----- | ----- | ----- | |
| FROM PARENT..... | | | | |
| Income (loss) from operations..... | 24,382 | (15,694) | 16,806 | |
| OTHER INCOME (EXPENSE): | | | | |
| Interest expense..... | (12,799) | - | - | |
| Other, net..... | 85 | - | - | |
| | ----- | ----- | ----- | |
| Interest and other expense, net..... | (12,714) | - | - | |
| INCOME (LOSS) BEFORE INCOME TAXES..... | 11,668 | (15,694) | 16,806 | |
| PROVISION FOR INCOME TAXES..... | 4,492 | 420 | 8 | (e) |
| | ----- | ----- | ----- | |
| NET INCOME (LOSS)..... | \$ 7,176 | \$ (16,114) | \$ 16,798 | |
| | ===== | ===== | ===== | |
| EARNINGS PER SHARE: | | | | |
| Basic earnings per share..... | \$ 0.18 | | | |
| | ===== | | | |
| Diluted earnings per share..... | \$ 0.18 | | | |
| | ===== | | | |
| SHARES USED IN THE COMPUTATION OF EARNINGS (LOSS) PER SHARE: | | | | |
| Basic..... | 39,388,158 | | | |
| | ===== | | | |
| Diluted..... | 39,423,220 | | | |
| | ===== | | | |

See note to unaudited pro forma financial statements.

21

INTEGRATED ELECTRICAL SERVICES, INC.

NOTE TO UNAUDITED PRO FORMA FINANCIAL STATEMENTS

1. Unaudited Pro Forma Statement of Operations:

The Unaudited Pro Forma Statement of Operations for the year ended September 30, 2002 and for the six months ended March 31, 2003 for IES and Subsidiaries reflects the historical results of IES.

Pro Forma Adjustments consist of the following:

- (a) Reflects the reduction in administrative bonus payments to the management of the Company on plans that will not continue.
- (b) Reflects the reversal of management fees recorded by the previous owners of the Company.
- (c) Reflects the reversal of the provision for loss on disposal of assets which

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resulted from the liquidation basis of accounting. This liquidation basis of accounting resulted from the transaction.

- (d) Reflects the reversal of the impairment charge recorded for amounts due to the Company which resulted from the liquidation basis of accounting. This liquidation basis of accounting resulted from the transaction.
- (e) Reflects the incremental provision for federal and state income taxes at a 38.5% overall tax rate.

22

(C) EXHIBITS

23.1 Consent of Brockmann, Armour and Co., LLC

23

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Current Report to be signed on its behalf by the undersigned, thereunto duly authorized.

INTEGRATED ELECTRICAL SERVICES, INC.

By: /s/ William W. Reynolds

William W. Reynolds
Executive Vice President and
Chief Financial Officer

Dated: May 12, 2003

24

Exhibit 23.1

CONSENT OF INDEPENDENT AUDITORS

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We consent to the incorporation by reference in the Registration Statements (Forms S-8 and S-4 File Nos. 333-67113, 333-45447, 333-45449, 333-91041, 333-31608, 333-32624, 333-50031, 333-62636 and 333-68274) of Integrated Electrical Services, Inc. of our report dated May 5, 2003, with respect to the financial statements of Encompass Electrical Technologies - Rocky Mountains, Inc. d/b/a Riviera Electric, Inc. included in this Form 8-K.

BROCKMANN, ARMOUR & CO., LLC

Denver, Colorado

May 5, 2003