Mistras Group, Inc.
Form 10-Q
April 09, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended February 29, 2012

Or

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

For the transition period to

Commission file number 001- 34481

Mistras Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**22-3341267** (I.R.S. Employer Identification No.)
195 Clarksville Road **Princeton Junction, New Jersey** (Address of principal executive offices)	**08550** (Zip Code)

(609) 716-4000
(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes o 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). x Yes o No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o Yes x No

As of April 2, 2012, the registrant had 27,938,173 shares of common stock outstanding.

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PART I FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

Mistras Group, Inc. and Subsidiaries
Unaudited Consolidated Balance Sheets
(in thousands, except share data)

	February 29, 2012	May 31, 2011
ASSETS		
Current Assets		
Cash and cash equivalents	$ 7,931	$ 10,879
Accounts receivable, net	95,257	78,031
Inventories, net	13,173	9,830
Deferred income taxes	1,324	1,278
Prepaid expenses and other current assets	9,354	6,761
Total current assets	127,039	106,779
Property, plant and equipment, net	58,570	49,168
Intangible assets, net	33,559	27,304
Goodwill	80,053	64,146
Other assets	1,511	1,240
Total assets	$ 300,732	$ 248,637
LIABILITIES, PREFERRED STOCK AND EQUITY		
Current Liabilities		
Current portion of long-term debt	$ 5,963	$ 7,226
Current portion of capital lease obligations	6,644	5,853
Accounts payable	7,142	6,656
Accrued expenses and other current liabilities	40,332	28,028
Income taxes payable	466	2,825
Total current liabilities	60,547	50,588
Long-term debt, net of current portion	34,645	14,625
Obligations under capital leases, net of current portion	12,847	9,623
Deferred income taxes	2,425	2,863
Other long-term liabilities	5,197	3,452
Total liabilities	115,661	81,151
Commitments and contingencies		
Preferred stock, 10,000,000 shares authorized		
Equity		
Common stock, $0.01 par value, 200,000,000 shares authorized, 27,938,173 and 27,667,122 shares issued and outstanding as of February 29, 2012 and May 31, 2011, respectively	279	277
Additional paid-in capital	185,984	180,594
Retained earnings (accumulated deficit)	204	(14,017)
Accumulated other comprehensive (loss) income	(1,675)	303
Total Mistras Group, Inc. stockholders equity	184,792	167,157
Noncontrolling interest	279	329
Total equity	185,071	167,486
Total liabilities, preferred stock and equity	$ 300,732	$ 248,637

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

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Mistras Group, Inc. and Subsidiaries
Unaudited Consolidated Statements of Operations
(in thousands, except per share data)

	Three months ended		Nine months ended	
	February 29, 2012	**February 28, 2011**	**February 29, 2012**	**February 28, 2011**
Revenues:				
Services	$ 94,253	$ 72,411	$ 281,097	$ 216,616
Products	9,865	6,802	28,688	19,844
Total revenues	104,118	79,213	309,785	236,460
Cost of revenues:				
Cost of services	66,336	50,696	194,270	147,754
Cost of products sold	4,238	2,460	12,094	7,804
Depreciation related to services	3,760	3,307	10,639	9,252
Depreciation related to products	200	153	563	467
Total cost of revenues	74,534	56,616	217,566	165,277
Gross profit	29,584	22,597	92,219	71,183
Selling, general and administrative expenses	20,806	16,005	59,565	47,099
Research and engineering	578	514	1,769	1,638
Depreciation and amortization	1,805	1,385	4,787	3,889
Acquisition-related costs	849		510	
Legal reserve				351
Income from operations	5,546	4,693	25,588	18,206
Other expenses				
Interest expense	814	596	2,620	1,957
Loss on extinguishment of long-term debt	113		113	
Income before provision for income taxes	4,619	4,097	22,855	16,249
Provision for income taxes	1,548	1,690	8,672	6,562
Net income	3,071	2,407	14,183	9,687
Net (income) loss attributable to noncontrolling interests, net of taxes	(34)	36	38	26
Net income attributable to Mistras Group, Inc.	$ 3,037	$ 2,443	$ 14,221	$ 9,713
Earnings per common share (see Note 4):				
Basic	$ 0.11	$ 0.09	$ 0.51	$ 0.36
Diluted	$ 0.11	$ 0.09	$ 0.50	$ 0.36
Weighted average common shares outstanding:				
Basic	27,921	26,667	27,794	26,665
Diluted	28,829	26,919	28,563	26,824

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

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Mistras Group, Inc. and Subsidiaries

Unaudited Consolidated Statements of Stockholders Equity

(in thousands)

	Common Stock Shares	Common Stock Amount	Additional paid-in capital	Retained earnings (accumulated deficit)	Accumulated other comprehensive income (loss)	Total Mistras Group, Inc. Stockholders Equity	Noncontrolling Interest	Total Equity
Nine months ended February 28, 2011:								
Balance at May 31, 2010	26,664	$ 267	$ 162,054	$ (30,448)	$ (1,587)	$ 130,286	$ 268	$ 130,554
Net income				9,713		9,713	(26)	9,687
Other comprehensive income, net of tax:								
Foreign currency translation adjustment					880	880	5	885
Comprehensive Income						10,593	(21)	10,572
Stock compensation	1		2,680			2,680		2,680
Exercise of stock options	5		30			30		30
Noncontrolling interest in subsidiary							117	117
Balance at February 28, 2011	26,670	$ 267	$ 164,764	$ (20,735)	$ (707)	$ 143,589	$ 364	$ 143,953
Nine months ended February 29, 2012:								
Balance at May 31, 2011	27,667	$ 277	$ 180,594	$ (14,017)	$ 303	$ 167,157	$ 329	$ 167,486
Net income				14,221		14,221	(38)	14,183
Other comprehensive income, net of tax:								
Foreign currency translation adjustment					(1,978)	(1,978)	(12)	(1,990)
Comprehensive Income						12,243	(50)	12,193
Stock compensation	14		3,791			3,791		3,791
Net settlement on vesting of restricted stock units	36		(281)			(281)		(281)
Excess tax benefit from stock compensation			405			405		405
Exercise of stock options	221	2	1,475			1,477		1,477
Balance at February 29, 2012	27,938	$ 279	$ 185,984	$ 204	$ (1,675)	$ 184,792	$ 279	$ 185,071

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

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Mistras Group, Inc. and Subsidiaries

Unaudited Consolidated Statements of Cash Flows

(in thousands)

	Nine months ended February 29, 2012	Nine months ended February 28, 2011
Cash flows from operating activities		
Net income attributable to Mistras Group, Inc.	$ 14,221	$ 9,713
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	15,989	13,608
Deferred income taxes	(479)	171
Provision for doubtful accounts	189	45
Loss on extinguishment of long-term debt	113	
(Gain) loss on sale of assets	(40)	38
Amortization of deferred financing costs	116	127
Stock compensation expense	3,791	2,680
Interest rate swap		(210)
Noncontrolling interest	(38)	(26)
Foreign currency loss (gain)	231	(310)
Changes in operating assets and liabilities, net of effect of acquisitions of businesses		
Accounts receivable	(10,160)	(6,620)
Inventories	(2,624)	(1,377)
Prepaid expenses and other current assets	(1,386)	(1,743)
Other assets	(42)	971
Accounts payable	(1,310)	410
Income taxes payable	(2,302)	(302)
Accrued expenses and other current liabilities	4,703	1,468
Net cash provided by operating activities	20,972	18,643
Cash flows from investing activities		
Purchase of property, plant and equipment	(6,407)	(6,051)
Purchase of intangible assets	(437)	(398)
Acquisition of businesses, net of cash acquired	(26,273)	(18,301)
Proceeds from sale of equipment	301	170
Net cash used in investing activities	(32,816)	(24,580)
Cash flows from financing activities		
Repayment of capital lease obligations	(5,136)	(4,631)
Repayment of long-term debt	(4,420)	(6,808)
Net borrowings from revolver	19,050	5,000
Net (repayments) proceeds from other short-term borrowings	(1,868)	2,722
Proceeds from borrowings of long-term debt	837	42
Payment of financing costs	(623)	
Taxes paid related to net share settlement of equity awards	(281)	
Excess tax benefit from stock compensation	405	
Proceeds from the exercise of stock options	1,477	30
Net cash provided by (used in) financing activities	9,441	(3,645)
Effect of exchange rate changes on cash and cash equivalents	(545)	105
Net change in cash and cash equivalents	(2,948)	(9,477)
Cash and cash equivalents		
Beginning of period	10,879	16,037
End of period	$ 7,931	$ 6,560
Supplemental disclosure of cash paid		
Interest	$ 1,720	$ 2,058

Income taxes	$	11,995	$	6,581
Noncash investing and financing				
Equipment acquired through capital lease obligations	$	8,613	$	3,678
Issuance of notes payable and other debt obligations primarily related to acquisitions	$	2,444	$	1,637

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

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Mistras Group, Inc. and Subsidiaries

Notes to Unaudited Consolidated Financial Statements

(tabular dollars in thousands, except per share data)

1. Description of Business & Basis of Presentation

Description of Business

Mistras Group, Inc. and subsidiaries (the Company) is a leading one source global provider of technology-enabled asset protection solutions used to evaluate the structural integrity and reliability of critical energy, industrial and public infrastructure. The Company combines industry-leading products and technologies, expertise in mechanical integrity (MI) and non-destructive testing (NDT) services and proprietary data analysis software to deliver a comprehensive portfolio of customized solutions, ranging from routine inspections to complex, plant-wide asset integrity assessments and management. These mission critical solutions enhance customers ability to extend the useful life of their assets, increase productivity, minimize repair costs, comply with governmental safety and environmental regulations, manage risk and avoid catastrophic disasters. Given the role the services of the Company play in ensuring the safe and efficient operation of infrastructure, the Company has historically provided a majority of its services to its customers on a regular, recurring basis. The Company serves a global customer base of companies with asset-intensive infrastructure, including companies in the oil and gas, fossil and nuclear power, alternative and renewable energy, public infrastructure, chemicals, aerospace and defense, transportation, primary metals and metalworking, pharmaceuticals and food processing industries.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair statement have been included. Operating results for the three and nine months ended February 29, 2012 are not necessarily indicative of the results that may be expected for the year ending May 31, 2012. The balance sheet at May 31, 2011 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements. You should read these unaudited consolidated financial statements together with the historical consolidated financial statements of the Company as filed with the Securities and Exchange Commission.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Mistras Group, Inc. and its wholly or majority-owned subsidiaries. Where the Company s ownership interest is less than 100%, the noncontrolling interests are reported in stockholders equity in the accompanying consolidated balance sheets. The noncontrolling interest in net income, net of tax, is classified separately in the accompanying consolidated statements of operations.

All significant intercompany accounts and transactions have been eliminated in consolidation. Mistras Group, Inc. s and its subsidiaries fiscal years end on May 31 except for the companies in the International segment, which end on April 30. The effect of this difference in timing of reporting foreign operations on the consolidated results of operations and consolidated financial position is not significant.

Reclassification

Certain amounts in prior periods have been reclassified to conform to the current year presentation. Such reclassifications did not have a material effect on the Company s financial condition or results of operations as previously reported.

Revision of Prior Period Financial Statements

The Company has revised the consolidated statement of cash flows for the nine months ended February 28, 2011 to reflect the cash flows associated with the financing of an insurance premium as cash flows from financing activities. Such cash flows were previously reported in operating activities. A summary of the revisions to the consolidated statements of cash flows for the nine months ended February 28, 2011 is as follows:

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	Nine months months ended February 28, 2011		
	As previously reported	Revision	As revised
Net cash flows provided by operating activities	$ 21,365	$ (2,722)	$ 18,643
Net cash flows used in investing activities	(24,580)		(24,580)
Net cash flows provided by financing activities	(6,367)	2,722	(3,645)
Effects of exchange rate changes on cash and cash equivalents	105		105
Net increase in cash and cash equivalents during the period	(9,477)		(9,477)

These revisions had no impact on the annual statement of cash flows as presented in the 2011 Form 10-K.

2. Summary of Significant Accounting Policies

Revenue Recognition

Revenue recognition policies for the various sources of revenues are as follows:

Services

The Company predominantly derives revenues by providing its services on a time and material basis and recognizes revenues when services are rendered. At the end of any reporting period, there may be earned but unbilled revenues that are accrued. Payments received in advance of revenue recognition are reflected as deferred revenues.

Software

Revenues from the sale of perpetual licenses are recognized upon the delivery and acceptance of the software. Revenues from term licenses are recognized ratably over the period of the license. Revenues from maintenance, unspecified upgrades and technical support are recognized ratably over the period such items are delivered. For multiple-element arrangement software contracts that include non-software elements, and where the software is essential to the functionality of the non-software elements (collectively referred to as software multiple-element arrangements), the Company applies the rules as noted below.

Products

Revenues from product sales are recognized when risk of loss and title passes to the customer. The exceptions to this accounting treatment would be for multiple-element arrangements (described below) or those situations where specialized installation or customer acceptance is required. Payments received in advance of revenue recognition are reflected as deferred revenues.

Percentage of Completion

A portion of the Company s revenues are generated from engineering and manufacturing of custom products under long-term contracts that may last from several months to several years, depending on the contract. Revenues from long-term contracts are recognized on the percentage-of-completion method of accounting. Under the percentage-of-completion method of accounting, revenues are recognized as work is performed. The percentage of completion at any point in time is based on total costs or total labor dollars incurred to date in relation to the total estimated costs or total labor dollars estimated at completion. The percentage of completion is then applied to the total contract revenue to determine the amount of revenue to be recognized in the period. Application of the percentage-of-completion method of accounting requires the use of estimates of costs to be incurred for the performance of the contract. Contract costs include all direct materials, direct labor costs and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs, and all costs associated with operation of equipment. The cost estimation process is based upon the professional knowledge and experience of the Company s engineers, project managers and financial professionals. Factors that are considered in estimating the work to be completed include the availability and productivity of labor, the nature and complexity of the work to be performed, the effect of change orders, the availability of materials, the effect of any delays in project

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performance and the recoverability of any claims. Whenever revisions of estimated contract costs and contract values indicate that the contract costs will exceed estimated revenues, thus creating a loss, a provision for the total estimated loss is recorded in that period.

Multiple-element Arrangements

The Company occasionally enters into transactions that represent multiple-element arrangements, which may include any combination of services, software, and hardware. When a sales arrangement contains multiple elements, such as hardware and services and/or software products, the Company allocates revenue to each element based on a selling price hierarchy. The selling price for a deliverable is based on its vendor specific objective evidence (VSOE) if available, third party evidence (TPE) if VSOE is not available, or estimated selling price (ESP) if neither VSOE nor TPE is available. The Company has historically utilized the VSOE due to the nature of its products. In multiple element arrangements where more-than-incidental software deliverables are included, revenue is allocated to each separate unit of accounting for each of the non-software deliverables and to the software deliverables as a group using the relative selling prices of each of the deliverables in the arrangement based on the aforementioned selling price hierarchy.

Use of Estimates

These unaudited consolidated financial statements have been prepared in conformity with GAAP, which requires management to make estimates and assumptions about future events that affect the reported amounts of assets and liabilities, 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 these estimates. The more significant estimates include valuation of goodwill and intangible assets, useful lives of long-lived assets, acquisition-related contingent consideration, allowance for doubtful accounts, inventory valuation, reserves for self-insured workers compensation and health benefits and provision for income taxes.

Goodwill and Intangible Assets

Goodwill represents the excess of the purchase price over the fair market value of net assets of the acquired business at the date of acquisition. The Company tests for impairment annually, in its fiscal fourth quarter, using a two-step process. The first step identifies potential impairment by comparing the fair value of the Company s reporting units to its carrying value. If the fair value is less than the carrying value, the second step measures the amount of impairment, if any. The impairment loss is the amount by which the carrying amount of goodwill exceeds the implied fair value of that goodwill. The most recent annual test for impairment performed for fiscal 2011 did not identify any instances of impairment and there were no events through February 29, 2012 that warranted a reconsideration of the impairment test results.

Intangible assets are recorded at cost. Intangible assets with finite lives are amortized on a straight-line basis over their estimated useful lives.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and accounts receivable. At times, cash deposits may exceed the limits insured by the Federal Deposit Insurance Corporation. The Company believes it is not exposed to any significant credit risk or risk of nonperformance of financial institutions.

The Company sells primarily to large companies, extends reasonably short collection terms, performs credit evaluations and does not require collateral. The Company maintains reserves for potential credit losses.

The Company has one customer, BP plc. (BP), which accounted for 16% and 21% of revenues for the three months ended February 29, 2012 and February 28, 2011, respectively, and 16% and 17% of revenues for the nine months ended February 29, 2012 and February 28, 2011, respectively. Accounts receivable from this customer were approximately 14% and 15% of total accounts receivable, net as of February 29, 2012 and May 31, 2011, respectively. The relationship with BP is comprised of separate contracts for non-destructive testing and inspection services with multiple affiliated entities within the broad BP organization. The Company conducts business with various divisions or affiliates of the BP organization through numerous contracts covering many segments of BP s business including downstream (refinery), midstream (pipelines) and upstream (exploration). These contracts are typically negotiated locally with the specific BP division or

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affiliate, are of varying lengths, have different start and end dates and differ in terms of the scope of work and nature of services provided. Most contracts are based on time and materials.

Equity-based Compensation

The Company measures the cost of employee services received in exchange for an award of equity instruments based upon the grant-date fair value of the award. The Company uses the straight-line attribution method for allocating compensation costs and recognizes the fair value of each equity award on a straight-line basis over the vesting period of the related awards.

The Company uses the Black-Scholes option-pricing model to estimate the fair value of the stock option awards as of the grant date. The Black-Scholes model, by its design, is highly complex and dependent upon key data inputs estimated by management. The primary data inputs with the greatest degree of judgment are the expected term of stock option awards and the estimated volatility of the Company s common stock price. The Black-Scholes model is sensitive to changes in these two variables. Since the Company s initial public offering (IPO), the expected term of the Company s stock options is generally determined using the mid-point between the vesting period and the end of the contractual term. Expected stock price volatility is typically based on the daily historical trading data for a period equal to the expected term. Because the Company s historical trading data only dates back to October 8, 2009, the first trading date after its IPO, the Company has estimated expected volatility using an analysis of the stock price volatility of comparable peer companies. Prior to the Company s IPO, the exercise price equaled the estimated fair market value of the Company s common stock, as determined by its board of directors. Since the Company s IPO, the exercise price of stock option grants is determined using the closing market price of the Company s common stock on the date of grant.

Recent Accounting Pronouncements

In October 2009, the FASB issued Accounting Standards Update (ASU) 2009-13, Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements (a consensus of the FASB Emerging Issues Task Force), which requires companies to allocate the overall consideration in multiple-element arrangements to each deliverable by using a best estimate of the selling price of individual deliverables in the arrangement in the absence of vendor-specific objective evidence or other third-party evidence of the selling price. Effective June 1, 2011, the Company adopted, on a prospective basis, the provisions of this updated accounting standard related to revenue recognition associated with contractual arrangements involving multiple elements. The adoption of this pronouncement did not have a material impact on the Company s consolidated financial statements.

In April 2010, the FASB issued ASU 2010-17, Revenue Recognition Milestone Method (Topic 605): Milestone Method of Revenue Recognition (a consensus of the FASB Emerging Issues Task Force). ASU 2010-17 provides guidance on applying the milestone method to milestone payments for achieving specified performance measure when those payments are related to uncertain future events limited to transactions involving research and development. Entities can make an accounting policy election to recognize arrangement consideration received for achieving specified performance measures during the period in which the milestones are achieved, provided certain criteria are met. Effective

June 1, 2011, the Company adopted, on a prospective basis, the provisions of this updated accounting standard related to milestones. The adoption of this pronouncement did not have a material impact on the Company s consolidated financial statements.

In June 2011, the FASB issued ASU 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income. ASU 2011-05 allows an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. This authoritative guidance eliminates the option to present the components of other comprehensive income as part of the statement of equity. ASU 2011-05 does not change the items that must be reported in other comprehensive income, when an item of other comprehensive income must be reclassified to net income, or the Company s option to present components of other comprehensive income either net of related tax effects or before related tax effects, nor does it affect how earnings per share is calculated or presented. ASU 2011-05 requires retrospective application, and it is effective for fiscal years and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. The Company does not expect that the adoption of this pronouncement will have a material impact on the Company s consolidated financial statements.

In September 2011, the FASB issued ASU 2011-08, Intangibles-Goodwill and Other (Topic 350): Testing Goodwill for Impairment. ASU 2011-08 permits an entity to first perform a qualitative assessment to determine whether it is more likely

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Mistras Group, Inc. and Subsidiaries
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than not that the fair value of a reporting unit is less than its carrying value. If it is concluded that this is the case, it is then necessary to perform the currently prescribed two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. ASU 2011-08 is effective for the Company in fiscal 2013 and earlier adoption is permitted. The Company does not expect that the adoption of this pronouncement will have a material impact on the Company s consolidated financial statements.

3. Capitalization

Common Stock

In May 2011, the Company completed a secondary offering of 3,754,061 shares of common stock at a price of $16.00 per share. The Company sold 989,660 shares and 2,764,401 shares were sold by a selling stockholder. The Company received net proceeds of approximately $14.7 million from the offering. The Company used the net proceeds for general corporate purposes including the reduction of outstanding indebtedness, acquisitions, capital expenditures and working capital.

Dividends on common stock will be paid when, and if, declared by the board of directors. Each holder of common stock is entitled to vote on all matters and is entitled to one vote for each share held.

Equity Awards

In September 2009, the Company s board of directors and shareholders adopted and approved the 2009 Long-Term Incentive Plan (the 2009 Plan), which became effective upon the closing of the IPO. Awards may be in the form of stock options, restricted stock units and other forms of stock-based incentives, including stock appreciation rights and deferred stock rights. The term of each incentive and non-qualified stock option is ten years. Vesting generally occurs over a period of four years, the expense for which is recorded on a straight-line basis over the requisite service period. The 2009 Plan allows for the grant of awards of up to approximately 2,286,000 shares of common stock, of which 1,705,000 shares were available for future grants as of February 29, 2012. Prior to the Company s IPO in October 2009, the Company had two stock option plans: (i) the 1995 Incentive Stock Option and Restricted Stock Purchase Plan (the 1995 Plan), and (ii) the 2007 Stock Option Plan (the 2007 Plan). No additional awards may be granted from these two plans. As of February 29, 2012, there was an aggregate of approximately 2,630,000 stock options outstanding and approximately 443,000 unvested restricted stock units outstanding under the 2009 Plan, the 2007 Plan, and the 1995 Plan.

The fair value of the Company s stock option awards for the nine months ended February 28, 2011 was estimated at the date of grant using the Black-Scholes option-pricing model with the range of assumptions below. No stock options were granted during the nine months ended February 29, 2012.

	Nine months ended February 28, 2011
Dividend yield	0.0%
Expected volatility	44%
Risk-free interest rate	2.6%
Expected term (years)	6.3

The Company recognized stock-based compensation expense related to stock option awards of approximately $0.8 million for the each of the three month periods ended February 29, 2012 and February 28, 2011. For each of the nine month periods ended February 29, 2012 and February 28, 2011, the Company recognized stock-based compensation expense related to stock option awards of $2.4 million. As of February 29, 2012, there was approximately $4.6 million of unrecognized compensation costs, net of estimated forfeitures, related to stock option awards, which are expected to be recognized over a remaining weighted average period of 1.5 years. Cash proceeds from and the aggregate intrinsic value of stock options exercised during the three and nine months ended February 29, 2012 and February 28, 2011 were as follows:

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(tabular dollars in thousands, except per share data)

	Three months ended		Nine months ended	
	February 29, 2012	February 28, 2011	February 29, 2012	February 28, 2011
Cash proceeds from options exercised	$ 152	$ 30	$ 1,477	$ 30
Aggregate intrinsic value of options exercised	$ 337	$ 43	$ 3,399	$ 43

The Company also recognized approximately $0.5 million and $0.1 million in stock-based compensation expense related to restricted stock unit awards during the three months ended February 29, 2012 and February 28, 2011, respectively. For the nine months ended February 29, 2012 and February 28, 2011, the Company recognized stock-based compensation expense related to restricted stock unit awards of $1.1 million and $0.3 million, respectively. As of February 29, 2012, there was approximately $6.1 million of unrecognized compensation costs, net of estimated forfeitures, related to restricted stock unit awards, which are expected to be recognized over a remaining weighted average period of 3.3 years.

In October 2011, the Company granted approximately 9,000 shares of fully-vested common stock to its five non-employee directors, in connection with its non-employee director compensation plan. These shares had a grant date fair value of approximately $0.2 million, which was recorded as stock-based compensation expense during the nine months ended February 29, 2012.

During the nine months ended February 29, 2012, approximately 52,000 restricted stock units vested, the fair value of which was $0.5 million. Upon vesting, restricted stock units are generally net share-settled to cover the required withholding tax and the remaining amount is converted into an equivalent number of shares of common stock. The restricted stock units that vested in the first nine months of fiscal 2012 were net-share settled such that the Company withheld shares with value equivalent to the employees minimum statutory obligation for the applicable income and other employment taxes, and remitted the cash to the appropriate taxing authorities. The Company withheld approximately 16,000 shares based on the value of the restricted stock units on their vesting date as determined by the Company s closing stock price. Total payments for the employees tax obligations to the taxing authorities were $0.3 million and are reflected as a financing activity within the consolidated statements of cash flows. These net-share settlements had the effect of share repurchases by the Company as they reduced and retired the number of shares that otherwise would have been issued as a result of the vesting and did not represent an expense to the Company.

4. Earnings per Share

Basic earnings per share is computed by dividing net income by the weighted-average number of shares outstanding during the period. Diluted earnings per share is computed by dividing net income by the sum of (1) the weighted-average number of shares of common stock outstanding during the period, and (2) the dilutive effect of assumed conversion of equity awards using the treasury stock method. With respect to the number of weighted-average shares outstanding (denominator), diluted shares reflects: (i) only the exercise of options to acquire common stock to the extent that the options exercise prices are less than the average market price of common shares during the period and (ii) the pro forma vesting of restricted stock units.

The following table sets forth the computations of basic and diluted earnings per share:

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(tabular dollars in thousands, except per share data)

	Three months ended		Nine months ended	
	February 29, 2012	**February 28, 2011**	**February 29, 2012**	**February 28, 2011**
Basic earnings per share				
Numerator:				
Net income attributable to Mistras Group, Inc.	$ 3,037	$ 2,443	$ 14,221	$ 9,713
Denominator:				
Weighted average common shares outstanding	27,921	26,667	27,794	26,665
Basic earnings per share	$ 0.11	$ 0.09	$ 0.51	$ 0.36
Diluted earnings per share:				
Numerator:				
Net income attributable to Mistras Group, Inc.	$ 3,037	$ 2,443	$ 14,221	$ 9,713
Denominator:				
Weighted average common shares outstanding	27,921	26,667	27,794	26,665
Dilutive effect of stock options outstanding	795	202	688	137
Dilutive effect of restricted stock units outstanding	113	50	81	22
	28,829	26,919	28,563	26,824
Diluted earnings per share	$ 0.11	$ 0.09	$ 0.50	$ 0.36

5. Acquisitions

The Company completed the acquisition of eight companies during the nine months ended February 29, 2012. These acquisitions were asset protection companies specializing in advanced ultrasonic inspection, NDT services and inspection, ultrasonic testing (UT) and acoustic emission (AE) products and systems, and in-house component inspection. These companies were acquired to complement the service and product offerings within the Services, Products and Systems, and International segments. Three of the acquired companies were asset purchases that met the definition of acquisitions of businesses under the provision of FASB Accounting Standards Codification (ASC) 805-10-20. In the remaining acquisitions, the Company acquired 100% of the common stock of the acquirees. Five of the acquired companies have been integrated into the International segment; two of the acquired companies have been integrated into the Services segment; and one of the acquired companies has been integrated into the Products segment. In addition to the cash and debt consideration related to the acquisitions completed in fiscal 2012, the Company accrued a liability of approximately $3.3 million, which represents the estimated fair value of contingent consideration expected to be payable in the event that certain of the acquired companies achieve specific performance metrics over the next four years of operations. The total potential contingent consideration ranges from zero to $4.5 million for acquisitions completed in fiscal 2012.

Assets and liabilities of the acquired businesses were included in the consolidated balance sheets as of February 29, 2012 based on their estimated fair value on the date of acquisition as determined in a purchase price allocation, using available information and making assumptions management believes are reasonable. The Company is still in the process of completing its valuations of the intangible assets for these acquisitions. These valuations and purchase price allocations are expected to be finalized prior to the end of the Company s fiscal year ending May 31, 2012. The results of operations of each of the acquisitions completed in fiscal 2012 are reported in each respective operating segment s statement of operations from the date of acquisition. The Company s preliminary allocation of purchase price for these acquisitions is included in the table below. The following table summarizes the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition:

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	Nine months ended	
	February 29, 2012	February 28, 2011
Number of entities	8	4
Cash paid	$ 27,514	$ 18,301
Subordinated notes issued	2,444	1,637
Debt and other liabilities assumed	3,095	1,100
Contingent consideration	3,445	697
Purchase price	$ 36,498	$ 21,735
Current net assets acquired	3,801	127
Property, plant and equipment	6,350	6,341
Deferred tax asset	130	41
Intangibles	9,710	6,465
Goodwill	16,507	8,878
Less: noncontrolling interest		(117)
Net assets acquired	$ 36,498	$ 21,735

The amortization period of intangible assets acquired ranges from one to fifteen years. The Company recorded approximately $16.5 million of goodwill in connection with its fiscal 2012 acquisitions, reflecting the strategic fit and revenue and earnings growth potential of these businesses. Substantially all of the goodwill recognized is expected to be deductible for tax purposes.

Revenues included in the consolidated statement of operations for the three and nine months ended February 29, 2012 from these acquisitions for the period subsequent to the closing of each transaction was approximately $10.6 million and $12.9 million, respectively. Loss from operations included in the consolidated statement of operations for each of the three and nine month periods ended February 29, 2012 from these acquisitions for the period subsequent to the closing of each transaction was approximately ($0.5) million.

The unaudited pro forma information for the periods set forth below gives effect to the fiscal 2012 acquisitions as if they had occurred at the beginning of each period presented. The pro forma information is presented for informational purposes only and is not necessarily indicative of the results of operations that actually would have been achieved had the acquisitions been consummated as of that time (unaudited, in thousands):

	Three months ended		Nine months ended	
	February 29, 2012	February 28, 2011	February 29, 2012	February 28, 2011
Revenues	$ 117,241	$ 90,287	$ 347,412	$ 268,065
Income from operations	$ 5,119	$ 4,899	$ 27,041	$ 19,268

During the three and nine month periods ended February 29, 2012, the Company incurred acquisition-related costs of $1.0 million and $1.4 million, respectively, in connection with due diligence, professional fees, and other expenses for its fiscal 2012 acquisition activity. Additionally, the Company adjusted the fair value of certain acquisition-related contingent consideration liabilities. For the three month and nine month periods ended February 29, 2012 the adjustments resulted in a net decrease of approximately $0.1 million and $0.9 million, respectively, to the Company s acquisition-related contingent consideration liabilities, which were approximately $7.5 million as of February 29, 2012 and recorded on the balance sheet

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in accrued expenses and other liabilities. These adjustments also resulted in a corresponding net increase to income from operations of approximately $0.1 million and $0.9 million for the three and nine month periods ended February 29, 2012, respectively. Both the fair value adjustments to acquisition-related contingent consideration liabilities and the acquisition-related expenses have been classified as acquisition-related costs in the statement of operations for the three and nine months ended February 29, 2012. Acquisition-related costs for the Company s fiscal 2011 acquisition activity were insignificant for the three and nine months ended February 28, 2011.

6. Accounts Receivable, net

Accounts receivable consist of the following:

	As of February 29, 2012		As of May 31, 2011	
Trade accounts receivable	$	97,363	$	79,800
Allowance for doubtful accounts		(2,106)		(1,769)
Total	$	95,257	$	78,031

7. Inventories, net

Inventories consist of the following:

	As of February 29, 2012		As of May 31, 2011	
Raw materials	$	2,912	$	2,832
Work in process		1,991		1,531
Finished goods		6,170		3,623
Supplies		2,100		1,844
Total	$	13,173	$	9,830

Inventories are net of reserves for slow-moving and obsolete inventory of approximately $1.2 million and $1.0 million as of February 29, 2012 and May 31, 2011, respectively.

8. Property, Plant and Equipment, net

Property, plant and equipment consist of the following:

	Useful Life (Years)	As of February 29, 2012	As of May 31, 2011
Land		$ 2,213	$ 2,210
Building and improvements	30-40	17,632	14,779
Office furniture and equipment	5-8		