

Primoris Services Corp  
Form 10-Q  
November 06, 2018  
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2018

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 0001-34145

Edgar Filing: Primoris Services Corp - Form 10-Q

Primoris Services Corporation

(Exact name of registrant as specified in its charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	20-4743916 (I.R.S. Employer Identification No.)
2100 McKinney Avenue, Suite 1500 Dallas, Texas (Address of Principal Executive Offices)	75201 (Zip Code)

Registrant's telephone number, including area code: (214) 740-5600

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 No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
	Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Edgar Filing: Primoris Services Corp - Form 10-Q

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

At November 5, 2018, 51,204,959 shares of the registrant's common stock, par value \$0.0001 per share, were outstanding.

---

Table of Contents

PRIMORIS SERVICES CORPORATION

INDEX

	Page No.
<u>Part I. Financial Information</u>	
<u>Item 1. Financial Statements:</u>	
<u>—Condensed Consolidated Balance Sheets at September 30, 2018 and December 31, 2017 (Unaudited)</u>	3
<u>—Condensed Consolidated Statements of Income for the three and nine months ended September 30, 2018 and 2017 (Unaudited)</u>	4
<u>—Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2018 and 2017 (Unaudited)</u>	5
<u>—Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and 2017 (Unaudited)</u>	6
<u>—Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	8
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	33
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	51
<u>Item 4. Controls and Procedures</u>	51
<u>Part II. Other Information</u>	
<u>Item 1. Legal Proceedings</u>	52
<u>Item 1A. Risk Factors</u>	52
<u>Item 6. Exhibits</u>	52
<u>Signatures</u>	53

Table of Contents

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## PRIMORIS SERVICES CORPORATION

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In Thousands, Except Share Amounts)

(Unaudited)

	September 30, 2018	December 31, 2017
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents (\$15,729 and \$60,256 related to VIEs. See Note 11)	\$ 60,039	\$ 170,385
Accounts receivable, net	473,045	291,589
Contract assets	382,492	265,902
Prepaid expenses and other current assets	22,383	15,338
Total current assets	937,959	743,214
Property and equipment, net	369,123	311,777
Deferred tax assets	13,441	—
Intangible assets, net	85,813	44,800
Goodwill	208,130	153,374
Other long-term assets	6,680	2,575
Total assets	\$ 1,621,146	\$ 1,255,740
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 241,288	\$ 140,943
Contract liabilities	219,232	169,377
Accrued liabilities	130,382	76,027
Dividends payable	3,072	3,087
Current portion of long-term debt	63,947	65,464
Total current liabilities	657,921	454,898
Long-term debt, net of current portion	306,093	193,351
Deferred tax liabilities	—	13,571
Other long-term liabilities	64,652	31,737
Total liabilities	1,028,666	693,557
Commitments and contingencies (See Note 17)		
Stockholders' equity		

Edgar Filing: Primoris Services Corp - Form 10-Q

Common stock—\$.0001 par value; 90,000,000 shares authorized; 51,204,959 and 51,448,753 issued and outstanding at September 30, 2018 and December 31, 2017	5	5
Additional paid-in capital	155,051	160,502
Retained earnings	431,764	395,961
Accumulated other comprehensive income	577	—
Noncontrolling interest	5,083	5,715
Total stockholders' equity	592,480	562,183
Total liabilities and stockholders' equity	\$ 1,621,146	\$ 1,255,740

See Accompanying Notes to Condensed Consolidated Financial Statements

3

---

Table of Contents

## PRIMORIS SERVICES CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(In Thousands, Except Per Share Amounts)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Revenue	\$ 908,902	\$ 608,311	\$ 2,061,808	\$ 1,800,978
Cost of revenue	802,397	537,890	1,839,324	1,591,021
Gross profit	106,505	70,421	222,484	209,957
Selling, general and administrative expenses	51,604	42,321	132,049	126,835
Merger and related costs	3,827	238	13,190	1,555
Operating income	51,074	27,862	77,245	81,567
Other income (expense):				
Investment income	—	6,066	—	6,066
Foreign exchange (loss) gain	(69)	167	1,444	299
Other income (expense), net	32	(39)	(751)	(52)
Interest income	932	228	1,544	411
Interest expense	(6,448)	(2,198)	(11,637)	(6,605)
Income before provision for income taxes	45,521	32,086	67,845	81,686
Provision for income taxes	(10,716)	(9,952)	(14,633)	(28,644)
Net income	\$ 34,805	\$ 22,134	\$ 53,212	\$ 53,042
Less net income attributable to noncontrolling interests	(2,114)	(1,537)	\$ (8,118)	\$ (3,209)
Net income attributable to Primoris	\$ 32,691	\$ 20,597	\$ 45,094	\$ 49,833
Dividends per common share	\$ 0.060	\$ 0.055	\$ 0.180	\$ 0.170
Earnings per share:				
Basic	\$ 0.64	\$ 0.40	\$ 0.88	\$ 0.97
Diluted	\$ 0.63	\$ 0.40	\$ 0.87	\$ 0.96
Weighted average common shares outstanding:				
Basic	51,403	51,441	51,471	51,491
Diluted	51,735	51,707	51,760	51,751

See Accompanying Notes to Condensed Consolidated Financial Statements





Table of Contents

PRIMORIS SERVICES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In Thousands, Except Per Share Amounts)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Net income	\$ 34,805	\$ 22,134	\$ 53,212	\$ 53,042
Other comprehensive income, net of tax:				
Foreign currency translation adjustments	200	—	577	—
Comprehensive income	35,005	22,134	53,789	53,042
Less net income attributable to noncontrolling interests	(2,114)	(1,537)	(8,118)	(3,209)
Comprehensive income attributable to Primoris	\$ 32,891	\$ 20,597	\$ 45,671	\$ 49,833

See Accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

## PRIMORIS SERVICES CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands)

(Unaudited)

	Nine Months Ended September 30,	
	2018	2017
Cash flows from operating activities:		
Net income	\$ 53,212	\$ 53,042
Adjustments to reconcile net income to net cash (used in) provided by operating activities (net of effect of acquisitions):		
Depreciation	47,708	43,064
Amortization of intangible assets	8,287	6,184
Intangible asset impairment	—	477
Stock-based compensation expense	748	911
Gain on short-term investments	—	(5,980)
Gain on sale of property and equipment	(3,212)	(3,880)
Other non-cash items	180	131
Changes in assets and liabilities:		
Accounts receivable	(78,819)	54,865
Contract assets	(85,817)	(42,011)
Other current assets	11,061	7,186
Other long-term assets	(957)	(2,745)
Accounts payable	24,099	(17,813)
Contract liabilities	(11,061)	46,210
Accrued liabilities	16,400	17,848
Other long-term liabilities	5,298	3,943
Net cash (used in) provided by operating activities	(12,873)	161,432
Cash flows from investing activities:		
Purchase of property and equipment	(80,766)	(57,346)
Issuance of a note receivable	(15,000)	—
Proceeds from a note receivable	15,000	—
Proceeds from sale of property and equipment	9,655	7,027

Edgar Filing: Primoris Services Corp - Form 10-Q

Purchase of short-term investments	—	(13,588)
Sale of short-term investments	—	350
Cash paid for acquisitions, net of cash and restricted cash acquired	(111,030)	(66,205)
Net cash used in investing activities	(182,141)	(129,762)
Cash flows from financing activities:		
Borrowings under revolving line of credit	170,000	—
Payments on revolving line of credit	(170,000)	—
Proceeds from issuance of long-term debt	239,467	30,000
Repayment of long-term debt and capital leases	(127,363)	(41,279)
Payment of debt issuance cost	(1,041)	(631)
Proceeds from issuance of common stock purchased under a long-term incentive plan	1,498	1,148
Payment of contingent earnout liability	(1,200)	—
Cash distribution to non-controlling interest holders	(8,750)	—
Repurchase of common stock	(8,479)	(4,999)
Dividends paid	(9,271)	(8,497)
Net cash provided by (used in) financing activities	84,861	(24,258)
Effect of exchange rate changes on cash and cash equivalents	(193)	—
Net change in cash and cash equivalents	(110,346)	7,412
Cash and cash equivalents at beginning of the period	170,385	135,823
Cash and cash equivalents at end of the period	\$ 60,039	\$ 143,235

See Accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

	Nine Months Ended September 30, 2018      2017 (Unaudited)	
Cash paid:		
Interest	\$ 11,658	\$ 6,236
Income taxes, net of refunds received	\$ 5,379	\$ 25,618

SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES

	Nine Months Ended September 30, 2018      2017 (Unaudited)	
Obligations incurred for the acquisition of property	\$ —	\$ 4,163
Dividends declared and not yet paid	\$ 3,072	\$ 2,829

See Accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Dollars In Thousands, Except Share and Per Share Amounts)

(Unaudited)

Note 1—Nature of Business

Organization and operations — Primoris Services Corporation is a holding company of various construction and product engineering subsidiaries. Our underground and directional drilling operations install, replace and repair natural gas, petroleum, telecommunications and water pipeline systems, including large diameter pipeline systems. Our industrial, civil and engineering operations build and provide maintenance services to industrial facilities including power plants, petrochemical facilities, and other processing plants; construct multi-level parking structures; and engage in the construction of highways, bridges and other environmental construction activities. Our transmission and distribution operations install, replace and repair gas and electric utility systems. We are incorporated in the state of Delaware, and our corporate headquarters are located at 2100 McKinney Avenue, Suite 1500, Dallas, Texas 75201. Unless specifically noted otherwise, as used throughout these condensed consolidated financial statements, “Primoris”, “the Company”, “we”, “our”, “us” or “its” refers to the business, operations and financial results of us and our wholly-owned subsidiaries.

Reportable Segments — We segregate our business into five reportable segments: the Power, Industrial and Engineering (“Power”) segment, the Pipeline and Underground (“Pipeline”) segment, the Utilities and Distribution (“Utilities”) segment, the Transmission and Distribution (“Transmission”) segment, which is a new reportable segment created in connection with the acquisition of Willbros Group, Inc. (“Willbros”), and the Civil segment. See Note 18 – “Reportable Segments” for a brief description of the reportable segments and their operations.

The classification of revenue and gross profit for segment reporting purposes can at times require judgment on the part of management. Our segments may perform services across industries or perform joint services for customers in multiple industries. To determine reportable segment gross profit, certain allocations, including allocations of shared and indirect costs, such as facility costs, equipment costs and indirect operating expenses were made.

Acquisition of Willbros Group, Inc. — On June 1, 2018, we completed our acquisition of Willbros for approximately \$111.0 million, net of cash and restricted cash acquired. Willbros is a specialty energy infrastructure contractor serving the oil and gas and power industries through its utility transmission and distribution, oil and gas, and Canadian operations, which principally executes industrial and power projects. The utility transmission and distribution operations formed the Transmission segment, the oil and gas operations are included in the Pipeline segment, and the Canadian operations are included in the Power segment. See Note 6— “Business Combinations”.

Other Acquisitions — On May 26, 2017, we acquired the net assets of Florida Gas Contractors (“FGC”) for \$37.7 million; on May 30, 2017, we acquired certain engineering assets for approximately \$2.3 million; and on June 16, 2017, we acquired the net assets of Coastal Field Services (“Coastal”) for \$27.5 million. FGC operations are included in the Utilities segment, the engineering assets are included in the operations of the Power segment, and Coastal operations are included in the Pipeline segment. See Note 6— “Business Combinations”.

Joint Ventures —We own a 50% interest in two separate joint ventures, both formed in 2015. The Carlsbad Power Constructors joint venture (“Carlsbad”) is engineering and constructing a gas-fired power generation facility, and the ARB Inc. & B&M Engineering Co. joint venture (“Wilmington”) is also engineering and constructing a gas-fired power generation facility. Both projects are located in Southern California. The joint venture operations are included as part of the Power segment. As a result of determining that we are the primary beneficiary of the two variable interest entities (“VIEs”), the results of the Carlsbad and Wilmington joint ventures are consolidated in our financial statements. The Wilmington project was substantially complete as of December 31, 2017, and the Carlsbad project is expected to be completed in 2018. Financial information for the joint ventures is presented in Note 11 – “Noncontrolling Interests”.

#### Note 2—Basis of Presentation

Interim condensed consolidated financial statements — The interim condensed consolidated financial statements for the three and nine month periods ended September 30, 2018 and 2017 have been prepared in accordance with Rule 10-01 of Regulation S-X of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). As such, certain disclosures, which would substantially duplicate the disclosures contained in our Annual Report on Form 10-K,

Table of Contents

filed on February 26, 2018, which contains our audited consolidated financial statements for the year ended December 31, 2017, have been omitted.

This Third Quarter 2018 Report on Form 10-Q should be read in concert with our most recent Annual Report on Form 10-K. The interim financial information is unaudited. In the opinion of management, the interim information includes all adjustments (consisting of normal recurring adjustments) necessary for the fair presentation of the interim financial information.

Reclassification — Certain previously reported amounts have been reclassified to conform to the current period presentation.

Customer concentration — We operate in multiple industry segments encompassing the construction of commercial, industrial and public works infrastructure assets primarily throughout the United States. Typically, the top ten customers in any one calendar year generate revenue in excess of 50% of total revenue; however, the group that comprises the top ten customers varies from year to year.

During the three and nine months ended September 30, 2018, revenue generated by the top ten customers were approximately \$483.0 million and \$1,045.9 million, respectively, which represented 53.1% and 50.7%, respectively, of total revenue during the applicable period. During the three and nine months ended September 30, 2018, a Midwest utility customer represented 7.9% and 8.4% of total revenue, respectively, and a California utility customer represented 8.2% and 8.6% of total revenue, respectively.

During the three and nine months ended September 30, 2017, revenues generated by the top ten customers were approximately \$317.2 million and \$1,058.5 million, respectively, which represented 52.2% and 58.8%, respectively, of total revenues during the applicable period. During the three and nine months ended September 30, 2017, a California utility project represented 10.6% and 8.8% of total revenues, respectively, and a state department of transportation customer represented 8.4% and 9.8% of total revenues, respectively.

At September 30, 2018, approximately 10.2% of our accounts receivable were due from one customer, and that customer provided 8.4% of our revenue for the nine months ended September 30, 2018. In addition, of total accounts receivable, approximately 4.4% are from one customer with whom we are currently engaged in a dispute resolution. See Note 17 – “Commitments and Contingencies”.

At September 30, 2017, approximately 10.8% of our accounts receivable were due from one customer, and that customer provided 7.9% of our revenue for the nine months ended September 30, 2017. In addition, approximately

11.2% of total accounts receivable at September 30, 2017 were from one customer with whom we are currently engaged in a dispute resolution.

Multiemployer plans — Various of our subsidiaries are signatories to collective bargaining agreements. These agreements require that we participate in and contribute to a number of multiemployer benefit plans for our union employees at rates determined by the agreements. The trustees for each multiemployer plan determine the eligibility and allocations of contributions and benefit amounts, determine the types of benefits, and administer the plan. To the extent that any plans are underfunded, the Employee Retirement Income Security Act of 1974, as amended by the Multi-Employer Pension Plan Amendments Act of 1980, requires that if we were to withdraw from an agreement or if a plan is terminated, we may incur a withdrawal obligation. The potential withdrawal obligation may be significant. In accordance with Generally Accepted Accounting Principles (“GAAP”), any withdrawal liability would be recorded when it is probable that a liability exists and can be reasonably estimated. In November 2011, we withdrew from the Central States Southeast and Southwest Areas Pension Fund multiemployer plan, and fully paid off the withdrawal liability in the third quarter of 2018 as discussed in Note 17 — “Commitments and Contingencies”. We have no plans to withdraw from any other agreements.

Derivative Instruments and Hedging Activities — We recognize all derivative instruments as either assets or liabilities on the balance sheet at their respective fair values. Our use of derivatives consists of an interest rate swap agreement. The interest rate swap agreement was entered into to improve the predictability of cash flows from interest payments related to variable rate debt for the duration of the term loan. The interest rate swap matures in July 2023 and is not designated as a hedge for accounting purposes. Therefore, the change in the fair value of the derivative asset or



Table of Contents

liability is reflected in net income in the Condensed Consolidated Statements of Income (mark-to-market accounting). Cash flows from derivatives settled are reported as cash flow from operating activities.

Note 3—Recent Accounting Pronouncements

Recently adopted accounting pronouncements

In May 2014, the FASB issued ASU No. 2014-09, “Revenue from Contracts with Customers (Topic 606)”, with several clarifying updates issued during 2016 and 2017. The new standard is effective for reporting periods beginning after December 15, 2017 and supersedes all prior revenue recognition standards including the guidance in ASC Topic 605, “Revenue Recognition”. Under Topic 606, revenue recognition occurs when promised goods or services are transferred to customers in amounts that reflect the consideration to which the company expects to be entitled to in exchange for those goods or services. We adopted Topic 606 as of January 1, 2018 using the modified retrospective transition method. See Note 4 — “Revenue” for further details.

In November 2016, the FASB issued ASU 2016-18, “Statement of Cash Flows (Topic 230)”, which requires a reporting entity to include restricted cash and restricted cash equivalents in its cash and cash-equivalent balances presented in the entity’s statement of cash flows. A reconciliation between the statement of financial position and the statement of cash flows must be disclosed when the balance sheet includes more than one line item for cash, cash equivalents, restricted cash and restricted cash equivalents. Transfers between non-restricted and restricted cash should not be presented as cash flow activities in the statement of cash flows. Furthermore, an entity with a material restricted cash balance must disclose information regarding the nature of the restrictions. ASU 2016-18 is effective for annual periods beginning after December 15, 2017, including interim periods within those annual reporting periods. We adopted the ASU as of January 1, 2018, and it did not have a material impact on our Condensed Consolidated Statements of Cash Flows.

In January 2017, the FASB issued ASU 2017-01, "Business Combinations (Topic 805): Clarifying the Definition of a Business", which changes the definition of a business to assist entities with evaluating when a set of acquired assets and activities is a business. ASU 2017-01 requires an entity to evaluate if substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or a group of similar identifiable assets; if so, the set of transferred assets and activities is not a business. ASU 2017-01 is effective for interim and annual reporting periods beginning after December 15, 2017. We adopted the ASU as of January 1, 2018, and it did not impact the determination of our business combinations.

In May 2017, the FASB issued ASU 2017-09, “Compensation — Stock Compensation (Topic 718) — Scope of Modification Accounting”. The ASU amends the scope of modification accounting for share-based payment arrangements. The amendments in the ASU clarify when to account for a change in the terms or conditions of

share-based payment awards as a modification under ASC 718, “Compensation — Stock Compensation”. The ASU is effective for interim and annual reporting periods beginning after December 15, 2017. We adopted the ASU as of January 1, 2018, and it did not have a material impact on our consolidated financial statements.

In March 2018, the FASB issued ASU No. 2018-05, “Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118”. The ASU added guidance previously issued by the Securities and Exchange Commission (“SEC”) in Staff Accounting Bulletin No. 118 (“SAB 118”) to ASC 740 “Income Taxes”. SAB 118 was issued by the SEC in December 2017 to provide guidance for accounting implications of U.S. tax reform under the Tax Cuts and Jobs Act (the “Tax Act”). We have evaluated the potential impacts of SAB 118 and have applied this guidance to our consolidated financial statements and related disclosures beginning in the fourth quarter of our fiscal year 2017. See Note 14 — “Income Taxes” for additional information on SAB 118 and the impacts of the Tax Act.

#### Recently issued accounting pronouncements not yet adopted

In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842)”. In July 2018, the FASB issued two updates to ASU 2016-02, ASU 2018-10, “Codification Improvements to Topic 842, Leases”, and ASU 2018-11, “Leases (Topic 842): Targeted Improvements”. ASU 2016-02 will require recognition of operating leases with lease terms of more than twelve months on the balance sheet as both assets for the rights and liabilities for the obligations created by the leases. The ASU will require disclosures that provide qualitative and quantitative information for the lease assets and liabilities recorded in the financial statements. The standard is effective for fiscal years beginning after December 15, 2018, and initially required a modified retrospective transition method where a company applies the new

Table of Contents

leases standard at the beginning of the earliest period presented in the financial statements. ASU 2018-11 added an optional transition method where a company applies the new leases standard at the adoption date and recognizes a cumulative effect adjustment to the opening balance of retained earnings. We intend to take advantage of the transition practical expedients permitted with the new standard, which among other things, allows us to carryforward the historical lease classification. In addition, we expect to elect the hindsight practical expedient to determine the reasonably certain lease term for existing leases. We also plan to make an accounting policy election that will keep leases with an initial term of 12 months or less off of the balance sheet and will result in recognizing those lease payments in the Consolidated Statements of Income on a straight-line basis over the lease term.

While we are continuing to assess all potential impacts of the ASUs, we expect total liabilities to increase by \$110.0 to \$125.0 million. We expect the right of use assets to approximate the lease liability as of the date of adoption with any difference between these amounts recorded as an adjustment to retained earnings as of January 1, 2019. These estimates, which are based on our current lease portfolio may change as we continue to evaluate the new standard and as we implement a new lease accounting information system. The estimates could also change due to changes in the lease portfolio, which could include lease volume, lease commencement dates, and renewal option and lease termination expectations. We do not believe the ASUs will materially affect our consolidated net income. We will update our estimates each quarter as changes occur.

We do not believe the ASUs will have a notable impact on our liquidity. Additionally, the ASUs will have no impact on our debt covenant compliance as we have already revised our credit agreements to address the impact of the ASUs.

In January 2017, the FASB issued ASU 2017-04, "Simplifying the Test for Goodwill Impairment". ASU 2017-04 removes the second step of the goodwill impairment test, which requires a hypothetical purchase price allocation. A goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. ASU 2017-04 is effective for interim and annual reporting periods beginning after December 15, 2019 and will be applied prospectively. We do not expect the adoption of ASU 2017-04 to have an impact on our financial position, results of operations, or cash flows.

In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement", which eliminates certain disclosure requirements for recurring and nonrecurring fair value measurements. The ASU eliminates such disclosures as the amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy, and adds new disclosure requirements for Level 3 measurements. This ASU is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years, with early adoption permitted for any eliminated or modified disclosures. We are currently evaluating the impact this ASU will have on our disclosures.

Note 4—Revenue

On January 1, 2018, we adopted Topic 606 using the modified retrospective method applied to those contracts that were not completed as of January 1, 2018. In adopting Topic 606, we changed our accounting policy for revenue recognition. Results for periods prior to January 1, 2018 are not adjusted and continue to be reported in accordance with our historic accounting under ASC Topic 605. The cumulative impact of adopting Topic 606 was immaterial and did not require an adjustment to retained earnings. However, we reclassified prior year balance sheet and cash flow amounts to conform to current year presentation.

We generate revenue under a range of contracting types, including fixed-price, unit-price, time and material, and cost reimbursable plus fee contracts. A substantial portion of our revenue is derived from contracts that are fixed-price or unit-price and is recognized over time as work is completed because of the continuous transfer of control to the customer (typically using an input measure such as costs incurred to date relative to total estimated costs at completion to measure progress). For time and material and cost reimbursable plus fee contracts, revenue is recognized primarily on an input basis, based on contract costs incurred as defined within the respective contracts. Costs to obtain contracts are generally not significant and are expensed in the period incurred.

We evaluate whether two or more contracts should be combined and accounted for as one single performance obligation and whether a single contract should be accounted for as more than one performance obligation. Topic 606 defines a performance obligation as a contractual promise to transfer a distinct good or service to a customer. A

Table of Contents

contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. Our evaluation requires significant judgment and the decision to combine a group of contracts or separate a contract into multiple performance obligations could change the amount of revenue and profit recorded in a given period. The majority of our contracts have a single performance obligation, as the promise to transfer the individual goods or services is not separately identifiable from other promises in the contract and, therefore, is not distinct. However, occasionally we have contracts with multiple performance obligations. For contracts with multiple performance obligations, we allocate the contract's transaction price to each performance obligation using the observable standalone selling price, if available, or alternatively our best estimate of the standalone selling price of each distinct performance obligation in the contract. The primary method used to estimate standalone selling price is the expected cost plus a margin approach for each performance obligation.

As of September 30, 2018, we had \$1.73 billion of remaining performance obligations. We expect to recognize approximately 81% of our remaining performance obligations as revenue during the next four quarters and substantially all of the remaining balance by the year-end 2020.

Accounting for long-term contracts involves the use of various techniques to estimate total transaction price and costs. For long-term contracts, transaction price, estimated cost at completion and total costs incurred to date are used to calculate revenue earned. Unforeseen events and circumstances can alter the estimate of the costs and potential profit associated with a particular contract. Total estimated costs, and thus contract revenue and income, can be impacted by changes in productivity, scheduling, the unit cost of labor, subcontracts, materials and equipment. Additionally, external factors such as weather, client needs, client delays in providing permits and approvals, labor availability, governmental regulation and politics may affect the progress of a project's completion, and thus the timing of revenue recognition. To the extent that original cost estimates are modified, estimated costs to complete increase, delivery schedules are delayed, or progress under a contract is otherwise impeded, cash flow, revenue recognition and profitability from a particular contract may be adversely affected.

The nature of our contracts gives rise to several types of variable consideration, including contract modifications (change orders and claims), liquidated damages, volume discounts, performance bonuses, incentive fees, and other terms that can either increase or decrease the transaction price. We estimate variable consideration as the most likely amount to which we expect to be entitled. We include estimated amounts in the transaction price to the extent we believe we have an enforceable right, and it is probable that a significant reversal of cumulative revenue recognized will not occur. Our estimates of variable consideration and the determination of whether to include estimated amounts in the transaction price are based largely on an assessment of our anticipated performance and all information (historical, current and forecasted) that is reasonably available to us at this time.

Contract modifications result from changes in contract specifications or requirements. We consider unapproved change orders to be contract modifications for which customers have not agreed to both scope and price. We consider claims to be contract modifications for which we seek, or will seek, to collect from customers, or others, for customer-caused changes in contract specifications or design, or other customer-related causes of unanticipated additional contract costs on which there is no agreement with customers. Claims can also be caused by non-customer-caused changes, such as rain or other weather delays. Costs associated with contract modifications are

included in the estimated costs to complete the contracts and are treated as project costs when incurred. In most instances, contract modifications are for goods or services that are not distinct, and, therefore, are accounted for as part of the existing contract. The effect of a contract modification on the transaction price, and our measure of progress for the performance obligation to which it relates, is recognized as an adjustment to revenue on a cumulative catch-up basis. In some cases, settlement of contract modifications may not occur until after completion of work under the contract.

As a significant change in one or more of these estimates could affect the profitability of our contracts, we review and update our contract-related estimates regularly. We recognize adjustments in estimated profit on contracts under the cumulative catch-up method. Under this method, the cumulative impact of the profit adjustment is recognized in the period the adjustment is identified. Revenue and profit in future periods of contract performance are recognized using the adjusted estimate. In the three and nine months ended September 30, 2018, revenue recognized from performance obligations satisfied in previous periods was \$2.5 million and \$27.5 million, respectively. If at any time the estimate of contract profitability indicates an anticipated loss on a contract, the projected loss is recognized in full, including any previously recognized profit, in the period it is identified and recognized as an “accrued loss provision” which is included in “Contract liabilities” on the Condensed Consolidated Balance Sheets. For contract revenue

Table of Contents

recognized over time, the accrued loss provision is adjusted so that the gross profit for the contract remains zero in future periods.

At September 30, 2018, we had approximately \$90.4 million of unapproved contract modifications included in the aggregate transaction prices. These contract modifications were in the process of being negotiated in the normal course of business. Approximately \$82.9 million of the contract modifications had been recognized as revenue on a cumulative catch-up basis through September 30, 2018.

In all forms of contracts, we estimate the collectability of contract amounts at the same time that we estimate project costs. If we anticipate that there may be issues associated with the collectability of the full amount calculated as the transaction price, we may reduce the amount recognized as revenue to reflect the uncertainty associated with realization of the eventual cash collection. For example, when a cost reimbursable project exceeds the client's expected budget amount, the client frequently requests an adjustment to the final amount. Similarly, some utility clients reserve the right to audit costs for significant periods after performance of the work.

The timing of when we bill our customers is generally dependent upon agreed-upon contractual terms, milestone billings based on the completion of certain phases of the work, or when services are provided. Sometimes, billing occurs subsequent to revenue recognition, resulting in unbilled revenue, which is a contract asset. Also, we sometimes receive advances or deposits from our customers before revenue is recognized, resulting in deferred revenue, which is a contract liability.

The caption "Contract assets" in the Condensed Consolidated Balance Sheets represents the following:

- unbilled revenue (formerly costs and estimated earnings in excess of billings), which arise when revenue has been recorded but the amount will not be billed until a later date;
- retainage amounts for the portion of the contract price earned by us for work performed, but held for payment by the customer as a form of security until we reach certain construction milestones; and
- contract materials for certain job specific materials not yet installed, which are valued using the specific identification method relating the cost incurred to a specific project.

Contract assets consist of the following (in thousands):

September 30,      December 31,

Edgar Filing: Primoris Services Corp - Form 10-Q

	2018	2017
Unbilled revenue	\$ 262,510	\$ 160,092
Retention receivable	91,473	66,586
Contract materials (not yet installed)	28,509	39,224
	\$ 382,492	\$ 265,902

Contract assets increased by \$116.6 million compared to December 31, 2017 due primarily to a \$30.8 million increase from the acquisition of Willbros in the second quarter of 2018 and higher unbilled revenue from our legacy operations.

The caption “Contract liabilities” in the Condensed Consolidated Balance Sheets represents deferred revenue (formerly billings in excess of costs and estimated earnings) on billings in excess of contract revenue recognized to date, and the accrued loss provision.

Contract liabilities consist of the following (in thousands):

	September 30, 2018	December 31, 2017
Deferred revenue	\$ 200,865	\$ 159,310
Accrued loss provision	18,367	10,067
	\$ 219,232	\$ 169,377



Table of Contents

Contract liabilities increased by \$49.9 million compared to December 31, 2017 primarily due to a \$61.0 million increase from the acquisition of Willbros in the second quarter of 2018, partially offset by lower deferred revenue from our legacy operations.

Revenue recognized for the nine months ended September 30, 2018, that was included in the contract liability balance at December 31, 2017 was approximately \$145.4 million.

The following tables present our revenue disaggregated into various categories.

Master Service Agreements (“MSA”) and Non-MSA revenue was as follows (in thousands):

Segment	For the three months ended September 30, 2018		
	MSA	Non-MSA	Total
Power	\$ 48,004	\$ 133,818	\$ 181,822
Pipeline	14,986	198,087	213,073
Utilities	227,192	42,460	269,652
Transmission	100,227	21,299	121,526
Civil	—	122,829	122,829
Total	\$ 390,409	\$ 518,493	\$ 908,902

Segment	For the nine months ended September 30, 2018		
	MSA	Non-MSA	Total
Power	\$ 90,074	\$ 425,304	\$ 515,378
Pipeline	34,479	326,782	361,261
Utilities	515,295	149,919	665,214
Transmission	135,744	28,236	163,980
Civil	—	355,975	355,975
Total	\$ 775,592	\$ 1,286,216	\$ 2,061,808

Revenue by contract type was as follows (in thousands):

Edgar Filing: Primoris Services Corp - Form 10-Q

For the three months ended September 30, 2018

Segment	Fixed-price	Unit-price	Cost	
			(1)	Total
Power	\$ 85,561	\$ 10,371	\$ 85,890	\$ 181,822
Pipeline	41,772	7,924	163,377	213,073
Utilities	42,763	144,611	82,278	269,652
Transmission	20,259	84,646	16,621	121,526
Civil	21,380	90,418	11,031	122,829
Total	\$ 211,735	\$ 337,970	\$ 359,197	\$ 908,902

---

(1) Includes time and material and cost reimbursable plus fee contracts.