

INFRASOURCE SERVICES INC

Form 10-Q

November 04, 2005

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
Form 10-Q**

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

**For the quarterly period ended September 30, 2005**

**OR**

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

**For the transition period from to**

**Commission file number 001-32164  
INFRASOURCE SERVICES, INC.**

*(Exact name of registrant as specified in its charter)*

**Delaware**  
*(State or other jurisdiction of  
incorporation or organization)*

**03-0523754**  
*(I.R.S. Employer  
Identification No.)*

**100 West Sixth Street, Suite 300, Media, PA  
19063**

*(Zip Code)*

**(610) 480-8000**

*(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. Yes  No

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

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

At October 20, 2005, there were 39,639,258 shares of InfraSource Services, Inc. Common Stock, par value of \$.001, outstanding.

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**For the Quarter Ended September 30, 2005  
FORM 10-Q  
INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**

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| <u>Certification pursuant to Section 1350 of Chapter 63</u>  |               |

**Table of Contents****PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****INFRASOURCE SERVICES, INC. AND SUBSIDIARIES  
Condensed Consolidated Balance Sheets**

|  | December 31,<br>2004                                | September 30,<br>2005 |
|--|---|-----------------------|
|  | (Unaudited)<br>(In thousands, except<br>share data) |                       |
| Current assets:  |   |                       |
| Cash and cash equivalents  | \$ 21,222   | \$ 2,520              |
| Restricted cash  | 5,000   |                       |
| Contract receivables (less allowances for doubtful accounts of<br>\$3,305 and \$2,868, respectively) | 104,840   | 138,731               |
| Costs and estimated earnings in excess of billings   | 59,640  | 105,933               |
| Inventories  | 9,864   | 10,504                |
| Deferred income taxes  | 2,886   | 2,125                 |
| Other current assets   | 10,781  | 11,083                |
| Current assets discontinued operations   | 10,699  |                       |
| <br>Total current assets   | <br>224,932   | <br>270,896           |
| Property and equipment (less accumulated depreciation of<br>\$30,636 and \$49,511, respectively)     |   |                       |
|  | 143,532   | 144,070               |
| Goodwill   | 134,478   | 134,750               |
| Intangible assets (less accumulated amortization of \$14,950 and<br>\$18,342, respectively)          | 6,795   | 2,484                 |
| Deferred charges and other assets, net   | 11,766  | 11,851                |
| Deferred income taxes  | 1,187   |                       |
| Noncurrent assets discontinued operations  | 1,732   |                       |
| <br>Total assets   | <br>\$ 524,422                                      | <br>\$ 564,051        |
| Current liabilities:   |   |                       |
| Current portion of long-term debt and capital lease obligations                                      | \$ 900  | \$ 881                |
| Note payable related party   |   | 1,000                 |
| Revolving credit facility borrowings   |   | 27,000                |
| Other liabilities related parties  | 3,904   | 9,400                 |
| Accounts payable   | 33,342  | 32,690                |
| Accrued compensation and benefits  | 17,525  | 22,608                |
| Other current and accrued liabilities  | 19,570  | 22,048                |
| Accrued insurance reserves   | 26,042  | 28,229                |
| Billings in excess of costs and estimated earnings   | 10,728  | 11,685                |
| Deferred revenues  | 5,359   | 6,467                 |
| Current liabilities discontinued operations  | 8,526   |                       |

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|   |            |            |
|---|------------|------------|
| Total current liabilities   | 125,896    | 162,008    |
| Long-term debt, net of current portion  | 83,878     | 83,219     |
| Long-term debt related party  | 1,000      |            |
| Deferred revenues   | 16,935     | 16,629     |
| Other long-term liabilities related parties   | 8,493      |            |
| Deferred income taxes   |            | 3,322      |
| Other long-term liabilities   | 4,226      | 4,304      |
| Non-current liabilities discontinued operations   | 11         |            |
| Total liabilities   | 240,439    | 269,482    |
| Commitments and contingencies   |            |            |
| Shareholders' equity:   |            |            |
| Preferred stock, \$.001 par value (authorized 12,000,000 shares; 0 shares issued and outstanding)                             |            |            |
| Common stock \$.001 par value (authorized 120,000,000 shares; issued and outstanding 38,942,728 and 39,283,591, respectively) | 39         | 39         |
| Treasury stock at cost (0 and 29,870 respectively)  |            | (137)      |
| Additional paid-in capital  | 272,954    | 277,460    |
| Deferred compensation   | (329)      | (2,115)    |
| Retained earnings   | 10,911     | 18,809     |
| Accumulated other comprehensive income  | 408        | 513        |
| Total shareholders' equity  | 283,983    | 294,569    |
| Total liabilities and shareholders' equity  | \$ 524,422 | \$ 564,051 |

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

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Operations**

|   | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Three Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2005</b> |
|---|--|--|---|---|
| <b>(Unaudited)</b>  |  |  |   |   |
| <b>(In thousands, except per share data)</b>  |  |  |   |   |
| Contract revenues   | \$ 161,876   | \$ 229,880   | \$ 450,220  | \$ 642,180  |
| Cost of revenues  | 136,194  | 197,769  | 377,205   | 570,622   |
| Gross profit  | 25,682   | 32,111   | 73,015  | 71,558  |
| Selling, general and administrative expenses  | 16,405   | 20,354   | 46,548  | 54,854  |
| Merger related costs  | (334)  | 66   | (334)   | 218   |
| Provision (recoveries) of uncollectible accounts  | 104  | 61   | (367)   | 145   |
| Amortization of intangible assets   | 2,420  | 1,001  | 10,989  | 4,311   |
| Income from operations  | 7,087  | 10,629   | 16,179  | 12,030  |
| Interest income   | 228  | 132  | 350   | 354   |
| Interest expense and amortization of debt discount  | (1,969)  | (2,170)  | (8,161)   | (5,872)   |
| Loss on early extinguishment of debt  |  |  | (5,549)   |   |
| Other income, net   | 1,390  | 735  | 2,253   | 5,749   |
| Income before income taxes  | 6,736  | 9,326  | 5,072   | 12,261  |
| Income tax expense  | 2,760  | 4,021  | 2,029   | 5,255   |
| Income from continuing operations   | 3,976  | 5,305  | 3,043   | 7,006   |
| Discontinued operations:  |  |  |   |   |
| Income (loss) from discontinued operations (net of income tax provision (benefit) of \$282, \$(359), \$289 and \$(625), respectively) | 483  | (529)  | 461   | (898)   |
| Gain on disposition of discontinued operations (net of income tax provision of \$413, \$1,432,  | 593  | 1,790  | 593   | 1,790   |

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\$413 and \$1,432,  
respectively)

|  |    |        |    |        |    |        |    |        |
|--|----|--------|----|--------|----|--------|----|--------|
| Net income   | \$ | 5,052  | \$ | 6,566  | \$ | 4,097  | \$ | 7,898  |
| Basic income per share:                            |    |        |    |        |    |        |    |        |
| Income from continuing operations                  | \$ | 0.10   | \$ | 0.14   | \$ | 0.09   | \$ | 0.18   |
| Income (loss) from discontinued operations         |    | 0.01   |    | (0.01) |    | 0.01   |    | (0.02) |
| Gain on disposition of discontinued operations     |    | 0.02   |    | 0.04   |    | 0.02   |    | 0.04   |
| Net income   | \$ | 0.13   | \$ | 0.17   | \$ | 0.12   | \$ | 0.20   |
| Weighted average basic common shares outstanding   |    |        |    |        |    |        |    |        |
|  |    | 38,690 |    | 39,139 |    | 33,924 |    | 39,059 |
| Diluted income per share:                          |    |        |    |        |    |        |    |        |
| Income from continuing operations                  | \$ | 0.10   | \$ | 0.13   | \$ | 0.09   | \$ | 0.18   |
| Income (loss) from discontinued operations         |    | 0.01   |    | (0.01) |    | 0.01   |    | (0.02) |
| Gain on disposition of discontinued operations     |    | 0.02   |    | 0.04   |    | 0.02   |    | 0.04   |
| Net income   | \$ | 0.13   | \$ | 0.16   | \$ | 0.12   | \$ | 0.20   |
| Weighted average diluted common shares outstanding |    |        |    |        |    |        |    |        |
|  |    | 39,653 |    | 40,090 |    | 34,918 |    | 40,008 |

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

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statement of Shareholders' Equity**

|  | Common Stock |        | Treasury Stock |          | Additional<br>Paid-In<br>Capital | Deferred<br>Compensation | Accumulated<br>Other<br>Comprehensive<br>Income | Retained<br>Earnings | Total      |
|--|--------------|--------|----------------|----------|----------------------------------|--------------------------|---|----------------------|------------|
|  | Shares       | Amount | Shares         | Amount   |                                  |                          |   |                      |            |
| (Unaudited)  |              |        |                |          |                                  |                          |   |                      |            |
| (In thousands, except share amounts)                           |              |        |                |          |                                  |                          |   |                      |            |
| Balance as of<br>December 31,<br>2004                          | 38,942,728   | \$ 39  |                | \$       | \$ 272,954                       | \$ (329)                 | \$ 408  | \$ 10,911            | \$ 283,983 |
| Vesting of early<br>exercised<br>options                       | 98,285       |        |                |          | 452                              |                          |   |                      | 452        |
| Treasury stock   | 29,870       |        | (29,870)       | (137)    | 137                              |                          |   |                      |            |
| Unearned<br>compensation                                       |              |        |                |          | 2,092                            | (2,092)                  |   |                      |            |
| Amortization of<br>unearned<br>compensation                    |              |        |                |          |                                  | 306                      |   |                      | 306        |
| Stock options<br>exercised                                     | 135,704      |        |                |          | 686                              |                          |   |                      | 686        |
| Income tax<br>benefit from<br>options<br>exercised             |              |        |                |          | 457                              |                          |   |                      | 457        |
| Issuance of<br>shares under<br>employee stock<br>purchase plan | 77,004       |        |                |          | 682                              |                          |   |                      | 682        |
| Net income   |              |        |                |          |                                  |                          |   | 7,898                | 7,898      |
| Other<br>comprehensive<br>income                               |              |        |                |          |                                  |                          | 105   |                      | 105        |
| Balance as of<br>September 30,<br>2005                         | 39,283,591   | \$ 39  | (29,870)       | \$ (137) | \$ 277,460                       | \$ (2,115)               | \$ 513  | \$ 18,809            | \$ 294,569 |

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



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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Cash Flows**

|  | Nine Months<br>Ended<br>September 30,<br>2004 | Nine Months<br>Ended<br>September 30,<br>2005 |
|--|---|---|
|  | (Unaudited)<br>(In thousands)                 |   |
| Cash flows used in operating activities:   |   |   |
| Income from continuing operations  | \$ 3,043                                      | \$ 7,006                                      |
| Adjustments to reconcile income from continuing operations to cash used in operating activities: |   |   |
| Depreciation   | 17,577  | 20,714  |
| Amortization of intangibles  | 10,989  | 4,311   |
| Deferred income taxes  | (7,827)                                       | 5,121   |
| Gain on sale of fixed assets   | (1,247)                                       | (1,837)                                       |
| Loss on early extinguishment of debt   | 5,549   |   |
| Reversal of litigation judgment  |   | (4,279)                                       |
| Other  | (1,179)                                       | (243)   |
| Changes in operating assets and liabilities, net of effects of acquisitions:                     |   |   |
| Contract receivables, net  | (13,892)                                      | (34,035)                                      |
| Contract receivables due from related parties, net   | 14,617  |   |
| Costs and estimated earnings in excess of billings, net  | (34,598)                                      | (45,336)                                      |
| Inventories  | (2,112)                                       | (639)   |
| Other current assets   | 3,514   | 3,755   |
| Deferred charges and other assets  | 2,660   | 311   |
| Accounts payable   | 3,024   | (652)   |
| Other liabilities related parties  |   | (2,988)                                       |
| Other current and accrued liabilities  | (9,772)                                       | 8,309   |
| Accrued insurance reserves   | 3,873   | 2,187   |
| Deferred revenue   | 6,013   | 802   |
| Other liabilities  | (674)   | (165)   |
| Net cash flows used in operating activities from continuing operations                           | (442)   | (37,658)                                      |
| Gain on sale of discontinued operations  | (1,006)                                       | (3,222)                                       |
| Net cash flows provided by (used in) operating activities from discontinued operations           | 2,141   | (362)   |
| Net cash flows provided by (used in) operating activities  | 693   | (41,242)                                      |
| Cash flows used in investing activities:   |   |   |
| Acquisitions of businesses, net of cash acquired   | (49,571)                                      | (38)  |
| Proceeds from restricted cash  |   | 5,000   |

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|  |          |          |
|--|----------|----------|
| Proceeds from sale of discontinued operations                              | 8,616    | 7,117    |
| Proceeds from sales of equipment   | 3,299    | 4,091    |
| Additions to property and equipment  | (17,283) | (21,681) |
| Net cash flows used in investing activities from continuing operations     | (54,939) | (5,511)  |
| Net cash flows used in investing activities from discontinued operations   | (653)    | (197)    |
| Net cash flows used in investing activities                                | (55,592) | (5,708)  |
| Cash flows from financing activities:                                      |          |          |
| Increase in revolving credit facility borrowings                           | 4,000    | 27,000   |
| Repayments of long-term debt and capital lease obligations                 | (83,766) | (679)    |
| Proceeds from exercise of stock options and employee stock purchase plan   | 2,250    | 1,368    |
| Proceeds from sale of common stock   | 128,093  |          |
| Net cash flows provided by financing activities from continuing operations | 50,577   | 27,689   |
| Net cash flows used in financing activities from discontinued operations   | (1,000)  |          |
| Net cash flows provided by financing activities                            | 49,577   | 27,689   |
| Cash and cash equivalents:   |          |          |
| Net decrease in cash and cash equivalents                                  | (5,322)  | (19,261) |
| Cash and cash equivalents transferred (to) from discontinued operations    | (488)    | 559      |
| Cash and cash equivalents beginning of period                              | 12,013   | 21,222   |
| Cash and cash equivalents end of period                                    | \$ 6,203 | \$ 2,520 |

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

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|   | <b>Nine Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2005</b> |
|---|---|---|
|   | <b>(Unaudited)<br/>(In thousands)</b>                   |   |
| <b>Supplemental Disclosure of Non-Cash Investing and<br/>Financing Activities:</b>                              |   |   |
| Distribution of property and equipment owed to related party  | \$ 7,218  | \$  |
| Loss on early extinguishment of the note payable to Exelon  | 5,549   |   |
| Acquisition of all the voting interests of Maslonka for \$77,571 in January, 2004                               |   |   |
| Assets acquired and liabilities assumed were as follows:  |   |   |
| Fair value of assets acquired   | 41,093  |   |
| Goodwill  | 59,644  |   |
| Liability to sellers for taxes and cash holdback  | (1,704)   |   |
| Liabilities assumed   | (23,166)  |   |
| Equity issued to sellers  | (50,671)  |   |
| Cash paid for acquisition, net of cash acquired   | (25,196)  |   |
| Acquisition of substantially all of the assets of Utilitrax for \$5,168 in August, 2004                         |   |   |
| Assets acquired and liabilities assumed were as follows:  |   |   |
| Fair value of assets acquired   | \$ 3,073  | \$  |
| Goodwill  | 2,319   |   |
| Receivable from seller for management agreements  | 290   |   |
| Liabilities assumed   | (224)   |   |
| Cash paid for acquisition, net of cash acquired   | (5,458)   |   |
| Acquisition of substantially all of the assets of certain EnStructure companies for \$21,208 in September, 2004 |   |   |
| In conjunction with this acquisition, assets acquired and liabilities assumed were as follows:                  |   |   |
| Fair value of assets acquired   | \$ 22,431   | \$ 38   |
| Receivable from seller for management agreements  | 535   |   |
| Liability to sellers for cash holdback  | (2,000)   |   |
| Liabilities assumed   | (1,223)   |   |
| Cash paid for acquisition, net of cash acquired   | (19,743)  | (38)  |

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

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
**(Unaudited)**

**1. Organization and Basis of Presentation**

InfraSource Services, Inc. ( *InfraSource* ) was organized on May 30, 2003 as a Delaware corporation. *InfraSource* and its wholly owned subsidiaries are referred to herein as the *Company*, *we*, *us*, or *our* . We operate in two business segments. Our principal segment, Infrastructure Construction Services ( *ICS* ), provides design, engineering, procurement, construction, testing, and maintenance services for utility infrastructure. Our *ICS* customers include electric power utilities, natural gas utilities, telecommunication customers, government entities and heavy industrial companies, such as petrochemical, processing and refining businesses. Our Telecommunication Services ( *TS* ) segment provides design, procurement, construction, and maintenance services for telecommunications infrastructure as well as leasing point to point telecommunications infrastructure in select markets. Our *TS* customers include communication service providers, large industrial customers such as pharmaceutical companies, school districts and other entities with high bandwidth telecommunication needs. We operate in multiple territories throughout the United States and do not have significant operations or assets in countries outside the United States.

On September 24, 2003, we acquired all of the voting interests of *InfraSource Incorporated* and certain of its wholly owned subsidiaries (collectively, the *InfraSource Group* ), pursuant to a merger transaction (the *Merger* ). On May 12, 2004, we completed our initial public offering ( *IPO* ) of 8,500,000 shares of common stock. *OCM/GFI Power Opportunities Fund, L.P.* and *OCM Principal Opportunities Fund, L.P.* (collectively, the *Principal Stockholders* ), both Delaware limited partnerships, own approximately 64% of our common stock.

The accompanying unaudited condensed consolidated financial statements reflect our financial position as of December 31, 2004 and September 30, 2005; our results of operations for the three and nine months ended September 30, 2004 and 2005; and our cash flows for the nine months ended September 30, 2004 and 2005. The accompanying condensed consolidated financial statements are unaudited and have been prepared in accordance with the rules and regulations of the U.S. Securities and Exchange Commission ( *SEC* ). These financial statements include all adjustments that we consider necessary for a fair presentation of financial position, results of operations and cash flows for the interim periods presented. The December 31, 2004 condensed consolidated balance sheet data were derived from audited financial statements, but do not include all disclosures required by accounting principles generally accepted in the United States of America. The results for interim periods are not necessarily indicative of results to be expected for a full year or future interim periods. These financial statements should be read in conjunction with our financial statements and related notes included in our Report on Form 10-K for the year ended December 31, 2004.

Certain amounts in the accompanying statements have been reclassified for comparative purposes.

**2. Recently Issued Accounting Pronouncements**

In December 2004, the Financial Accounting Standards Board ( *FASB* ) issued Statement of Financial Accounting Standards ( *SFAS* ) No. 123R *Share Based Payment*. *SFAS* No. 123R is a revision to *SFAS* No. 123 *Accounting for Stock-Based Compensation*, and supersedes Accounting Principles Board ( *APB* ) Opinion No. 25 *Accounting for Stock Issued to Employees*, and Related Interpretations and amends *FASB* Statement No. 95, *Statement of Cash Flows*. *SFAS* No. 123R requires a public entity to expense the cost of employee services received in exchange for an award of equity instruments. *SFAS* No. 123R provides guidance on valuing and expensing these awards, as well as disclosure requirements of these equity arrangements. As modified by the *SEC* on April 15, 2005, *SFAS* No. 123R is effective for the first annual or interim reporting period of the registrant's first fiscal year that begins after June 15, 2005. We are required to adopt the provisions of *SFAS* No. 123R effective January 1, 2006, at which time we will begin recognizing an expense for unvested share-based compensation that has been issued or will be issued after that date. *SFAS* No. 123R permits an issuer to use either a prospective or one of two modified versions of

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retrospective application under which financial statements for prior periods are adjusted on a basis consistent with the pro forma disclosures required for those periods by the original SFAS No. 123. Under the retroactive options, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented.

As permitted by SFAS No. 123, we currently account for share-based compensation to employees using the intrinsic value method of APB Opinion No. 25 and, as such, we generally recognize no compensation cost for employee stock options. The impact of the adoption of SFAS No. 123R cannot be predicted at this time because it will depend on levels of share-based compensation granted in the future. However, valuation of employee stock options under SFAS No. 123R is similar to SFAS No. 123, with minor exceptions. For information about what our reported results of operations and earnings per share would have been had we adopted SFAS No. 123, see the pro forma disclosure in Note 9. Accordingly, the adoption of the fair value method of SFAS No. 123R will likely have a significant impact on our results of operations, although it will have no impact on our overall financial position. We have not yet completed the analysis of the ultimate impact that SFAS No. 123R will have on our results of operations. We plan to adopt SFAS No. 123R using the prospective method.

In December 2004, the FASB issued Staff Position ( FSP ) No. 109-1, Application of FASB No. 109, Accounting for Income Taxes , to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004 . The American Jobs Creation Act of 2004 ( AJCA ) introduces a special 3% tax deduction, which is phased up to 9%, on qualified production activities. FSP No. 109-1 clarifies that this tax deduction should be accounted for as a special tax deduction in accordance with SFAS No. 109. Pursuant to the AJCA and the guidance provided to date, we will likely be viewed as engaging in qualified production activities and, thus, be able to claim this tax deduction in 2005. We do not expect these new tax provisions to have a significant impact on our consolidated financial position, results of operations or cash flows.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3 . This Statement replaces APB Opinion No. 20, Accounting Changes, and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements, and changes the requirements for the accounting for and reporting of a change in accounting principle. SFAS No. 154 applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. When a pronouncement includes specific transition provisions, those provisions should be followed. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. We will adopt the provisions of SFAS No. 154 beginning January 1, 2006. We do not believe that adoption of the provisions of SFAS No. 154 will have a material impact on our consolidated financial statements.

**3. Acquisitions*****Maslonka***

On January 27, 2004, we acquired all of the voting interests of Maslonka & Associates ( Maslonka ), a complementary infrastructure services business, for total purchase price consideration of \$83.1 million, which included the issuance of 4,330,820 shares of our common stock, cash, transaction costs and purchase price contingencies. The value of the shares issued to Maslonka stockholders was determined to be approximately \$50.7 million. The allocation of the purchase price was subject to a working capital adjustment and settlement of holdback adjustments to the purchase price in accordance with the terms of the acquisition agreement. Under terms of the holdback provisions, we withheld \$6.6 million in cash and 957,549 shares of common stock. We finalized the working capital adjustment in July 2005 and released half of the holdback equal to \$3.3 million in cash and 478,775 shares of common stock to the sellers in accordance with the agreement. The

**Table of Contents****INFRASOURCE SERVICES, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements (Continued)**

balance of the holdback is expected to be released in January 2006. Of the cash holdback amount, \$5.5 million was contingent upon Maslonka's achievement of certain performance targets as well as satisfaction of any indemnification obligations owed to us. In the fourth quarter of 2004, based on an evaluation of the performance targets detailed in the acquisition agreement, we recorded the \$5.5 million additional contingent purchase price. The estimated working capital settlement recorded in the second quarter of 2005 caused an increase to our goodwill balance of approximately \$0.2 million. The final working capital settlement reached in July 2005 was consistent with our estimate. The results of Maslonka are included in our consolidated results beginning January 27, 2004.

Additionally, at the time of the acquisition, Maslonka had an outstanding letter of credit collateralized with a \$5.0 million time deposit account provided by the Maslonka stockholders, which we acquired in the acquisition. As required under the acquisition agreement, we reimbursed the Maslonka stockholders for the \$5.0 million in the third quarter of 2004. After giving effect to the holdback and the reimbursement of the time deposit account, the amount paid at closing was \$26.7 million in cash and 3,373,271 shares of our common stock. We financed the cash portion of the Maslonka acquisition with cash on hand and the issuance of 5,931,950 shares of our common stock to our principal stockholders and certain members of our management team for cash of \$27.5 million.

Intangible assets consisting of construction backlog have been valued at \$11.5 million and are being amortized over the life of the related contracts, which range from one to two years. The amortization of these intangible assets as well as the goodwill currently estimated at \$63.0 million is not deductible for tax purposes. Since Maslonka is part of our ICS segment, all resulting goodwill is included in the ICS segment.

***Utili-Trax***

On August 18, 2004, we acquired substantially all of the assets and assumed certain liabilities of Utili-Trax Contracting Partnerships, LLC ( Utili-Trax ), which provides underground and overhead construction services for electric cooperatives and municipal utilities throughout the upper Midwest, for total purchase price consideration of \$5.3 million in cash, including transaction costs. The intangible asset valued at \$0.9 million relates to a customer volume agreement which is being amortized over the life of the contract. The purchase price has been allocated to the assets acquired and liabilities assumed based on their estimated fair value, which resulted in goodwill of \$1.3 million. The amortization of intangible assets and goodwill are deductible for tax purposes. The results of Utili-Trax are included in our consolidated results beginning August 18, 2004. Since Utili-Trax is part of our ICS segment, all resulting goodwill is included in the ICS segment.

***EnStructure***

On September 3, 2004, we acquired substantially all of the assets and assumed certain liabilities of EnStructure Corporation's ( EnStructure ) operating companies: Sub-Surface Construction Company, Flint Construction Company and Iowa Pipeline Associates, for total purchase price consideration of \$20.9 million in cash, including transaction costs. EnStructure, the construction services business of SEMCO Energy, Inc., provides construction services within the utilities, oil and gas markets throughout the Midwestern, Southern and Southeastern regions of the United States. Intangible assets consisting of construction backlog and a volume agreement have been valued at \$1.3 million and are being amortized over the life of the related contracts which range one to five years. The amortization of these intangible assets is deductible for tax purposes. The results of EnStructure are included in our consolidated results beginning September 3, 2004. The fair value of the EnStructure net assets exceeded the purchase price. Therefore, as described in SFAS No. 141, *Business Combinations*, we decreased the eligible assets by the excess amount.

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

**Pro Forma Financial Information**

The following table provides pro forma unaudited consolidated statements of operations data as if the Maslonka, Utili-Trax and EnStructure acquisitions had occurred on January 1, 2004:

|  | <b>Three Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2004</b> |
|--|--|---|
| Contract revenues                                  | \$ 176,470   | \$ 509,453  |
| Net income (loss)                                  | 3,058  | (18,244)  |
| <i>Earnings Per Share Data:</i>                    |  |   |
| Weighted average basic common shares outstanding   | 38,690   | 34,974  |
| Weighted average diluted common shares outstanding | 39,653   | 34,974  |
| Basic net income (loss) per share                  | \$ 0.08  | \$ (0.52)   |
| Diluted net income (loss) per share                | 0.08   | (0.52)  |

Pro forma results of operations for the three and nine months ended September 30, 2004 presented above have been adjusted to reflect Maslonka, Utili-Trax and EnStructure historical operating results prior to their acquisitions, after giving effect to adjustments directly attributable to the transactions that are expected to have a continuing effect. Such adjustments include (1) the amortization of intangible assets acquired and recorded in accordance with the provisions of SFAS No. 141, and related income tax effects; (2) the effects of depreciation expense resulting from changes in lives and book basis of certain fixed assets; (3) the elimination of interest expense resulting from the repayment of Maslonka debt and additional interest expense associated with a note issued to the seller and related income tax effects; and (4) the issuance of our common stock to the sellers in the Maslonka acquisition and to the Principal Stockholders and certain members of our management to finance a portion of the purchase price.

The pro forma results for the nine months ended September 30, 2004 include a charge of \$31.3 million for deferred compensation expense, which was recorded in Maslonka's historical results of operations, and \$1.5 million for transaction costs related to the Maslonka acquisition. The above pro forma information is not necessarily indicative of the results of operations that would have occurred had the 2004 acquisitions been made as of January 1, 2004, or of results that may occur in the future.

**4. Discontinued Operations**

During 2003, subsequent to the Merger, we committed to a plan to sell substantially all of the assets of OSP Consultants, Inc. and subsidiaries (OSP). On September 21, 2004, we completed the sale of substantially all of the assets of RJE Telecom, Inc. (RJE), a wholly owned subsidiary of OSP, for aggregate cash proceeds of \$9.4 million, net of transaction costs. The RJE sale completed our commitment to sell substantially all of the assets of OSP. RJE was part of our TS segment.

In the third quarter of 2004, we committed to a plan to sell substantially all of the assets of Utility Locate & Mapping Services, Inc. (ULMS). In the second quarter of 2005, we committed to a plan to sell substantially all of the assets of Electric Services, Inc. (ESI). Both ULMS and ESI are part of our ICS segment. In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the financial position, results of operations and cash flows of OSP, ULMS and ESI are reflected as discontinued operations in our accompanying condensed consolidated financial statements. For the three and nine months ended September 30, 2004, OSP, ULMS and ESI are reflected as discontinued operations, while for the three and nine months ended September 30, 2005 only ULMS and ESI are reflected as discontinued operations since RJE was sold in 2004.





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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

The tables below present balance sheet and statement of operations information for the previously mentioned discontinued operations.

Balance sheet information:

|  | <b>December 31,<br/>2004</b> | <b>September 30,<br/>2005</b> |
|--|------------------------------|-------------------------------|
| <b>(In thousands)</b>                      |                              |                               |
| Cash and cash equivalents                  | \$ 559                       | \$                            |
| Contract receivables, net                  | 6,153                        |                               |
| Other current assets                       | 3,987                        |                               |
| <br>Total current assets                   | <br>10,699                   |                               |
| Property and equipment, net                | 1,626                        |                               |
| Other long-term assets, net                | 106                          |                               |
| <br>Total assets                           | <br>12,431                   |                               |
| <br>Accounts payable and other liabilities | <br>8,526                    |                               |
| Deferred income taxes long term            | 11                           |                               |
| <br>Total liabilities                      | <br>8,537                    |                               |
| <br>Net assets                             | <br>\$ 3,894                 | <br>\$                        |

Statement of operations information:

|                       | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> |
|-----------------------|--|--|---|---|
| <b>(In thousands)</b> |  |  |   |   |
| Contract revenues     | \$ 14,450  | \$ 1,436   | \$ 35,283   | \$ 12,769   |
| Pre-tax income (loss) | 765  | (888)  | 750   | (1,523)   |

**5. Costs And Estimated Earnings In Excess Of Billings and Contract Losses**

Included in costs and estimated earnings in excess of billings are costs related to claims of approximately \$4.7 million and \$11.5 million at December 31, 2004 and September 30, 2005, respectively. Claim amounts are related to a delay in the anticipated start date of one of our electric transmission projects and claims related to permit delays, changes in scope and environmental impacts on a large underground utility construction project. Estimated revenue up to but not exceeding costs incurred is recognized when realization is probable and amounts are estimable. Profit from claims is recorded in the period such amounts are agreed to with the customer.

Included in our nine month results of operations for 2005 is a \$9.0 million contract loss related to an underground utility construction project. This project, which began in late January 2005 and is expected to be completed in the

fourth quarter of 2005, had an original contract value of approximately \$18.0 million. Consistent with our revenue recognition policy for contracts that are in a forecasted loss position, in the second quarter of 2005, we recognized the entire loss expected at that time of \$8.5 million. During the third quarter of 2005, we recognized an additional loss of \$0.5 million. The loss is attributable primarily to lower than expected productivity, higher materials costs, and unforeseen delays.

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

**6. Goodwill and Intangible Assets**

Our goodwill and intangible assets are comprised of:

|                                       | December 31,<br>2004 | September 30,<br>2005 |
|---------------------------------------|----------------------|-----------------------|
| (In thousands)                        |                      |                       |
| Goodwill                              | \$ 134,478           | \$ 134,750            |
| Intangible assets:                    |                      |                       |
| Construction backlog                  | \$ 17,184            | \$ 16,265             |
| Volume agreements                     | 4,561                | 4,561                 |
| <b>Total intangible assets</b>        | <b>21,745</b>        | <b>20,826</b>         |
| Accumulated amortization:             |                      |                       |
| Construction backlog                  | (13,491)             | (15,426)              |
| Volume agreements                     | (1,459)              | (2,916)               |
| <b>Total accumulated amortization</b> | <b>(14,950)</b>      | <b>(18,342)</b>       |
| Intangible assets, net                | \$ 6,795             | \$ 2,484              |

The goodwill balance as of September 30, 2005 was \$126.3 million and \$8.5 million for the ICS and TS segments, respectively. The goodwill balance as of December 31, 2004 was \$126.0 million and \$8.5 million for the ICS and TS segments, respectively.

As a result of the adoption of SFAS No. 142, Goodwill and Intangible Assets, goodwill is subject to an assessment for impairment using a two-step fair value-based test with the first step performed at least annually, or more frequently if events or circumstances exist that indicate that goodwill may be impaired. We complete our annual analysis of our reporting units at each fiscal year end. The first step compares the fair value of a reporting unit to its carrying amount, including goodwill. If the carrying amount of the reporting unit exceeds its fair value, the second step is then performed. The second step compares the carrying amount of the reporting unit's goodwill to the fair value of the goodwill. If the fair value of the goodwill is less than the carrying amount, an impairment loss would be recorded as a reduction to goodwill and a corresponding charge to operating expense. No provisions for goodwill impairments were recorded during the three and nine months ended September 30, 2004 and 2005.

Amortization expense of intangible assets was \$2.4 million and \$1.0 million for the three months ended September 30, 2004 and 2005, respectively, and \$11.0 million and \$4.3 million for the nine months ended September 30, 2004 and 2005, respectively. Once an intangible asset is fully amortized, we net the accumulated amortization against the intangible asset to remove the asset.

The estimated aggregate amortization expense of intangible assets for the next five succeeding fiscal years is:

|  | (In thousands) |
|--|----------------|
| For the year ended December 31, 2005 (excludes the nine months ended September 30, 2005) | \$ 562         |

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|       |          |
|-------|----------|
| 2006  | 1,078    |
| 2007  | 458      |
| 2008  | 227      |
| 2009  | 159      |
| Total | \$ 2,484 |

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

**7. Debt**

On June 10, 2005, while in the process of evaluating the extent of the loss for an underground utility construction project (see Note 5), we obtained a Second Amendment and Waiver to our credit facility which excluded the anticipated effect of the loss from our debt covenant calculations through July 25, 2005. Based on our further evaluation of the loss, estimated to be \$9.0 million, we are currently not required to enter into any further amendment or waiver because our credit facility includes a clause in our debt covenant calculations that allows for the exclusion of extraordinary, unusual or non-recurring expenses or losses, as defined, provided that the amounts shall not, in the aggregate exceed \$10.0 million for any fiscal year.

**8. Computation of Per Share Earnings**

The following table is a reconciliation of the numerators and denominators of the basic and diluted income (loss) per share computation.

|   | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> |
|---|--|--|---|---|
| <b>(In thousands, except per share amounts)</b>   |  |  |   |   |
| Income from continuing operations (numerator)   | \$ 3,976   | \$ 5,305   | \$ 3,043  | \$ 7,006  |
| Income (loss) from discontinued operations, net of tax expense (benefit) of \$282, \$(359), \$289 and \$(625), respectively | 483  | (529)  | 461   | (898)   |
| Gain on disposition of discontinued operations, net of tax of \$413, \$1,432, \$413 and \$1,432, respectively               | 593  | 1,790  | 593   | 1,790   |
| Net income  | \$ 5,052   | \$ 6,566   | \$ 4,097  | \$ 7,898  |
| Weighted average basic common shares outstanding (denominator)  | 38,690   | 39,139   | 33,924  | 39,059  |
| Potential common stock arising from stock options   | 963  | 951  | 994   | 949   |
| Weighted average diluted common shares outstanding (denominator)  | 39,653   | 40,090   | 34,918  | 40,008  |
| Basic net income per share  | \$ 0.13  | \$ 0.17  | \$ 0.12   | \$ 0.20   |
| Diluted net income per share  | 0.13   | 0.16   | 0.12  | 0.20  |

Included in potential common stock arising from stock options for the nine months ended September 30, 2005 are early exercises of unvested stock option awards, which are excluded from the weighted average basic common shares outstanding calculation. For the three months ended September 30, 2004 and 2005 there were 685,003 shares and 0 shares, respectively, and for the nine months ended September 30, 2004 and 2005 there were 685,003 shares and

604,880 shares, respectively, under option grants excluded from the calculation of diluted earnings per share as the effect of these shares would have been anti-dilutive.

**9. Stock-Based Compensation**

As permitted by SFAS No. 123, we account for stock-based compensation in accordance with APB No. 25. Under APB No. 25, we recognize no compensation expense related to employee stock options unless options are granted at a price below the market price on the day of the grant. Had we applied the fair value

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recognition provisions of SFAS No. 123 to stock-based employee compensation, net income and basic and diluted net income per share would have been as follows:

|  | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> |
|--|--|--|---|---|
| <b>(In thousands, except per share amounts)</b>  |  |  |   |   |
| Net income as reported   | \$ 5,052   | \$ 6,566   | \$ 4,097  | \$ 7,898  |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of relative tax effects | (226)  | (328)  | (635)   | (478)   |
| Add: Total stock-based employee compensation expense, net of related tax effects included in the determination of net income as reported     | 20   | 155  | 208   | 175   |
| Pro forma net income   | \$ 4,846   | \$ 6,393   | \$ 3,670  | \$ 7,595  |
| <i>Basic and diluted income per share:</i>   |  |  |   |   |
| Basic net income per share as reported   | \$ 0.13  | \$ 0.17  | \$ 0.12   | \$ 0.20   |
| Basic net income per share pro forma   | 0.13   | 0.16   | 0.11  | 0.19  |
| Diluted net income per share as reported   | 0.13   | 0.16   | 0.12  | 0.20  |
| Diluted net income per share pro forma   | 0.12   | 0.16   | 0.11  | 0.19  |

**10. Concentration of Credit Risk**

We derive a significant portion of our revenues from a small group of customers. Our top ten customers accounted for 42% and 48%, of our consolidated revenues for the three months ended September 30, 2004 and 2005, respectively, and 49% and 47% of our consolidated revenues for the nine months ended September 30, 2004 and 2005, respectively. Exelon Corporation ( Exelon ) accounted for approximately 14% and 18%, our consolidated revenues for the three and nine months ended September 30, 2004, respectively, and 16%, and 21% of our consolidated revenues for the three and nine months ended September 30, 2005, respectively. Additionally, for the nine months ended September 30, 2004, Western Area Power Administration accounted for approximately 12% of our consolidated revenues.

At December 31, 2004 and September 30, 2005, accounts receivable due from Exelon, inclusive of amounts due from a prime contractor for Exelon work, represented 20% and 19%, respectively, of our total accounts receivable balance.

**11. Other Income, Net**

Other income, net for the nine months ended September 30, 2005 includes a reversal of a \$3.8 million charge for a litigation judgment recorded in 2003 (see Note 15).



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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

**12. Comprehensive Income (Loss)**

The following table presents the components of comprehensive income for the periods presented:

|                                      | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> |
|--------------------------------------|--|--|---|---|
| <b>(In thousands)</b>                |  |  |   |   |
| Net income                           | \$ 5,052   | \$ 6,566   | \$ 4,097  | \$ 7,898  |
| Other comprehensive income<br>(loss) | (204)  | 18   | 195   | 105   |
| <b>Comprehensive income</b>          | <b>\$ 4,848</b>  | <b>\$ 6,584</b>  | <b>\$ 4,292</b>   | <b>\$ 8,003</b>   |

Other comprehensive income during the three and nine months ended September 30, 2004 and 2005 was comprised of changes in the fair value of interest rate cap and swap agreements designated and qualifying as cash flow hedges under the provisions of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended by SFAS Nos. 137, 138 and 149, net of reclassifications to net income.

**13. Segment Information**

We operate in two business segments. Our principal segment, ICS, provides design, engineering, procurement, construction, testing, and maintenance services for utility infrastructure. Our ICS customers include electric power utilities, natural gas utilities, telecommunication customers, government entities and heavy industrial companies, such as petrochemical, processing and refining businesses. Our ICS services are provided by four of our operating units, all of which have been aggregated into one reportable segment due to their similar economic characteristics, customer bases, products and production and distribution methods. Our TS segment, consisting of a single operating unit, provides design, procurement, construction, and maintenance services for telecommunications infrastructure as well as leasing point to point telecommunications infrastructure in select markets. Our TS customers include communication service providers, large industrial customers such as pharmaceutical companies, school districts and other entities with high bandwidth telecommunication needs. A business included in our TS segment is a regulated public telecommunications utility, with facilities in Delaware, Maryland, New Jersey and Pennsylvania. During 2004, we changed to two reporting segments and all prior periods presented have been restated. We operate in multiple territories throughout the United States and do not have significant operations or assets in countries outside the United States.

Performance measurement and resource allocation for the reportable segments are based on many factors. The primary financial measures we use to evaluate our segment operations are contract revenues and income (loss) from operations as adjusted, a non-GAAP financial measure. Income (loss) from operations as adjusted excludes amortization expense related to intangibles as a result of our acquisitions. We exclude amortization to facilitate our evaluation of operating unit performance as we believe amortization expense does not reflect the core operations of our business segments. A reconciliation of income (loss) from operations as adjusted to the nearest GAAP equivalent, income (loss) from operations is provided below.

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

We do not allocate corporate costs to our segments for internal management reporting. Corporate and eliminations includes unallocated corporate costs and elimination of revenues between reporting segments which are not significant. The following tables present segment information by period:

| <b>Three Months Ended September 30, 2004</b>       | <b>Infrastructure</b>            |                                       | <b>Corporate<br/>and<br/>Eliminations</b> | <b>Total</b> |
|--|----------------------------------|---------------------------------------|---|--------------|
|  | <b>Construction<br/>Services</b> | <b>Telecommunication<br/>Services</b> |   |              |
|  | <b>(In thousands)</b>            |                                       |   |              |
| Revenues   | \$ 154,280                       | \$ 7,643                              | \$ (47)                                   | \$ 161,876   |
| Income (loss) from operations as adjusted          | 7,610                            | 3,632                                 | (1,735)                                   | 9,507        |
| Depreciation                                       | 5,405                            | 749                                   | 109                                       | 6,263        |
| Amortization                                       | 2,420                            |                                       |   | 2,420        |
| Total assets                                       | 343,079                          | 70,387                                | 89,086                                    | 502,552      |
| Capital expenditures                               | 3,063                            | 2,473                                 | 113                                       | 5,649        |
| <b>reconciliation:</b>                             |                                  |                                       |   |              |
| Income (loss) from operations as adjusted          | \$ 7,610                         | \$ 3,632                              | \$ (1,735)                                | \$ 9,507     |
| Less: Amortization                                 | 2,420                            |                                       |   | 2,420        |
| Income (loss) from operations                      | 5,190                            | 3,632                                 | (1,735)                                   | 7,087        |
| Interest income                                    | 27                               |                                       | 201                                       | 228          |
| Interest expense and amortization of debt discount | (1,475)                          | (173)                                 | (321)                                     | (1,969)      |
| Other income (expense), net                        | 1,426                            | 2                                     | (38)                                      | 1,390        |
| Income (loss) before income taxes                  | \$ 5,168                         | \$ 3,461                              | \$ (1,893)                                | \$ 6,736     |

| <b>Three Months Ended September 30, 2005</b> | <b>Infrastructure</b>            |                                       | <b>Corporate<br/>and<br/>Eliminations</b> | <b>Total</b> |
|--|----------------------------------|---------------------------------------|---|--------------|
|  | <b>Construction<br/>Services</b> | <b>Telecommunication<br/>Services</b> |   |              |
|  | <b>(In thousands)</b>            |                                       |   |              |
| Revenues                                     | \$ 219,461                       | \$ 9,884                              | \$ 535                                    | \$ 229,880   |
| Income (loss) from operations as adjusted    | 10,326                           | 4,065                                 | (2,761)                                   | 11,630       |
| Depreciation                                 | 6,173                            | 892                                   | 52  | 7,117        |
| Amortization                                 | 1,001                            |                                       |   | 1,001        |
| Total assets                                 | 382,772                          | 82,162                                | 99,117                                    | 564,051      |
| Capital expenditures                         | 2,400                            | 3,839                                 | 38  | 6,277        |
| <b>reconciliation:</b>                       |                                  |                                       |   |              |
| Income (loss) from operations as adjusted    | \$ 10,326                        | \$ 4,065                              | \$ (2,761)                                | \$ 11,630    |
| Less: Amortization                           | 1,001                            |                                       |   | 1,001        |

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|  |          |          |            |          |
|--|----------|----------|------------|----------|
| Income (loss) from operations                      | 9,325    | 4,065    | (2,761)    | 10,629   |
| Interest income                                    | 88       |          | 44         | 132      |
| Interest expense and amortization of debt discount | (1,844)  | (69)     | (257)      | (2,170)  |
| Other income (expense), net                        | 678      | (8)      | 65         | 735      |
| Income (loss) before income taxes                  | \$ 8,247 | \$ 3,988 | \$ (2,909) | \$ 9,326 |

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

| Nine Months Ended September 30, 2004               | Infrastructure           |                               | Corporate<br>and<br>Eliminations | Total      |
|--|--------------------------|-------------------------------|----------------------------------|------------|
|  | Construction<br>Services | Telecommunication<br>Services |                                  |            |
| <b>(In thousands)</b>                              |                          |                               |                                  |            |
| Revenues   | \$ 429,810               | \$ 20,699                     | \$ (289)                         | \$ 450,220 |
| Income (loss) from operations as adjusted          | 27,976                   | 9,090                         | (9,898)                          | 27,168     |
| Depreciation                                       | 15,180                   | 2,099                         | 298                              | 17,577     |
| Amortization                                       | 10,989                   |                               |                                  | 10,989     |
| Total assets                                       | 343,079                  | 70,387                        | 89,086                           | 502,552    |
| Capital expenditures                               | 9,609                    | 7,332                         | 342                              | 17,283     |
| <b>reconciliation:</b>                             |                          |                               |                                  |            |
| Income (loss) from operations as adjusted          | \$ 27,976                | \$ 9,090                      | \$ (9,898)                       | \$ 27,168  |
| Less: Amortization                                 | 10,989                   |                               |                                  | 10,989     |
| Income (loss) from operations                      | 16,987                   | 9,090                         | (9,898)                          | 16,179     |
| Interest income                                    | 99                       |                               | 251                              | 350        |
| Interest expense and amortization of debt discount | (6,222)                  | (1,032)                       | (907)                            | (8,161)    |
| Loss on early extinguishment of debt               | (4,586)                  | (878)                         | (85)                             | (5,549)    |
| Other income (expense), net                        | 2,247                    | 29                            | (23)                             | 2,253      |
| Income (loss) before income taxes                  | \$ 8,525                 | \$ 7,209                      | \$ (10,662)                      | \$ 5,072   |

| Nine Months Ended September 30, 2005      | Infrastructure           |                               | Corporate<br>and<br>Eliminations | Total      |
|---|--------------------------|-------------------------------|----------------------------------|------------|
|   | Construction<br>Services | Telecommunication<br>Services |                                  |            |
| <b>(In thousands)</b>                     |                          |                               |                                  |            |
| Revenues                                  | \$ 609,994               | \$ 29,968                     | \$ 2,218                         | \$ 642,180 |
| Income (loss) from operations as adjusted | 14,203                   | 12,117                        | (9,979)                          | 16,341     |
| Depreciation                              | 17,994                   | 2,573                         | 147                              | 20,714     |
| Amortization                              | 4,311                    |                               |                                  | 4,311      |
| Total assets                              | 382,772                  | 82,162                        | 99,117                           | 564,051    |
| Capital expenditures                      | 9,482                    | 11,799                        | 400                              | 21,681     |
| <b>reconciliation:</b>                    |                          |                               |                                  |            |
| Income (loss) from operations as adjusted | \$ 14,203                | \$ 12,117                     | \$ (9,979)                       | \$ 16,341  |
| Less: Amortization                        | 4,311                    |                               |                                  | 4,311      |
| Income (loss) from operations             | 9,892                    | 12,117                        | (9,979)                          | 12,030     |

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|  |          |           |            |           |
|--|----------|-----------|------------|-----------|
| Interest income                                    | 184      |           | 170        | 354       |
| Interest expense and amortization of debt discount | (5,048)  | (181)     | (643)      | (5,872)   |
| Other income (expense), net                        | 1,911    | (11)      | 3,849      | 5,749     |
| Income (loss) before income taxes                  | \$ 6,939 | \$ 11,925 | \$ (6,603) | \$ 12,261 |

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements (Continued)**

The following table represents information regarding revenues by end market:

|                    | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>Nine<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> |
|--------------------|--|--|---|---|
| Electric           | \$ 75,074  | \$ 110,622   | \$ 259,022  | \$ 346,127  |
| Gas                | 66,153   | 83,310   | 139,362   | 202,315   |
| Telecommunications | 14,284   | 27,476   | 36,264  | 72,265  |
| Other              | 6,365  | 8,472  | 15,572  | 21,473  |
|                    | <b>\$ 161,876</b>  | <b>\$ 229,880</b>  | <b>\$ 450,220</b>   | <b>\$ 642,180</b>   |

Electric, gas and other end market revenues are entirely part of the ICS segment, while telecommunications end market revenue is included in both the ICS and TS segments. Approximately 54% and 36%, of our telecommunications end market revenues for the three months ended September 30, 2004 and 2005, respectively, and approximately 57% and 41%, of our telecommunications end market revenues for the nine months ended September 30, 2004 and 2005, respectively, were from the TS segment.

**14. Related Party Transactions**

As of September 30, 2005, we had \$5.2 million due to the former owners of Blair Park Services, Inc. and Sunesys, Inc. (collectively Blair Park ) accrued in other liabilities related parties on our condensed consolidated balance sheet for additional contingent purchase price consideration. Blair Park was acquired by InfraSource Incorporated in 2001.

As of September 30, 2005, we have \$4.2 million due to the Maslonka shareholders, including Martin Maslonka, an employee and holder of more than 5% of our common stock, accrued in other liabilities related parties on our condensed consolidated balance sheet. Of this amount, \$3.3 million is holdback consideration from our acquisition of Maslonka (see Note 3). The remaining net balance relates to payments and collections we made on the shareholders behalf which require cash settlement. On August 11, 2005 we also granted the Maslonka shareholders, who are also our employees, 167,556 shares of restricted stock (41,889 of which were granted to Martin Maslonka) valued at \$2.2 million, of which 25% vest in January of 2006 and the remainder vest four years from the date of grant. For the three and nine months ended September 30, 2005, the Company recorded a charge of \$0.3 million to selling, general and administrative expenses in the condensed consolidated statement of operations.

Maslonka is the issuer of a \$1.0 million installment promissory note in favor of Martin Maslonka. The promissory note bears interest at an annual rate of 8.5%, and interest is payable in equal monthly payments. The promissory note matures on June 30, 2006.

We lease our Maslonka headquarters in Mesa, Arizona and our Maslonka Texas field office in San Angelo, Texas from EC Source, LLC, which is wholly owned by Martin Maslonka. Our leases for these two properties will run through February 2009, subject to a five-year renewal option. Pursuant to these leases, we expect to incur total annual lease payments of \$0.2 million.

We lease office and warehouse space from Coleman Properties of which three officers of Blair Park are general partners. The lease for this space was to run through October 2005, subject to a 6 year renewal option. The terms of the lease provided for an increase in rental payments equal to the increase in the Consumer Price Index. In October, 2005 we renewed the lease for three years and our annual payments under this agreement are approximately \$0.1 million.

We also lease ducts in two river bores under the Delaware River from Coleman Properties. Our lease commenced on May 1, 2005 and has a term of five years, with an option to extend. Our annual lease payment

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**INFRASOURCE SERVICES, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements (Continued)**

is \$0.02 million for each pair of fiber installed in the conduit up to a maximum of \$0.2 million per year if additional ducts are leased.

We lease office and warehouse facilities in Michigan which are owned by an employee and his family members. Our leases for these properties will run through May 2007 and September 2006. Pursuant to these leases, we expect to incur total annual lease payments of \$0.3 million.

**15. Commitments and Contingencies**

In January 2004, a judgment was entered against us in Superior Court of Fulton County, Georgia in the amount of \$3.8 million, including \$3.2 million in punitive damages. We had \$3.8 million accrued on our condensed consolidated balance sheet as of December 31, 2004 for this judgment. The judgment upheld allegations by the plaintiff that in 1999 InfraSource Incorporated (formerly known as Exelon Infrastructure Services, Inc.) had fraudulently induced the plaintiff to incur expenses in connection with a proposed business acquisition that was never consummated.

On March 22, 2005, the Court of Appeals of Georgia issued an opinion reversing the \$3.8 million judgment against us. On April 25, 2005, the plaintiff filed a petition requesting the Supreme Court of Georgia to review and reverse the opinion of the Court of Appeals.

Based on the Court of Appeals decision, we reversed the \$3.8 million litigation accrual for the original judgment against us which had been recorded in 2003. Additionally, we reversed \$0.5 million in interest expense which we had been accruing since the judgment date as stipulated by the original judgment. For the nine months ended September 30, 2005, \$3.8 million of income is included in other income, net and \$0.5 million is included as a reduction in interest expense.

On September 19, 2005, the Supreme Court of Georgia denied the petition for certiorari filed by the plaintiff.

Pursuant to our service contracts, we generally indemnify our customers for the services we provide thereunder. Furthermore, because our services are integral to the operation and performance of the electric power transmission and distribution infrastructure, we may become subject to lawsuits or claims for any failure of the systems that we work on, even if our services are not the cause for such failures, and we could be subject to civil and criminal liabilities to the extent that our services contributed to any property damage or blackout. The outcome of these proceedings could result in significant costs and diversion of management's attention to our business. Payments of significant amounts, even if reserved, could adversely affect our reputation and liquidity position.

From time to time, we are a party to various other lawsuits, claims and other legal proceedings that arise in the ordinary course of our business. These actions typically seek, among other things, compensation for alleged personal injury, breach of contract, property damage, punitive damages, civil penalties or other losses, or injunctive or declaratory relief. With respect to such lawsuits, claims and proceedings, we accrue reserves when it is probable a liability has been incurred and the amount of loss can be reasonably estimated. We do not believe any of these proceedings currently pending, individually or in the aggregate, would be expected to have a material adverse effect on our results of operations, cash flows, or financial condition.



**Table of Contents****Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Forward-Looking and Cautionary Statements**

In this Quarterly Report on Form 10-Q, we have made forward-looking statements. Generally, these forward-looking statements can be identified by words like may, will, should, expect, intend, anticipate, estimate, predict, potential, or continue or the negative of those words and other comparable words. These forward-looking statements generally relate to our plans, objectives and expectations for future operations and are based upon our current estimates and projections of future results or trends. Although we believe that our plans and objectives reflected in or suggested by these forward-looking statements are reasonable, we may not achieve these plans or objectives. These statements are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from those contemplated by the statements. These statements only reflect our predictions. Except as required by law, we will not update forward-looking statements even though our situation may change in the future. With respect to forward-looking statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

The factors that could affect future results and could cause those results to differ materially from those expressed in the forward-looking statements include, but are not limited to, those described under Item 1, Business Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2004 and other risks outlined in our filings with the Securities and Exchange Commission ( SEC ).

**Introduction**

The following discussion should be read in conjunction with the unaudited condensed consolidated financial statements and notes of InfraSource Services, Inc. and its wholly owned subsidiaries included elsewhere in this Quarterly Report on Form 10-Q and with the Management Discussion and Analysis of Financial Condition and Results of Operations, Business Risk Factors, and audited financial statements and notes included in our Annual Report on Form 10-K.

**Overview**

We are one of the largest specialty contractors serving the utility transmission and distribution infrastructure in the United States based on market share. We operate in two business segments. Our principal segment, Infrastructure Construction Services ( ICS ), provides design, engineering, procurement, construction, testing, and maintenance services for utility infrastructure. Our ICS customers include electric power utilities, natural gas utilities, telecommunication customers, government entities and heavy industrial companies, such as petrochemical, processing and refining businesses. Our Telecommunication Services ( TS ) segment provides design, procurement, construction, and maintenance services for telecommunications infrastructure as well as leasing point to point telecommunications infrastructure in select markets. Our TS customers include communication service providers, large industrial customers such as pharmaceutical companies, school districts and other entities with high bandwidth telecommunication needs. We operate in multiple territories throughout the United States and do not have significant operations or assets in countries outside the United States. Refer to Note 13 to our condensed consolidated financial statements for additional information.

During the third quarter of 2005:

We experienced significant revenue growth as compared to the third quarter of 2004 due to increased demand for electric transmission and distribution services, our mid-third quarter 2004 acquisitions of EnStructure Corporation s ( EnStructure ) operating companies and Utili-Trax Contracting Partnerships, LLC ( Utili-Trax ), and additional amounts of telecom fiber to the premises ( FTTP ) construction services.

Our gross profit increased \$6.4 million, as compared to the third quarter of 2004, due to the \$68.0 million increase in revenues, a \$1.9 million credit to insurance expense as a result of actuarial

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estimates reflecting favorable loss development in our self insurance retentions, and an increase in the volume of higher margin telecommunication services. These increases were offset, in part, by a proportionately smaller increase in the volume of higher margin aerial electric transmission work, proportionately higher increases in the volume of lower margin underground electric transmission and other electric work, and the overall effect of rising fuel costs.

We had revenues of \$229.9 million for the three months ended September 30, 2005, of which 48% was attributable to electric power customers, 36% to natural gas customers, 12% to telecommunications customers, and 4% to ancillary services. Approximately \$9.9 million or 36% of the telecommunications revenue was derived from our TS segment for the three months ended September 30, 2005. For the nine months ended September 30, 2005, we had revenues of \$642.2 million, of which 54% was attributable to electric power customers, 32% to natural gas customers, 11% to telecommunications customers, and 3% to ancillary services. Approximately \$30.0 million or 41% of the telecommunications revenue was derived from our TS segment for the nine months ended September 30, 2005. Our top ten customers accounted for 48% and 47% of our consolidated revenues for the three and nine months ended September 30, 2005, respectively. Exelon Corporation ( Exelon ) accounted for 16% and 21% of our consolidated revenues for the three and nine months ended September 30, 2005, respectively.

We had revenues of \$161.9 million for the three months ended September 30, 2004, of which 46% was attributable to electric power customers, 41% to natural gas customers, 9% to telecommunications customers, and 4% to ancillary services. Approximately \$7.6 million or 54% of the telecommunications revenue was derived from our TS segment for the three months ended September 30, 2004. For the nine months ended September 30, 2004, we had revenues of \$450.2 million, of which 58% was attributable to electric power customers, 31% to natural gas customers, 8% to telecommunications customers, and 3% to ancillary services. Approximately \$20.7 million or 57% of the telecommunications revenue was derived from our TS segment for the nine months ended September 30, 2004. Our top ten customers accounted for 42% and 49% of our consolidated revenues for the three and nine months ended September 30, 2004, respectively. Exelon accounted for approximately 14% and 18% of our consolidated revenues for the three and nine months ended September 30, 2004, respectively.

Our consolidated backlog was \$819 million as of September 30, 2005, 3% lower than our consolidated backlog of \$844 million as of June 30, 2005 and 17% lower than our backlog of \$989 million as of September 30, 2004. The decline in our backlog reflects the seasonal nature of our business and the timing of recent awards. Our ICS backlog was \$706 million as of September 30, 2005, 5% lower than our ICS backlog of \$740 million as of June 30, 2005 and 20% lower than our ICS backlog of \$884 million as of September 30, 2004. Our TS backlog was \$113 million as of September 30, 2005, 9% higher than our TS backlog of \$104 million as of June 30, 2005 and 8% higher than our TS backlog of \$105 million as of September 30, 2004.

**2004 Acquisitions**

*Maslonka:* On January 27, 2004, we acquired all of the voting interests of Maslonka & Associates ( Maslonka ), a complementary infrastructure services business, for total purchase price consideration of \$83.1 million, which included the issuance of 4,330,820 shares of our common stock, cash, transaction costs and purchase price contingencies. The value of the shares issued to Maslonka stockholders was determined to be approximately \$50.7 million. The allocation of the purchase price was subject to a working capital adjustment and settlement of holdback adjustments to the purchase price in accordance with the terms of the acquisition agreement. Under terms of the holdback provisions, we withheld \$6.6 million in cash and 957,549 shares of common stock. We finalized the working capital adjustment in July 2005 and released half of the holdback equal to \$3.3 million in cash and 478,775 shares of common stock to the sellers in accordance with the agreement. The balance of the holdback is expected to be released in January 2006. Of the cash holdback amount, \$5.5 million was contingent upon Maslonka's achievement of certain performance targets as well as satisfaction of any indemnification obligations owed to us. In the fourth quarter of 2004, based on an evaluation of the performance targets detailed in the acquisition agreement, we recorded the \$5.5 million additional contingent purchase price. The estimated working capital settlement recorded in the second quarter of 2005 caused an increase to our goodwill balance of approximately \$0.2 million. The final working capital

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settlement reached in July 2005 was consistent with our estimate. The results of Maslonka are included in our consolidated results beginning January 27, 2004. We financed the cash portion of the Maslonka acquisition with cash on hand and the issuance of 5,931,950 shares of our common stock to our principal stockholders and certain members of our management team for cash of \$27.5 million. The purchase price has been allocated to the assets acquired and liabilities assumed based on their estimated fair value, which resulted in goodwill of \$63.0 million.

*Utili-Trax:* On August 18, 2004, we acquired substantially all of the assets and assumed certain liabilities of Utili-Trax, which provides underground and overhead construction services for electric cooperatives and municipal utilities throughout the upper Midwest, for total purchase price consideration of \$5.3 million in cash, including transaction costs. The results of Utili-Trax are included in our consolidated results beginning August 18, 2004. The purchase price has been allocated to the assets acquired and liabilities assumed based on their estimated fair value, which resulted in goodwill of \$1.3 million.

*EnStructure:* On September 3, 2004, we acquired substantially all of the assets and assumed certain liabilities of EnStructure's operating companies, Sub-Surface Construction Company, Flint Construction Company and Iowa Pipeline Associates, for total purchase price consideration of \$20.9 million in cash, including transaction costs. EnStructure, the construction services business of SEMCO Energy, Inc., provides construction services within the utilities, oil and gas markets throughout the Midwestern, Southern and Southeastern regions of the United States. The results of EnStructure are included in our consolidated results beginning September 3, 2004. The fair value of the EnStructure net assets exceeded the purchase price. Therefore, as described in Statement of Financial Accounting Standards ( SFAS ) No. 141, Business Combinations , we decreased the eligible assets by the excess amount.

***Discontinued Operations***

During 2003 we committed to a plan to sell substantially all of the assets of OSP Consultants, Inc. and subsidiaries ( OSP ). On September 21, 2004, we completed the sale of substantially all of the assets of RJE Telecom, Inc. ( RJE ), a wholly owned subsidiary of OSP, for aggregate cash proceeds of \$9.4 million, net of transaction costs. The RJE sale completed our commitment to sell substantially all of the assets of OSP. RJE was part of our TS segment.

In the third quarter of 2004, we committed to a plan to sell substantially all of the assets of Utility Locate & Mapping Services, Inc. ( ULMS ). In the second quarter of 2005, we committed to a plan to sell substantially all of the assets of Electric Services, Inc. ( ESI ). Both ULMS and ESI are part of our ICS segment. In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets , the financial position, results of operations and cash flows of OSP, ULMS and ESI are reflected as discontinued operations in our accompanying condensed consolidated financial statements. For the three and nine months ended September 30, 2004, OSP, ULMS and ESI are reflected as discontinued operations. For the three and nine months ended September 30, 2005, ULMS and ESI are reflected as discontinued operations, until the date of their dispositions.

On August 1, 2005, we sold all the common stock of ESI for aggregate cash proceeds, net of transaction costs for approximately \$6.5 million subject to a working capital adjustment.

On August 1, 2005, we sold certain assets of ULMS for aggregate cash proceeds, net of transaction costs for \$0.3 million and received a cash advance of \$0.3 million from the buyer for contingent consideration.

**Results of Operations*****Seasonality and Cyclical***

Our results of operations are subject to seasonal variations. During the winter months, demand for new projects and new maintenance service arrangements is lower in some geographic areas due to reduced construction activity, especially for services to natural gas distribution customers. During the winter months, our ICS business segment typically experiences lower gross and operating margins. However, demand for repair and maintenance services attributable to damage caused by inclement weather during the winter

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months may partially offset the loss of revenues from lower demand for new projects and new maintenance service arrangements. Our working capital needs generally follow these seasonal patterns. Additionally, our industry can be highly cyclical as evidenced by the increases in spending for electric transmission projects and declines in spending in the independent power producers generation sector. As a result, our volume of business may be adversely affected by declines in new projects in various geographic regions or industries in the United States. The financial condition of our customers and their access to capital, variations in the margins of projects performed during any particular quarter, the timing and magnitude of acquisition assimilation costs, regional economic conditions and timing of acquisitions may also materially affect quarterly results. Accordingly, our operating results in any particular quarter may not be indicative of the results that can be expected for any other quarter or for the entire year.

Our TS segment is not significantly affected by seasonality.

The following analysis includes a comparison of the results of our operations for the three months ended September 30, 2005 with the three months ended September 30, 2004 and for the nine months ended September 30, 2005 with the nine months ended September 30, 2004.

**Company Results***Three months ended September 30, 2005 compared to the three months ended September 30, 2004*

|  | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2004</b> | <b>% of<br/>Revenue</b> | <b>Three<br/>Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>% of<br/>Revenue</b> |
|--|--|-------------------------|--|-------------------------|
| <b>(Thousands of dollars)</b>                      |  |                         |  |                         |
| Contract Revenues                                  | \$ 161,876   | 100%                    | \$ 229,880   | 100%                    |
| Gross profit                                       | 25,682   | 16%                     | 32,111   | 14%                     |
| Selling, general and administrative expenses       | 16,405   | 10%                     | 20,354   | 9%                      |
| Merger related costs                               | (334)  | 0%                      | 66   | 0%                      |
| Provision for uncollectible accounts               | 104  | 0%                      | 61   | 0%                      |
| Amortization of intangible assets                  | 2,420  | 2%                      | 1,001  | 0%                      |
| Income from operations                             | 7,087  | 4%                      | 10,629   | 5%                      |
| Interest income                                    | 228  | 0%                      | 132  | 0%                      |
| Interest expense and amortization of debt discount | (1,969)  | (1)%                    | (2,170)  | (1)%                    |
| Other income, net                                  | 1,390  | 1%                      | 735  | 0%                      |
| Loss before income taxes                           | 6,736  | 4%                      | 9,326  | 4%                      |
| Income tax benefit                                 | 2,760  | 2%                      | 4,021  | 2%                      |
| Income from continuing operations                  | \$ 3,976   | 2%                      | \$ 5,305   | 2%                      |

*Revenues:* Revenues increased \$68.0 million, or 42%, to \$229.9 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004 due to increases of \$22.7 million from other electric work, which resulted from increased utility distribution and industrial electric services, \$17.2 million from underground natural gas work, which resulted from a combination of internal growth and our mid-third quarter 2004 acquisition of EnStructure, \$13.2 million from telecommunications work, which resulted from an increase in dark fiber leases and demand for underground telecommunications infrastructure scopes of work, \$6.9 million from aerial

electric transmission work, and \$6.0 million from new underground electric transmission projects.

*Gross profit:* Gross profit increased \$6.4 million, or 25%, to \$32.1 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004 due primarily to the \$68.0 million increase in revenues, a \$1.9 million credit to insurance expense as a result of actuarial estimates reflecting favorable loss development in our self insured retentions, and an increase in the volume of higher

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margin telecommunication services. These increases were offset, in part, by a proportionately smaller increase in the volume of higher margin aerial electric transmission work, proportionately higher increases in the volume of lower margin underground electric transmission and other electric work, and the overall effect of rising fuel costs.

*Selling, general and administrative expenses:* Selling, general and administrative expenses increased \$3.9 million, or 24%, to \$20.4 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004. The increase is primarily due to a \$1.7 million charge for due diligence related to an abandoned acquisition, \$0.8 million for Sarbanes-Oxley compliance, payroll and related costs to support growth in our business and incremental expenses incurred from our mid-third quarter 2004 acquisitions. Selling, general and administrative expenses decreased as a percentage of revenue from 10.1% for the three months ended September 30, 2004 to 8.9% for the three months ended September 30, 2005.

*Merger related costs:* Merger related costs increased \$0.4 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004. For the three months ended September 30, 2005, we recorded a charge to expense of \$0.1 million for retention bonuses earned by employees during the period. These retention bonuses were accrued at the closing of the September 24, 2003 merger transaction (the Merger ) in which we acquired all of the voting interests of InfraSource Incorporated and certain of its wholly owned subsidiaries, however, during 2004, we determined that a portion of these bonuses provides a benefit to periods subsequent to the Merger, and recorded a benefit of \$(0.3) million for the three months ended September 30, 2004.

*Amortization of intangible assets:* Amortization of intangible assets decreased \$1.4 million, or 59%, to \$1.0 million during the three months ended September 30, 2005 compared to \$2.4 million for three months ended September 30, 2004. The decrease was primarily due to a lesser amount of construction backlog amortization in 2005 compared to 2004, due to the completion of the Path 15 project and other acquired contracts in the previous year.

*Interest income:* Interest income decreased \$0.1 million, or 42%, to \$0.1 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004, due to a lower average cash balance in the current period.

*Interest expense and amortization of debt discount:* We incurred \$2.2 million of interest expense for the three months ended September 30, 2005, an increase of \$0.2 million as compared to the three months ended September 30, 2004, principally due to a higher average debt balance in the current year.

*Other income, net:* Other income, net decreased \$0.7 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004 due to income of \$1.0 million from a key man life insurance policy earned in the prior period which is absent in the current period, offset in part, by additional gains on equipment sales of \$0.2 million in the three months ended September 30, 2005.

*Provision for income taxes:* The provision for income taxes for the three months ended September 30, 2005 was \$4.0 million, compared to \$2.8 million for the three months ended September 30, 2004. The increase is due to an increase in our pre-tax income, as well as, an increase in our effective tax rate.

*Discontinued operations, net of tax:* For the three months ended September 30, 2005, we recorded a loss from discontinued operations of \$(0.5) million compared to income from discontinued operations of \$0.5 million for the three months ended September 30, 2004. These amounts reflect the operations of ULMS, OSP, and ESI for the three months ended September 30, 2004 and ULMS and ESI for the three months ended September 30, 2005. On August 1, 2005, we sold all of the common stock of ESI and certain assets of ULMS for a gain of \$1.8 million, net of tax.

**Table of Contents***Nine months ended September 30, 2005 compared to the nine months ended September 30, 2004*

|  | Nine Months<br>Ended<br>September 30,<br>2004 | % of<br>Revenue | Nine Months<br>Ended<br>September 30,<br>2005 | % of<br>Revenue |
|--|---|-----------------|---|-----------------|
| <b>(In thousands)</b>                              |   |                 |   |                 |
| Contract Revenues                                  | \$ 450,220                                    | 100%            | \$ 642,180                                    | 100%            |
| Gross profit                                       | 73,015  | 16%             | 71,558  | 11%             |
| Selling, general and administrative expenses       | 46,548  | 10%             | 54,854  | 8%              |
| Merger related costs                               | (334)   | 0%              | 218   | 0%              |
| Provision (recoveries) of uncollectible accounts   | (367)   | 0%              | 145   | 0%              |
| Amortization of intangible assets                  | 10,989  | 3%              | 4,311   | 1%              |
| Income from operations                             | 16,179  | 3%              | 12,030  | 2%              |
| Interest income                                    | 350   | 0%              | 354   | 0%              |
| Interest expense and amortization of debt discount | (8,161)                                       | (2)%            | (5,872)                                       | (1)%            |
| Loss on early extinguishment of debt               | (5,549)                                       | (1)%            |   | 0%              |
| Other income, net                                  | 2,253   | 1%              | 5,749   | 1%              |
| Income before income taxes                         | 5,072   | 1%              | 12,261  | 2%              |
| Income tax expense                                 | 2,029   | 0%              | 5,255   | 1%              |
| Income from continuing operations                  | \$ 3,043                                      | 1%              | \$ 7,006                                      | 1%              |

*Revenues:* Revenues increased \$192.0 million, or 43%, to \$642.2 million for the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004 due to increases of \$76.2 million from other electric work, which resulted from increased utility distribution and industrial electric services, \$63.0 million from underground natural gas work, which resulted from a combination of internal growth and our mid-third quarter 2004 acquisition of EnStructure, \$36.0 million from telecommunications work, which resulted from an increase in dark fiber leases and demand for underground telecommunications infrastructure scopes of work, and \$19.6 million from new underground electric transmission projects. These increases were partially offset by a decrease of \$8.7 million in aerial electric transmission revenues primarily due to the substantial progress recognized on the Path 15 project during the nine months ended September 30, 2004 and the absence of projects of that scale in 2005.

*Gross profit:* Gross profit decreased \$1.5 million, to \$71.6 million for the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004. Gross profit margin declined from 16.2% in the previous year to 11.1% in the current year due primarily due to a decrease in the volume of higher margin aerial electric transmission work, increases in the volume of lower margin underground electric transmission, natural gas distribution and other electric work, a \$9.0 million loss related to an underground utility construction project (see Note 5 to our condensed consolidated financial statements) and the overall effect of rising fuel costs, offset in part, by a credit to insurance expense of \$1.9 million as a result of updated actuarial estimates reflecting favorable loss development in our self insured retentions and an increase in the volume of higher margin telecommunications work.

*Selling, general and administrative expenses:* Selling, general and administrative expenses increased \$8.3 million, or 18%, to \$54.9 million for the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004. The increase is primarily due to expenses of \$1.9 million incurred for Sarbanes-Oxley

compliance, a \$1.7 million charge for due diligence related to an abandoned acquisition, incremental expenses incurred from our mid-third quarter acquisitions, and additional personnel hired to grow the business internally. The increase over the prior period was partially offset by expenses of \$2.4 million incurred in the nine months ended September 30, 2004 for accounting and other fees related to our IPO. Selling, general and administrative expenses decreased as a percentage of revenue from 10.3% for the nine months ended September 30, 2004 to 8.5% for the nine months ended September 30, 2005.



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*Merger related costs:* For the nine months ended September 30, 2005, we recorded a charge to expense of \$0.2 million for retention bonuses earned by employees during the period. These retention bonuses were accrued at the closing of the September 24, 2003 Merger in which we acquired all of the voting interests of InfraSource Incorporated and certain of its wholly owned subsidiaries, however, during 2004, we determined that a portion of these bonuses provides a benefit to periods subsequent to the Merger, and recorded a benefit of \$(0.3) for the nine months ended September 30, 2004.

*Provision (recoveries) of uncollectible accounts:* During the nine months ended September 30, 2004, we recorded net recoveries of \$0.4 million related to settlements with customers whose balances had previously been provided for with an allowance. Significant favorable settlements were absent in the current year.

*Amortization of intangible assets:* Amortization of intangible assets decreased \$6.7 million, or 61%, to \$4.3 million during the nine months ended September 30, 2005 compared to \$11.0 million for nine months ended September 30, 2004. The decrease was primarily due to a lesser amount of construction backlog amortization in 2005 compared to 2004, due to the completion of the Path 15 project and other acquired contracts in the previous year.

*Interest expense and amortization of debt discount:* We incurred \$5.9 million of interest expense for the nine months ended September 30, 2005, a decrease of \$2.3 million from the nine months ended September 30, 2004, principally due to a lower average debt balance in the current year. We reduced a portion of our debt during the second quarter of 2004 with a portion of the proceeds from our IPO. Interest expense also decreased by approximately \$0.5 million due to the reversal of accrued interest related to a litigation judgment which was reversed in the second quarter (see Note 15 to our condensed consolidated financial statements).

*Loss on early extinguishment of debt:* During the nine months ended September 30, 2004, we recorded a charge of \$5.5 million related to the early extinguishment of a note payable to Exelon.

*Other income, net:* Other income, net increased by \$3.5 million for the nine months ended September 30, 2005 compared to the nine months ended 2004. The increase was primarily due to the reversal of a \$3.8 million charge for a litigation judgment recorded in 2003 (see Note 15 to our condensed consolidated financial statements) and gains on equipment sales of \$1.8 million compared to the prior period gains of \$1.2 million, partially offset by income of \$1.0 million from a key man life insurance policy earned in the nine months ended September 30, 2004 which is absent in the nine months ended September 30, 2005.

*Provision for income taxes:* The provision for income taxes for the nine months ended September 30, 2005 was \$5.3 million, compared to \$2.0 million for the nine months ended September 30, 2004. The increase is due to an increase in our pre-tax income, as well as, an increase in our effective tax rate.

*Discontinued operations, net of tax:* Loss from discontinued operations for the nine months ended September 30, 2005 was \$(0.9) million compared to income from discontinued operations of \$0.4 million for the nine months ended September 30, 2004. These amounts reflect the operations of ULMS, OSP, and ESI for the nine months ended September 30, 2004 and ULMS and ESI for the nine months ended September 30, 2005. We sold the stock of ESI and certain assets of ULMS on August 1, 2005. We recorded a gain, net of tax, from the sale of discontinued operations of \$1.8 million for the three months ended September 30, 2005 compared to \$0.6 million, net of tax, for the three months ended September 30, 2004.

**Segment Results**

We manage our operations in two segments, ICS and TS. The primary financial measures we use to evaluate our segment operations are contract revenues and income from operations as adjusted, a non-GAAP financial measure. Income from operations as adjusted, excludes amortization expense related to intangibles as a result of our acquisitions. We exclude amortization to facilitate our evaluation of operating unit performance as we believe amortization expense does not reflect the core operations of our business segments. A reconciliation of income from operations as adjusted to the nearest GAAP equivalent, income (loss) from operations, is provided in Note 13 to our condensed consolidated financial statements, included in Item 1 of this Form 10-Q.

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Our corporate overhead expenses are not allocated to our segments because we evaluate segment performance prior to the allocation of corporate expenses.

**Three months ended September 30, 2005 compared to the three months ended September 30, 2004**

|                                      | Three Months Ended<br>September 30, |                   | Change           |            |
|--------------------------------------|-------------------------------------|-------------------|------------------|------------|
|                                      | 2004                                | 2005              | \$               | %          |
| (In thousands)                       |                                     |                   |                  |            |
| <b>Revenue:</b>                      |                                     |                   |                  |            |
| Infrastructure Construction Services | \$ 154,280                          | \$ 219,461        | \$ 65,181        | 42%        |
| Telecommunication Services           | 7,643                               | 9,884             | 2,241            | 29%        |
| Total segment revenues               | 161,923                             | 229,345           | 67,422           | 42%        |
| Corporate and eliminations           | (47)                                | 535               | 582              | 1,238%     |
| <b>Total revenue</b>                 | <b>\$ 161,876</b>                   | <b>\$ 229,880</b> | <b>\$ 68,004</b> | <b>42%</b> |

|  | Three Months Ended<br>September 30, |                  | Change          |            |
|--|-------------------------------------|------------------|-----------------|------------|
|  | 2004                                | 2005             | \$              | %          |
| (In thousands)                                   |                                     |                  |                 |            |
| <b>Income from operations as adjusted:</b>       |                                     |                  |                 |            |
| Infrastructure Construction Services             | \$ 7,610                            | \$ 10,326        | \$ 2,716        | 36%        |
| Telecommunication Services                       | 3,632                               | 4,065            | 433             | 12%        |
| Total segment income from operations as adjusted | 11,242                              | 14,391           | 3,149           | 28%        |
| Corporate and eliminations                       | (1,735)                             | (2,761)          | (1,026)         | (59)%      |
| <b>Total income from operations as adjusted</b>  | <b>\$ 9,507</b>                     | <b>\$ 11,630</b> | <b>\$ 2,123</b> | <b>22%</b> |

**ICS**

*Revenues:* ICS revenues increased \$65.2 million, or 42%, to \$219.5 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004 primarily due to increases of \$22.7 million from other electric work, which resulted from increased utility distribution and industrial electric services, \$17.2 million from underground natural gas work, which resulted from a combination of internal growth and our mid-third quarter 2004 acquisition of EnStructure, \$11.0 million from underground telecommunications infrastructure scopes of work, \$6.9 million from aerial transmission work, and \$6.0 million from new underground electric transmission projects.

*Income from operations as adjusted:* Income from operations as adjusted increased by \$2.7 million, or 36%, to \$10.3 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004. This increase was primarily due to the increase in revenues, partially offset by lower gross profit margins and

higher selling, general and administrative costs. Our lower gross profit margins resulted from a decrease in the volume of higher margin aerial electric transmission work, increases in the volume of lower margin natural gas distribution and other electric work, a \$9.0 million loss related to an underground utility construction project and the overall effect of rising fuel costs. Selling, general and administrative costs increased by \$1.3 million primarily as a result of additional personnel hired to grow the business internally.

**TS**

*Revenues:* TS revenues increased \$2.2 million, or 29%, to \$9.9 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004 due to an increase in dark fiber leases, as well as, an increase in facility construction services, which include the build-out of telecommunication infrastructure.

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*Income from operations as adjusted:* Income from operations as adjusted increased \$0.4 million, or 12%, to \$4.1 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004. This increase was primarily due to an increase in gross profit from increased revenue, partially offset by an increase of \$0.2 million in selling, general and administrative costs primarily due to additional payroll and related costs.

**Corporate**

The loss from operations as adjusted for corporate and eliminations increased by \$1.0 million for the three months ended September 30, 2005 compared to the three months ended September 30, 2004. Increased revenues from providing administrative services were offset by an increase in selling, general, and administrative expenses of \$2.5 million primarily due to a \$1.7 million charge for due diligence related to an abandoned acquisition, expenses of \$0.8 million related to Sarbanes-Oxley compliance and additional professional and legal fees.

***Nine months ended September 30, 2005 compared to the nine months ended September 30, 2004***

|                                      | Nine Months Ended<br>September 30, |                   | Change            |            |
|--------------------------------------|------------------------------------|-------------------|-------------------|------------|
|                                      | 2004                               | 2005              | \$                | %          |
| <b>(In thousands)</b>                |                                    |                   |                   |            |
| <b>Revenue:</b>                      |                                    |                   |                   |            |
| Infrastructure Construction Services | \$ 429,810                         | \$ 609,994        | \$ 180,184        | 42%        |
| Telecommunication Services           | 20,699                             | 29,968            | 9,269             | 45%        |
| Total segment revenues               | 450,509                            | 639,962           | 189,453           | 42%        |
| Corporate and eliminations           | (289)                              | 2,218             | 2,507             | 867%       |
| <b>Total revenue</b>                 | <b>\$ 450,220</b>                  | <b>\$ 642,180</b> | <b>\$ 191,960</b> | <b>43%</b> |

|  | Nine Months Ended<br>September 30, |                  | Change             |              |
|--|------------------------------------|------------------|--------------------|--------------|
|  | 2004                               | 2005             | \$                 | %            |
| <b>(In thousands)</b>                            |                                    |                  |                    |              |
| <b>Income from operations as adjusted:</b>       |                                    |                  |                    |              |
| Infrastructure Construction Services             | \$ 27,976                          | \$ 14,203        | \$ (13,773)        | (49)%        |
| Telecommunication Services                       | 9,090                              | 12,117           | 3,027              | 33%          |
| Total segment income from operations as adjusted | 37,066                             | 26,320           | (10,746)           | (29)%        |
| Corporate and eliminations                       | (9,898)                            | (9,979)          | (81)               | (1)%         |
| <b>Total income from operations as adjusted</b>  | <b>\$ 27,168</b>                   | <b>\$ 16,341</b> | <b>\$ (10,827)</b> | <b>(40)%</b> |

**ICS**

*Revenues:* ICS revenues increased \$180.2 million, or 42%, to \$610.0 million for the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004 due to increases of \$76.2 million from

other electric work, which resulted from increased utility distribution and industrial electric services, \$63.0 million from underground natural gas work, which resulted from a combination of internal growth and our mid-third quarter 2004 acquisition of EnStructure, \$26.7 million from underground telecommunications infrastructure scopes of work, and \$19.6 million from new underground electric transmission projects. These increases were partially offset by a decrease of \$8.7 million in aerial electric transmission revenues primarily due to the substantial progress recognized on the Path 15 project during the nine months ended September 30, 2004 and the absence of projects of that scale in 2005.

*Income from operations as adjusted:* Income from operations as adjusted decreased by \$13.8 million, or 49%, to \$14.2 million for the nine months ended September 30, 2005 compared to the nine months ended

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September 30, 2004. This decrease was primarily due to lower gross margins and higher selling, general and administrative costs. Our lower gross margins resulted from a decrease in the volume of higher margin aerial electric transmission work, increases in the volume of lower margin natural gas distribution and other electric work, a \$9.0 million loss related to an underground utility construction project (see Note 5 to our condensed consolidated financial statements) and the overall effect of rising fuel costs. Selling, general and administrative costs increased by \$4.8 million, primarily due to incremental expenses incurred from our third quarter 2004 acquisitions and additional personnel hired to grow the business internally.

**TS**

*Revenues:* TS revenues increased \$9.3 million, or 45%, to \$30.0 million for the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004 due to an increase in dark fiber leases, as well as, an increase in facility construction services, which include the build-out of telecommunication infrastructure.

*Income from operations as adjusted:* Income from operations as adjusted increased \$3.0 million, or 33%, to \$12.1 million for the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004. This increase was primarily due to an increase in gross margins from the increased revenue, partially offset by an increase of \$0.8 million in selling, general and administrative costs primarily related to higher payroll and related costs.

**Corporate**

The loss from operations as adjusted for corporate and eliminations increased by \$0.1 million for the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004 due to an increase of \$2.8 million for revenue related to administrative services we provide to one of our customers, offset by an increase in corporate expenses. Corporate expenses increased \$2.9 million primarily due to expenses of \$1.9 for Sarbanes-Oxley compliance, a \$1.7 million charge for due diligence related to an abandoned acquisition and additional payroll and related costs.

**Liquidity and Capital Resources*****Cash and Working Capital Requirements***

Our working capital needs are influenced by the seasonality of our business. We generally experience a need for additional working capital during the spring when we increase our level of outdoor construction in weather-affected regions of the country. Conversely, we generally convert working capital assets to cash during the winter months. We expect capital expenditures to range from \$5.0 million to \$10.0 million during the remainder of 2005, which could vary depending on the expected award and timing of the commencement of dark fiber contracts. We have reduced our capital expenditures over the past two years as a result of improved equipment utilization and an increase in the use of leasing arrangements.

We anticipate that our cash on hand of \$2.5 million as of September 30, 2005, our credit facility and our future cash flow from operations will provide sufficient cash to enable us to meet our future operating needs, debt service requirements and planned capital expenditures. However, we may find it necessary or desirable to seek additional financing to support our capital needs and provide funds for strategic initiatives, such as acquisitions. Accordingly, this may require us to increase our credit facility or complete equity-based financing, such as the issuance of common stock or preferred stock, which would be dilutive to our existing shareholders.

***Sources and Uses of Cash***

As of September 30, 2005, we had cash and cash equivalents of \$2.5 million, working capital of \$108.9 million and long-term debt of \$84.1 million principally consisting of term loans under our credit facility. As of September 30, 2005, we had \$27.0 million in borrowings under the revolving portion of our credit facility and \$29.2 million in letters of credit outstanding thereunder, leaving \$28.8 million available for

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additional borrowings. On June 10, 2005, while in the process of evaluating the extent of the loss for an underground utility construction project (see Note 5 to our condensed consolidated financial statements), we obtained a Second Amendment and Waiver to our credit facility which excluded the anticipated effect of the loss from our debt covenant calculations through July 25, 2005. Based on our further evaluation of the loss, estimated to be \$9.0 million, we are currently not required to enter into any further amendment or waiver as our credit facility allows for the exclusion of extraordinary, unusual or non-recurring expenses or losses, as defined, provided that the amounts shall not, in the aggregate exceed \$10.0 million for any fiscal year. As of October 24, 2005, borrowings under the revolving portion of our credit facility have decreased to \$18.5 million. As of December 31, 2004, we had cash and cash equivalents of \$21.2 million, restricted cash of \$5.0 million, working capital of \$99.0 million and long-term debt of \$85.8 million.

During the nine months ended September 30, 2005, our contract receivables and costs and estimated earnings in excess of billings, net of billings in excess of costs and estimated earnings increased 52%. The overall increase was due primarily to growth in our revenues and seasonality of work. A significant portion of the increase was related to one of our largest customers.

Included in costs and estimated earnings in excess of billings are costs related to claims of approximately \$4.7 million and \$11.5 million at December 31, 2004 and September 30, 2005, respectively. Claim amounts are related to a delay in the anticipated start date of one of our electric transmission projects and claims related to permit delays, changes in scope and environmental impacts on a large underground utility construction project. Estimated revenue up to but not exceeding costs incurred is recognized when realization is probable and amounts are estimable. Profit from claims is recorded in the period such amounts are agreed to with the customer.

*Cash from operating activities from continuing operations.* During the nine months ended September 30, 2005, net cash used in operating activities from continuing operations was \$37.7 million compared to \$0.4 million for the nine months ended September 30, 2004. The principal source of operating cash during the nine months ended September 30, 2005 was payments received from customers for contract services performed. The principal uses of operating cash during the nine months ended September 30, 2005 were payments for labor and materials related to performance of services and selling, general, and administrative expenses. Changes in operating assets and liabilities during the nine months ended September 30, 2005 used \$68.5 million of operating cash flow from continuing operations, while during the nine months ended September 30, 2004 changes in operating assets and liabilities used \$27.3 million in operating cash flow from continuing operations. The greater use of cash from changes in operating assets and liabilities from continuing operations for the nine months ended September 30, 2005 included a \$79.4 million increase in contracts receivable, including from related parties, and costs and estimated earnings in excess of billings, net, compared to a \$33.9 million increase during the nine months ended September 30, 2004 and a \$6.0 million increase in deferred revenue for the nine months ended September 30, 2004 versus a \$0.8 million increase for the nine months ended September 30, 2005. The increase in contracts receivable and costs and estimated earnings in excess of billings, net, is primarily due to the increase in contract revenues in the current year. Partially offsetting this use of cash is an increase in accounts payable and other current and accrued liabilities of \$7.7 million during the nine months ended September 30, 2005 as compared to a decrease of \$6.7 million during the nine months ended September 30, 2004.

*Cash from investing activities from continuing operations.* During the nine months ended September 30, 2005, net cash used by investing activities from continuing operations was \$5.5 million compared to cash used by investing activities from continuing operations of \$54.9 million for the nine months ended September 30, 2004. The primary use of cash for the nine months ended September 30, 2005 was for the purchases of equipment of \$21.7 million, offset in part, by cash proceeds from the sale of discontinued operations of \$7.1 million, proceeds from the sale of equipment of \$4.1 million, and the release of \$5.0 million from restricted cash. The principal uses of cash during the nine months ended September 30, 2004 were cash payments at closing for the acquisition of Maslonka, net of cash acquired, and purchases of equipment of \$17.3 million, offset in part by \$8.6 million in cash proceeds from the sale of discontinued operations and \$3.3 million proceeds from sales of equipment.

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*Cash from financing activities from continuing operations.* During the nine months ended September 30, 2005, net cash provided by financing activities from continuing operations was \$27.7 million compared to net cash provided by financing activities from continuing operations of \$50.6 million for the nine months ended September 30, 2004. The sources of cash from financing activities for the nine months ended September 30, 2005 were \$27.0 million of borrowings under our revolving credit facility and proceeds of \$1.4 million from the exercise of stock options and employee stock purchase plan, offset by repayments of long-term debt and capital leases of \$0.7 million. The primary source of cash from financing activities for the nine months ended September 30, 2004 were \$128.1 million of proceeds from the issuance of our common stock, \$100.8 million of which was from our IPO and the remainder was from issuances to principal shareholders and certain members of management in conjunction with the acquisition of Maslonka. A portion of the IPO proceeds were used to repay \$50.2 million of our long-term debt and the \$30.0 million principal amount of our subordinated note with Exelon.

During the nine months ended September 30, 2005, net cash transferred from discontinued operations was \$0.6 million compared to cash transferred to discontinued operations of (\$0.5) million for the nine months ended September 30, 2004. For the nine months ended September 30, 2005, cash used by operating activities from discontinued operations was \$0.4 million and cash used in investing activities from discontinued operations was \$0.2 million. The investing activities related to purchases of equipment.

**Contractual Obligations and Other Commitments**

As of September 30, 2005, our future contractual obligations, including payments under capital leases, were as follows (in thousands):

| Long-Term Debt and Interest Payments             | Payments due by Period |          |          |          |          |            | Total      |
|--|------------------------|----------|----------|----------|----------|------------|------------|
|  | 2005                   | 2006     | 2007     | 2008     | 2009     | Thereafter |            |
|  | (In thousands)         |          |          |          |          |            |            |
| Senior credit facility                           | \$ 214                 | \$ 853   | \$ 853   | \$ 853   | \$ 853   | \$ 80,405  | \$ 84,031  |
| Bank notes                                       | 28                     | 41       |          |          |          |            | 69         |
| Projected interest payments on long-term debt(1) | 1,138                  | 4,956    | 5,603    | 5,545    | 5,488    | 4,078      | 26,808     |
| Total  | \$ 1,380               | \$ 5,850 | \$ 6,456 | \$ 6,398 | \$ 6,341 | \$ 84,483  | \$ 110,908 |

| Other Contractual Obligations(2) | Payments due by Period |           |       |       |       |            | Total     |
|----------------------------------|------------------------|-----------|-------|-------|-------|------------|-----------|
|                                  | 2005                   | 2006      | 2007  | 2008  | 2009  | Thereafter |           |
| Contingent earnout(3)            | \$                     | \$ 8,493  | \$    | \$    | \$    | \$         | \$ 8,493  |
| Other long-term liabilities:     |                        |           |       |       |       |            |           |
| Non-vested options exercised     | 23                     | 355       | 21    |       |       | 549        | 948       |
| Other                            |                        | 3,051     | 54    | 54    | 54    | 143        | 3,356     |
| Total                            | \$ 23                  | \$ 11,899 | \$ 75 | \$ 54 | \$ 54 | \$ 692     | \$ 12,797 |

(1)





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We have an obligation to pay an earnout pursuant to a Stock Purchase Agreement, dated as of November 15, 2000, among InfraSource Incorporated, Blair Park Services, Inc., Sunesys, Inc. and the shareholders named therein. As of September 30, 2005, a \$5.2 million liability was included in other liabilities related parties in our condensed consolidated financial statements. This amount will increase if these businesses continue to perform successfully in 2005. The earnout is payable in the first quarter of 2006.

Pursuant to the terms of the Maslonka acquisition agreement, a portion of the consideration was subject to a holdback provision. Under the terms of the holdback, we withheld \$6.6 million in cash and 957,549 shares of the common stock we issued to the sellers. We finalized the working capital adjustment in July 2005 and released \$3.3 million in cash and 478,775 shares of common stock to the sellers in accordance with the agreement. The balance of the holdback is expected to be released in January 2006. We paid accrued interest on the cash portion of the holdback amount released to the sellers. The sellers are entitled to exercise voting rights with respect to the shares of common stock subject to the holdback provision. As of September 30, 2005, based upon our current assessment of the achievement of specified targets, we have accrued \$3.3 million in other liabilities related parties in our condensed consolidated financial statements.

***Related Party Transactions***

As of September 30, 2005, we had \$5.2 million due to the former owners of Blair Park Services, Inc. and Sunesys, Inc. (collectively Blair Park ) accrued in other liabilities related parties on our condensed consolidated balance sheet for additional contingent purchase price consideration. Blair Park was acquired by InfraSource Incorporated in 2001.

As of September 30, 2005, we have \$4.2 million due to the Maslonka shareholders, including Martin Maslonka, an employee and holder of more than 5% of our common stock, accrued in other liabilities related parties on our condensed consolidated balance sheet. Of this amount, \$3.3 million is holdback consideration from our acquisition of Maslonka (see Note 3 to our condensed consolidated financial statements). The remaining net balance relates to payments and collections we made on the shareholders behalf which require cash settlement. On August 11, 2005 we also granted the Maslonka shareholders, who are also our employees, 167,556 shares of restricted stock (41,889 of which were granted to Martin Maslonka) valued at \$2.2 million, of which 25% vest in January of 2006 and the remainder vest four years from the date of grant. For the three and nine months ended September 30, 2005, the Company recorded a charge of \$0.3 million to selling, general and administrative expenses in the condensed consolidated statement of operations.

Maslonka is the issuer of a \$1.0 million installment promissory note in favor of Martin Maslonka. The promissory note bears interest at an annual rate of 8.5%, and interest is payable in equal monthly payments. The promissory note matures on June 30, 2006.

We lease our Maslonka headquarters in Mesa, Arizona and our Maslonka Texas field office in San Angelo, Texas from EC Source, LLC, which is wholly owned by Martin Maslonka. Our leases for these two properties will run through February 2009, subject to a five-year renewal option. Pursuant to these leases, we expect to incur total annual lease payments of \$0.2 million.

We lease office and warehouse space from Coleman Properties of which three officers of Blair Park are general partners. The lease for this space was to run through October 2005, subject to a 6 year renewal option. The terms of the lease provided for an increase in rental payments equal to the increase in the Consumer Price Index. In October, 2005 we renewed the lease for three years and our annual payments under this agreement are approximately \$0.1 million.

We also lease ducts in two river bores under the Delaware River from Coleman Properties. Our lease commenced on May 1, 2005 and has a term of five years, with an option to extend. Our annual lease payment

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is \$0.02 million for each pair of fiber installed in the conduit up to a maximum of \$0.2 million per year if additional ducts are leased.

We lease office and warehouse facilities in Michigan which are owned by an employee and his family members. Our leases for these properties will run through September 2006 and May 2007. Pursuant to these leases, we expect to incur total annual lease payments of \$0.3 million.

***New Accounting Pronouncements***

In December 2004, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 123R Share Based Payment. SFAS No. 123R is a revision to SFAS No. 123 Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board ( APB ) Opinion No. 25 Accounting for Stock Issued to Employees, and Related Interpretations and amends FASB Statement No. 95, Statement of Cash Flows. SFAS No. 123R requires a public entity to expense the cost of employee services received in exchange for an award of equity instruments. SFAS No. 123R provides guidance on valuing and expensing these awards, as well as disclosure requirements of these equity arrangements. As modified by the SEC on April 15, 2005, SFAS No. 123R is effective for the first annual or interim reporting period of the registrant's first fiscal year that begins after June 15, 2005. We are required to adopt the provisions of SFAS No. 123R effective January 1, 2006, at which time we will begin recognizing an expense for unvested share-based compensation that has been issued or will be issued after that date. SFAS No. 123R permits an issuer to use either a prospective or one of two modified versions of retrospective application under which financial statements for prior periods are adjusted on a basis consistent with the pro forma disclosures required for those periods by the original SFAS No. 123. Under the retroactive options, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented.

As permitted by SFAS No. 123, we currently account for share-based compensation to employees using the intrinsic value method of APB Opinion No. 25 and, as such, we generally recognize no compensation cost for employee stock options. The impact of the adoption of SFAS No. 123R cannot be predicted at this time because it will depend on levels of share-based compensation granted in the future. However, valuation of employee stock options under SFAS No. 123R is similar to SFAS No. 123, with minor exceptions. For information about what our reported results of operations and earnings per share would have been had we adopted SFAS No. 123, see the pro forma disclosure in Note 9 to our condensed consolidated financial statements. Accordingly, the adoption of the fair value method of SFAS No. 123R will likely have a significant impact on our results of operations, although it will have no impact on our overall financial position. We have not yet completed the analysis of the ultimate impact that SFAS No. 123R will have on our results of operations. We plan to adopt SFAS No. 123R using the prospective method.

In December 2004, the FASB issued Staff Position ( FSP ) No. 109-1, Application of FASB No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004. The American Jobs Creation Act of 2004 ( AJCA ) introduces a special 3% tax deduction, which is phased up to 9%, on qualified production activities. FSP No. 109-1 clarifies that this tax deduction should be accounted for as a special tax deduction in accordance with SFAS No. 109. Pursuant to the AJCA and the guidance provided to date, we will likely be viewed as engaging in qualified production activities and, thus, be able to claim this tax deduction in 2005. We do not expect these new tax provisions to have a significant impact on our consolidated financial position, results of operations or cash flows.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3. This Statement replaces APB Opinion No. 20, Accounting Changes, and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements, and changes the requirements for the accounting for and reporting of a change in accounting principle. SFAS No. 154 applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. When a pronouncement includes specific transition provisions, those provisions should be followed. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal



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years beginning after December 15, 2005. We will adopt the provisions of SFAS No. 154 beginning January 1, 2006. We do not believe that adoption of the provisions of SFAS No. 154 will have a material impact on our consolidated financial statements.

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risks including those related to potential adverse changes in interest rates and fuel prices as discussed below. We have not historically used derivative financial instruments for trading or to speculate on changes in interest rates or commodity prices.

*Interest Rates.* On October 10, 2003, we entered into an interest rate swap agreement and an interest rate cap agreement with a term of three years, both of which qualify as cash flow hedges, to hedge the variability of cash flows related to our variable rate term loan. We are not exposed to any significant market risks, foreign currency exchange risk or interest rate risk from the use of derivative financial instruments.

The sensitivity analysis below, which illustrates our hypothetical potential market risk exposure, estimates the effects of hypothetical sudden and sustained changes in the applicable market conditions on 2005 earnings. The sensitivity analysis presented does not consider any additional actions we may take to mitigate our exposure to such changes. The hypothetical changes and assumptions may be different from what actually occurs in the future.

As of September 30, 2005, our \$84.0 million term loan facility was subject to floating interest rates. On October 10, 2003, we entered into an interest rate swap on a \$70.0 million notional amount where we pay a fixed rate of 2.395% in exchange for three month LIBOR until October 10, 2006. Effective October 11, 2005, the notional amount of the interest rate swap decreased to \$30.0 million. We also purchased a 4.00% interest rate cap that matures October 10, 2006 on \$20.0 million of notional amount. Effective October 11, 2005, the notional amount of the interest rate cap increased to \$40.0 million. As of September 30, 2005, we had \$14.0 million of our term loans subject to some floating rate risk. As such, we are exposed to earnings and fair value risk due to changes in interest rates with respect to our long-term obligations. The detrimental effect on our pre-tax earnings of a hypothetical 50 basis point increase in interest rates would be approximately \$0.1 million. As of September 30, 2005, we had \$27.0 million in borrowings under the revolving portion of our credit facility.

*Gasoline and Diesel Fuel.* We have market risk for changes in the price of gasoline and diesel fuel. To the extent we cannot mitigate increases in fuel prices through surcharges and other contract provisions with our customers, our operating income will be affected. As of September 30, 2005 we did not have any fuel hedges in place.

**Item 4. CONTROLS AND PROCEDURES*****Disclosure Controls and Procedures***

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures as of the end of the period covered by this report were effective, in all material respects, to provide reasonable assurance that the information required to be disclosed by the Company in reports filed under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

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***Internal Control Over Financial Reporting***

No change in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II OTHER INFORMATION**

**Item 1. LEGAL PROCEEDINGS.**

In January 2004, a judgment was entered against us in Superior Court of Fulton County, Georgia in the amount of \$3.8 million, including \$3.2 million in punitive damages. We had \$3.8 million accrued on our condensed consolidated balance sheet as of December 31, 2004 for this judgment. The judgment upheld allegations by the plaintiff that in 1999 InfraSource Incorporated (formerly known as Exelon Infrastructure Services, Inc.) had fraudulently induced the plaintiff to incur expenses in connection with a proposed business acquisition that was never consummated.

On March 22, 2005, the Court of Appeals of Georgia issued an opinion reversing the \$3.8 million judgment against us. On April 25, 2005, the plaintiff filed a petition requesting the Supreme Court of Georgia to review and reverse the opinion of the Court of Appeals.

Based on the Court of Appeals decision, we reversed the \$3.8 million litigation accrual for the original judgment against us which had been recorded in 2003. Additionally, we reversed \$0.5 million in interest expense which we had been accruing since the judgment date as stipulated by the original judgment. For the nine months ended September 30, 2005, \$3.8 million of income is included in other income (expense), net and \$0.5 million is included as a reduction in interest expense.

On September 19, 2005, the Supreme Court of Georgia denied the petition for certiorari filed by the plaintiff.

**Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.**

None.

**Item 3. DEFAULTS UPON SENIOR SECURITIES.**

None.

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

None.

**Item 5. OTHER INFORMATION.**

None.

**Item 6. EXHIBITS**

- 3.1 Form of Restated Certificate of Incorporation of InfraSource Services, Inc.(1)
- 3.1.1 Form of Certificate of Amendment to the Restated Certificate of Incorporation of InfraSource Services, Inc.(1)
- 3.2 Form of Amended and Restated Bylaws of InfraSource Services, Inc.(1)
- 3.3 Specimen of stock certificate.(1)
- 4.1 Stockholders Agreement, dated as of September 24, 2003, by and among InfraSource Services, Inc. (f/k/a the Dearborn Holdings Corporation) and its Security Holders party thereto.(2)

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|      |   |
|------|---|
| 4.2  | Registration Rights Agreement, dated as of April 20, 2004, by and among InfraSource Services, Inc. OCM Principal Opportunities Fund II, L.P., OCM/ GFI Power Opportunities Funds, L.P., Martin Maslonka, Thomas B. Tilford, Mark C. Maslonka, Justin Campbell, Joseph Gabbard, Sidney Strauss, Jon Maslonka, David R. Helwig, Terence R. Montgomery and Paul M. Daily.(1) |
| 31.1 | Rule 13a-14(a)/ Rule 15d-14(a) Certification of Chief Executive Officer.*   |
| 31.2 | Rule 13a-14(a)/ Rule 15d-14(a) Certification of Chief Financial Officer.*   |
| 32.1 | Certification pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code.*  |

\* Filed herewith

- (1) Filed as an exhibit to the Registrant's Registration Statement on Form S-1, Amendment No. 3 (Registration No. 333-112375) filed with the Commission on April 29, 2004.
- (2) Filed as an exhibit to the Registrant's Registration Statement on Form S-1 (Registration No. 333-112375) filed with the Commission on January 30, 2004.

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**SIGNATURES**

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

INFRASOURCE SERVICES, INC.  
(Registrant)  
By: /s/ TERENCE R. MONTGOMERY

Terence R. Montgomery  
*Chief Financial Officer and Senior Vice President*

Date: November 4, 2005



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**EXHIBIT INDEX**

|      |   |
|------|---|
| 31.1 | Rule 13a-14(a)/ Rule 15d-14(a) Certification of Chief Executive Officer.                    |
| 31.2 | Rule 13a-14(a)/ Rule 15d-14(a) Certification of Chief Financial Officer.                    |
| 32.1 | Certification pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code. |