

H&E Equipment Services, Inc.

Form 10-Q

November 14, 2006

Table of Contents

**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, 2006

**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: 000-51759

H&E Equipment Services, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State of Incorporation)

81-0553291

(I.R.S. Employer Identification No.)

**11100 Mead Road, Suite 200, Baton Rouge,
Louisiana**

(Address of principal executive offices)

70816

(Zip code)

(225) 298-5200

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 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 a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-Accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Number of shares of common stock, par value \$0.01 per share, of the registrant outstanding as of November 8, 2006 was 38,192,094 shares.

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES
TABLE OF CONTENTS
SEPTEMBER 30, 2006

	Page
<u>PART I. FINANCIAL INFORMATION</u>	4
<u>Item 1. Financial Statements:</u>	4
<u>Condensed Consolidated Balance Sheets as of September 30, 2006 (Unaudited) and December 31, 2005</u>	4
<u>Condensed Consolidated Statements of Operations (Unaudited) for the Three and Nine Months Ended September 30, 2006 and 2005</u>	5
<u>Condensed Consolidated Statement of Members' Deficit and Stockholders' Equity (Unaudited) for the Nine Months Ended September 30, 2006</u>	6
<u>Condensed Consolidated Statements of Cash Flows (Unaudited) for the Nine Months Ended September 30, 2006 and 2005</u>	7
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	9
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	39
<u>Item 4. Controls and Procedures</u>	39
<u>PART II. OTHER INFORMATION</u>	40
<u>Item 1. Legal Proceedings</u>	40
<u>Item 1A. Risk Factors</u>	40
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	40
<u>Item 3. Defaults upon Senior Securities</u>	41
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	41
<u>Item 5. Other Information</u>	41
<u>Item 6. Exhibits</u>	42
<u>Signatures</u>	42
<u>Certification Pursuant to Section 302</u>	
<u>Certification Pursuant to Section 302</u>	
<u>Certification Pursuant to Section 1350</u>	

Table of Contents

Special Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the federal securities laws. Statements that are not historical facts, including statements about our beliefs and expectations, are forward-looking statements. Forward-looking statements include statements preceded by, followed by or that include the words may, could, would, should, believe, expect, anticipate, plan, estimate, target, project, expressions. These statements include, among others, statements regarding our expected business outlook, anticipated financial and operating results, our business strategy and means to implement the strategy, our objectives, the amount of capital expenditures, the likelihood of our success in expanding our business, financing plans, budgets, working capital needs and sources of liquidity.

Forward-looking statements are only predictions and are not guarantees of performance. These statements are based on our management's beliefs and assumptions, which in turn are based on currently available information. Important assumptions relating to the forward-looking statements include, among others, assumptions regarding demand for our products, the expansion of product offerings geographically or through new applications, the timing and cost of planned capital expenditures, competitive conditions and general economic conditions. These assumptions could prove inaccurate. Forward-looking statements also involve known and unknown risks and uncertainties, which could cause actual results that differ materially from those contained in any forward-looking statement. Many of these factors are beyond our ability to control or predict. Such factors include, but are not limited to, the following:

general economic conditions and construction activity in the markets where we operate in North America;

relationships with new equipment suppliers;

increased maintenance and repair costs;

our substantial leverage;

the risks associated with the expansion of our business;

our possible inability to integrate any businesses we acquire;

competitive pressures;

compliance with laws and regulations, including those relating to environmental matters and corporate governance matters; and

other factors discussed under "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2005 and under Item 1A "Risk Factors" in our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006.

Except as required by applicable law, including the securities laws of the United States and the rules and regulations of the Securities and Exchange Commission ("SEC"), we are under no obligation to publicly update or revise any forward-looking statements after we file this Quarterly Report, whether as a result of any new information, future events or otherwise. Investors, potential investors and other readers are urged to consider the above mentioned factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on such forward-looking statements. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results or performance. For a more detailed discussion of some of the foregoing risk and uncertainties, see Item 1A "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2005, and Item 1A "Risk Factors" in our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006, as well as other reports and registration statements filed by us with the SEC. All of our annual, quarterly and current reports and amendments thereto, filed with the SEC are available on our website under the Investor Relations link. For more information about us and the announcements we make from time to time, visit our

website at www.he-equipment.com.

Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements.**

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Amounts in thousands, except share amounts)

	Balances at	
	September	December
	30,	31,
	2006	2005
	(Unaudited)	
ASSETS		
Cash	\$ 5,053	\$ 5,627
Receivables, net of allowance for doubtful accounts of \$2,714 and \$2,364, respectively	109,730	99,523
Inventories, net of reserve for obsolescence of \$807 and \$975, respectively	116,325	81,093
Prepaid expenses and other assets	4,474	1,378
Rental equipment, net of accumulated depreciation of \$150,902 and \$133,943, respectively	429,219	308,036
Property and equipment, net of accumulated depreciation of \$25,377 and \$21,142, respectively	28,339	18,284
Deferred financing costs and other intangible assets, net of accumulated amortization of \$4,896 and \$7,250, respectively	9,449	8,184
Goodwill	30,455	8,572
Total assets	\$ 733,044	\$ 530,697
LIABILITIES, MEMBERS DEFICIT AND STOCKHOLDERS EQUITY		
Liabilities:		
Amounts due on senior secured credit facility	\$ 26,265	\$ 106,451
Accounts payable	62,174	56,173
Manufacturer flooring plans payable	130,020	93,728
Accrued expenses payable and other liabilities	33,621	22,798
Related party obligation	709	869
Notes payable	2,400	521
Senior secured notes, net of original issue discount of \$23 and \$1,127, respectively	4,477	198,873
Senior subordinated notes, net of original issue discount of \$8,943 at December 31, 2005		44,057
Senior unsecured notes	250,000	
Deferred income taxes	5,411	645
Deferred compensation payable	3,215	11,722
Total liabilities	518,292	535,837
Commitments and contingencies		
Members deficit		(5,140)

Stockholders equity:

Preferred stock, \$0.01 par value, 25,000,000 shares authorized; no shares issued at September 30, 2006 and December 31, 2005, respectively

Common stock, \$0.01 par value, 175,000,000 shares authorized; 38,192,094 and no shares issued and outstanding at September 30, 2006 and December 31, 2005, respectively

	382		
Additional paid-in capital	204,328		
Retained earnings	10,042		
Total stockholders equity	214,752		
Total liabilities, members deficit and stockholders equity	\$ 733,044	\$	530,697

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

Table of Contents

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For the three and nine months ended September 30, 2006 and 2005
(Unaudited)
(Amounts in thousands, except per share amounts)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2006	2005	2006	2005
Revenues:				
Equipment rentals	\$ 67,327	\$ 50,409	\$ 185,333	\$ 136,576
New equipment sales	60,673	36,152	173,333	99,867
Used equipment sales	29,668	26,751	97,387	76,332
Parts sales	21,024	16,986	61,574	51,202
Service revenues	14,074	10,409	39,782	29,459
Other	11,369	7,749	31,472	21,300
Total revenues	204,135	148,456	588,881	414,736
Cost of revenues:				
Rental depreciation	20,644	14,354	56,674	39,394
Rental expense	10,339	12,015	31,427	35,024
New equipment sales	53,321	31,783	151,615	87,803
Used equipment sales	21,708	20,325	71,253	58,043
Parts sales	14,895	11,972	43,499	36,105
Service revenues	5,045	3,980	14,343	10,973
Other	9,436	7,229	27,005	21,700
Total cost of revenues	135,388	101,658	395,816	289,042
Gross profit	68,747	46,798	193,065	125,694
Selling, general and administrative expenses	34,118	28,219	108,545	81,342
Gain on sales of property and equipment, net	241	118	400	15
Income from operations	34,870	18,697	84,920	44,367
Other income (expense):				
Interest expense	(9,060)	(10,557)	(29,342)	(30,982)
Loss on early extinguishment of debt	(40,771)		(40,771)	
Other, net	245	85	675	255
Total other expense, net	(49,586)	(10,472)	(69,438)	(30,727)
Income (loss) before provision (benefit) for income taxes	(14,716)	8,225	15,482	13,640
Provision (benefit) for income taxes	(3,185)		3,290	171

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Net income (loss)	\$ (11,531)	\$ 8,225	\$ 12,192	\$ 13,469
Net income (loss) per common share:				
Basic	\$ (0.30)	\$ 0.32	\$ 0.33	\$ 0.53
Diluted	\$ (0.30)	\$ 0.32	\$ 0.33	\$ 0.53
Weighted average common shares outstanding:				
Basic	38,070	25,492	36,550	25,492
Diluted	38,070	25,492	36,587	25,492

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

Table of Contents

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF MEMBERS' DEFICIT AND STOCKHOLDERS
EQUITY

For the nine months ended September 30, 2006
(Unaudited)

(Amounts in thousands, except share amounts)

	Common Stock		Additional		Total	
	Shares	Amount	Paid-in	Retained	Stockholders	Members
			Capital	Earnings	Equity	Deficit
Balances at						
January 1, 2006		\$	\$	\$	\$	\$ (5,140)
Net income for the period						
January 1, 2006 through						
February 2, 2006						2,150
Effect of the						
Reorganization						
Transactions	25,492,019	255	(3,245)		(2,990)	2,990
Common stock issued on						
February 3, 2006 pursuant						
to initial public offering,						
net of \$15,915 issue costs	12,578,125	126	206,892		207,018	
Issuance of common stock	121,950	1			1	
Stock-based compensation			681		681	
Net income for the period						
February 3, 2006 through						
September 30, 2006				10,042	10,042	
Balances at September 30,						
2006	38,192,094	\$ 382	\$ 204,328	\$ 10,042	\$ 214,752	\$

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

Table of Contents

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the nine months ended September 30, 2006 and 2005
(Unaudited)
(Amounts in thousands)

	Nine Months Ended	
	September 30,	
	2006	2005
Cash flows from operating activities:		
Net income	\$ 12,192	\$ 13,469
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation on property and equipment	5,010	3,752
Depreciation on rental equipment	56,674	39,394
Amortization of loan discounts and deferred financing costs	2,056	2,044
Amortization of other intangible assets	34	82
Provision for losses on accounts receivable	1,457	1,096
Provision for inventory obsolescence	18	30
Provision for deferred income taxes	2,692	
Non-cash compensation expense	681	
Loss on early extinguishment of debt	40,771	
Gain on sales of property and equipment, net	(400)	(15)
Gain on sales of rental equipment, net	(23,339)	(16,199)
Changes in operating assets and liabilities, net of impact of acquisition:		
Receivables, net	(4,363)	(15,269)
Inventories	(58,315)	(36,378)
Prepaid expenses and other assets	(4,437)	(2,058)
Accounts payable	5,513	19,188
Manufacturer flooring plans payable	36,292	11,456
Accrued expenses payable and other liabilities	7,021	16,426
Deferred compensation payable	(8,507)	864
Net cash provided by operating activities	71,050	37,882
Cash flows from investing activities:		
Acquisition of businesses, net of cash acquired	(56,961)	
Purchases of property and equipment	(13,353)	(5,672)
Purchases of rental equipment	(174,372)	(117,723)
Proceeds from sales of property and equipment	1,841	725
Proceeds from sales of rental equipment	76,068	61,494
Net cash used in investing activities	(166,777)	(61,176)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net of issue costs	207,018	
Borrowings on senior secured credit facility	718,819	424,867
Payments on senior secured credit facility	(799,005)	(398,955)
Proceeds from issuance of senior unsecured notes	250,000	
Principal payment of senior secured notes	(214,608)	

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Principal payment of senior subordinated notes	(59,155)	
Payments of deferred financing costs	(8,816)	(10)
Payments of related party obligation	(225)	(225)
Proceeds from issuance of notes payable	1,271	
Principal payments of notes payable	(146)	(181)
Payments on capital lease obligations		(1,120)
Net cash provided by financing activities	95,153	24,376
Net increase (decrease) in cash	(574)	1,082
Cash, beginning of period	5,627	3,358
Cash, end of period	\$ 5,053	\$ 4,440

Table of Contents

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
For the nine months ended September 30, 2006 and 2005
(Unaudited)
(Amounts in thousands)

	Nine Months Ended	
	September 30,	
	2006	2005
Supplemental schedule of noncash investing activities:		
Assets transferred from new and used inventory to rental fleet	\$ 23,980	\$ 19,573
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	\$ 24,880	\$ 22,084
Income taxes	\$ 576	\$ 171

As of September 30, 2006 and 2005, we had \$130.0 million and \$62.7 million, respectively, in manufacturer flooring plans payable outstanding, which are used to finance purchases of inventory and rental equipment.

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

Table of Contents

H&E EQUIPMENT SERVICES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
September 30, 2006

(1) Organization and Nature of Operations

Basis of Presentation

In connection with our initial public offering of common stock in February 2006 (see note 3 to the condensed consolidated financial statements for further information regarding our initial public offering), we converted H&E Equipment Services L.L.C. (H&E LLC), a Louisiana limited liability company and the wholly-owned operating subsidiary of H&E Holding L.L.C. (Holdings), into H&E Equipment Services, Inc., a Delaware corporation. Prior to our initial public offering, our business was conducted through H&E LLC. In order to have an operating Delaware corporation as the issuer of our initial public offering, immediately prior to the closing of the initial public offering, on February 3, 2006, H&E LLC and Holdings merged with and into us (H&E Equipment Services, Inc.), with us surviving the reincorporation merger as the operating company. Effective February 3, 2006, H&E LLC and Holdings no longer existed. In these transactions (collectively, the Reorganization Transactions), holders of preferred limited liability company interests and holders of common limited liability company interests in H&E Holdings received shares of our common stock. All references to common stock share and per share amounts included in our condensed consolidated statements of operations for the three and nine months ended September 30, 2006 and 2005 have been retroactively adjusted to reflect the Reorganization Transactions as if the Reorganization Transactions had taken place as of the beginning of the earliest period presented.

Our condensed consolidated financial statements include the financial position and results of operations of H&E Equipment Services, Inc. and its wholly-owned subsidiaries H&E Finance Corp., GNE Investments, Inc., Great Northern Equipment, Inc., and our recent acquisition, as described in note 4 to the condensed consolidated financial statements, of Eagle High Reach Equipment, Inc. (H&E California Holdings, Inc.) and Eagle High Reach Equipment, LLC (H&E Equipment Services (California LLC)), consummated on February 28, 2006, collectively referred to herein as we or us or our or the Company.

The accompanying unaudited interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted pursuant to such regulations. In the opinion of management, all adjustments (consisting of all normal and recurring adjustments) considered necessary for a fair presentation have been included. Certain items in the prior periods have been reclassified to make the presentation consistent with the current reporting periods. Operating results for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006, and therefore, the results and trends in these interim condensed consolidated financial statements may not be the same for the entire year. These interim condensed consolidated financial statements should be read in conjunction with the annual consolidated financial statements and related notes in our Annual Report on Form 10-K for the year ended December 31, 2005.

The nature of our business is such that short-term obligations are typically met by cash flows generated from long-term assets. Consequently, consistent with industry practice, the accompanying condensed consolidated balance sheets are presented on an unclassified basis.

Nature of Operations

As one of the largest integrated equipment services companies in the United States focused on heavy construction and industrial equipment, we rent, sell and provide parts and service support for four core categories of specialized equipment: (1) hi-lift or aerial platform equipment, (2) cranes, (3) earthmoving equipment and (4) industrial lift trucks. By providing equipment sales, rental, on-site parts and repair and maintenance functions under one roof, we are a one-stop provider for our customers varied equipment needs. This full-service approach provides us with multiple points of customer contact, enables us to maintain an extremely high quality rental fleet, as well as an effective distribution channel for fleet disposal and provides cross-selling opportunities among our new and used

equipment sales, rental, parts sales and service operations.

Table of Contents**(2) Significant Accounting Policies**

We describe our significant accounting policies in note 1 of the notes to consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2005.

Use of Estimates

We prepare our condensed consolidated financial statements in accordance with U.S. generally accepted accounting principles, which requires management to use its judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. These assumptions and estimates could have a material effect on our financial statements. Actual results may differ materially from those estimates. We review our estimates on an ongoing basis based on information currently available, and changes in facts and circumstances may cause us to revise these estimates.

Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 123(R), Share-Based Payment, (SFAS 123(R)), which revises SFAS No. 123 and supersedes APB Opinion No. 25 and related interpretations. SFAS 123(R) requires all share-based payment transactions, including grants of stock options, restricted stock awards, performance-based awards, shares appreciation rights and employee stock purchase plans to be valued at fair value on the date of grant, and to be expensed over the requisite service period. SFAS 123(R) is effective for the annual reporting period beginning after June 15, 2005. SFAS 123(R) became effective for us on January 1, 2006. For the nine months ended September 30, 2006, we incurred approximately \$0.7 million of non-cash compensation expense related to stock grants and stock options.

In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections (SFAS 154). SFAS 154 replaces APB Opinion No. 20 (APB 20), Accounting Changes and FASB Statement No. 3, Reporting Accounting Charges in Interim Financial Statements. SFAS 154 requires that a voluntary change in accounting principle be applied retrospectively with all prior period financial statements presented on the new accounting principle, unless it is impracticable to do so. SFAS 154 also provides that a correction of errors in previously issued financial statements should be termed a restatement. APB 20 previously required most voluntary changes in accounting principle to be recognized by including in net income at the period of change the cumulative effect of changing to the new accounting principle. In addition, SFAS 154 carries forward without change the guidance contained in APB 20 for reporting a correction of an error in previously issued financial statements and a change in accounting estimate. SFAS 154 became effective for accounting principle changes and corrections of errors in previously issued financial statements made after January 1, 2006. We applied SFAS 154 in connection with the restatement of our consolidated financial statements included in our Form 10-Q/A for the three-month period ended March 31, 2006.

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 (FIN 48), which clarifies the accounting for uncertainty in income taxes recognized in accordance with FASB Statement No. 109 (SFAS 109). FIN 48 clarifies the application of SFAS 109 by defining criteria that an individual tax position must meet for any part of the benefit of that position to be recognized in the financial statements. Additionally, FIN 48 provides guidance on the measurement, derecognition, classification and disclosure of tax positions, along with accounting for the related interest and penalties. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. Management is currently assessing the impact of adopting FIN 48 but does not expect that it will have a material impact on our financial position, results of operations and cash flows.

In June 2006, EITF Issue No. 06-3 (EITF 06-3) became authoritative GAAP. EITF 06-3 addresses how taxes collected from customers and remitted to governmental authorities should be presented in the statement of operations. EITF 06-3 permits companies to present either on a gross or net basis sales and other taxes that are imposed on and concurrent with revenue-producing transactions between a seller and a customer. The gross method includes the taxes in revenues and costs; the net basis excludes the taxes from revenues. We currently collect significant amounts of sales taxes from customers and remit those taxes to various governmental agencies as prescribed by the taxing jurisdictions in which we operate. In accordance with EITF 06-03, we present such taxes on a net basis.

Table of Contents

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 108 (SAB 108), Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements, which provides interpretive guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. Specifically, SAB 108 requires that public companies utilize a dual-approach to assessing quantitative effects of financial misstatements. This dual approach includes both an income statement focused assessment and a balance sheet focused assessment. The guidance in SAB 108 must be applied to annual financial statements for fiscal years ending after November 15, 2006. The Company is currently assessing the impact of adopting SAB 108 but does not expect that it will have a material effect on our consolidated financial position or results of operations.

In September 2006, the FASB issued Statement No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. SFAS 157 is effective for fiscal years beginning after December 15, 2007. Management is currently assessing the impact of adopting SFAS 157 but does not expect that it will have a material effect on our consolidated financial position or results of operations.

(3) Initial Public Offering and Use of Proceeds

We completed an initial public offering of our common stock, par value \$.01 per share, on February 3, 2006. In the offering, we sold 12,578,125 shares for an aggregate offering price of \$226.4 million. Net proceeds to us, after deducting underwriting discounts and commissions and offering expenses, totaled approximately \$207.0 million. Aggregate underwriting discounts and commissions totaled approximately \$15.9 million and aggregate offering expenses totaled approximately \$3.6 million.

We used the net offering proceeds to us of \$207.0 million as follows:

\$56.9 million to complete our acquisition of Eagle High Reach Equipment, Inc. and all of the equity interests of its subsidiary, Eagle High Reach Equipment, LLC (together, Eagle), on February 28, 2006. For information on the Eagle acquisition, see note 4 to the condensed consolidated financial statements.

\$30.3 million to purchase rental equipment under operating leases;

\$8.6 million to pay deferred compensation owed to one of our current executives and a former executive; and

\$96.6 million to repay outstanding principal indebtedness under our senior secured credit facility.

Additionally, we paid \$8.0 million to Bruckmann, Rosser, Sherill & Co., L.L.C. (an affiliate of Bruckmann, Rosser, Sherill & Co., L.P. and Bruckmann, Rosser, Sherill & Co. II, L.P., two of our principal stockholders) in connection with the termination of a management services agreement. The remaining net proceeds of approximately \$6.6 million were used for general corporate purposes.

(4) Acquisition

We completed, effective as of February 28, 2006, the previously announced acquisition of all of the capital stock of Eagle High Reach Equipment, Inc. and all of the equity interests of its subsidiary, Eagle High Reach Equipment, LLC for an estimated consideration of approximately \$66.2 million, consisting of cash paid of \$59.9 million, liabilities assumed of \$3.6 million, liabilities incurred of \$2.1 million, and transaction costs of \$0.6 million. The Eagle purchase price was determined based on the expected cash flows from the Eagle business and negotiation with the sellers. The purchase price was funded out of the proceeds from our recently completed initial public offering (see note 3 to the condensed consolidated financial statements for further information on our initial public offering). Prior to the acquisition Eagle was a privately-held construction and industrial equipment rental company. Eagle serves the southern California construction and industrial markets out of four locations. This acquisition marks our initial entry into the southern California market and is consistent with our business strategy. For further information on our business strategy, see Item 1 of Part I of our Annual Report on Form 10-K for the year ended December 31, 2005.

The Eagle acquisition has been accounted for using the purchase method of accounting. The aggregate purchase price has been

Table of Contents

allocated to the assets acquired and liabilities assumed based on an estimate of their fair values as determined by a valuation performed by an independent national firm. The excess of the purchase price over the fair value of the net identifiable tangible and intangible assets acquired has been allocated to goodwill. Goodwill generated from the acquisition was recognized given the expected contribution of Eagle to the overall corporate strategy. We estimate that approximately \$9.9 million of the goodwill acquired will be tax deductible. Additionally, we are in the process of evaluating the allocation of Eagle goodwill to our reporting units. Our operating results for the nine month period ended September 30, 2006 include the operating results of Eagle since the date of acquisition, February 28, 2006.

The following table summarizes our purchase price allocation based on fair values of the Eagle assets acquired and liabilities assumed in February 2006 (amounts in thousands).

Cash	\$ 32
Receivables	7,300
Inventories	915
Rental equipment	32,235
Property and equipment	3,153
Prepaid expenses and other assets	654
Goodwill	21,883
Accounts payable	(483)
Accrued expenses payable and other liabilities	(2,349)
Deferred income taxes	(2,073)
Notes payable	(755)
Net assets acquired	\$ 60,512

The following table contains pro forma condensed consolidated statements of operations information for the three and nine month periods ended September 30, 2006 and 2005, as if the Eagle transaction had occurred at the beginning of each respective period presented (amounts in thousands except per share data).

	Three Month Period Ended		Nine Month Period Ended	
	September 30,		September 30,	
	2006	2005	2006	2005
Total revenues	\$ 204,135	\$ 157,208	\$ 594,209	\$ 438,969
Gross profit	68,747	51,039	194,839	137,647
Operating income	34,870	20,058	84,212	46,922
Net income (loss)	\$ (11,531)	\$ 8,928	\$ 11,842	\$ 15,133
Basic net income (loss) per common share	\$ (0.30)	\$ 0.35	\$ 0.32	\$ 0.59
Diluted net income (loss) per common share	\$ (0.30)	\$ 0.35	\$ 0.32	\$ 0.59

Net income (loss) and the resulting net income (loss) per common share for the three and nine months ended September 30, 2006 includes the \$40.8 million, or \$32.0 million after tax, loss on early extinguishment of debt. See note 7 to the condensed consolidated financial statements for additional information on these transactions.

The pro forma information above is presented for illustrative purposes only and may not be indicative of the results of operations that would have actually occurred had the Eagle transaction occurred as presented. Further, the above pro forma amounts do not consider any potential synergies or integration costs that may result from the transaction. In addition, future results may vary significantly from the results reflected in such pro forma information.

(5) Stock-Based Compensation

We adopted our 2006 Stock-Based Incentive Compensation Plan (the "Stock Incentive Plan") in January 2006 prior to the Company's initial public offering of common stock. The Stock Incentive Plan was further amended and restated with the approval of our stockholders at the 2006 annual meeting of the stockholders of the Company to provide for

the inclusion of non-employee directors as persons eligible to receive awards under the Stock Incentive Plan. Prior to the adoption of the Stock Incentive Plan, no share-based payment arrangements existed. The Stock Incentive Plan is administered by the Compensation Committee of our Board of Directors, which selects persons eligible to receive awards and determines the number of shares and/or options subject to each award, the terms, conditions, performance measures, if any, and other provisions of the award. Under the Stock Incentive Plan, we

Table of Contents

may offer deferred shares or restricted shares of our common stock and grant options, including both incentive stock options and nonqualified stock options, to purchase shares of our common stock.

SFAS 123(R) became effective for us in the first quarter of our current fiscal year ending December 31, 2006. Under the provisions of SFAS 123(R), stock-based compensation is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the requisite employee service period (generally the vesting period of the grant).

Non-vested Stock

On February 22, 2006, we issued non-vested stock grants for 121,950 shares of our common stock. These stock awards may not be sold or otherwise transferred until certain restrictions have lapsed. The unrecognized compensation cost related to these awards is expected to be expensed over the period the restrictions lapse (one to three years). Compensation expense was determined based on the \$24.60 market price of our stock at the date of grant applied to the total number of shares that were anticipated to fully vest. As of September 30, 2006, we have unrecognized compensation expense of \$2.4 million associated with these awards. Compensation expense related to these awards included in selling, general and administrative expenses in the accompanying condensed consolidated statements of operations for the three and nine months ended September 30, 2006 was \$0.3 million and \$0.6 million, respectively. At September 30, 2006, there were 121,950 non-vested shares outstanding.

Stock Options

On February 22, 2006, stock options for 45,000 shares of our common stock were granted by the Company, subject to stockholder approval of the amendment to and restatement of the Stock Incentive Plan at the Company's annual meeting of stockholders, with an exercise price of \$24.60 per share, the market price of our stock on the date of grant. These options vest in three equal parts over three years and expire ten years from the date of grant. On June 6, 2006, the Company's stockholders approved the amendment to and restatement of the Stock Incentive Plan.

The Company uses the Black-Scholes option pricing model to estimate the fair value of stock-based awards. The following assumptions were used in determining the estimated fair value for these awards:

Risk-free interest rate	5.00%
Expected life of options (in years)	6.0
Expected volatility	35.00%
Expected annual dividend yield	

The assumptions above are based on multiple factors. Since the Company is a new public entity with limited historical data on the price of its publicly traded common shares and has no history of share-based payments exercise activity, the Company, as provided for in SEC Staff Accounting Bulletin No. 107, used a simplified method for determining the options expected term and based its estimate of expected volatility on the historical, expected or implied volatility of similar entities within our industry whose share or option prices are publicly available.

At September 30, 2006, there was \$0.6 million of unrecognized compensation cost related to these stock options awards that is expected to be recognized over a period of 2.4 years. Compensation expense related to these awards included in selling, general and administrative expenses in the accompanying condensed consolidated statements of operations was \$0.1 million for the three and nine months ended September 30, 2006, respectively. At September 30, 2006, 45,000 options were outstanding with a grant-date value of \$14.62 per share. The weighted average exercise price of options outstanding is \$24.60. The market price of our common stock at September 30, 2006 was \$24.39 as compared to an exercise price of \$24.60 to be paid by the optionee. None of the options outstanding were exercisable as of September 30, 2006.

Shares available for future stock-based payment awards under our Stock Incentive Plan were 4,401,467 shares as of September 30, 2006.

(6) Earnings per Share

Earnings per common share for the three and nine months ended September 30, 2006 and 2005 are based on the weighted average number of common shares outstanding during the period and have been retroactively adjusted for the three and nine month periods

Table of Contents

ended September 30, 2006 and 2005, to reflect the Reorganization Transactions as if the Reorganization Transactions had occurred at the beginning of the earliest year presented. The following table sets forth the computation of basic and diluted net income (loss) per common share for the three and nine months ended September 30, 2006 and 2005 (amounts in thousands, except per share amounts).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Basic net income (loss) per share:				
Net income (loss)	\$ (11,531)	\$ 8,225	\$ 12,192	\$ 13,469
Weighted average number of common shares outstanding	38,070	25,492	36,550	25,492
Net income (loss) per common share basic	\$ (0.30)	\$ 0.32	\$ 0.33	\$ 0.53
Diluted net income per share:				
Net income (loss)	\$ (11,531)	\$ 8,225	\$ 12,192	\$ 13,469
Weighted average number of common shares outstanding	38,070	25,492	36,550	25,492
Effect of dilutive securities:				
Effect of dilutive stock options and non-vested stock			37	
Weighted average number of shares outstanding diluted	38,070	25,492	36,587	25,492
Net income (loss) per common share diluted	\$ (0.30)	\$ 0.32	\$ 0.33	\$ 0.53
Common shares excluded from the denominator as anti-dilutive:				
Stock options and non-vested stock		53		

(7) Senior Unsecured Notes

On August 4, 2006, the Company completed its cash tender offer and consent solicitation for their 11 1/8% senior secured notes due 2012 and 12 1/2% senior subordinated notes due 2013 (collectively, the Notes). Additionally, the Company announced the closing of its previously announced private offering of \$250 million aggregate principal amount of its 8 3/8% senior unsecured notes due 2016 (the New Notes).

Net proceeds to us, after deducting underwriting commissions, totaled approximately \$245.3 million. The Company used the net proceeds of the offering of the New Notes, together with cash on hand and borrowings under its existing senior secured credit facility, to purchase \$195.5 million in aggregate principal amount of the senior secured notes (representing approximately 97.8% of the previously outstanding senior secured notes), and the \$53.0 million in aggregate principal amount of the senior subordinated notes (representing 100% of the previously outstanding senior subordinated notes) that were validly tendered pursuant to the tender offer and consent solicitation. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the senior secured notes was \$217.6 million. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the senior subordinated notes was approximately \$60.1 million. Aggregate offering expenses totaled approximately \$1.9 million.

In connection with the above transactions, the Company recorded a one-time loss on the early extinguishment of debt in the three month period ended September 30, 2006 of approximately \$40.8 million, or approximately \$32.0 million after-tax, reflecting payment of the \$25.3 million of tender premiums and other estimated costs of \$0.5 million in connection with the tender offer and consent solicitation, combined with the write off of approximately \$5.4 million of unamortized deferred financing costs of the Notes and \$9.6 million of remaining unamortized original

issue discount on the Notes.

The amendments to the indentures pursuant to which the Notes were issued which were proposed in connection with the tender offer and consent solicitation became operative on August 4, 2006. The amendments to the indentures eliminate substantially all of the restrictive covenants and eliminate or modify certain events of default and related provisions contained in the indentures.

The New Notes were issued at par and require semiannual interest payments on January 15th and July 15th of each year, beginning on July 15, 2007. No principal payments are due until maturity (January 15, 2016). We may redeem some or all of the New Notes on or after July 15, 2011, at the applicable redemption prices plus accrued and unpaid interest and additional interest, if any, to the date of redemption. Additionally, we may redeem up to 35% of the aggregate principal amount of the notes using net cash proceeds from equity offerings completed on or prior to July 15, 2009.

Table of Contents

The New Notes rank equal in right of payment to all of our and our guarantors' existing and future unsecured senior indebtedness and senior in right of payment to any of our or our guarantors' future subordinated indebtedness. The New Notes are effectively junior in priority to our and our guarantors' obligations under all of our existing and future secured indebtedness, including borrowings under our senior secured credit facility, the \$4.5 million of senior secured notes outstanding at September 30, 2006, and any other secured obligations, in each case, to the extent of the value of the assets securing such obligations. The New Notes are also effectively junior to all liabilities (including trade payables) of our non-guarantor subsidiaries.

Concurrently with the closing of the private offering, the Company entered into an Amended and Restated Credit Agreement (the "Amended Credit Agreement"), amending and restating the Company's senior secured credit agreement primarily to, (i) increase the principal amount of availability of the credit facility from \$165.0 million to \$250.0 million; (ii) reduce the applicable unused line fee margin in respect of undrawn commitments to 0.25%; (iii) increase the advance rate on rental fleet assets from the lesser of 100% of net book value or 80% of orderly liquidation value to the lesser of 100% of net book value or 85% of orderly liquidation value; (iv) extend the maturity date of the facility from February 10, 2009 to August 4, 2011; and (v) add H&E Equipment Services (California), LLC as a borrower. Furthermore, the Amended Credit Agreement changed the measurement frequency of our computed Leverage Ratio from a monthly calculation to a quarterly calculation. The Company paid \$1.4 million to the

Lenders in connection with this Amended Credit Agreement and incurred other transaction costs of approximately \$0.2 million. As of September 30, 2006, we had \$26.3 million of outstanding borrowings under our senior secured credit facility with \$215.4 million of additional borrowing availability, net of \$8.3 million of issued standby letters of credit. As of September 30, 2006, the Company was in compliance with its financial covenant under its Amended and Restated Credit Agreement.

On October 3, 2006, the Company and the guarantors filed a Form S-4 Registration Statement, as subsequently amended on October 11, 2006, with respect to an offer to exchange the New Notes for notes of the Company being issued in a transaction registered under the Securities Act of 1933, as amended, having terms identical in all material respects to the New Notes (except that the exchange notes will not contain terms with respect to transfer restrictions). Upon the Form S-4 Registration Statement being declared effective on October 13, 2006, the Company launched the exchange offer. The exchange offer expired on November 13, 2006, with \$250.0 million of the aggregate principal amount, or 100%, of the New Notes exchanged for new notes registered under the Securities Act of 1933, as amended.

(8) Segment Information

We have identified five reportable segments: equipment rentals, new equipment sales, used equipment sales, parts sales and service revenue. These segments are based upon how management of the Company allocates resources and assesses performance. Non-segmented revenues and non-segmented costs relate to equipment support activities including transportation, hauling, parts freight and damage-waiver charges and are not allocated to the other reportable segments. There were no sales between segments for any of the periods presented. Selling, general and administrative expenses as well as all other income and expense items below gross profit are not generally allocated to reportable segments.

The Company does not compile discrete financial information by its segments other than the information presented below. The following table presents information about the Company's reportable segments (amounts in thousands).

	For the Three Months Ended September 30, 2006		For the Nine Months Ended September 30, 2006	
	2006	2005	2006	2005
Revenues:				
Equipment rentals	\$ 67,327	\$ 50,409	\$ 185,333	\$ 136,576
New equipment sales	60,673	36,152	173,333	99,867
Used equipment sales	29,668	26,751	97,387	76,332
Parts sales	21,024	16,986	61,574	51,202
Service revenue	14,074	10,409	39,782	29,459

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Total segmented revenues	192,766	140,707	557,409	393,436
Non-segmented revenues	11,369	7,749	31,472	21,300
Total revenues	\$ 204,135	\$ 148,456	\$ 588,881	\$ 414,736
Gross Profit:				
Equipment rentals	\$ 36,344	\$ 24,040	\$ 97,232	\$ 62,158
New equipment sales	7,352	4,369	21,718	12,064
Used equipment sales	7,960	6,426	26,134	18,289

15

Table of Contents

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Parts sales	6,129	5,014	18,075	15,097
Service revenue	9,029	6,429	25,439	18,486
Total segmented gross profit	66,814	46,278	188,598	126,094
Non-segmented gross profit (loss)	1,933	520	4,467	(400)
Total gross profit	\$ 68,747	\$ 46,798	\$ 193,065	\$ 125,694

	Balances at	
	September 30, 2006	December 31, 2005
Segment identified assets:		
Equipment sales	\$ 95,192	\$ 62,344
Equipment rentals	429,219	308,036
Parts and service	21,133	18,749
Total segment identified assets	545,544	389,129
Non-segment identified assets	187,500	141,568
Total assets	\$ 733,044	\$ 530,697

The Company operates primarily in the United States and had minimal international sales for any of the periods presented. No one customer accounted for more than 10% of the Company's revenues on an overall or segment basis for any of the periods presented.

(9) Condensed Consolidating Financial Information of Guarantor Subsidiaries

All of the indebtedness of H&E Equipment Services, Inc. is guaranteed by GNE Investments, Inc. and its wholly-owned subsidiary Great Northern Equipment, Inc., H&E Equipment Services (California), LLC (formerly known as Eagle High Reach Equipment, LLC), and H&E California Holdings, Inc. (formerly known as Eagle High Reach Equipment, Inc.). The guarantor subsidiaries are all wholly-owned and the guarantees, made on a joint and several basis, are full and unconditional (subject to subordination provisions and subject to a standard limitation which provides that the maximum amount guaranteed by each guarantor will not exceed the maximum amount that can be guaranteed without making the guarantee void under fraudulent conveyance laws). There are no restrictions on the Company's ability to obtain funds from the guarantor subsidiaries by dividend or loan.

The consolidating financial statements of H&E Equipment Services, Inc. and its subsidiaries are included below. The financial statements for H&E Finance Corp., the subsidiary co-issuer, are not included within the consolidating financial statements because H&E Finance Corp. has no assets or operations. The financial statements of H&E Equipment Services (California), LLC and H&E California Holdings, Inc. included are from the date of the Company's acquisition of Eagle, February 28, 2006, to September 30, 2006 and as of September 30, 2006.

Table of Contents

CONDENSED CONSOLIDATING BALANCE SHEET
(Amounts in thousands)

	As of September 30, 2006			
	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Assets:				
Cash	\$ 4,972	\$ 81	\$	\$ 5,053
Receivables, net	96,511	13,219		109,730
Inventories, net	112,432	3,893		116,325
Prepaid expenses and other assets	4,320	154		4,474
Rental equipment, net	368,520	60,699		429,219
Property and equipment, net	23,823	4,516		28,339
Deferred financing costs and other intangible assets, net	9,449			9,449
Investment in guarantor subsidiaries	12,044		(12,044)	
Goodwill	30,455			30,455
Total assets	\$ 662,526	\$ 82,562	\$ (12,044)	\$ 733,044
Liabilities and Stockholders Equity:				
Amount due on senior secured credit facility	\$ 26,265	\$	\$	\$ 26,265
Accounts payable	62,153	21		62,174
Manufacturer flooring plans payable	130,020			130,020
Accrued expenses payable and other liabilities	32,712	909		33,621
Intercompany balance	(68,839)	68,839		
Related party obligation	709			709
Notes payable	1,651	749		2,400
Senior secured notes, net of discount	4,477			4,477
Senior unsecured notes	250,000			250,000
Deferred income taxes	5,411			5,411
Deferred compensation payable	3,215			3,215
Total liabilities	447,774	70,518		518,292
Stockholders equity	214,752	12,044	(12,044)	214,752
Total liabilities and stockholders equity	\$ 662,526	\$ 82,562	\$ (12,044)	\$ 733,044

Table of Contents

CONDENSED CONSOLIDATING BALANCE SHEET
(Amounts in thousands)

	As of December 31, 2005			
	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Assets:				
Cash	\$ 5,610	\$ 17	\$	\$ 5,627
Receivables, net	95,427	4,096		99,523
Inventories, net	76,533	4,560		81,093
Prepaid expenses and other assets	1,378			1,378
Rental equipment, net	298,708	9,328		308,036
Property and equipment, net	17,526	758		18,284
Deferred financing costs, net	8,184			8,184
Investment in guarantor subsidiaries	7,025		(7,025)	
Goodwill	8,572			8,572
Total assets	\$ 518,963	\$ 18,759	\$ (7,025)	530,697
Liabilities and Members Equity (Deficit):				
Amount due on senior secured credit facility	\$ 102,980	\$ 3,471	\$	\$ 106,451
Accounts payable	56,173			56,173
Manufacturer flooring plans payable	93,728			93,728
Accrued expenses payable and other liabilities	22,696	102		22,798
Intercompany balance	(8,161)	8,161		
Related party obligation	869			869
Notes payable	521			521
Senior secured notes, net of discount	198,873			198,873
Senior subordinated notes, net of discount	44,057			44,057
Deferred income taxes	645			645
Deferred compensation payable	11,722			11,722
Total liabilities	524,103	11,734		535,837
Members equity (deficit)	(5,140)	7,025	(7,025)	(5,140)
Total liabilities and members equity (deficit)	\$ 518,963	\$ 18,759	\$ (7,025)	\$ 530,697

Table of Contents

CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
(Amounts in thousands)

Three Months Ended September 30, 2006

	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Revenues:				
Equipment rentals	\$ 56,205	\$ 11,122	\$	\$ 67,327
New equipment sales	58,659	2,014		60,673
Used equipment sales	27,270	2,398		29,668
Parts sales	20,162	862		21,024
Service revenue	13,528	546		14,074
Other	9,855	1,514		11,369
Total revenues	185,679	18,456		204,135
Cost of revenues:				
Rental depreciation	17,548	3,096		20,644
Rental expense	8,912	1,427		10,339
New equipment sales	51,557	1,764		53,321
Used equipment sales	20,066	1,642		21,708
Parts sales	14,298	597		14,895
Service revenue	4,874	171		5,045
Other	8,040	1,396		9,436
Total cost of revenues	125,295	10,093		135,388
Gross profit:				
Equipment rentals	29,745	6,599		36,344
New equipment sales	7,102	250		7,352
Used equipment sales	7,204	756		7,960
Parts sales	5,864	265		6,129
Service revenue	8,654	375		9,029
Other	1,815	118		1,933
Gross profit	60,384	8,363		68,747
Selling, general and administrative expenses	30,499	3,619		34,118
Equity in earnings of guarantor subsidiaries	3,192		(3,192)	
Gain on sale of property and equipment	139	102		241
Income from operations	33,216	4,846	(3,192)	34,870
Other income (expense):				
Interest expense	(7,397)	(1,663)		(9,060)
Loss on early extinguishment of debt	(40,771)			(40,771)
Other, net	236	9		245

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Total other expense, net	(47,932)	(1,654)		(49,586)
Income (loss) before provision (benefit) for income taxes	(14,716)	3,192	(3,192)	(14,716)
Income tax provision (benefit)	(3,185)			(3,185)
Net income (loss)	\$ (11,531)	\$ 3,192	\$ (3,192)	\$ (11,531)

Table of Contents

CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
(Amounts in thousands)

Three Months Ended September 30, 2005

	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Revenues:				
Equipment rentals	\$ 48,222	\$ 2,187	\$	\$ 50,409
New equipment sales	34,861	1,291		36,152
Used equipment sales	25,482	1,269		26,751
Parts sales	16,372	614		16,986
Service revenue	10,033	376		10,409
Other	7,427	322		7,749
Total revenues	142,397	6,059		148,456
Cost of revenues:				
Rental depreciation	13,689	665		14,354
Rental expense	11,766	249		12,015
New equipment sales	30,656	1,127		31,783
Used equipment sales	19,367	958		20,325
Parts sales	11,549	423		11,972
Service revenue	3,881	99		3,980
Other	6,914	315		7,229
Total cost of revenues	97,822	3,836		101,658
Gross profit:				
Equipment rentals	22,767	1,273		24,040
New equipment sales	4,205	164		4,369
Used equipment sales	6,115	311		6,426
Parts sales	4,823	191		5,014
Service revenue	6,152	277		6,429
Other	513	7		520
Gross profit	44,575	2,223		46,798
Selling, general and administrative expenses	26,804	1,415		28,219
Equity in loss of guarantor subsidiaries	483		(483)	
Gain on sale of property and equipment	106	12		118
Income from operations	18,360	820	(483)	18,697
Other income (expense):				
Interest expense	(10,216)	(341)		(10,557)
Other, net	81	4		85
Total other expense, net	(10,135)	(337)		(10,472)

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Income before provision for income taxes	8,225	483	(483)	8,225
Income tax provision				
Net income	\$ 8,225	\$ 483	\$ (483)	\$ 8,225

20

Table of Contents

CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
(Amounts in thousands)

Nine Months Ended September 30, 2006

	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Revenues:				
Equipment rentals	\$ 160,730	\$ 24,603	\$	\$ 185,333
New equipment sales	167,944	5,389		173,333
Used equipment sales	90,354	7,033		97,387
Parts sales	59,319	2,255		61,574
Service revenue	38,444	1,338		39,782
Other	28,119	3,353		31,472
Total revenues	544,910	43,971		588,881
Cost of revenues:				
Rental depreciation	49,741	6,933		56,674
Rental expense	27,592	3,835		31,427
New equipment sales	146,990	4,625		151,615
Used equipment sales	66,340	4,913		71,253
Parts sales	41,968	1,531		43,499
Service revenue	13,934	409		14,343
Other	23,849	3,156		27,005
Total cost of revenues	370,414	25,402		395,816
Gross profit:				
Equipment rentals	83,397	13,835		97,232
New equipment sales	20,954	764		21,718
Used equipment sales	24,014	2,120		26,134
Parts sales	17,351	724		18,075
Service revenue	24,510	929		25,439
Other	4,270	197		4,467
Gross profit	174,496	18,569		193,065
Selling, general and administrative expenses	98,378	10,167		108,545
Equity in earnings of guarantor subsidiaries	5,019		(5,019)	
Gain on sale of property and equipment	268	132		400
Income from operations	81,405	8,534	(5,019)	84,920
Other income (expense):				
Interest expense	(25,814)	(3,528)		(29,342)
Loss on early extinguishment of debt	(40,771)			(40,771)
Other, net	662	13		675

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Total other expense, net	(65,923)	(3,515)		(69,438)
Income before income taxes	15,482	5,019	(5,019)	15,482
Income tax provision	3,290			3,290
Net income	\$ 12,192	\$ 5,019	\$ (5,019)	\$ 12,192

21

Table of Contents

CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
(Amounts in thousands)

Nine Months Ended September 30, 2005

	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Revenues:				
Equipment rentals	\$ 131,408	\$ 5,168	\$	\$ 136,576
New equipment sales	95,976	3,891		99,867
Used equipment sales	71,218	5,114		76,332
Parts sales	49,593	1,609		51,202
Service revenue	28,464	995		29,459
Other	20,443	857		21,300
Total revenues	397,102	17,634		414,736
Cost of revenues:				
Rental depreciation	37,702	1,692		39,394
Rental expense	34,248	776		35,024
New equipment sales	84,485	3,318		87,803
Used equipment sales	54,294	3,749		58,043
Parts sales	34,990	1,115		36,105
Service revenue	10,695	278		10,973
Other	20,806	894		21,700
Total cost of revenues	277,220	11,822		289,042
Gross profit:				
Equipment rentals	59,458	2,700		62,158
New equipment sales	11,491	573		12,064
Used equipment sales	16,924	1,365		18,289
Parts sales	14,603	494		15,097
Service revenue	17,769	717		18,486
Other	(363)	(37)		(400)
Gross profit	119,882	5,812		125,694
Selling, general and administrative expenses	77,377	3,965		81,342
Equity in loss of guarantor subsidiaries	982		(982)	
Gain (loss) on sale of property and equipment	(6)	21		15
Income from operations	43,481	1,868	(982)	44,367
Other income (expense):				
Interest expense	(30,091)	(891)		(30,982)
Other, net	250	5		255
Total other expense, net	(29,841)	(886)		(30,727)

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Income before provision for income taxes	13,640	982	(982)	13,640
Provision for income taxes	171			171
Net income	\$ 13,469	\$ 982	\$ (982)	\$ 13,469

22

Table of Contents

CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
(Amounts in thousands)

Nine Months Ended September 30, 2006

	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Cash flows from operating activities:				
Net income	\$ 12,192	\$ 5,019	\$ (5,019)	\$ 12,192
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation on property and equipment	4,466	544		5,010
Depreciation on rental equipment	49,852	6,822		56,674
Amortization of other intangible assets	34			34
Amortization of loan discounts and deferred financing costs	2,056			2,056
Provision for losses on accounts receivable	1,457			1,457
Provision for inventory obsolescence	18			18
Gain on sale of property and equipment	(268)	(132)		(400)
Gain on sale of rental equipment	(16,293)	(7,046)		(23,339)
Provision for deferred taxes	2,692			2,692
Non-cash compensation expense	681			681
Loss on early extinguishment of debt	40,771			40,771
Equity in earnings of guarantor subsidiaries	(5,019)		5,019	
Changes in operating assets and liabilities:				
Receivables, net	(2,678)	(1,685)		(4,363)
Inventories, net	(31,572)	(26,743)		(58,315)
Prepaid expenses and other assets	(2,941)	(1,496)		(4,437)
Accounts payable	5,980	(467)		5,513
Manufacturer flooring plans payable	36,292			36,292
Accrued expenses payable and other liabilities	6,214	807		7,021
Intercompany balance	(60,678)	60,678		
Deferred compensation payable	(8,507)			(8,507)
Net cash provided by operating activities	34,749	36,301		71,050
Cash flows from investing activities:				
Acquisition of businesses, net of cash acquired	(15,051)	(41,910)		(56,961)
Purchases of property and equipment	(12,377)	(976)		(13,353)
Purchases of rental equipment	(177,421)	3,049		(174,372)
Proceeds from sale of property and equipment	1,882	(41)		1,841
Proceeds from sale of rental equipment	69,705	6,363		76,068
Net cash used in investing activities	(133,262)	(33,515)		(166,777)
Cash flows from financing activities:				
Proceeds from issuance of common stock, net of issue costs	207,018			207,018
Borrowings on senior secured credit facility	718,819			718,819

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Payments on senior secured credit facility	(795,534)	(3,471)	(799,005)
Proceeds from issuance of senior unsecured notes, net of issue costs	250,000		250,000
Principal payment of senior secured notes	(214,608)		(214,608)
Principal payment of senior subordinated notes	(59,155)		(59,155)
Payments of deferred financing costs	(8,816)		(8,816)
Payments of related party obligation	(225)		(225)
Proceeds from issuance of notes payable	1,271		1,271
Principal payments of notes payable	(895)	749	(146)
Net cash provided by (used in) financing activities	97,875	(2,722)	95,153
Net increase (decrease) in cash	(638)	64	(574)
Cash, beginning of period	5,610	17	5,627
Cash, end of period	\$ 4,972	\$ 81	\$ 5,053

Table of Contents

CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
(Amounts in thousands)

Nine Months Ended September 30, 2005

	H&E Equipment Services	Guarantor Subsidiaries	Elimination	Consolidated
Cash flows from operating activities:				
Net income	\$ 13,469	\$ 982	\$ (982)	\$ 13,469
Adjustments to reconcile net income to net cash provided by (used in) operating activities:				
Depreciation on property and equipment	3,602	150		3,752
Depreciation on rental equipment	37,702	1,692		39,394
Amortization of other intangible assets	82			82
Amortization of loan discounts and deferred financing costs	2,044			2,044
Provision for losses on accounts receivable	997	99		1,096
Provision for obsolescence	30			30
Gain on sale of property and equipment	6	(21)		(15)
Gain on sale of rental equipment	(14,860)	(1,339)		(16,199)
Equity in earnings of guarantor subsidiaries	(982)		982	
Changes in operating assets and liabilities:				
Receivables, net	(14,546)	(723)		(15,269)
Inventories, net	(36,742)	364		(36,378)
Prepaid expenses and other assets	(2,058)			(2,058)
Accounts payable	19,188			19,188
Manufacturer flooring plans payable	11,456			11,456
Accrued expenses payable and other liabilities	16,317	109		16,426
Intercompany balance	5,095	(5,095)		
Deferred compensation payable	864			864
Net cash provided by (used in) operating activities	41,664	(3,782)		37,882
Cash flows from investing activities:				
Purchases of property and equipment	(5,215)	(457)		(5,672)
Purchases of rental equipment	(117,010)	(713)		(117,723)
Proceeds from sale of property and equipment	712	13		725
Proceeds from sale of rental equipment	56,566	4,928		61,494
Net cash provided by (used in) investing activities	(64,947)	3,771		(61,176)
Cash flows from financing activities:				
Borrowings on senior secured credit facility	424,867			424,867
Payments on senior secured credit facility	(398,955)			(398,955)
Payment of deferred financing costs	(10)			(10)
Payment of related party obligation	(225)			(225)
Principal payments of notes payable	(181)			(181)

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

Payments on capital lease obligations	(1,120)			(1,120)
Net cash provided by financing activities	24,376			24,376
Net increase (decrease) in cash	1,093	(11)		1,082
Cash, beginning of period	3,334	24		3,358
Cash, end of period	\$ 4,427	\$ 13	\$	\$ 4,440

24

Table of Contents

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion summarizes the financial position of H&E Equipment Services, Inc. and its subsidiaries as of September 30, 2006, and the results of their operations for the three and nine month periods ended September 30, 2006, and should be read in conjunction with (i) the unaudited condensed consolidated financial statements and notes thereto included elsewhere in this Quarterly Report on Form 10-Q and (ii) the consolidated financial statements and accompanying notes to our Annual Report on Form 10-K for the year ended December 31, 2005.

Overview

Background

As one of the largest integrated equipment services companies in the United States focused on heavy construction and industrial equipment, we rent, sell and provide parts and service support for four core categories of specialized equipment: (1) hi-lift or aerial platform equipment, (2) cranes, (3) earthmoving equipment and (4) industrial lift trucks. By providing equipment rental, sales, on-site parts, repair and maintenance functions under one roof, we are a one-stop provider for our customers' varied equipment needs. This full service approach provides us with multiple points of customer contact, enables us to maintain an extremely high quality rental fleet, as well as an effective distribution channel for fleet disposal and provides cross-selling opportunities among our new and used equipment sales, rental, parts sales and service operations.

As of November 8, 2006, we operated 47 full-service facilities throughout the Intermountain, Southwest, Gulf Coast, West Coast and Southeast regions of the United States. Our work force includes distinct, focused sales forces for our new and used equipment sales and rental operations, highly-skilled service technicians, product specialists and regional managers. We focus our sales and rental activities on, and organize our personnel principally by, our four equipment categories. We believe this allows us to provide specialized equipment knowledge, improve the effectiveness of our rental and sales force and strengthen our customer relationships. In addition, we have branch managers at each location who are responsible for managing their assets and financial results. We believe this fosters accountability in our business, and strengthens our local and regional relationships.

Through our predecessor companies, we have been in the equipment services business for approximately 45 years. H&E Equipment Services L.L.C. was formed in June 2002 through the combination of Head & Engquist, a wholly-owned subsidiary of Gulf Wide, and ICM. Head & Engquist, founded in 1961, and ICM, founded in 1971, were two leading regional, integrated equipment service companies operating in contiguous geographic markets. In a June 2002 transaction, Head & Engquist and ICM were merged with and into Gulf Wide, which was renamed H&E Equipment Services L.L.C. Prior to the combination, Head & Engquist operated 25 facilities in the Gulf Coast region, and ICM operated 16 facilities in the Intermountain region of the United States.

In connection with our initial public offering in February 2006, we converted H&E LLC into H&E Equipment Services, Inc. Prior to our initial public offering, our business was conducted through H&E LLC. In order to have an operating Delaware corporation as the issuer for our initial public offering, H&E Equipment Services, Inc. was formed as a Delaware corporation and wholly-owned subsidiary of H&E Holdings, and immediately prior to the closing of our initial public offering, on February 3, 2006, H&E LLC and H&E Holdings merged with and into us (H&E Equipment Services, Inc.), with us surviving the reincorporation merger as the operating company.

Critical Accounting Policies

Item 7, included in Part II of our Annual Report on Form 10-K for the year ended December 31, 2005 present the accounting policies and related estimates that we believe are the most critical to understanding our consolidated financial statements, financial condition, and results of operations and cash flows, and which require complex management judgment and assumptions, or involve uncertainties. These include, among other things, revenue recognition, the adequacy of the allowance for doubtful accounts, the propriety of our estimated useful life of rental equipment and property and equipment, the potential impairment of long-lived assets including goodwill, obsolescence reserves on inventory, and deferred income taxes, including the valuation of any related deferred tax assets.

Information regarding our other accounting policies is included in the notes to our consolidated financial statements in Item 8 of Part II of our Annual Report on Form 10-K for the year ended December 31, 2005.

Table of Contents

Business Segments

We have five reportable segments because we derive our revenues from five principal business activities: (1) equipment rentals; (2) new equipment sales; (3) used equipment sales; (4) parts sales; and (5) repair and maintenance services. These segments are based upon how we allocate resources and assess performance. In addition, we also have non-segmented revenues and costs that relate to equipment support activities.

Equipment Rentals. Our rental operation primarily rents our four core types of construction and industrial equipment. We have an extremely well-maintained rental fleet and our own dedicated sales force, focused by equipment type. We actively manage the size, quality, age and composition of our rental fleet based on our analysis of key measures such as time utilization, rental rate trends and targets, and equipment demand which we closely monitor. We maintain fleet quality through regional quality control managers and our parts and services operations.

New Equipment Sales. Our new equipment sales operation sells new equipment in all four product categories. We have a retail sales force focused by equipment type that is separate from our rental sales force. Manufacturer purchase terms and pricing are managed by our product specialists.

Used Equipment Sales. Our used equipment sales are generated primarily from sales of used equipment from our rental fleet, as well as from sales of inventoried equipment that we acquire through trade-ins from our equipment customers and through selective purchases of high quality used equipment. Used equipment is sold by our dedicated retail sales force. Our used equipment sales are an effective way for us to manage the size and composition of our rental fleet and provides a profitable distribution channel for disposal of rental equipment.

Parts Sales. Our parts business sells new and used parts for the equipment we sell, and also provides parts to our own rental fleet. To a lesser degree, we also sell parts for equipment produced by manufacturers whose products we neither rent nor sell. In order to provide timely parts and service support to our customers as well as our own rental fleet, we maintain an extensive parts inventory.

Services. Our services operation provides maintenance and repair services for our customers' equipment and to our own rental fleet at our facilities as well as at our customers' locations. As the authorized distributor for numerous equipment manufacturers, we are able to provide service to that equipment that will be covered under the manufacturer's warranty.

Our non-segmented revenues and costs relate to equipment support activities that we provide, such as transportation, hauling, parts freight, and damage waivers, and are not generally allocated to reportable segments.

For additional information about our business segments, see note 8 to the condensed consolidated financial statements in this Quarterly Report on Form 10-Q.

Revenue Sources

We generate all of our total revenues from our five business segments and our non-segmented equipment support activities. Equipment rentals and new equipment sales account for more than half of our total revenues. For the nine months ended September 30, 2006, approximately 31.5% of our total revenues were attributable to equipment rentals, 29.4% of our total revenues were attributable to new equipment sales, 16.5% were attributable to used equipment sales, 10.5% were attributable to parts sales, 6.8% were attributable to our service revenues and 5.3% were attributable to non-segmented other revenues.

The equipment that we sell, rent and service is principally used in the construction industry, as well as by companies for commercial and industrial uses such as plant maintenance and turnarounds. As a result, our total revenues are affected by several factors including, but not limited to, the demand for and availability of rental equipment, rental rates, the demand for new and used equipment, the level of construction and industrial activities, spending levels by our customers, adverse weather conditions and general economic conditions. For a discussion of the impact of seasonality on our revenues, see *Seasonality* below.

Equipment Rentals. Revenues from equipment rentals depend on rental rates. Because rental rates are impacted by competition in specific regions and markets, we continuously monitor and adjust rental rates. We have a rental rate initiative driven by management to increase rental rates. Equipment rental revenue is also impacted by the availability of equipment and by time utilization (equipment usage based on customer demand). We generate reports on, among other things, time utilization,

Table of Contents

demand pricing (rental rate pricing based on physical utilization), and rental rate trends on a piece-by-piece basis for our rental fleet. We recognize revenues from equipment rentals in the period earned, over the contract term, regardless of the timing of billing to customers.

New Equipment Sales. We optimize revenues from new equipment sales by selling equipment through a professional in-house retail sales force focused by product type. While sales of new equipment are impacted by the availability of equipment from the manufacturer, we believe our status as a leading distributor for some of our key suppliers improves our ability to obtain equipment. New equipment sales are an important component of our integrated model due to customer interaction and service contact; new equipment sales also lead to future parts and service revenues. We recognize revenue from the sale of new equipment at the time of delivery to, or pick-up by, the customer and when all obligations under the sales contract have been fulfilled and collectibility is reasonably assured.

Used Equipment Sales. We generate the majority of our used equipment sales revenues by selling equipment from our rental fleet. The remainder of used equipment sales revenues comes from the sale of inventoried equipment that we acquire through trade-ins from our equipment customers and selective purchases of high-quality used equipment. Our policy is not to offer specified-price trade-in arrangements on equipment for sale. Sales of our rental fleet equipment allow us to manage the size, quality, composition and age of our rental fleet, and provide a profitable distribution channel for disposal of rental equipment. We recognize revenue for the sale of used equipment in the same manner that we recognize revenue from new equipment sales.

Parts Sales. We generate revenues from the sale of new and used parts for equipment that we rent or sell, as well as for other makes of equipment. Our product support sales representatives are instrumental in generating our parts revenues. They are product specialists and receive performance incentives for achieving certain sales levels. Most of our parts sales come from our extensive in-house parts inventory. Our parts sales provide us with a relatively stable revenue stream that is less sensitive to the economic cycles that affect our rental and equipment sales operations. We recognize revenues from parts sales at the time of delivery to, or pick-up by, the customer and when all obligations under the sales contract have been fulfilled and collectibility is reasonably assured.

Services. We derive our services revenues from maintenance and repair services to customers for their owned equipment. In addition to repair and maintenance on an as-needed or scheduled basis, we also provide ongoing preventative maintenance services to industrial customers. Our after-market service provides a high-margin, relatively stable source of revenue through changing economic cycles. We recognize services revenues at the time services are rendered.

Non-Segmented Revenues. Our non-segmented other revenue consists of billings to customers for equipment support and activities including: transportation, hauling, parts freight and loss damage waiver charges. We recognize revenue for support services at the time we generate an invoice for such services and after the services have been provided.

Principal Costs and Expenses

Our largest expenses are the costs to purchase the new equipment we sell, the costs associated with the used equipment we sell, rental expenses, rental depreciation and costs associated with parts sales and services, all of which are included in cost of revenues. For the nine months ended September 30, 2006, our total cost of revenues was approximately \$395.8 million. Our operating expenses consist principally of selling, general and administrative expense. For the nine months ended September 30, 2006, our selling, general and administrative expenses were approximately \$108.5 million. In addition, we have interest expense related to our debt instruments. Operating expenses and all other income and expense items below the gross profit line of our condensed consolidated statement of income are not generally allocated to our reportable segments.

Cost of Revenues:

Rental Depreciation. Depreciation of rental equipment represents the depreciation costs attributable to rental equipment. Estimated useful lives vary based upon type of equipment. Generally, we depreciate cranes and aerial work platforms over a ten year estimated useful life, earthmoving over a five year estimated useful life with a 25% salvage value, and industrial lift-trucks over a seven year estimated useful life. Attachments and other smaller type equipment are depreciated over a three year estimated useful life.

Rental Expense. Rental expense represents the costs associated with rental equipment, including, among other things, the cost of servicing and maintaining our rental equipment, property taxes on our fleet, equipment operating lease expense and other

Table of Contents

miscellaneous costs of rental equipment. As discussed in Note 3 to the condensed consolidated financial statements, we used a portion of the proceeds from our initial public offering in February 2006 to purchase our rental equipment under operating leases.

New Equipment Sales. Cost of new equipment sold consists of the equipment cost of the new equipment that is sold.

Used Equipment Sales. Cost of used equipment sold consists of the net book value of rental equipment for used equipment sold from our rental fleet, the amount of credit given to the customer towards the new equipment for trade-ins and the equipment cost for used equipment purchased for sale.

Parts Sales. Cost of parts sales represents costs attributable to the sale of parts directly to customers.

Service Support. Cost of service revenue represents costs attributable to service provided for the maintenance and repair of customer-owned equipment and equipment then on-rent by customers.

Non-Segmented Other. These expenses include costs associated with providing transportation, hauling, parts freight, and damage waiver including, among other items, drivers wages fuel costs, shipping costs, and our costs related to damage waiver policies.

Selling, General and Administrative Expenses:

Our selling, general and administrative expenses include sales and marketing expenses, payroll and related costs, insurance expense, professional fees, property and other taxes, administrative overhead, and depreciation associated with property and equipment (other than rental equipment). These expenses are not generally allocated to our reportable segments.

Interest Expense:

Interest expense represents the interest on our outstanding debt instruments, including indebtedness outstanding under our senior secured credit facility, senior secured notes due 2012 and senior unsecured notes due 2016 and notes payable. Additionally, interest expense for the periods presented includes interest on our senior subordinated notes through August 4, 2006, the date upon which these notes were repaid. Interest expense also includes non-cash interest expense related to the amortization cost of (1) deferred financing costs and (2) original issue discount related to our senior secured notes and senior subordinated notes (through August 4, 2006). See Note 7 to the condensed consolidated financial statements in this quarterly report for additional information on our recent refinancing.

Principal Cash Flows

We generate cash primarily from our operating activities and historically we have used cash flows from operating activities, manufacturer floor plan financings and available borrowings under our revolving senior secured credit facility as the primary sources of funds to purchase our inventory and to fund working capital and capital expenditures.

Rental Fleet

A significant portion of our overall value is in our rental fleet equipment. Our rental fleet, as of September 30, 2006, consisted of 18,173 units having an original acquisition cost (which we define as the cost originally paid to manufacturers or the original amount financed under operating leases) of approximately \$648.07 million. As of September 30, 2006, our rental fleet composition was as follows (dollars in millions):

	Units	% of Total Units	Original Acquisition Cost	% of Original Acquisition Cost	Average Age in Months
Aerial Work Platforms	13,765	75.7%	\$ 433.7	66.9%	45.1
Cranes	355	1.9%	75.0	11.6%	44.5
Earthmoving	1,030	5.7%	79.5	12.3%	17.9
Lift Trucks	1,377	7.6%	38.3	5.9%	27.7
Other	1,646	9.1%	21.6	3.3%	31.8
Total	18,173	100.0%	\$ 648.1	100.0%	41.0

Table of Contents

Determining the optimal age and mix for our rental fleet equipment is subjective and requires considerable estimates by management. We constantly evaluate the mix, age and quality of the equipment in our rental fleet in response to current economic conditions, competition and customer demand. On average, we decreased the age of our rental fleet by approximately 1.5 months during the nine months ended September 30, 2006 exclusive of Eagle. When combined with Eagle, we decreased the average age of our rental fleet by approximately 0.1 months. The average age of the acquired Eagle fleet was approximately 57.8 months. The Eagle fleet has de-aged in excess of one year since our acquisition of Eagle. The majority of the de-aging has occurred, by design, with the fleet assigned to our Eagle operations. We have made significant progress in reducing Eagle's fleet age through a combination of disposing of older fleet and adding new fleet. We increased our overall gross rental fleet, through the normal course of business activities, by approximately \$40.6 million during the nine months ended September 30, 2006, and \$125.7 million when combined with the Eagle fleet. We acquired approximately \$70.1 million of gross rental fleet in the Eagle acquisition. We also increased for the nine month period ended September 30, 2006, our average rental rates by approximately 5.0%. The mix among our four core product lines remained consistent with that of prior years. As a result of our in-house service capabilities and extensive maintenance program, we believe our fleet is extremely well-maintained.

The mix and age of our rental fleet, as well as our cash flows, are impacted by the normal sales of equipment from the rental fleet and the capital expenditures to acquire new rental fleet equipment. In making acquisition decisions, we evaluate current market conditions, competition, manufacturers' availability, pricing and return on investment over the estimated life of the specific equipment, among other things.

Principal External Factors that Affect our Businesses

We are subject to a number of external factors that may adversely affect our businesses. These factors, and other factors, are discussed Item 1A- Risk Factors of our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006, as well as in Item 1A Risk Factors of our Annual Report on Form 10-K for the year ended December 31, 2005, include:

Spending levels by customers. Rentals and sales of equipment to the construction industry and to industrial companies constitute a significant portion of our revenues. As a result, we depend upon customers in these businesses and their ability and willingness to make capital expenditures to rent or buy specialized equipment. Accordingly, our business is impacted by fluctuations in customers' spending levels on capital expenditures.

Economic downturns. The demand for our products is dependent on the general economy, the industries in which our customers operate or serve, and other factors. Downturns in the general economy or in the construction and manufacturing industries can cause demand for our products to materially decrease.

Adverse weather. Adverse weather in a geographic region in which we operate may depress demand for equipment in that region. Our equipment is primarily used outdoors and, as a result, prolonged adverse weather conditions may prohibit our customers from continuing their work projects. The adverse weather also has a seasonal impact in parts of our Intermountain region.

We believe that our integrated business tempers the effects of downturns in a particular segment. For a discussion of seasonality, see Seasonality below.

Results of Operations

The tables included in the period comparisons below provide summaries of our revenues and gross profits for our business segments and non-segmented revenues. The period-to-period comparisons of financial results are not necessarily indicative of future results.

Our operating results for the three and nine months ended September 30, 2006 include the operating results of Eagle since the date of acquisition, February 28, 2006.

Table of Contents**Three Months Ended September 30, 2006 Compared to the Three Months Ended September 30, 2005 Revenues.**

	Three Months Ended		Total Dollar Change	Total Percentage Change
	September 30, 2006	September 30, 2005		
	(in millions, except percentages)			
Segment Revenues:				
Equipment rentals	\$ 67.3	\$ 50.4	\$ 16.9	33.5%
New equipment sales	60.7	36.2	24.5	67.7%
Used equipment sales	29.7	26.8	2.9	10.8%
Parts sales	21.0	17.0	4.0	23.5%
Services revenues	14.1	10.4	3.7	35.6%
Non-Segmented revenues	11.3	7.7	3.6	46.8%
Total revenues	\$ 204.1	\$ 148.5	\$ 55.6	37.4%

Total Revenues. Our total revenues were \$204.1 million for the three months ended September 30, 2006 compared to \$148.5 million for the same period in 2005, an increase of \$55.6 million, or 37.4%. Revenues increased for all reportable segments primarily as a result of increased customer demand for our products and services. Total revenues related to Eagle included in our 2006 operating results for the three months ended September 30, 2006 were \$10.5 million.

Equipment Rental Revenues. Our revenues from equipment rentals for the three months ended September 30, 2006 increased \$16.9 million, or 33.5%, to \$67.3 million from \$50.4 million for the same three-month period in 2005. The increase is primarily a result of improved rental rates and larger fleet size. Rental revenues increased for all four core product lines. Revenues from aerial work platforms increased \$13.0 million, cranes increased \$0.6 million, earthmoving increased \$1.2 million, lift trucks increased \$1.0 million and other equipment rentals increased \$1.1 million. Total equipment rental revenues for the three months ended September 30, 2006 related to Eagle included in our 2006 operating results were \$8.2 million. Rental equipment dollar utilization (quarterly rental revenues divided by the average quarterly original rental fleet equipment costs for three months ended September 30) was approximately 42.4% in 2006 compared to 39.9% in 2005.

New Equipment Sales Revenues. Our new equipment sales for the three months ended September 30, 2006 increased \$24.5 million, or 67.7%, to \$60.7 million from \$36.2 million for the comparable period in 2005. Sales of new cranes increased \$18.3 million, aerial work platforms increased \$3.0 million, new earthmoving sales increased \$3.1 million and new lift trucks increased \$1.1 million. Other new equipment sales decreased by \$1.0 million. Total new equipment sales revenues for the three months ended September 30, 2006 related to Eagle included in our 2006 operating results were \$0.3 million.

Used Equipment Sales Revenues. Our used equipment sales increased \$2.9 million, or 10.8%, to \$29.7 million for the three months ended September 30, 2006 from \$26.8 million for the same period in 2005. For the three month period ended September 30, 2006, our used equipment sales from the fleet were approximately 148.2% of net book value compared to 135.8% for the three month period ended September 30, 2005. Total used equipment sales revenues for the three months ended September 30, 2006 related to Eagle included in our 2006 operating results were \$0.7 million.

Parts Sales Revenues. Our parts sales increased \$4.0 million, or 23.5%, to \$21.0 million for the three months ended September 30, 2006 from \$17.0 million in the 2005 comparable period. Of the \$4.0 million increase for the three months ended September 30, 2006, \$0.2 million was attributable to Eagle. The remaining increase was primarily attributable to increased customer demand for parts.

Service Revenues. Our service revenues for the three months ended September 30, 2006 increased \$3.7 million, or 35.6%, to \$14.1 million from \$10.4 million for the same period last year primarily attributable to increased customer demand for service support.

Non-Segmented Revenues. Our non-segmented other revenues consisted primarily of equipment support activities including

Table of Contents

transportation, hauling, parts freight and damage waiver charges. For the three months ended September 30, 2006, our other revenue increased \$3.6 million, or 46.8%, over the same period last year. These support activities increased due to a combination of the increases in charge-out rates and in the volume of our primary business activities, combined with Eagle revenues of \$1.0 million in the current period.

Gross Profit.

	Three Months Ended		Total Dollar Change	Total Percentage Change
	September 30, 2006	September 30, 2005		
	(in millions, except for percentages)			
Segment Gross Profit:				
Equipment rentals	\$ 36.3	\$ 24.0	\$ 12.3	51.3%
New equipment sales	7.4	4.4	3.0	68.2%
Used equipment sales	8.0	6.4	1.6	25.0%
Parts sales	6.1	5.0	1.1	22.0%
Services	9.0	6.4	2.6	40.6%
Non-Segmented gross profit (loss)	1.9	0.6	1.3	216.7%
Total gross profit	\$ 68.7	\$ 46.8	\$ 21.9	46.8%

Total Gross Profit. Our total gross profit was \$68.7 million for the three months ended September 30, 2006 compared to \$46.8 million for the three months ended September 30, 2005, a \$21.9 million, or 46.8%, increase. Gross profit increased primarily as a result of increased rental revenues combined with reduced rental expense. In addition, we were able to sell our used equipment at a higher gross margin largely due to an increase in demand for well-maintained used equipment. Total gross profit margin for three months ended September 30, 2006 was 33.7%, an increase of 2.2% from the 31.5% gross profit margin for the same three-month period in 2005. Total gross profit related to Eagle included in our operating results for the three months ended September 30, 2006 was \$5.1 million. Our gross profit was attributable to:

Equipment Rentals Gross Profit. Our gross profit from equipment rentals for the three months ended September 30, 2006 increased \$12.3 million, or 51.3%, to \$36.3 million from \$24.0 million in the same period in 2005. The increase is primarily a result of an \$16.9 million increase in rental revenue and a \$1.6 million decrease in rental expense. Eagle's rental operations contributed \$4.7 million of the total gross profit increase for the period. These improvements in gross profit were partially offset by a \$6.2 million increase in rental depreciation expense as a result of a larger fleet.

New Equipment Sales Gross Profit. Our new equipment sales gross profit for the three months ended September 30, 2006 increased \$3.0 million, or 68.2%, to \$7.4 million compared to \$4.4 million for the same period last year. The increase in new equipment sales gross profit is primarily attributable to higher new equipment sales revenue and the mix of equipment sold.

Used Equipment Sales Gross Profit. Our used equipment sales gross profit for the three months ended September 30, 2006 increased \$1.6 million, or 25.0%, to \$8.0 million from the \$6.4 million for the same period in 2005, of which Eagle contributed \$0.2 million of the increase. The remaining increase in used equipment sales gross profit was primarily the result of higher used equipment sales, improved margins and the mix of used equipment sold.

Parts Sales Gross Profit. For the three months ended September 30, 2006, our parts sales revenue gross profit increased \$1.1 million, or 22.0%, to \$6.1 million from \$5.0 million for the same period in 2005. The increase was primarily attributable to increased customer demand for parts service.

Service Revenues Gross Profit. For the three months ended September 30, 2006, our service revenues gross profit increased \$2.6 million, or 40.6%, to \$9.0 million from \$6.4 million for the same period in 2005. The increase was

primarily attributable to increased customer demand for service support and improved margins as a result of a continued focus on increasing charge-out rates.

Non-Segmented Revenues Gross Profit. For the three months ended September 30, 2006, our non-segmented revenues gross profit improved \$1.3 million, or 216.7%, on a 46.8% improvement in revenues over the three months ended September 30, 2005. These improvements are largely due to a strategic focus on these equipment support activities.

Selling, General and Administrative Expenses. Selling, general and administrative (SG&A) expenses increased \$5.9 million,

Table of Contents

or 20.9%, to \$34.1 million for the three months ended September 30, 2006 compared to \$28.2 million for the same period last year. The increase was primarily related to increased headcount and higher employee related benefit costs. As a percent of total revenues, SG&A expenses were 16.7% in the third quarter of 2006, down from 19.0% in the prior year, reflecting the fixed cost nature of certain SG&A costs combined with higher revenues in the current year compared to the prior year.

Other Income (Expense). For the three months ended September 30, 2006, our other expense increased by \$39.1 million to \$49.6 million compared to \$10.5 million for the same period in 2005. Included in the current year other income (expense) is a \$40.8 million expense related to the early extinguishment of debt in connection with our refinancing (see discussion below). The remainder of the change reflects \$1.5 million of lower interest expense resulting from a decrease in average outstanding borrowings this year as a result of our February 2006 paydown of outstanding principal balances on our senior secured credit facility from the proceeds of our initial public offering (see note 3 to the condensed consolidated financial statements for further information on our initial public offering). We had no subsequent borrowings under the senior secured credit facility until August 4, 2006. Additionally, the lower interest expense is reflective of the Company's refinancing as further described below. Offsetting these lower interest costs were higher interest costs associated with an increase in our manufacturer flooring plans payables used to finance inventory purchases.

On August 4, 2006, the Company completed their previously announced cash tender offer and consent solicitation for their 11 1/8% senior secured notes due 2012 and 12 1/2% senior subordinated notes due 2013 (collectively, the Notes). Additionally, the Company announced the closing of its previously announced private offering of \$250 million aggregate principal amount of its 8 3/8% senior unsecured notes due 2016 (the New Notes).

Net proceeds to us, after deducting underwriting commissions, totaled approximately \$245.3 million. The Company used the net proceeds of the offering of the New Notes, together with cash on hand and borrowings under its existing senior secured credit facility, to purchase \$195.5 million in aggregate principal amount of the senior secured notes (representing approximately 97.8% of the previously outstanding senior secured notes), and the \$53.0 million in aggregate principal amount of the senior subordinated notes (representing 100% of the previously outstanding senior subordinated notes) that were validly tendered pursuant to the tender offer and consent solicitation. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the senior secured notes was \$217.6 million. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the Senior Subordinated Notes was approximately \$60.1 million. Aggregate offering expenses totaled approximately \$1.9 million.

In connection with the above transactions, the Company recorded a one-time loss on early extinguishment of debt in the quarterly period ended September 30, 2006 of approximately \$40.8 million, or approximately \$32.0 million after-tax, reflecting payment of the \$25.3 million of tender premiums and other estimated costs of \$0.5 million in connection with the tender offer and consent solicitation, combined with the write off of approximately \$5.4 million of unamortized deferred financing costs of the Notes and \$9.6 million of remaining unamortized original issue discount on the Notes.

Income Taxes. Effective with the Company's Reorganization Transactions on February 3, 2006, we are a C-corporation for income tax purposes. Prior to the Reorganization Transactions, we were a limited liability company that elected to be treated as a C-corporation for income tax purposes. At the end of the third quarter of 2005, we had recorded a valuation allowance for the entire amount of our net deferred income tax assets. The valuation allowance was recorded given the cumulative losses incurred and our belief that it was more likely than not that we would not be able to recover the net deferred income tax assets. At the end of the third quarter of 2006, we have a net deferred tax liability, and the valuation allowance has been reversed. Based on available evidence, both positive and negative, we believe our deferred tax assets at September 30, 2006 are fully realizable through future reversals of existing taxable temporary differences and future taxable income, and not subject to any limitations.

The provision for income taxes is based upon the expected effective income tax rate applicable to the full year. The effective income tax rate for the three months ended September 30, 2006 was 21.6%, compared to 0% for the three months ended September 30, 2005. The increase in our effective income tax rate from last year was primarily due to increased taxable income resulting in higher state income tax and federal alternative minimum tax liability and the

reversal of our deferred tax asset valuation allowance in the first quarter of this year.

Table of Contents**Nine Months Ended September 30, 2006 Compared to the Nine Months Ended September 30, 2005 Revenues.**

	Nine Months Ended		Total Dollar Change	Total Percentage Change
	September 30, 2006	September 30, 2005		
	(in millions, except percentages)			
Segment Revenues:				
Equipment rentals	\$ 185.3	\$ 136.6	\$ 48.7	35.6%
New equipment sales	173.3	99.9	73.4	73.5%
Used equipment sales	97.4	76.3	21.1	27.7%
Parts sales	61.6	51.2	10.4	20.3%
Services revenues	39.8	29.4	10.4	35.4%
Non-Segmented revenues	31.5	21.3	10.2	47.9%
Total revenues	\$ 588.9	\$ 414.7	\$ 174.2	42.0%

Total Revenues. Our total revenues were \$588.9 million for the nine months ended September 30, 2006 compared to \$414.7 million for the same nine-month period in 2005, an increase of \$174.2 million, or 42.0%. Revenues increased for all reportable segments primarily as a result of increased customer demand for our products and services. Total revenues related to Eagle included in our 2006 operating results for the nine months ended September 30, 2006 were \$22.6 million.

Equipment Rental Revenues. Our revenues from equipment rentals for the nine months ended September 30, 2006 increased \$48.7 million, or 35.6%, to \$185.3 million from \$136.6 million for the same nine-month period in 2005. The increase is primarily a result of improved rental rates and larger fleet size. Rental revenues increased for all four core product lines. Revenues from aerial work platforms increased \$34.8 million, cranes increased \$3.5 million, earthmoving increased \$5.9 million, lift trucks increased \$2.6 million and other equipment rentals increased \$1.9 million. Total equipment rental revenues for the nine months ended September 30, 2006 related to Eagle included in our 2006 operating results were \$17.8 million. Rental equipment dollar utilization (quarterly rental revenues divided by the average quarterly original rental fleet equipment costs for the nine months ended September 30) was approximately 41.4% in 2006 compared to 37.8% in 2005.

New Equipment Sales Revenues. Our new equipment sales for the nine months ended September 30, 2006 increased \$73.4 million, or 73.5%, to \$173.3 million from \$99.9 million for the comparable period in 2005. Sales of new cranes increased \$45.1 million, aerial work platforms increased \$9.1 million, new earthmoving sales increased \$16.5 million and new lift trucks increased \$1.2 million. Other new equipment sales increased by \$1.5 million. Total new equipment sales revenues related to Eagle for the nine months ended September 30, 2006 included in our 2006 operating results were \$0.4 million.

Used Equipment Sales Revenues. Our used equipment sales increased \$21.1 million, or 27.7%, to \$97.4 million for the nine months ended September 30, 2006 from \$76.3 million for the same period in 2005. In 2006, our used equipment sales from the fleet were approximately 144.3% of net book value compared to 135.8% for the nine month period ended September 30, 2005. Total used equipment sales revenues for the nine months ended September 30, 2006 related to Eagle included in our 2006 operating results were \$1.7 million.

Parts Sales Revenues. Our parts sales increased \$10.4 million, or 20.3%, to \$61.6 million for the nine months ended September 30, 2006 from \$51.2 million in the 2005 comparable period. The increase was primarily attributable to increased customer demand for parts. Parts sales related to Eagle for the period were \$0.3 million.

Service Revenues. Our service revenues for the nine months ended September 30, 2006 increased \$10.4 million, or 35.4%, to \$39.8 million from \$29.4 million for the same period last year primarily attributable to increased customer

demand for service support.

Non-Segmented Revenues. Our non-segmented other revenues consisted primarily of equipment support activities including transportation, hauling, parts freight and damage waiver charges. For the nine months ended September 30, 2006, our other revenue increased \$10.2 million, or 47.9%, over the same period last year. These support activities increased due to a combination of the increases in charge-out rates and in the volume of our primary business activities, combined with Eagle revenues of \$2.2 million in the current period.

Table of Contents**Gross Profit.**

	Nine Months Ended		Total Dollar Change	Total Percentage Change
	September 30, 2006	September 30, 2005		
	(in millions, except for percentages)			
Segment Gross Profit:				
Equipment rentals	\$ 97.2	\$ 62.2	\$ 35.0	56.3%
New equipment sales	21.7	12.1	9.6	79.3%
Used equipment sales	26.1	18.3	7.8	42.6%
Parts sales	18.1	15.1	3.0	19.9%
Services	25.5	18.4	7.1	38.6%
Non-Segmented gross profit (loss)	4.5	(0.4)	4.9	1,225.0%
Total gross profit	\$ 193.1	\$ 125.7	\$ 67.4	53.6%

Total Gross Profit. Our total gross profit was \$193.1 million for the nine months ended September 30, 2006 compared to \$125.7 million for the nine months ended September 30, 2005, a \$67.4 million, or 53.6%, increase. Gross profit increased primarily as a result of increased rental revenues combined with reduced rental expense. In addition, due to the increase in customer demand for new and well-maintained used equipment, we were able to sell our equipment at a higher gross margin. Total gross profit margin for nine months ended September 30, 2006 was 32.8%, an increase of 2.5% from the 30.3% gross profit margin for the same nine-month period in 2005. Total gross profit related to Eagle included in our operating results for the nine months ended September 30, 2006 was \$10.8 million. Our gross profit was attributable to:

Equipment Rentals Gross Profit. Our gross profit from equipment rentals for the nine months ended September 30, 2006 increased \$35.0 million, or 56.3%, to \$97.2 million from \$62.2 million in the same period in 2005. The increase is primarily a result of a \$48.7 million increase in rental revenue and a \$3.6 million decrease in rental expense. Eagle's rental operations contributed \$10.0 million of the total gross profit increase for the period. These improvements in gross profit were offset by a \$17.3 million increase in rental depreciation expense as a result of a larger fleet.

New Equipment Sales Gross Profit. Our new equipment sales gross profit for the nine months ended September 30, 2006 increased \$9.6 million, or 79.3%, to \$21.7 million compared to \$12.1 million for the same period last year. The increase in new equipment sales gross profit is primarily attributable to higher new equipment sales revenue, improved margins and the mix of equipment sold.

Used Equipment Sales Gross Profit. Our used equipment sales gross profit for the nine months ended September 30, 2006 increased \$7.8 million, or 42.6%, to \$26.1 million from the \$18.3 million for the same period in 2005. The increase in used equipment sales gross profit was primarily the result of higher used equipment sales, improved margins and the mix of used equipment sold.

Parts Sales Gross Profit. For the nine months ended September 30, 2006, our parts sales revenue gross profit increased \$3.0 million, or 19.9%, to \$18.1 million from \$15.1 million for the same period in 2005. The increase was primarily attributable to increased customer demand for parts service.

Service Revenues Gross Profit. For the nine months ended September 30, 2006, our service revenues gross profit increased \$7.1 million, or 38.6%, to \$25.5 million from \$18.4 million for the same period in 2005, of which Eagle contributed \$0.1 million of the increase. The remaining increase was primarily attributable to increased customer demand for service support and improved margins.

Non-Segmented Revenues Gross Profit. For the nine months ended September 30, 2006, our non-segmented revenues gross profit was \$4.5 million, an improvement of \$4.9 million over the prior year comparable period, which is primarily due to a 47.9% improvement in revenues over the nine months ended September 30, 2005. These

improvements are largely due to a strategic focus on these equipment support activities.

Selling, General and Administrative Expenses. Selling, general and administrative (SG&A) expenses increased \$27.2 million, or 33.4%, to \$108.5 million for the nine months ended September 30, 2006 compared to \$81.3 million for the same period last year. The increase was primarily related to increased headcount and higher employee related benefit costs combined with a one-time,

Table of Contents

nonrecurring expense of \$8.0 million to terminate a management services agreement in connection with our initial public offering of common stock (see also note 3 to the condensed consolidated financial statements for further information on our initial public offering). As a percent of total revenues, SG&A expenses were 18.4% in 2006 down from 19.6% in the prior year, reflecting the fixed cost nature of certain SG&A costs combined with higher revenues in the current year compared to the prior year, which was largely impacted by the \$8.0 million non-recurring expense item above.

Other Income (Expense). For the nine months ended September 30, 2006, our net other expense increased by \$38.7 million to \$69.4 million compared to \$30.7 million for the same period in 2005. Included in the current year other income (expense) is a \$40.8 million charge related to the early extinguishment of debt in connection with our refinancing (see discussion below). The remainder of the change reflects \$1.7 million of lower interest expense resulting from a decrease in average outstanding borrowings as a result of our February 2006 paydown of outstanding principal balances on our senior secured credit facility from the proceeds of our initial public offering (see note 3 to the condensed consolidated financial statements for further information on our initial public offering). We had no subsequent borrowings under the senior secured credit facility until August 4, 2006. Additionally, the lower interest expense is reflective of the Company's refinancing as further discussed below. Offsetting these lower interest costs were higher interest costs associated with an increase in our manufacturer flooring plans payable used to finance inventory purchases. Additionally, net other income increased \$0.4 million for the comparative periods as a result of interest income earned during the period.

On August 4, 2006, the Company completed their previously announced cash tender offer and consent solicitation for their 11 1/8% senior secured notes due 2012 and 12 1/2% senior subordinated notes due 2013 (collectively, the Notes). Additionally, the Company announced the closing of its previously announced private offering of \$250 million aggregate principal amount of its 8 3/8% senior unsecured notes due 2016 (the New Notes).

Net proceeds to us, after deducting underwriting commissions, totaled approximately \$245.3 million. The Company used the net proceeds of the offering of the New Notes, together with cash on hand and borrowings under its existing senior secured credit facility, to purchase \$195.5 million in aggregate principal amount of the senior secured notes (representing approximately 97.8% of the previously outstanding senior secured notes), and the \$53.0 million in aggregate principal amount of the senior subordinated notes (representing 100% of the previously outstanding senior subordinated notes) that were validly tendered pursuant to the tender offer and consent solicitation. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the senior secured notes was \$217.6 million. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the Senior Subordinated Notes was approximately \$60.1 million. Aggregate offering expenses totaled approximately \$1.9 million.

In connection with the above transactions, the Company recorded a one-time loss on early extinguishment of debt in the quarterly period ended September 30, 2006 of approximately \$40.8 million, or approximately \$32.0 million after-tax, reflecting payment of the \$25.3 million of tender premiums and other estimated costs of \$0.5 million in connection with the tender offer and consent solicitation, combined with the write off of approximately \$5.4 million of unamortized deferred financing costs of the Notes and \$9.6 million of remaining unamortized original issue discount on the Notes.

Income Taxes. Effective with the Company's Reorganization Transactions on February 3, 2006, we are a C-corporation for income tax purposes. Prior to the Reorganization Transactions, we were a limited liability company that elected to be treated as a C-corporation for income tax purposes. At the end of the third quarter of 2005, we had recorded a valuation allowance for the entire amount of our net deferred income tax assets. The valuation allowance was recorded given the cumulative losses incurred and our belief that it was more likely than not that we would not be able to recover the net deferred income tax assets. At the end of the third quarter of 2006, we have a net deferred tax liability, and the valuation allowance has been reversed. Based on available evidence, both positive and negative, we believe our deferred tax assets at September 30, 2006 are fully realizable through future reversals of existing taxable temporary differences and future taxable income, and not subject to any limitations.

The provision for income taxes is based upon the expected effective income tax rate applicable to the full year. The effective income tax rate for the nine months ended September 30, 2006 was 21.3%, compared to 1.3% for the nine

months ended September 30, 2005. The increase in our effective income tax rate was primarily due to increased taxable income resulting in higher state income tax and federal alternative minimum tax liability and the reversal of our deferred tax asset valuation allowance in the first quarter of this year.

Liquidity and Capital Resources

Table of Contents

Cash flow from operating activities. Our cash provided by operating activities for the nine months ended September 30, 2006 was \$71.1 million. Our cash flows from operations were primarily attributable to our reported net income of \$12.2 million, which, when adjusted for non-cash expense items, such as depreciation, deferred income taxes and amortization and gains on the sale of long-lived assets provided positive cash flows of \$97.8 million. These cash flows from operating activities were positively impacted by increases of \$5.5 million in accounts payable and an increase of \$36.3 million in manufacturer flooring plans payable, primarily due to an increase in inventory purchases. Offsetting these positive cash flows from operations were increases in our inventories of \$58.3 and net cash payments of \$8.5 million in deferred compensation liabilities. The increase in our inventories reflects our strategy of maintaining adequate inventories to meet the increasing customer demand.

For the nine months ended September 30, 2005, our cash used by operating activities was \$37.9 million. Our cash flows operations were primarily attributable to our reported net income of \$13.5 million, which, when adjusted for non-cash expense items, such as depreciation, taxes and amortization, and gains on the sale of long-lived assets provided positive cash flows of \$43.7 million.. These cash flows from operating activities were positively impacted by increases of \$19.2 million in accounts payable and an increase of \$11.4 million in manufacturer flooring plans payable, primarily due to an increase in inventory purchases. These cash flows from operating activities were partially offset by increases in our receivables of \$15.3 million, an increase of inventories of \$36.4 million and an increase in prepaid and other assets of \$2.1 million.

Cash flow for investing activities. For the nine months ended September 30, 2006, cash used in our investing activities was \$166.8 million. This is a net result of our acquisition of Eagle (see note 4 to the condensed consolidated financial statements for further information) combined with rental and non-rental equipment purchases of \$187.7 million, offset by \$77.9 million in cash proceeds from the sale of rental and non-rental equipment. For the nine months ended September 30, 2005, cash used in by our investing activities was \$61.2 million. This is a net result of proceeds from the sale of rental and non-rental equipment of \$123.4 million, which was partially offset by purchases totaling \$62.2 million in rental and non-rental equipment.

Cash flow from financing activities. Cash provided by our financing activities for the nine months ended September 30, 2006 was \$95.2 million. We completed an initial public offering of our common stock in February 2006, resulting in total net proceeds to us, after deducting underwriting commissions and other fees and expenses, of approximately \$207.0 million (see note 3 to the condensed consolidated financial statements for further information related to our initial public offering).

As discussed above, the Company completed its refinancing in August 2006. Net proceeds to us, after deducting underwriting commissions, totaled approximately \$245.3 million. The Company used the net proceeds of the offering of the New Notes, together with cash on hand and borrowings under its existing senior secured credit facility, to purchase \$195.5 million in aggregate principal amount of the senior secured notes (representing approximately 97.8% of the previously outstanding senior secured notes), and the \$53.0 million in aggregate principal amount of the senior subordinated notes (representing 100% of the previously outstanding senior subordinated notes) that were validly tendered pursuant to the tender offer and consent solicitation. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the senior secured notes was \$217.6 million. The total principal amount, accrued and unpaid interest, consent fee amounts and premiums paid for the Senior Subordinated Notes was approximately \$60.1 million. Aggregate offering expenses totaled approximately \$1.9 million.

For the current year nine-month period, our total borrowings under the amended senior secured credit facility were \$718.8 million and total payments under the amended senior secured credit facility were \$799.0 million. Financing costs paid in cash related to Amendment No. 11 to our senior secured credit facility totaled \$0.2 million and \$1.6 million in financing costs were paid related to the amended and restated senior credit facility.

For the nine months ended September 30, 2005, cash provided by our financing activities was \$24.4 million. For the nine months ended September 30, 2005, our total borrowings under the amended senior secured credit facility were \$424.9 million and total payments under the amended senior secured credit facility in the same period were \$399.0 million. Payments on capital leases and other notes payable were \$1.3 million.

Senior Secured Credit Facility Amendments

Edgar Filing: H&E Equipment Services, Inc. - Form 10-Q

On February 3, 2006, the senior secured credit agreement, dated June 17, 2002, as amended, by and among the Company, Great Northern Equipment, Inc. (together with the Company, the Borrowers), GNE Investments, Inc., H&E Finance Corp., General Electric Capital Corporation and the Lenders party thereto (the Credit Agreement), was amended primarily to (1) approve, as described elsewhere in this Quarterly Report on Form 10-Q, the merger of H&E Holdings and H&E LLC with and into H&E

Table of Contents

Equipment Services, Inc., with H&E Equipment Services, Inc. surviving the reincorporation merger as the operating company, and to effectuate H&E Equipment Services, Inc. as a Borrower under the terms of the senior secured credit facility; and (2) require the proceeds of certain stock and debt issuances in excess of \$1,000,000 in the aggregate be used to prepay amounts outstanding under the senior secured credit facility in an amount equal to such proceeds. We did not pay an amendment fee relating to this amendment.

In February 2006, we used a portion of the proceeds from our initial public offering to repay \$96.6 million of outstanding indebtedness under the senior secured credit facility, and we paid accrued interest in the amount of \$0.2 million in March 2006.

On March 20, 2006, the senior secured credit agreement was further amended to (1) adjust the Applicable Revolver Index Margin, the Applicable Revolver LIBOR Margin and the Applicable L/C Margin to reflect tiered pricing based upon our monthly computed Leverage Ratio applied on a prospective basis commencing at least one day after the date of delivery to the Lenders of the monthly unaudited Financial Statements beginning after March 31, 2006; (2) adjust the Applicable Unused Line Fee Margin to reflect tiered pricing based upon our Excess Availability Percentage computed on the first day of a calendar month applied on a prospective basis commencing with the first adjustment to the Applicable Revolver Index Margin and Applicable Revolver LIBOR Margin; (3) eliminate the \$16.5 million block on availability of assets; (4) revise the financial covenants to (i) add a covenant requiring maintenance of a minimum Fixed Charge Coverage Ratio of 1.10 to 1.00, which is tested at the end of each fiscal month only if a Covenant Liquidity Event has occurred and is then continuing and (ii) eliminate all other Financial Covenants; and (5) revise the definitions of various other capitalized terms contained within the original senior secured credit agreement. In connection with this amendment, we paid fees to the Lenders of \$190,000.

As of July 12, 2006, we were granted a waiver under our senior secured credit agreement pursuant to which our lenders under our senior secured credit agreement waived our non-compliance with, and the effects of our non-compliance under, various representations and non-financial covenants contained in the senior secured credit agreement affected by the accounting adjustment in connection with the restatement as further described in note 10 to our consolidated financial statements included elsewhere in this in this Quarterly Report on Form 10-Q. As a result of the restatement, among other things, we would no longer be able to make the representations under our senior secured credit agreement concerning the conformity with GAAP of our previously delivered financial statements, or confirm our prior compliance with certain obligations concerning the maintenance of our books and records in accordance with GAAP. Because the restatement does not result in our having breached the financial covenant in the senior secured credit agreement, the waiver does not waive or modify the financial covenant. As a result of the waiver, we continue to have full access to our revolving credit facility under the senior secured credit agreement.

On August 4, 2006, the Company entered into an Amended and Restated Credit Agreement (the Amended Credit Agreement), amending and restating the Company's senior secured credit agreement primarily to, (i) increase the principal amount of availability of the credit facility from \$165.0 million to \$250.0 million, (ii) reduce the applicable unused line fee margin in respect of undrawn commitments to 0.25%, (iii) increase the advance rate on rental fleet assets from the lesser of 100% of net book value or 80% of orderly liquidation value to the lesser of 100% of net book value or 85% of orderly liquidation value, (iv) extend the maturity date of the facility from February 10, 2009 to August 4, 2011 and (v) add H&E Equipment Services (California), LLC was added as a borrower. Furthermore, the Amended Credit Agreement changed the measurement frequency of our computed Leverage Ratio from a monthly calculation to a quarterly calculation. The Company paid \$1.4 million to the Lenders in connection with this Amended Credit Agreement and incurred other transaction costs of approximately \$0.2 million. As of November 8, 2006, we had \$18.9 million of outstanding borrowings under our senior secured credit facility with \$222.9 million of additional borrowing availability, net of \$8.3 million of issued standby letters of credit. As of September 30, 2006, the Company was in compliance with its financial covenant under the Amended Credit Agreement.

Cash Requirements Related to Operations

Our principal sources of liquidity have been from cash provided by operations and the sales of new, used and rental fleet equipment, proceeds from the issuance of debt, and borrowings available under our amended and restated senior secured credit facility. In February 2006, we also completed an initial public offering of our common stock (see note 3 to the condensed consolidated financial statements for further information)..

Our principal uses of cash have been to fund operating activities and working capital, purchase of rental fleet equipment and property and equipment, fund payments due under operating leases and manufacturer flooring plans payable, and to meet debt service requirements. In February 2006, we completed the Eagle acquisition (see note 4 to the condensed consolidated financial statements for further information). In the future, we may pursue additional strategic acquisitions. We anticipate that these uses will be the principal demands on our cash in the future.

Table of Contents

The amount of our future capital expenditures will depend on a number of factors including general economic conditions and growth prospects. Our gross rental fleet capital expenditures for the nine months ended September 30, 2006 were \$198.4 million, including \$24.0 million of non-cash transfers from new and used equipment to rental fleet inventory, primarily to replace the rental fleet equipment we sold during the period. Our gross property and equipment capital expenditures for the nine months ended September 30, 2006 were \$13.4 million. We anticipate that our gross rental fleet capital expenditures for the remainder of 2006 will be used to primarily replace the rental fleet equipment we anticipate selling during 2006 as well as to meet increased demand. We anticipate that we will fund these rental fleet capital expenditures with the proceeds from the sales of new, used and rental fleet equipment, cash flow from operations and, if required, from borrowings under our senior secured credit facility. In response to changing economic conditions, we believe we have the flexibility to modify our capital expenditures by adjusting them (either up or down) to match our actual performance. If we pursue any other strategic acquisitions during 2006, we may need to access available borrowings under our senior secured debt.

To service our debt, we will require a significant amount of cash. Our ability to pay interest and principal on our indebtedness (including the senior unsecured notes, the senior secured notes and obligations under the senior secured credit facility) and to satisfy our other debt obligations, will depend upon our future operating performance and the availability of borrowings under our senior secured credit facility and/or other debt and equity financing alternatives available to us, which will be affected by prevailing economic conditions and financial, business and other factors, some of which are beyond our control. Based on our current level of operations, we believe our cash flow from operations, available cash and available borrowings under the senior secured credit facility will be adequate to meet our future liquidity needs for the foreseeable future.

We cannot provide absolute assurance that our future cash flow from operations will be sufficient to meet our long-term obligations and commitments. If we are unable to generate sufficient cash flow from operations in the future to service our indebtedness and to meet our other commitments, we will be required to adopt one or more alternatives, such as refinancing or restructuring our indebtedness, selling material assets or operations or seeking to raise additional debt or equity capital. We cannot assure that any of these actions could be effected on a timely basis or on satisfactory terms or at all, or that these actions would enable us to continue to satisfy our capital requirements. In addition, our existing or future debt agreements, including the indentures and the amended senior secured credit facility, contain restrictive covenants, which may prohibit us from adopting any of these alternatives. Our failure to comply with these covenants could result in an event of default which, if not cured or waived, could result in the accelerations of all of our debt.

Contractual and Commercial Commitments Summary

Our contractual obligations and commercial commitments principally include obligations associated with our outstanding indebtedness and interest payments as of September 30, 2006. Amounts for 2006 represent the period October 1, 2006 through December 31, 2006.

	Total	Payments Due by Year			Thereafter
		2006	2007-2008	2009-2010	
		(Dollars in thousands)			
Long-term debt (including senior secured and senior unsecured notes payable)	\$ 254,882	\$ 31	\$ 303	\$ 48	\$ 254,500
Interest payments on senior secured notes (1)	2,936	183	1,001	1,001	751
Interest payments on senior unsecured notes (1)	208,340		40,840	41,875	125,625
Senior secured credit facility	26,265				26,265
Interest payments on senior secured credit facility (2)	1,149	59	474	474	142
	825	75	600	150	

Related party obligation (including interest) (3)					
Operating leases (4)	38,848	2,143	12,877	7,626	16,202
Other long-term obligations (5)	132,612	5,086	53,048	73,250	1,228
Total contractual cash obligations	\$ 665,857	\$ 7,577	\$ 109,143	\$ 124,424	\$ 424,713

(1) Future interest payments are calculated based on the assumption that all debt is outstanding until maturity. For debt instruments with variable interest rates, interest has been calculated for all periods using rates in effect on September 30, 2006.

(2) Future interest payments are calculated based on the assumption that all debt is outstanding until maturity. For debt instruments with variable interest rates, interest has been calculated for all future periods using rates in effect on September 30, 2006.

Table of Contents

- (3) Payments under the consulting and non-competition agreement with Mr. Thomas Engquist.
- (4) This includes total operating lease rental payments (including interest) having initial or remaining non-cancelable lease terms longer than one year.
- (5) Includes \$130.0 million in manufacturer flooring plans payable, which is used by the Company to finance purchases of inventory and rental equipment.

Additionally, as of September 30, 2006, we have standby letters of credit totaling \$8.3 million that expire in December 2006 and September 2007.

Seasonality

Although our business is not significantly impacted by seasonality, the demand for our rental equipment tends to be lower in the winter months. The level of equipment rental activities are directly related to commercial and industrial construction and maintenance activities. Therefore, equipment rental performance will be correlated to the levels of current construction activities. The severity of weather conditions can have a temporary impact on the level of construction activities.

Equipment sales cycles are also subject to some seasonality with the peak selling period during the spring season and extending through the summer. Parts and service activities are less affected by changes in demand caused by seasonality.

Inflation

Although we cannot accurately anticipate the effect of inflation on our operations, we believe that inflation has not had for the periods covered by this Quarterly Report on Form 10-Q, and is not likely in the foreseeable future to have, a material impact on our results of operations.

Acquisitions

We completed, effective as of February 28, 2006, the previously announced acquisition of all of the capital stock of Eagle High Reach Equipment, Inc. and all of the equity interests of its subsidiary, Eagle High Reach Equipment, LLC. See note 4 to the condensed consolidated financial statements in Part I, Item 1 of this Quarterly Report on Form 10-Q for further information on this acquisition. The Eagle purchase price was funded out of the proceeds from our recently completed initial public offering. Prior to our acquisition, Eagle was a privately-held construction and industrial equipment rental company. Eagle serves the southern California construction and industrial markets out of four locations.

We periodically engage in evaluations of potential acquisitions and start-up facilities. The success of our growth strategy depends, in part, on selecting strategic acquisition candidates at attractive prices and identifying strategic start-up locations. We expect to face competition for acquisition candidates, which may limit the number of acquisition opportunities and lead to higher acquisition costs. We may not have the financial resources necessary to consummate any acquisitions or to successfully open any new facilities in the future or the ability to obtain the necessary funds on satisfactory terms. For further information regarding our risks related to acquisitions, see Item 1A of Part I of our Annual Report on Form 10-K for the year ended December 31, 2005.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our earnings are affected by changes in interest rates due to the fact that interest on the amended senior secured credit facility is calculated based upon LIBOR plus 150 basis points as of September 30, 2006. At September 30, 2006, we had \$26.3 million under our senior secured credit facility. The average interest rate in effect on those borrowings at September 30, 2006 was 8.03%. A 1.0% increase in the effective rate on our outstanding borrowings of \$26.3 million would increase our interest expense by \$0.3 million on an annualized basis. We do not have significant exposure to changing interest rates on our fixed-rate senior secured notes, senior unsecured notes or on our other notes payables.

Item 4. Controls and Procedures

Management's Quarterly Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated

Table of Contents

to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required financial disclosure.

Our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively) have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our principal executive officer and principal financial officer have concluded that, as of September 30, 2006, the Company's disclosure controls and procedures are effective to provide reasonable assurance that material information required to be included in our periodic SEC reports is recorded, processed, summarized and reported within the time periods specified in rules and forms.

The design of any system of control is based upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated objectives under all future events, no matter how remote, or that the degree of compliance with the policies or procedures may not deteriorate. Because of its inherent limitations, disclosure controls and procedures may not prevent or detect all misstatements. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

Changes in Internal Controls

In connection with our initial public offering of common stock completed during the quarter ended March 31, 2006, we accounted for a one-time, nonrecurring payment, as a direct cost of the initial public offering, and as such, the payment was reflected as a charge to stockholders' equity in our unaudited interim financial statements for the three months ended March 31, 2006. Management concluded, after further review and consultation with BDO Seidman, LLP, our independent registered public accounting firm, that the payment should not be accounted for as a direct cost of the initial public offering and should instead be reflected as an expense in our consolidated income statement for the three months ended March 31, 2006. Management and our Audit Committee concluded to restate our unaudited interim financial statements for the three months ended March 31, 2006 to properly record and report the correct accounting treatment of this payment. Such restatement is contained in the Company's Form 10-Q/A for the quarterly period ended March 31, 2006, as filed with the SEC on July 14, 2006. To the extent we engage in non-routine transactions in the future, our disclosure controls and procedures now include consulting as appropriate with outside qualified consultants and performing additional levels of review by the Company's accounting personnel. Except for the item described above, there have been no changes during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION**Item 1. Legal Proceedings.**

We are party to various litigation matters, in most cases involving normal ordinary course and routine claims incidental to our business. We cannot estimate with certainty our ultimate legal and financial liability with respect to such pending matters. However, we believe, based on our examination of such pending matters, that our ultimate liability for such matters will not have a material adverse effect on our business or financial condition.

Item 1A. Risk Factors.

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A.- Risk Factors, in our Annual Report on Form 10-K for the year ended December 31, 2005, as well as the factors discussed in our Quarterly Report on Form 10-Q for the three month period ended June 30, 2006, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K and in our Quarterly Report on Form 10-Q for the three month period ended June 30, 2006, are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Table of Contents

Item 3. Defaults upon Senior Securities.

None.

Item 4. Submission of Matters to a Vote of Security Holders.

None.

Item 5. Other information.

None.

Table of Contents

Item 6. Exhibits.

A. Exhibits

31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

32.1 Certification pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).

SIGNATURES

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

H&E EQUIPMENT SERVICES, INC.

Dated: November 14, 2006

By: /s/ JOHN M. ENGQUIST
John M. Engquist
Chief Executive Officer
(Principal Executive Officer)

Dated: November 14, 2006

By: /s/ LESLIE S. MAGEE
Leslie S. Magee
Chief Financial Officer
(Principal Financial and Accounting Officer)

Table of Contents

EXHIBIT INDEX

31.1 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

31.2 Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).

32.1 Certification pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).