

POWELL INDUSTRIES INC  
Form 10-Q  
August 08, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2012

OR

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

Commission File Number 001-12488

**Powell Industries, Inc.**

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(Exact name of registrant as specified in its charter)

<b>Delaware</b> (State or other jurisdiction of incorporation or organization)	<b>88-0106100</b> (I.R.S. Employer Identification No.)
<b>8550 Mosley Drive,</b>  <b>Houston, Texas</b> (Address of principal executive offices)	<b>77075-1180</b> (Zip Code)
<b>Registrant's telephone number, including area code:</b>	
<b>(713) 944-6900</b>	

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  No

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

At July 26, 2012, there were 11,870,673 outstanding shares of the registrant's common stock, par value \$0.01 per share.

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**POWELL INDUSTRIES, INC. AND SUBSIDIARIES**

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**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Condensed Consolidated Financial Statements****POWELL INDUSTRIES, INC. AND SUBSIDIARIES****Condensed Consolidated Balance Sheets****(In thousands, except share and per share data)**

	<b>June 30, 2012</b>	<b>September 30, 2011</b>
	<b>(Unaudited)</b>	
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 106,835	\$ 123,466
Cash held in escrow		1,000
Accounts receivable, less allowance for doubtful accounts of \$1,096 and \$391, respectively	106,872	109,317
Costs and estimated earnings in excess of billings on uncompleted contracts	87,036	51,568
Inventories, net	40,616	36,640
Income taxes receivable	301	4,071
Deferred income taxes	4,189	3,580
Prepaid expenses and other current assets	3,702	7,040
<b>Total Current Assets</b>	<b>349,551</b>	<b>336,682</b>
Property, plant and equipment, net	77,269	59,637
Goodwill	1,003	1,003
Intangible assets, net	13,749	15,847
Other assets	7,909	8,507
<b>Total Assets</b>	<b>\$ 449,481</b>	<b>\$ 421,676</b>
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities:		
Current maturities of long-term debt and capital lease obligations	\$ 836	\$ 1,140
Income taxes payable	1,715	881
Accounts payable	54,827	56,893
Accrued salaries, bonuses and commissions	24,071	22,314
Billings in excess of costs and estimated earnings on uncompleted contracts	53,414	44,523
Accrued product warranty	4,427	4,603
Other accrued expenses	6,281	7,370
<b>Total Current Liabilities</b>	<b>145,571</b>	<b>137,724</b>
Long-term debt and capital lease obligations, net of current maturities	3,646	4,301
Deferred compensation	2,870	3,242
Other liabilities	1,069	1,066
<b>Total Liabilities</b>	<b>153,156</b>	<b>146,333</b>
Commitments and Contingencies (Note I)		
Equity:		
Stockholders' Equity:		
Preferred stock, par value \$.01; 5,000,000 shares authorized; none issued		

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Common stock, par value \$.01; 30,000,000 shares authorized; 11,869,873 and 11,752,393 shares issued and outstanding, respectively	119	117
Additional paid-in capital	37,623	34,343
Retained earnings	260,067	242,254
Accumulated other comprehensive income (loss)	(1,484)	(1,371)
<b>Total Stockholders' Equity</b>	<b>296,325</b>	<b>275,343</b>
Total Liabilities and Equity	\$ 449,481	\$ 421,676

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

**Table of Contents****POWELL INDUSTRIES, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Operations (Unaudited)****(In thousands, except per share data)**

	Three Months Ended		Nine Months Ended	
	June 30, 2012	June 30, 2011	June 30, 2012	June 30, 2011
Revenues	\$ 194,093	\$ 141,369	\$ 533,035	\$ 391,153
Cost of goods sold	150,250	119,505	434,577	318,548
Gross profit	43,843	21,864	98,458	72,605
Selling, general and administrative expenses	24,826	19,410	66,112	61,876
Amortization of intangible assets	704	1,237	2,111	3,658
Operating income	18,313	1,217	30,235	7,071
Gain on sale of investment				(1,229)
Interest expense	59	88	203	296
Interest income	(25)	(66)	(88)	(173)
Income before income taxes	18,279	1,195	30,120	8,177
Income tax provision	6,141	1,122	12,316	3,940
Net income	\$ 12,138	\$ 73	\$ 17,804	\$ 4,237
Earnings per share:				
Basic	\$ 1.03	\$ 0.01	\$ 1.51	\$ 0.36
Diluted	\$ 1.02	\$ 0.01	\$ 1.50	\$ 0.36
Weighted average shares:				
Basic	11,812	11,740	11,782	11,730
Diluted	11,861	11,812	11,834	11,806

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

**Table of Contents****POWELL INDUSTRIES, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Cash Flows (Unaudited)**

(In thousands)

	Nine Months Ended	
	June 30, 2012	June 30, 2011
<b>Operating Activities:</b>		
Net income	\$ 17,804	\$ 4,237
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation	7,703	7,790
Amortization	2,121	3,708
Stock-based compensation	894	1,117
Bad debt expense	509	82
Deferred income taxes	(273)	(5,440)
Gain on sale of investment in joint venture		(1,229)
Changes in operating assets and liabilities:		
Accounts receivable	2,071	(14,151)
Costs and estimated earnings in excess of billings on uncompleted contracts	(35,423)	(4,862)
Inventories	(3,961)	(2,612)
Prepaid expenses and other current assets	7,109	3,795
Accounts payable and income taxes payable	(1,257)	7,462
Accrued liabilities	490	(10,910)
Billings in excess of costs and estimated earnings on uncompleted contracts	8,880	33,511
Other	(208)	2,743
<b>Net cash provided by operating activities</b>	<b>6,459</b>	<b>25,241</b>
<b>Investing Activities:</b>		
Proceeds from sale of fixed assets	158	308
Purchases of property, plant and equipment	(25,546)	(4,072)
Decrease in cash held in escrow	1,000	
Proceeds from sale of investment in joint venture		1,229
<b>Net cash used in investing activities</b>	<b>(24,388)</b>	<b>(2,535)</b>
<b>Financing Activities:</b>		
Borrowings on Canadian revolving line of credit	7,992	4,947
Payments on Canadian revolving line of credit	(7,992)	(4,955)
Payments on industrial development revenue bonds	(400)	(400)
Short-term and other financing	1,822	(250)
<b>Net cash provided by (used in) financing activities</b>	<b>1,422</b>	<b>(658)</b>
Net (decrease) increase in cash and cash equivalents	(16,507)	22,048
Effect of exchange rate changes on cash and cash equivalents	(124)	(135)
Cash and cash equivalents at beginning of period	123,466	115,353
<b>Cash and cash equivalents at end of period</b>	<b>\$ 106,835</b>	<b>\$ 137,266</b>

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





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**POWELL INDUSTRIES, INC. AND SUBSIDIARIES**

*Notes to Condensed Consolidated Financial Statements (Unaudited)*

A. OVERVIEW AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

*Overview*

Powell Industries, Inc. (we, us, our, Powell or the Company) was incorporated in the state of Delaware in 2004 as a successor to a Nevada company incorporated in 1968. The Nevada corporation was the successor to a company founded by William E. Powell in 1947, which merged into the Company in 1977. Our major subsidiaries, all of which are wholly-owned, include: Powell Electrical Systems, Inc.; Transdyn, Inc.; Powell Industries International, Inc.; Switchgear & Instrumentation Limited (S&I) and Powell Canada Inc.

We develop, design, manufacture and service custom engineered-to-order equipment and systems for the management and control of electrical energy and other critical processes. Headquartered in Houston, Texas, we serve the transportation, environmental, energy, industrial and utility industries.

*Basis of Presentation*

These unaudited condensed consolidated financial statements include the accounts of Powell and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

These unaudited condensed consolidated financial statements have been prepared pursuant to the rules of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures, normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP), have been condensed or omitted pursuant to those rules and regulations. We believe that the disclosures made are adequate to make the information presented not misleading. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly state the financial position, results of operations and cash flows with respect to the interim consolidated financial statements have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year. The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP.

These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto of Powell and its subsidiaries included in Powell's Annual Report on Form 10-K for the year ended September 30, 2011, which was filed with the SEC on December 12, 2011.

*Use of Estimates*

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying footnotes. The most significant estimates used in our financial statements affect revenue and cost recognition for construction contracts, the allowance for doubtful accounts, provision for excess and obsolete inventory, goodwill and other intangible assets, self-insurance, warranty accruals, income taxes and estimates related to acquisition valuations. The amounts recorded for insurance claims, warranties, legal, income taxes and other contingent liabilities require judgments regarding the amount of expenses that will ultimately be incurred. We base our estimates on historical experience and on various other assumptions, as well as the specific circumstances surrounding these contingent liabilities, in evaluating the amount of liability that should be recorded. Estimates may change as new events occur, additional information becomes available or operating environments change. Actual results may differ from our estimates.

*New Accounting Standards*

In January 2010, the Financial Accounting Standards Board (FASB) issued updated guidance to amend the disclosure requirements related to recurring and nonrecurring fair value measurements. This update requires new disclosures about significant transfers of assets and liabilities between Level 1 and Level 2 of the fair value hierarchy (including the reasons for these transfers) and the reasons for any transfers in or out of Level 3. This update also requires a reconciliation of recurring Level 3 measurements about purchases, sales, issuances and settlements on a gross basis. In addition to these new disclosure requirements, this update clarifies certain



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existing disclosure requirements. For example, this update clarifies that reporting entities are required to provide fair value measurement disclosures for each class of assets and liabilities, rather than each major category of assets or liabilities. This update also clarifies the requirement for entities to disclose information about both the valuation techniques and inputs used in estimating Level 2 and Level 3 fair value measurements. This update became effective for us with the interim and annual reporting period beginning after December 15, 2009, our fiscal year 2011, except for the requirement to provide the Level 3 activity of purchases, sales, issuances and settlements on a gross basis, which became effective for us with the interim and annual reporting period beginning after December 15, 2010, our fiscal year 2012. We are not required to provide the amended disclosures for any previous periods presented for comparative purposes. Other than requiring additional disclosures, adoption of this update did not have a material impact on our consolidated financial statements.

In May 2011, the FASB issued accounting guidance related to fair value measurement, which amends current guidance to achieve common fair value measurement and disclosure requirements in U.S. GAAP and International Financial Reporting Standards. This guidance generally represents clarification of fair value measurement standards, but also includes instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed. This guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. We will adopt this guidance for our fiscal year beginning October 1, 2012. We do not expect this pronouncement to have a material effect on our consolidated financial statements.

In June 2011, the FASB issued new accounting guidance on the presentation of comprehensive income in financial statements. Entities are required to present total comprehensive income either in a single, continuous statement of comprehensive income or in two separate, but consecutive, statements. Under the single-statement approach, entities must include the components of net income, a total for net income, the components of other comprehensive income and a total for comprehensive income. Under the two-statement approach, entities must report an income statement and, immediately following, a statement of other comprehensive income. This new guidance will be effective for us beginning October 1, 2012, and will have financial presentation changes only.

In September 2011, the FASB issued new accounting guidance which simplifies how an entity is required to test goodwill for impairment. Under this guidance, an entity would be allowed to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. An entity would not be required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more likely than not that its fair value is less than its carrying amounts. This new guidance includes a number of factors to consider in conducting the qualitative assessment. This guidance is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, our fiscal year 2013. Early adoption is permitted; however, we will not adopt this guidance until October 1, 2012. This guidance is not expected to have a material impact on our reported results of operations or financial position.

In July 2012, the FASB issued an accounting standards update regarding the testing of indefinite-lived intangible assets for impairment. Under this update, an entity has the option to first assess qualitative factors to determine whether the existence of events and circumstances indicate that it is more likely than not that the indefinite-lived intangible asset is impaired. If, after assessing the events and circumstances, an entity concludes that it is more likely than not that the indefinite-lived intangible asset is impaired, then the entity is not required to take further action. However, if an entity concludes otherwise, it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment testing by comparing the fair value with the carrying amount. An entity also has the option to bypass the qualitative assessment for any indefinite-lived intangible asset in any period and proceed directly to performing the quantitative test. An entity will be able to resume performing the qualitative assessment in any subsequent period. This update is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012, our fiscal year 2013. Early adoption is permitted; however, we will not adopt this guidance until October 1, 2012. This guidance is not expected to have a material impact on our reported results of operations or financial position.

### *Subsequent Events*

We evaluated subsequent events through the time of filing this Quarterly Report on Form 10-Q. No significant events occurred subsequent to the balance sheet or prior to the filing of this report that would have a material impact on our consolidated financial statements or results of operations taken as a whole.

## B. FAIR VALUE MEASUREMENTS

We measure certain financial assets and liabilities at fair value. Fair value is defined as an exit price which represents the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in valuing an asset or liability. The accounting guidance requires the use of valuation techniques to measure fair value that maximize the use of observable inputs and minimize the use of unobservable inputs. As a basis for considering such assumptions and inputs, a fair value hierarchy has been established

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which identifies and prioritizes three levels of inputs to be used in measuring fair value.

The three levels of the fair value hierarchy are as follows:

Level 1 Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Inputs other than the quoted prices in active markets that are observable either directly or indirectly, including: quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active or other inputs that are observable or can be corroborated by observable market data.

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Level 3 Unobservable inputs that are supported by little or no market data and require the reporting entity to develop its own assumptions.

The following table summarizes the fair value of our assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2012 (in thousands):

	Fair Value Measurements at June 30, 2012			Fair Value at June 30, 2012
	Quoted Prices in	Significant Other	Significant	
	Active Markets for	Observable	Unobservable	
	Identical Assets (Level 1)	Inputs (Level 2)	Inputs (Level 3)	
<b>Assets</b>				
Cash equivalents	\$ 45,768	\$	\$	\$ 45,768
Foreign currency forward contracts		10		10
<b>Total</b>	<b>\$ 45,768</b>	<b>\$ 10</b>	<b>\$</b>	<b>\$ 45,778</b>
<b>Liabilities</b>				
Foreign currency forward contracts	\$	\$	\$	\$
<b>Total</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>

The following table summarizes the fair value of our assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2011 (in thousands):

	Fair Value Measurements at September 30, 2011			Fair Value at September 30, 2011
	Quoted Prices in	Significant Other	Significant	
	Active Markets for	Observable	Unobservable	
	Identical Assets (Level 1)	Inputs (Level 2)	Inputs (Level 3)	
<b>Assets</b>				
Cash equivalents	\$ 65,792	\$	\$	\$ 65,792
<b>Total</b>	<b>\$ 65,792</b>	<b>\$</b>	<b>\$</b>	<b>\$ 65,792</b>
<b>Liabilities</b>				
Foreign currency forward contracts	\$	\$	\$	\$
<b>Total</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>

Cash equivalents, primarily funds held in money market savings instruments, are reported at their current carrying value which approximates fair value due to the short-term nature of these instruments and are included in cash and cash equivalents in our Condensed Consolidated Balance Sheets.

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Foreign currency forward contracts are valued using an income approach which consists of a discounted cash flow model that takes into account the present value of future cash flows under the terms of the contracts using observable market spot and forward rates as of our reporting date, and are included in Level 2 inputs in the above table. We use these derivative instruments to mitigate non-functional currency transaction exposure on certain contracts with customers and vendors. We mitigate derivative credit risk by transacting with highly rated counterparties. We have evaluated the credit and non-performance risks associated with our derivative counterparties and believe them to be insignificant at June 30, 2012. All contracts are recorded at fair value and marked-to-market at the end of each reporting period, with unrealized gains and losses being included in accumulated other comprehensive income on our Condensed Consolidated Balance Sheets for that period. See Note H for further discussion regarding our derivative instruments.

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## C. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share data):

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2012	2011	2012	2011
<i>Numerator:</i>				
Net income attributable to Powell Industries, Inc.	\$ 12,138	\$ 73	\$ 17,804	\$ 4,237
<i>Denominator:</i>				
Weighted average basic shares	11,812	11,740	11,782	11,730
Dilutive effect of stock options and restricted stock units	49	72	52	76
Weighted average diluted shares with assumed conversions	11,861	11,812	11,834	11,806
<i>Net earnings per share:</i>				
Basic	\$ 1.03	\$ 0.01	\$ 1.51	\$ 0.36
Diluted	\$ 1.02	\$ 0.01	\$ 1.50	\$ 0.36

All options were included in the computation of diluted earnings per share for the three and nine months ended June 30, 2012 and 2011, respectively, as the options exercise price was less than the average market price of our common stock.

## D. DETAIL OF SELECTED BALANCE SHEET ACCOUNTS

*Allowance for Doubtful Accounts*

Activity in our allowance for doubtful accounts receivable consisted of the following (in thousands):

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2012	2011	2012	2011
Balance at beginning of period	\$ 1,043	\$ 1,508	\$ 391	\$ 907
Increase (decrease) to bad debt expense	(127)	(524)	509	82
Deductions for uncollectible accounts written off, net of recoveries	175	(221)	175	(225)
Increase (decrease) due to foreign currency translation	5	(4)	21	(5)
Balance at end of period	\$ 1,096	\$ 759	\$ 1,096	\$ 759

*Warranty Accrual*

Activity in our product warranty accrual consisted of the following (in thousands):

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	Three Months Ended		Nine Months Ended	
	June 30,		June 30,	
	2012	2011	2012	2011
Balance at beginning of period	\$ 4,783	\$ 5,763	\$ 4,603	\$ 5,929
Increase (decrease) to warranty expense	752	(148)	2,084	759
Deductions for warranty charges	(1,068)	(728)	(2,254)	(1,961)
Increase (decrease) due to foreign currency translation	(40)	191	(6)	351
Balance at end of period	\$ 4,427	\$ 5,078	\$ 4,427	\$ 5,078

*Inventories*

The components of inventories are summarized below (in thousands):

	June 30, 2012	September 30, 2011
Raw materials, parts and subassemblies	\$ 41,207	\$ 38,400
Work-in-progress	7,967	5,892
Provision for excess and obsolete inventory	(8,558)	(7,652)
Total inventories	\$ 40,616	\$ 36,640



**Table of Contents***Cost and Estimated Earnings on Uncompleted Contracts*

The components of costs and estimated earnings and related amounts billed on uncompleted contracts are summarized below (in thousands):

	June 30, 2012	September 30, 2011
Costs incurred on uncompleted contracts	\$ 528,599	\$ 475,525
Estimated earnings	160,668	131,367
	689,267	606,892
Less: Billings to date	655,645	599,847
<b>Net underbilled position</b>	<b>\$ 33,622</b>	<b>\$ 7,045</b>
Included in the accompanying balance sheets under the following captions:		
Costs and estimated earnings in excess of billings on uncompleted contracts underbilled	\$ 87,036	\$ 51,568
Billings in excess of costs and estimated earnings on uncompleted contracts overbilled	(53,414)	(44,523)
<b>Net underbilled position</b>	<b>\$ 33,622</b>	<b>\$ 7,045</b>

**E. OTHER INTANGIBLE ASSETS**

Intangible assets balances, subject to amortization, at June 30, 2012 and September 30, 2011 consisted of the following (in thousands):

	June 30, 2012			September 30, 2011		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
<b>Supply agreement</b>						
Balance, beginning of period	\$ 17,580	\$ (6,052)	\$ 11,528	\$ 17,580	\$ (4,881)	\$ 12,699
Amortization		(879)	(879)		(1,171)	(1,171)
Balance, end of period	\$ 17,580	\$ (6,931)	\$ 10,649	\$ 17,580	\$ (6,052)	\$ 11,528
<b>Purchased technology</b>						
Balance, beginning of period	\$ 11,747	\$ (7,759)	\$ 3,988	\$ 10,272	\$ (6,318)	\$ 3,954
Acquisition				1,500		1,500
Amortization		(1,404)	(1,404)		(1,689)	(1,689)
Foreign currency translation	9	228	237	(25)	248	223
Balance, end of period	\$ 11,756	\$ (8,935)	\$ 2,821	\$ 11,747	\$ (7,759)	\$ 3,988
<b>Non-competitve agreements</b>						
Balance, beginning of period	\$ 4,170	\$ (4,170)	\$	\$ 5,365	\$ (3,666)	\$ 1,699

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Amortization					(920)	(920)
Foreign currency translation				(35)		(35)
Impairment (a)				(1,160)	416	(744)
Balance, end of period	\$ 4,170	\$ (4,170)	\$	\$ 4,170	\$ (4,170)	\$
<b>Trade name</b>						
Balance, beginning of period	\$ 1,098	\$ (767)	\$ 331	\$ 5,437	\$ (938)	\$ 4,499
Amortization		(147)	(147)		(583)	(583)
Foreign currency translation		95	95	(124)	(1)	(125)
Impairment (a)				(4,215)	755	(3,460)
Balance, end of period	\$ 1,098	\$ (819)	\$ 279	\$ 1,098	\$ (767)	\$ 331
<b>Total</b>	<b>\$ 34,604</b>	<b>\$ (20,855)</b>	<b>\$ 13,749</b>	<b>\$ 34,595</b>	<b>\$ (18,748)</b>	<b>\$ 15,847</b>

(a) Represents an impairment charge recorded in fiscal 2011 related to the intangible assets of Powell Canada. All goodwill and intangible assets are reported in our Electrical Power Products business segment.

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Amortization of intangible assets recorded for the nine months ended June 30, 2012 and 2011 was \$2.1 million and \$3.7 million, respectively.

**F. COMPREHENSIVE INCOME**

Comprehensive income was as follows (in thousands):

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2012	2011	2012	2011
Net income	\$ 12,138	\$ 73	\$ 17,804	\$ 4,237
Unrealized gain (loss) on foreign currency translation, net of tax	(732)	(559)	(113)	1,514
Unrealized loss on derivative contracts, net of tax		(9)		(13)
Comprehensive income	\$ 11,406	\$ (495)	\$ 17,691	\$ 5,738

**G. LONG-TERM DEBT**

Long-term debt consisted of the following (in thousands):

	June 30, 2012	September 30, 2011
Industrial development revenue bonds	\$ 4,000	\$ 4,400
Capital lease obligations	482	1,041
Subtotal long-term debt and capital lease obligations	4,482	5,441
Less current portion	(836)	(1,140)
Total long-term debt and capital lease obligations	\$ 3,646	\$ 4,301

*US Revolver*

In March 2012, we amended our existing credit agreement (Amended Credit Agreement) with a major domestic bank. This amendment to our credit facility was made to increase the dollar limit on capital expenditures to allow us to support our continued expansions, including the Canadian Oil Sands and offshore production markets. The Amended Credit Agreement provides for a \$75.0 million revolving credit facility (US Revolver). Obligations are collateralized by the stock of certain of our subsidiaries.

The interest rate for amounts outstanding under the Amended Credit Agreement for the US Revolver is a floating rate based upon the higher of the Federal Funds Rate plus 0.5%, or the bank's prime rate. Once the applicable rate is determined, a margin ranging from negative 0.5% to 1.75%, as determined by our consolidated leverage ratio, is added to the applicable rate.

The US Revolver provides for the issuance of letters of credit which reduce the amounts which may be borrowed under the revolver. The amount available under the US Revolver was reduced by \$41.1 million for our outstanding letters of credit at June 30, 2012.

There were no borrowings outstanding under the US Revolver as of June 30, 2012. Amounts available under the US Revolver were \$33.9 million at June 30, 2012. The US Revolver expires on December 31, 2016.

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The Amended Credit Agreement contains certain restrictive and maintenance-type covenants, including restrictions on our ability to pay dividends, as well as restriction on the amount of capital expenditures allowed. It also contains financial covenants defining various financial measures and the levels of these measures with which we must comply, as well as a material adverse change clause. A material adverse change is defined as a material change in our operations, business, properties, liabilities or condition (financial or otherwise) or a material impairment of our ability to perform our obligations under our credit agreements.

The Amended Credit Agreement is collateralized by a pledge of 100% of the voting capital stock of each of our domestic subsidiaries and 66% of the voting capital stock of each non-domestic subsidiary, excluding Powell Canada. The Amended Credit Agreement provides for customary events of default and carries cross-default provisions with other existing debt agreements. If an event of default (as defined in the Amended Credit Agreement) occurs and is continuing, on the terms and subject to the conditions set forth in the Amended Credit Agreement, amounts outstanding under the Amended Credit Agreement may be accelerated and may become immediately due and payable. As of June 30, 2012, we were in compliance with all of the financial covenants of the Amended Credit Agreement.

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### *Canadian Revolver*

On December 15, 2009, we entered into a credit agreement with a major international bank (the Canadian Facility) to finance the acquisition of Powell Canada and provide additional working capital support for our operations in Canada. In March 2012, we reduced the Canadian Facility from a \$20.0 million CAD (approximately \$19.5 million) revolving credit facility (the Canadian Revolver) to \$10.0 million CAD (approximately \$9.8 million), and eliminated the restrictions on amounts which may be borrowed based on a borrowing base calculation.

The Canadian Revolver provides for the issuance of letters of credit which reduce the amounts which may be borrowed under the Canadian Revolver. As of June 30, 2012, there were no letters of credit outstanding under the Canadian Revolver.

There were no borrowings outstanding under the Canadian Revolver and \$9.8 million was available at June 30, 2012. The Canadian Facility expires on February 28, 2015. The interest rate for amounts outstanding under the Canadian Revolver is a floating interest rate based upon either the Canadian Prime Rate, or the lender's US Bank Rate. Once the applicable rate is determined, a margin of 0.375% to 1.125%, as determined by our consolidated leverage ratio, is added to the applicable rate.

The principal financial covenants are consistent with those in our Amended Credit Agreement. The Canadian Facility contains a material adverse effect clause. A material adverse effect is defined as a material change in the operations of Powell or Powell Canada in relation to our financial condition, property, business operations, expected net cash flows, liabilities or capitalization.

The Canadian Facility is secured by the assets of our Canadian operations and provides for customary events of default and carries cross-default provisions with our existing debt agreements. If an event of default (as defined in the Canadian Facility) occurs and is continuing, on the terms and subject to the conditions set forth in the Canadian Facility, amounts outstanding under the Canadian Facility may be accelerated and may become immediately due and payable. As of June 30, 2012, we were in compliance with all of the financial covenants of the Canadian Facility, and no borrowings were outstanding under this facility at June 30, 2012.

### *Industrial Development Revenue Bonds*

We borrowed \$8.0 million in October 2001 through a loan agreement funded with proceeds from tax-exempt industrial development revenue bonds (Bonds). These Bonds were issued by the Illinois Development Finance Authority and were used for the completion of our Northlake, Illinois facility. Pursuant to the Bond issuance, a reimbursement agreement between us and a major domestic bank required an issuance by the bank of an irrevocable direct-pay letter of credit (Bond LC) to the Bonds' trustee to guarantee payment of the Bonds' principal and interest when due. The Bond LC is subject to both early termination and extension provisions customary to such agreements, as well as various covenants, for which we were in compliance at June 30, 2012. While the Bonds mature in 2021, the reimbursement agreement requires annual redemptions of \$400,000 that commenced on October 25, 2002. A sinking fund is used for the redemption of the Bonds. At June 30, 2012, the balance in the restricted sinking fund was approximately \$334,000 and was recorded in cash and cash equivalents. The Bonds bear interest at a floating rate determined weekly by the Bonds' remarketing agent, which was the underwriter for the Bonds and is an affiliate of the bank. This interest rate was 0.60 % per year on June 30, 2012.

## **H. DERIVATIVE INSTRUMENTS AND HEDGING STRATEGIES**

We operate in various countries and have operations in the United Kingdom and Canada. These international operations expose us to market risk associated with foreign currency exchange rate fluctuations. We have entered into certain forward contracts to hedge the risk of certain foreign currency rate fluctuations. To the extent we choose to manage volatility associated with the net exposures, we enter into various financial transactions which we account for using the applicable accounting guidance for derivative instruments and hedging activities. Our objective is to hedge the variability in forecasted cash flow due to the foreign currency risk associated with certain long-term contracts. As of June 30, 2012, we held only derivatives that were designated as cash flow hedges related to the U.S. Dollar/British Pound Sterling exchange rate.

All derivatives are recognized on the Condensed Consolidated Balance Sheet at their fair value and classified based on the instrument's maturity date. The total notional amount of outstanding derivatives as of June 30, 2012 was \$0.7 million.

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The following table presents the fair value of derivative instruments included within the Condensed Consolidated Balance Sheets as of June 30, 2012:

	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value (in thousands)	Balance Sheet Location	Fair Value
<b>Derivatives designated as hedging instruments:</b>				
Foreign exchange forwards	Prepaid expenses and other current assets	\$ 10	Other accrued expenses	\$
<b>Total derivatives</b>		<b>\$ 10</b>		<b>\$</b>

There were no derivatives outstanding at September 30, 2011.

The following table presents the amounts affecting the Condensed Consolidated Statements of Operations for the three and nine month periods ended June 30, 2012:

	Amount of Gain (Loss) Recognized in Other Comprehensive Income on Derivatives		Location of Gain (Loss) Reclassified from Accumulated Other comprehensive Income into Income	Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income	
	Three Months Ended	Nine Months Ended		Three Months Ended	Nine Months Ended
	June 30, 2012 (in thousands)	June 30, 2012 (in thousands)		June 30, 2012 (in thousands)	June 30, 2012 (in thousands)
<b>Derivatives designated:</b>					
Derivatives designated as cash flow hedges:					
Foreign exchange forwards	\$	\$	Revenues	\$ 12	\$ 11
<b>Total designated cash flow hedges</b>	<b>\$</b>	<b>\$</b>		<b>\$ 12</b>	<b>\$ 11</b>

The following table presents the amounts affecting the Condensed Consolidated Statements of Operations for the three and nine month periods ended June 30, 2011:

Amount of Gain (Loss) Recognized in Other Comprehensive Income on	Amount of Gain (Loss) Reclassified from
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	Derivatives <sup>1</sup>		Location of Gain (Loss) Reclassified from Accumulated Other comprehensive Income into Income	Accumulated Other Comprehensive Income into Income <sup>1</sup>	
	Three Months Ended June 30, 2011 (in thousands)	Nine Months Ended June 30, 2011 (in thousands)		Three Months Ended June 30, 2011 (in thousands)	Nine Months Ended June 30, 2011 (in thousands)
<b>Derivatives designated:</b>					
Derivatives designated as cash flow hedges:					
Foreign exchange forwards	\$ (14)	\$ (19)	Revenues	\$ 3	\$ 45
<b>Total designated cash flow hedges</b>	<b>\$ (14)</b>	<b>\$ (19)</b>		<b>\$ 3</b>	<b>\$ 45</b>

<sup>1</sup> For the three and nine month periods ended June 30, 2011, we recorded in revenues an immaterial amount of ineffectiveness from cash flow hedges.

Refer to Note B for a description of how the above financial instruments are valued in accordance with the fair value measurement accounting guidance for the three and nine month periods ended June 30, 2012.

*Cash Flow Hedges*

The purpose of our foreign currency hedging activities is to protect us from the risk that the eventual cash flows resulting from transactions that are denominated in currencies other than the U.S. Dollar will be adversely affected by changes in exchange rates. We are currently hedging our exposure to the reduction in value of forecasted foreign currency cash flows through foreign currency forward agreements through October 31, 2012, for transactions denominated in the British Pound Sterling.

All changes in the fair value of outstanding cash flow hedge derivatives, except the ineffective portion, are recorded in accumulated other comprehensive income, until net income is affected by the variability of cash flows of the hedged transaction, or until it is probable that the forecasted transaction will not occur. In most cases, amounts recorded in accumulated other comprehensive income

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will be released to net income some time after the maturity of the related derivative. The Condensed Consolidated Statements of Operations classification of effective hedge results is the same as that of the underlying exposure. Results of hedges of revenue and product costs are recorded in revenue and costs of sales, respectively, when the underlying hedged transaction affects net income. Results of hedges of selling and administrative expense, if any, are recorded together with those costs when the related expense is recorded. In addition, any ineffective portion of the changes in the fair value of the derivatives designated as cash flow hedges are reported in the Condensed Consolidated Statements of Operations as the changes occur.

As of June 30, 2012, there were no deferred net losses (net of tax) on outstanding derivatives recorded in accumulated other comprehensive income expected to be reclassified to net income during the next 12 months as a result of underlying hedged transactions being recorded in net income. Actual amounts ultimately reclassified to net income are dependent on the exchange rates in effect when the derivative contracts that are currently outstanding mature. As of June 30, 2012, the maximum term over which we are hedging exposure to the variability of cash flows for our forecasted and recorded transactions is four months. For the three and nine months ended June 30, 2012, we recorded in selling, general and administrative expense an immaterial amount of ineffectiveness from cash flow hedges.

### *Credit Risk*

We are exposed to credit-related losses in the event of non-performance by counterparties to hedging instruments. In recent years, the ability of financial counterparties to perform under financial instruments has become less certain. We attempt to take into account the financial viability of counterparties in both valuing the instruments and determining their effectiveness as hedging instruments. If a counterparty was unable to perform, our ability to qualify for hedging certain transactions would be compromised and the realizable value of the financial instruments would be uncertain. As a result, our results of operations and cash flows would be impacted.

## I. COMMITMENTS AND CONTINGENCIES

### *Letters of Credit and Bonds*

Certain customers require us to post bank letter of credit guarantees or performance bonds issued by a surety. These guarantees and performance bonds assure that we will perform under the terms of our contract. In the event of default, the counterparty may demand payment from the bank under a letter of credit or performance by the surety under a performance bond. To date, there have been no significant expenses related to either for the periods reported. We were contingently liable for secured and unsecured letters of credit of \$41.1 million as of June 30, 2012, under our US Revolver. We also had performance and maintenance bonds totaling \$222.7 million that were outstanding with our sureties, with additional bonding capacity of \$377.3 million available, at June 30, 2012.

We have a facility agreement (Facility Agreement) between S&I and a large international bank. This \$11.7 million Facility Agreement provides S&I the ability to enter into forward exchange contracts, currency options and bank guarantees. At June 30, 2012, we had a total of \$8.5 million of bank guarantees outstanding under this Facility Agreement.

The Facility Agreement provides for financial covenants, customary events of default and carries cross-default provisions with our Amended Credit Facility. If an event of default (as defined in the Facility Agreement) occurs and is continuing, on the terms and subject to the conditions set forth in the Facility Agreement, obligations outstanding under the Facility Agreement may be accelerated and may become or be declared immediately due and payable.

### *Litigation*

We are involved in various legal proceedings, claims and other disputes arising in the ordinary course of business which, in general, are subject to uncertainties and the outcomes are not predictable. Although we can give no assurance about the outcome of pending or threatened litigation and the effect such outcomes may have on us, management believes that any ultimate liability resulting from the outcome of such proceedings, to the extent not otherwise provided or covered by insurance, will not have a material adverse effect on our consolidated financial position or results of operations or liquidity.

## J. STOCK-BASED COMPENSATION

Refer to our Annual Report on Form 10-K for the fiscal year ended September 30, 2011 for a full description of our existing stock-based compensation plans.





**Table of Contents***Restricted Stock Units*

In October 2010, we granted 34,566 restricted stock units (RSUs) with a fair value of \$30.79 per unit to certain officers and key employees of the Company. An additional 4,482 RSUs were granted in October 2010, with a fair value of \$32.12 per unit. The RSUs vest over a three-year period from their date of issuance. The fair value of the RSUs was based on the closing price of our common stock as reported on the NASDAQ Global Market (NASDAQ) on the grant dates. Sixty-percent of the actual amount of the RSUs earned will be based on the cumulative earnings as reported relative to the three-year performance cycle which began October 1 of the year granted, and ranges from 0% to 150% of the target RSUs granted. The remaining forty-percent of the RSUs are time-based and vest over a three-year period. The RSUs do not have voting rights of common stock, and the shares of common stock underlying the RSUs are not considered issued and outstanding until actually issued.

During the first quarter of fiscal 2012, we granted 32,894 performance-based RSUs with a fair value of \$31.18 per unit to certain officers and key employees of the Company. The RSUs vest over a three-year period from their date of issuance, and are earned over a three-year performance cycle.

During the first quarter of fiscal 2012, we also granted 21,931 time-based RSUs with a fair value of \$31.18 per unit to certain officers and key employees of the Company. The RSUs vest over a three-year period from their date of issuance, and are time-based.

RSU activity (number of shares) for us was as follows:

	<b>Number of Restricted Stock Units</b>	<b>Weighted Average Grant Date Fair Value Per Share</b>
Outstanding at September 30, 2010	87,454	\$ 38.96
Granted	39,048	30.94
Expired or cancelled	(35,746)	36.50
Vested/exercised	(21,378)	37.68
Outstanding at September 30, 2011	69,378	36.10
Granted	54,825	31.18
Expired or cancelled	(19,729)	40.48
Vested/exercised		
Outstanding at June 30, 2012	104,474	\$ 36.24

During the nine months ended June 30, 2012, we recorded compensation expense of \$0.7 million related to the RSUs. We recorded compensation expense of \$0.1 million related to the RSUs for the nine months ended June 30, 2011.

*Restricted Stock*

Under the 2006 Equity Compensation Plan (the 2006 Plan), any employee of the Company and its subsidiaries and consultants are eligible to participate in the plan and receive awards. Awards can take the form of options, stock appreciation rights, stock awards and performance unit awards.

We have a Restricted Stock Plan for the benefit of members of the Board of Directors of the Company (the Board) who, at the time of their service, are not employees of the Company or any of its affiliates. Subject to certain conditions and restrictions as determined by the Compensation Committee of the Board and proportionate adjustments in the event of stock dividends, stock splits and similar corporate transactions, each eligible director will receive 2,000 shares of restricted stock annually. In June 2012, 16,000 shares of restricted stock were issued to such directors at a price of \$37.50 per share. In June 2011, 16,000 shares of restricted stock were issued to such directors at a price of

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\$33.49 per share. The restricted stock grants vest 50% per year over a two-year period on each anniversary of the grant date.

In June 2012, 2,000 shares of restricted stock were issued under the 2006 Plan to the Chairman of the Board of Directors of the Company, who is an employee of the Company. These shares were issued at a price of \$37.50 per share. The restricted stock grant vests 50% per year over a two-year period on each anniversary of the grant date.

During the first quarter of fiscal 2011, 26,000 shares of restricted stock were issued to certain officers and key employees of the Company with a fair value ranging from \$30.79 to \$32.12 per share under the 2006 Plan. The restricted stock grant vests over a three-year period on each anniversary of the grant date. Compensation expense is recognized over a three-year period based on the price per share on the grant date. In conjunction with the separation of our former President and Chief Executive Officer (CEO) in September 2011, the remaining 7,601 shares issued to him that were unvested became immediately vested.

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During the nine months ended June 30, 2012, we recorded compensation expense of \$0.4 million related to restricted stock grants. We recorded compensation expense of \$0.8 million related to restricted stock grants for the nine months ended June 30, 2011.

*Stock Options*

Stock option activity for the nine months ended June 30, 2012 was as follows:

	Stock Options	Weighted Average Exercise Price	Remaining Weighted Average Contractual Term (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at September 30, 2011	97,550	\$ 18.44		
Granted				
Exercised	(97,550)	18.44		
Forfeited / Cancelled				
Outstanding at June 30, 2012		\$		\$
Exercisable at June 30, 2012		\$		\$

**K. BUSINESS SEGMENTS**

We manage our business through operating segments, which are comprised of two reportable business segments: Electrical Power Products and Process Control Systems. Electrical Power Products includes equipment and systems for the distribution and control of electrical energy. Process Control Systems consists principally of instrumentation, computer controls, communications and data management systems to control and manage critical processes.

The table below reflects certain information relating to our operations by reportable segment. All revenues represent sales from unaffiliated customers. The accounting policies of the business segments are the same as those described in the summary of significant accounting policies. Corporate expenses are allocated to the operating business segments primarily based on revenues. The corporate assets are mainly cash, cash equivalents and marketable securities.

Detailed information regarding our business segments is shown below (in thousands):

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2012	2011	2012	2011
Revenues:				
Electrical Power Products	\$ 186,272	\$ 134,425	\$ 510,910	\$ 370,143
Process Control Systems	7,821	6,944	22,125	21,010
Total	\$ 194,093	\$ 141,369	\$ 533,035	\$ 391,153

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<b>Gross profit:</b>				
Electrical Power Products	\$ 41,677	\$ 19,788	\$ 93,203	\$ 67,236
Process Control Systems	2,166	2,076	5,255	5,369
Total	\$ 43,843	\$ 21,864	\$ 98,458	\$ 72,605
<b>Income before income taxes:</b>				
Electrical Power Products	\$ 18,422	\$ 1,055	\$ 30,066	\$ 8,567
Process Control Systems	(143)	140	54	(390)
Total	\$ 18,279	\$ 1,195	\$ 30,120	\$ 8,177
<b>Depreciation and amortization expense:</b>				
Electrical Power Products	\$ 3,365	\$ 3,951	\$ 9,779	\$ 11,325
Process Control Systems	22	39	35	123
Total	\$ 3,387	\$ 3,990	\$ 9,814	\$ 11,448

Income before income taxes includes a \$1.2 million gain recorded in the second quarter of fiscal 2011 resulting from cash received from the sale of our 50% equity investment in Kazakhstan. This gain is recorded in our Electrical Power Products business segment.

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### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the accompanying condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and with our Annual Report on Form 10-K for the year ended September 30, 2011, which was filed with the Securities and Exchange Commission on December 12, 2011 and is available on the SEC's website at [www.sec.gov](http://www.sec.gov).*

### **CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

We are including the following discussion to inform our existing and potential shareholders generally of some of the risks and uncertainties that can affect our Company and to take advantage of the safe harbor protection for forward-looking statements that applicable federal securities law affords.

From time to time, our management or persons acting on our behalf make forward-looking statements to inform existing and potential shareholders about our Company. These statements may include projections and estimates concerning the timing and success of specific projects and our future backlog, revenues, income and capital spending. Forward-looking statements are generally accompanied by words such as estimate, project, predict, believe, expect, anticipate, plan, goal or other words that convey the uncertainty of future events or outcomes. In addition, sometimes we will specifically describe a statement as being a forward-looking statement and refer to this cautionary statement.

In addition, various statements in this Quarterly Report on Form 10-Q, including those that express a belief, expectation or intention, as well as those that are not statements of historical fact, are forward-looking statements. These forward-looking statements speak only as of the date of this report; we disclaim any obligation to update these statements unless required by securities law, and we caution you not to rely on them unduly. We have based these forward-looking statements on our current expectations and assumptions about future events. While our management considers these expectations and assumptions to be reasonable, they are inherently subject to significant business, economic, competitive, regulatory and other risks, contingencies and uncertainties, most of which are difficult to predict and many of which are beyond our control. These risks, contingencies and uncertainties relate to, among other matters, the following:

The ongoing economic uncertainty and financial market conditions have negatively impacted and may continue to impact our customer base, suppliers and backlog.

Our backlog is subject to unexpected adjustments and cancellations and, therefore, may not be a reliable indicator of our future earnings.

Our volume of fixed-price contracts and the use of percentage-of-completion accounting could result in volatility in our results of operations.

Fluctuations in the price and supply of raw materials used to manufacture our products may reduce our profits.

Our industry is highly competitive.

Our operations could be adversely impacted by the continuing effects from the U.S. government regulations on offshore deepwater and Outer Continental Shelf (OCS) drilling projects.

International and political events may adversely affect our operations.

Our acquisition strategy involves a number of risks.

Our operating results may vary significantly from quarter to quarter.

We may be unsuccessful at generating profitable internal growth.

The departure of key personnel could disrupt our business.

Our business requires skilled labor, and we may be unable to attract and retain qualified employees.

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Actual and potential claims, lawsuits and proceedings could ultimately reduce our profitability and liquidity and weaken our financial condition.

Unforeseen difficulties with the maintenance or operation of our enterprise resource planning system could adversely affect our internal controls and our business.

We carry insurance against many potential liabilities, and our management of risk may leave us exposed to unidentified or unanticipated risks.

We may incur additional healthcare costs arising from federal healthcare reform legislation.

Technological innovations by competitors may make existing products and production methods obsolete.

Catastrophic events could disrupt our business.

We believe the items we have outlined above are important factors that could cause estimates included in our financial statements to differ materially from actual results and those expressed in a forward-looking statement made in this report or elsewhere by us or on our behalf. We have discussed many of these factors in more detail in our Annual Report on Form 10-K for the year ended September 30, 2011. These factors are not necessarily all of the factors that could affect us. Unpredictable or unanticipated factors we have not discussed in this report could also have material adverse effects on actual results of matters that are the subject of our forward-looking statements. We do not intend to update our description of important factors each time a potential important factor arises, except as required by applicable securities laws and regulations. We advise our shareholders that they should (1) be aware that factors not referred to above could affect the accuracy of our forward-looking statements and (2) use caution when considering our forward-looking statements.

## **Overview**

We develop, design, manufacture and service custom engineered-to-order equipment and systems for the management and control of electrical energy and other critical processes. Headquartered in Houston, Texas, we serve the transportation, environmental, energy, industrial and utility industries. Our business operations are consolidated into two business segments: Electrical Power Products and Process Control Systems. Revenues and costs are primarily related to engineered-to-order equipment and systems which precludes us from providing detailed price and volume information.

The global markets in which Powell participates are capital-intensive and cyclical in nature. Cyclicity is driven by customer demand, global economic markets and potential environmental or regulatory impacts which affect the manner in which our customers proceed with capital projects. Our customers analyze various factors including the short-term demand for oil and electrical energy, the overall banking environment, federal and state budgets, the outlook for offshore drilling and related regulatory actions and the drive towards environmental controls over the type and way energy is produced and utilized. These factors have contributed to decisions by customers to delay or to change where they place new capital projects, which decreased our backlog of orders to \$282.3 million entering fiscal 2011, down \$83.5 million from the beginning of fiscal 2010. However, during fiscal 2011, orders received were \$725.2 million compared to \$466.8 million during fiscal 2010 and our backlog has increased to \$443.0 million at the beginning of fiscal 2012 (our current fiscal year). This resulted in an increase in backlog of 57% compared to the backlog at the beginning of fiscal 2011. Some of our orders received in fiscal 2011 are for large complex petrochemical and offshore oil and gas construction projects which will take several months to produce. Orders received during the first nine months of fiscal 2012 were \$525.1 million, a decrease of \$75.3 million from the same period of the prior year.

Execution challenges in the first three months of fiscal 2012 on certain large projects at Powell Canada have negatively impacted net income during fiscal 2012. These execution challenges resulted from scope changes and cost overruns on certain projects. The Company is currently pursuing recovery of certain of these costs. However, there is no assurance these costs can be recovered and costs recovered are recorded when change orders are approved by the customers.





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**Table of Contents****Results of Operations***Revenue and Gross Profit*

Consolidated revenues increased \$52.7 million to \$194.1 million in the third quarter of fiscal 2012 compared to \$141.4 million in the third quarter of fiscal 2011. For the third quarter of fiscal 2012, domestic revenues increased by 8.9% to \$105.5 million compared to the third quarter of 2011. Total international revenues were \$88.6 million in the third quarter of 2012 compared to \$44.6 million in the third quarter of 2011. Gross profit for the third quarter of fiscal 2012, as compared to the third quarter of fiscal 2011, increased by approximately \$22.0 million, to \$43.8 million, and gross profit as a percentage of revenues increased to 22.6% in the third quarter of fiscal 2012, compared to 15.5% in the third quarter of fiscal 2011. The increase in gross profit and gross profit as a percentage of revenues resulted from the mix of projects in our backlog, and increased production volume and reduced costs on project completion due to operational efficiencies.

For the nine months ended June 30, 2012, consolidated revenues increased \$141.8 million to \$533.0 million compared to \$391.2 million for the nine months ended June 30, 2011. For the first nine months of fiscal 2012, domestic revenues increased by 17.4% to \$307.9 million compared to the first nine months of fiscal 2011. Total international revenues increased to \$225.2 million in the first nine months of 2012 compared to \$128.9 million in the first nine months of fiscal 2011. Gross profit for the first nine months of fiscal 2012, as compared to the first nine months of fiscal 2011, increased by \$25.9 million, to \$98.5 million, as a result of increased production volume and reduced costs on project completion due to operational efficiencies. Gross profit as a percentage of revenues decreased slightly to 18.5% for the first nine months of fiscal 2012, compared to 18.6% for the first nine months of fiscal 2011 due to execution challenges on certain large projects at Powell Canada.

*Electrical Power Products*

Our Electrical Power Products business segment recorded revenues of \$186.3 million in the third quarter of fiscal 2012, compared to \$134.4 million for the third quarter of fiscal 2011. In the third quarter of 2012, revenues from public and private utilities were approximately \$38.7 million, compared to \$37.0 million in the third quarter of fiscal 2011. Revenues from industrial and commercial customers totaled \$137.3 million in the third quarter of 2012, an increase of \$47.4 million compared to the third quarter of fiscal 2011. Municipal and transit projects generated revenues of \$10.3 million in the third quarter of fiscal 2012 compared to \$7.5 million in the third quarter of fiscal 2011.

Business segment gross profit, as a percentage of revenues, was 22.4% in the third quarter of fiscal 2012, compared to 14.7% in the third quarter of fiscal 2011. This increase in gross profit as a percentage of revenues resulted primarily from increased production volume and reduced costs on project completion due to operational efficiencies.

For the nine months ended June 30, 2012, our Electrical Power Products segment recorded revenues of \$510.9 million, compared to \$370.1 million for the nine months ended June 30, 2011. In the first nine months of fiscal 2012, revenues from public and private utilities were approximately \$96.2 million, compared to \$101.5 million in the first nine months of fiscal 2011. Revenues from commercial and industrial customers totaled \$383.2 million in the first nine months of fiscal 2012, an increase of \$135.4 million compared to the first nine months of fiscal 2011. Municipal and transit projects generated revenues of \$31.5 million in the first nine months of fiscal 2012, compared to \$20.8 million in the first nine months of fiscal 2011.

For the nine months ended June 30, 2012, gross profit from the Electrical Power Products business segment, as a percentage of revenues, was 18.2%, compared to 18.2% for the nine months ended June 30, 2011. Gross profit as a percentage of revenue for the nine months ended June 2012 was negatively impacted by execution challenges in the first quarter of fiscal 2012 on certain large projects at Powell Canada.

*Process Control Systems*

Our Process Control Systems business segment recorded revenues of \$7.8 million in the third quarter of fiscal 2012, an increase from \$6.9 million in the third quarter of fiscal 2011. Business segment gross profit, as a percentage of revenues, decreased to 27.7% in the third quarter of fiscal 2012 compared to 29.9% in the third quarter of fiscal 2011.

For the nine months ended June 30, 2012, our Process Control Systems business segment recorded revenues of \$22.1 million, an increase from \$21.0 million for the nine months ended June 30, 2011. Business segment gross profit decreased as a percentage of revenues to 23.8% for the first nine months of fiscal 2012, compared to 25.6% for the first nine months of fiscal 2011. This decrease in gross profit as a percentage of revenues is related to the mix of projects.



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For additional information related to our business segments, see Note K of Notes to Condensed Consolidated Financial Statements.

### *Consolidated Selling, General and Administrative Expenses*

Consolidated selling, general and administrative expenses decreased to 12.8% of revenues in the third quarter of fiscal 2012 compared to 13.7% of revenues in the third quarter of fiscal 2011. Selling, general and administrative expenses were \$24.8 million for the third quarter of fiscal 2012, compared to \$19.4 million for the third quarter of fiscal 2011. This increase is primarily due to increases in short-term and long-term incentive compensation, resulting from increased earnings compared to the third quarter of fiscal 2011. Selling, general and administrative expenses decreased as a percentage of revenues as a result of our increase in revenues.

For the nine months ended June 30, 2012, consolidated selling, general and administrative expenses decreased to 12.4% of revenues, compared to 15.8% of revenues for the nine months ended June 30, 2011. Selling, general and administrative expenses were \$66.1 million for the first nine months of fiscal 2012, compared to \$61.9 million for the first nine months of fiscal 2011. This increase is primarily related to increased short-term and long-term incentive compensation resulting from higher earnings, as well as increased bad debt expense. Selling, general and administrative expenses decreased as a percentage of revenues as a result of our increase in revenues.

### *Gain on Sale of Investment*

Gain on sale of investment consists of a \$1.2 million gain recorded in the second quarter of fiscal 2011 that resulted from cash received from the sale of our 50% equity investment in a joint venture in Kazakhstan, which was previously a part of the acquisition of Powell Canada in fiscal 2010.

### *Provision for Income Taxes*

Our provision for income taxes reflects an effective tax rate on earnings before income taxes of 33.6% in the third quarter of fiscal 2012, compared to 93.9% in the third quarter of fiscal 2011. For the first nine months of fiscal 2012, our effective tax rate was 40.9%, compared to 48.2% for the first nine months of fiscal 2011. The effective tax rates for the third quarter of fiscal 2011, and the first nine months of fiscal 2012 and 2011 have been negatively impacted by our inability to record a tax benefit related to pre-tax losses in Canada.

### *Net Income*

In the third quarter of fiscal 2012, we generated net income of \$12.1 million, or \$1.02 per diluted share, compared to \$0.1 million, or \$0.01 per diluted share, in the third quarter of fiscal 2011. For the nine months ended June 30, 2012, we recorded net income of \$17.8 million, or \$1.50 per diluted share, compared to \$4.2 million, or \$0.36 per diluted share, for the nine months ended June 30, 2011.

### *Backlog*

The order backlog at June 30, 2012, was \$433.5 million, compared to \$443.0 million at September 30, 2011, and \$491.4 million at the end of the third quarter of fiscal 2011. New orders placed during the third quarter of fiscal 2012 totaled \$133.0 million compared to \$197.7 million in the third quarter of fiscal 2011. Backlog has decreased slightly due to the completion of certain oil and gas production and petrochemical projects.

## **Liquidity and Capital Resources**

Cash and cash equivalents decreased to \$106.8 million at June 30, 2012, primarily as a result of the recent purchases of land to build facilities in the United States and Canada during the first nine months of fiscal 2012 to support our continued expansion of the offshore production markets and the Canadian Oil Sands. As of June 30, 2012, current assets exceeded current liabilities by 2.4 times and our debt to total capitalization was 1.5%.

At June 30, 2012, we had cash and cash equivalents of \$106.8 million, compared to \$123.5 million at September 30, 2011. We have a \$75.0 million revolving credit facility in the U.S., which expires in December 2016. As of June 30, 2012, there were no amounts borrowed under this line of credit. We also have a \$9.8 million revolving credit facility in Canada. At June 30, 2012, there was no balance outstanding under the Canadian revolving credit facility. Total long-term debt and capital lease obligations, including current



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maturities, totaled \$4.5 million at June 30, 2012, compared to \$5.4 million at September 30, 2011. Letters of credit outstanding were \$41.1 million at June 30, 2012, compared to \$13.2 million at September 30, 2011, which reduce our availability under our US Revolver. Amounts available under the U.S. revolving credit facility were \$33.9 million at June 30, 2012. Amounts available under the Canadian revolving credit facility were \$9.8 million at June 30, 2012. For further information regarding our debt, see Notes G and I of Notes to Condensed Consolidated Financial Statements.

Approximately \$7.1 million of our cash at June 30, 2012, was held internationally for international operations. It is our intention to indefinitely reinvest all current and future foreign earnings internationally in order to ensure sufficient working capital and support and expand these operations. In the event that the Company elects to repatriate some or all of the foreign earnings that were previously deemed to be indefinitely reinvested outside the U.S., under current tax laws we would incur additional tax expense upon such repatriation.

We believe that cash available and borrowing capacity under our existing credit facility should be sufficient to finance anticipated operating activities, capital improvements and expansions, as well as debt repayments for the foreseeable future. We will continue to monitor the factors that drive our markets and strive to maintain our leadership and competitive advantage in the markets we serve while aligning our cost structures with market conditions.

### ***Operating Activities***

Cash provided by operating activities was \$6.5 million during the first nine months of fiscal 2012 and \$25.2 million during the first nine months of fiscal 2011. Cash flow from operations is primarily influenced by demand for our products and services and is impacted as our progress payment terms with our customers are matched with the payment terms with our suppliers. Cash flow from operations decreased during the first nine months of fiscal 2012 compared to the same period in the prior year, primarily due to cash used to support higher levels of business activity and the timing of billing milestones on certain large projects.

### ***Investing Activities***

Investments in property, plant and equipment during the first nine months of fiscal 2012 totaled \$25.5 million, compared to \$4.1 million during the first nine months of fiscal 2011. A significant portion of these investments has been to acquire land and build facilities in the United States and Canada to support our continued expansion in the offshore production markets and Canadian Oil Sands. During the first nine months of fiscal 2011, we received cash of \$1.2 million from the sale of our 50% equity investment in Kazakhstan.

### ***Financing Activities***

Net cash provided by financing activities was \$1.4 million for the first nine months of fiscal 2012 due to cash being received from the exercise of stock options that were set to expire on June 24, 2012. Net cash used in financing activities was \$0.7 million for the first nine months of fiscal 2011, resulting from payments made on capital lease agreements.

### **New Accounting Standards**

See Note A to our condensed consolidated financial statements included in this report for information on new accounting standards.

### **Critical Accounting Policies**

The discussion and analysis of our financial condition and results of operations are based on our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities known to exist at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. We evaluate our estimates on an ongoing basis, based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. There can be no assurance that actual results will not differ from those estimates.

There have been no material changes to our critical accounting policies as disclosed in our Annual Report on Form 10-K for the year ended September 30, 2011.



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**Table of Contents****Outlook**

The global markets in which Powell participates are capital-intensive and cyclical in nature. Cyclicity is driven by customer demand, global economic markets and potential environmental or regulatory impacts which affect the manner in which our customers proceed with large capital projects. Our customers analyze various factors including the short-term demand for oil and electrical energy, the overall banking environment, federal and state budgets, the outlook for offshore drilling and related regulatory actions and the drive towards environmental controls over the type and way energy is produced and utilized. These factors have contributed to decisions by customers to delay or to change where they place new capital projects, which decreased our backlog of orders to \$282.3 million entering fiscal 2011, down \$83.5 million from the beginning of fiscal 2010. However, during fiscal 2011, orders received were \$725.2 million compared to \$466.8 million during the same twelve-month period of fiscal 2010 and our backlog increased to \$443.0 million at the beginning of fiscal 2012. This resulted in an increase in backlog of 57% at the beginning of fiscal 2012 compared to the backlog at the beginning of fiscal 2011. Some of our orders received in fiscal 2011 are for large complex petrochemical and offshore oil and gas construction projects which will take several months to produce. Execution challenges on certain large projects at Powell Canada have negatively impacted our net income for fiscal 2012. These execution challenges resulted from scope changes and cost overruns on certain projects. The Company is currently pursuing recovery of certain of these costs. However, there is no assurance these costs can be recovered and costs recovered are recorded when change orders are approved by the customers. Orders received during the first nine months of fiscal 2012 were \$525.1 million, a decrease of approximately \$75.3 million from the same period of the prior year.

Growth in demand for energy is expected to continue over the long term. New infrastructure investments will be needed to ensure the available supply of petroleum products. New power generation and distribution infrastructure will also be needed to meet the growing demand for electrical energy. New power generation plants will also be needed to replace the aging facilities across the United States, as those plants reach the end of their life cycle. A heightened concern for environmental damage, together with the uncertainty of gasoline prices, has expanded the popularity of urban transit systems, which should drive demand for investment in transit infrastructure, contingent upon available financing. Opportunities for future projects continue, however, the timing and pricing of many of these projects is difficult to predict. The demand for our products and services should continue as investments in large capital-intensive infrastructure projects receive funding and support.

We believe that cash available and borrowing capacity under our existing credit facility should be sufficient to finance anticipated operational activities, capital improvements, market expansions and debt repayments for the foreseeable future. We will continue to monitor the factors that drive our markets and strive to maintain our leadership and competitive advantage and invest in the markets we serve while aligning our cost structures with market conditions.

We have recently acquired land and begun to build facilities in the United States and Canada to support our continued expansion in the offshore production markets and the Canadian Oil Sands. The total investment in land, buildings and equipment is to be funded with cash in the amount of approximately \$75 million.

**Item 3. *Quantitative and Qualitative Disclosures About Market Risk***

We are exposed to certain market risks arising from transactions we have entered into in the normal course of business. These risks primarily relate to fluctuations in interest rates, foreign exchange rates and commodity prices.

**Interest Rate Risk**

If we determine to borrow under one of our credit facilities, we will be subject to market risk resulting from changes in interest rates related to our floating rate bank credit facility. If we were to make such borrowings, a hypothetical 100 basis point increase in variable interest rates would not result in a material impact to our financial statements. While we do not currently have any derivative contracts to hedge our exposure to interest rate risk, we have in the past and may in the future enter into such contracts. During each of the past three years, we have not experienced a significant effect on our business due to changes in interest rates.

**Foreign Currency Transaction Risk**

We have operations that expose us to currency risk in the British Pound Sterling, the Canadian Dollar and to a lesser extent the Euro. Amounts invested in our foreign operations are translated into U.S. Dollars at the exchange rates in effect at the balance sheet date. The resulting translation adjustments are recorded as accumulated other comprehensive income (loss), a component of stockholders' equity in our consolidated balance sheets. We believe the exposure to the effects that fluctuating foreign currencies have on our consolidated results of operations is limited because the foreign operations primarily invoice customers and collect obligations in their





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respective currencies or U.S. Dollars. Our international operations are financed utilizing local credit facilities denominated in local currencies. Additionally, expenses associated with these transactions are generally contracted and paid for in the same local currencies. A 10% unfavorable change in the U.S. Dollar exchange rate, relative to other functional currencies in which we operate, would not materially impact our consolidated balance sheet at June 30, 2012.

During fiscal 2011 and the first nine months of fiscal 2012, we entered into eight foreign currency forward contracts to manage the volatility of future cash flows on certain long-term contracts that are denominated in the British Pound Sterling. The contracts are designated as cash flow hedges for accounting purposes. The changes in fair value related to the effective portion of the hedges are recognized as a component of accumulated other comprehensive income on our Condensed Consolidated Balance Sheets. At June 30, 2012, we recorded a net asset of approximately \$10,000 on our Condensed Consolidated Balance Sheets related to these transactions.

### **Commodity Price Risk**

We are subject to market risk from fluctuating market prices of certain raw materials. While such materials are typically available from numerous suppliers, commodity raw materials are subject to price fluctuations. We attempt to pass along such commodity price increases to our customers on a contract-by-contract basis to avoid a negative effect on profit margin. While we may do so in the future, we have not currently entered into any derivative contracts to hedge our exposure to commodity risk. We continue to experience price volatility with some of our key raw materials and components. Fixed price contracts may limit our ability to pass cost increases to our customers, thus negatively impacting our earnings. Fluctuations in commodity prices may have a material impact on our future earnings and cash flows.

### **Market Risk**

We are also exposed to general market and other risk and its potential impact on accounts receivable or costs and estimated earnings in excess of billings on uncompleted contracts. The amounts recorded may be at risk if our customers' ability to pay these obligations is negatively impacted by economic conditions. Our customers and their industries are typically engineering procurement and construction firms, oil and gas producers, oil and gas pipelines, refineries, petrochemical plants, electrical power generators, public and private utilities, co-generation facilities, mining/metals operations, pulp and paper plants, transportation authorities, governmental agencies and other large industrial customers. We maintain ongoing discussions with customers regarding contract status with respect to payment status, change orders and billing terms in an effort to monitor collections of amounts billed.

## **Item 4. *Controls and Procedures***

### **Evaluation of Disclosure Controls and Procedures**

We have established and maintain a system of disclosure controls and procedures that are designed to provide reasonable assurance that information required to be disclosed in our reports filed with the SEC pursuant to the Securities Exchange Act of 1934, as amended (Exchange Act) is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), as appropriate, to allow timely decisions regarding required disclosures.

Management, with the participation of our CEO and CFO, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this report. Based on such evaluation, our CEO and CFO have each concluded that as of the end of the period, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

### **Remediation of Previously Disclosed Material Weaknesses**

Management previously concluded as of September 30, 2011, that we did not maintain effective internal controls over financial reporting related to the financial close and reporting process, revenue recognition for long-term construction projects, cost accumulation and the revenue and accounts receivable processes for service contracts, all at Powell Canada. These control deficiencies resulted in the restatement of our interim consolidated financial statements for the quarterly periods ended March 31, 2011 and June 30, 2011. Accordingly, management determined that these control deficiencies constituted weaknesses in internal controls over financial reporting as of September 30, 2011. Management has hired new staff, conducted additional training and implemented procedural and review controls to remediate the material weaknesses noted above. We tested the implemented controls and found them to be effective and concluded as of June 30, 2012, these material weaknesses have been

remediated.

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**Changes in Internal Control over Financial Reporting**

Other than the remediation efforts described above, there have been no changes in our internal control over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION**

**Item 1. *Legal Proceedings***

We are involved in various legal proceedings, claims and other disputes arising in the ordinary course of business which, in general, are subject to uncertainties and the outcomes are not predictable. We do not believe that the ultimate conclusion of these disputes could materially affect our financial position or results of operations.

**Item 1A. *Risk Factors***

There are no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the fiscal year ended September 30, 2011.

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**Item 6. Exhibits**

<b>Number</b>	<b>Description of Exhibits</b>
3.1	Certificate of Incorporation of Powell Industries, Inc. filed with the Secretary of State of the State of Delaware on February 11, 2004 (filed as Exhibit 3.1 to our Form 8-A/A filed November 1, 2004, and incorporated herein by reference).
3.2	By-laws of Powell Industries, Inc. (filed as Exhibit 3.2 to our Form 8-A/A filed November 1, 2004, and incorporated herein by reference).
*31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a).
*31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a).
*32.1	Certification of Chief Executive Officer Pursuant to Section 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
*32.2	Certification of Chief Financial Officer Pursuant to Section 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

\* Filed herewith

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**SIGNATURES**

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

POWELL INDUSTRIES, INC.  
(Registrant)

August 8, 2012  
Date

By: /s/ Thomas W. Powell  
Thomas W. Powell  
Chairman of the Board

President and Chief Executive Officer  
  
(Principal Executive Officer)

August 8, 2012  
Date

By: /s/ Don R. Madison  
Don R. Madison  
Executive Vice President

Chief Financial and Administrative Officer  
  
(Principal Financial Officer)

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