

FLOTEK INDUSTRIES INC/CN/
Form 10-Q
August 08, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **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**

For the transition period from to

Commission File Number 1-13270

FLOTEK INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

90-0023731
(I.R.S. Employer
Identification No.)

2930 W. Sam Houston Parkway N. #300

Houston, TX
(Address of principal executive offices)

77043
(Zip Code)

(713) 849-9911
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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.

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 Rule 12b-2 of the Exchange Act). Yes No

As of July 27, 2012, there were 49,687,001 outstanding shares of Flotek Industries, Inc. common stock, \$0.0001 par value.

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****FLOTEK INDUSTRIES, INC.****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

(in thousands, except share data)

	June 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 10,725	\$ 46,682
Restricted cash	150	150
Accounts receivable, net of allowance for doubtful accounts of \$788 and \$571 at June 30, 2012 and December 31, 2011, respectively	42,392	44,567
Inventories, net	40,977	37,888
Deferred tax assets, net	827	841
Other current assets	5,012	1,933
Total current assets	100,083	132,061
Property and equipment, net	48,918	43,914
Goodwill	26,943	26,943
Other intangible assets, net	25,734	29,094
TOTAL ASSETS	\$ 201,678	\$ 232,012
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 16,570	\$ 18,562
Accrued liabilities	8,995	8,397
Income taxes payable	1,479	3,876
Interest payable	1,093	2,097
Convertible senior notes, net of discount	53,231	
Current portion of long-term debt	968	767
Total current liabilities	82,336	33,699
Convertible senior notes, net of discount		99,738
Long-term debt, less current portion	1,022	875
Warrant liability		16,622
Deferred tax liabilities, net	2,994	2,780
Total liabilities	86,352	153,714
Commitments and contingencies		
Stockholders equity:		

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Cumulative convertible preferred stock, \$0.0001 par value, 100,000 shares authorized; no shares issued and outstanding

Common stock, \$0.0001 par value, 80,000,000 shares authorized; 52,872,524 shares issued and 49,678,844 shares outstanding at June 30, 2012; 51,957,652 shares issued and 49,153,495 shares outstanding at

December 31, 2011	5	5
Additional paid-in capital	187,576	166,814
Accumulated other comprehensive income (loss)	(72)	(44)
Accumulated deficit	(70,026)	(86,810)
Treasury stock, at cost; 1,404,994 and 1,358,299 shares at June 30, 2012 and December 31, 2011, respectively	(2,157)	(1,667)
 Total stockholders' equity	 115,326	 78,298
 TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	 \$ 201,678	 \$ 232,012

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents**FLOTEK INDUSTRIES, INC.****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(in thousands, except per share data)**

	Three Months Ended June 30, 2012	2011	Six Months Ended June 30, 2012	2011
Revenue	\$ 78,303	\$ 55,918	\$ 157,498	\$ 108,823
Cost of revenue	45,278	33,674	91,022	65,434
Gross margin	33,025	22,244	66,476	43,389
Expenses:				
Selling, general and administrative	15,776	12,729	30,689	23,069
Depreciation and amortization	1,038	1,015	1,996	2,037
Research and development	622	594	1,454	1,093
Total expenses	17,436	14,338	34,139	26,199
Income from operations	15,589	7,906	32,337	17,190
Other income (expense):				
Loss on extinguishment of debt	(995)	(3,225)	(6,386)	(3,225)
Change in fair value of warrant liability	6,524	3,253	2,649	10,807
Interest expense	(2,164)	(4,489)	(4,415)	(9,346)
Other income (expense), net	(343)	3	(350)	20
Total other income (expense)	3,022	(4,458)	(8,502)	(1,744)
Income before income taxes	18,611	3,448	23,835	15,446
Income tax expense	(5,433)	(1,322)	(7,051)	(2,946)
Net income	13,178	2,126	16,784	12,500
Accrued dividends and accretion of discount on preferred stock				(4,868)
Net income attributable to common stockholders	\$ 13,178	\$ 2,126	\$ 16,784	\$ 7,632
Earnings per common share:				
Basic earnings per common share	\$ 0.27	\$ 0.05	\$ 0.35	\$ 0.19
Diluted earnings per common share	\$ 0.25	\$ 0.04	\$ 0.33	\$ 0.17
Weighted average common shares:				
Weighted average common shares used in computing basic earnings per common share	48,227	44,749	47,890	41,180
Weighted average common shares used in computing diluted earnings per common share	54,032	47,433	50,586	45,523

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See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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FLOTEK INDUSTRIES, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income	\$ 13,178	\$ 2,126	\$ 16,784	\$ 12,500
Other comprehensive loss:				
Foreign currency translation adjustment	(41)	(24)	(28)	(25)
Comprehensive income	\$ 13,137	\$ 2,102	\$ 16,756	\$ 12,475

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents**FLOTEK INDUSTRIES, INC.****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

	Six Months Ended June 30,	
	2012	2011
Cash flows from operating activities:		
Net income	\$ 16,784	\$ 12,500
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Change in fair value of warrant liability	(2,649)	(10,807)
Depreciation and amortization	5,501	4,964
Amortization of deferred financing costs	530	1,987
Accretion of debt discount	2,031	2,657
Gain on sale of assets	(2,475)	(1,428)
Stock compensation expense	5,877	2,698
Deferred income tax provision	746	(160)
Excess tax benefit related to share-based awards	(518)	(229)
Non-cash loss on extinguishment of debt	4,270	3,225
Change in current assets and liabilities:		
Accounts receivable	2,175	(11,048)
Inventories	(3,089)	(8,429)
Accrued liabilities	604	(1,152)
Interest payable	(1,004)	(30)
Accounts payable	(1,992)	1,254
Other current assets	(2,321)	(1,806)
Income taxes payable	(2,397)	2,414
Net cash provided by (used in) operating activities	22,073	(3,390)
Cash flows from investing activities:		
Capital expenditures	(9,478)	(3,657)
Proceeds from sale of assets	2,618	2,279
Purchase of patents and other intangible assets	(29)	(220)
Net cash used in investing activities	(6,889)	(1,598)
Cash flows from financing activities:		
Repayments of indebtedness	(51,535)	(32,871)
Excess tax benefit related to share-based awards	518	229
Purchase of treasury stock	(490)	(199)
Proceeds from sale of common stock		29,438
Proceeds from exercise of stock options	131	109
Proceeds from exercise of warrants	263	4,581
Debt issuance costs		(1,000)
Net cash (used in) provided by financing activities	(51,113)	287
Effect of exchange rate changes on cash and cash equivalents held or due in a foreign currency	(28)	(25)
Net decrease in cash and cash equivalents	(35,957)	(4,726)

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Cash and cash equivalents at the beginning of period	46,682	19,863
Cash and cash equivalents at the end of period	\$ 10,725	\$ 15,137

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

Table of Contents**FLOTEK INDUSTRIES, INC.****UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY****(in thousands)**

	Common Stock		Treasury Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total
	Shares Issued	Par Value	Shares	Cost				
Balance, December 31, 2011	51,958	\$ 5	1,358	\$ (1,667)	\$ 166,814	\$ (44)	\$ (86,810)	\$ 78,298
Net income							16,784	16,784
Other comprehensive loss						(28)		(28)
Stock warrants exercised	217				263			263
Fair value of warrant liability reclassified to additional paid-in-capital					13,973			13,973
Stock options exercised	38				131			131
Treasury stock purchased			40	(490)				(490)
Restricted stock granted	660							
Restricted stock forfeited			7					
Excess tax benefit related to share-based awards					518			518
Stock compensation expense					5,877			5,877
Balance, June 30, 2012	52,873	\$ 5	1,405	\$ (2,157)	\$ 187,576	\$ (72)	\$ (70,026)	\$ 115,326

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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FLOTEK INDUSTRIES, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Organization and Significant Accounting Policies

Organization and Nature of Operations

Flotek Industries, Inc. (Flotek or the Company) is a global developer and supplier of drilling and production related products and services. Flotek's strategic focus, and that of all diversified wholly-owned subsidiaries (collectively referred to as the Company), includes oilfield specialty chemicals and logistics, down-hole drilling tools and down-hole production tools used in the energy and mining industries. The Company's strategic focus also includes material handling automation as well as loading facility logistics and blending functionality for a variety of bulk materials. Flotek's products and services enable customers to drill wells more efficiently to realize increased production from existing wells and to decrease future and existing well operating costs. Major customers include leading oilfield service providers, major as well as independent oil and gas exploration and production companies, and onshore and offshore drilling contractors.

The Company is headquartered in Houston, Texas, with operational locations in Colorado, Louisiana, New Mexico, North Dakota, Oklahoma, Pennsylvania, Texas, Utah, Wyoming and The Netherlands. Products are marketed domestically and internationally in over 20 countries. Flotek was initially incorporated under the laws of the Province of British Columbia on May 17, 1985. On October 23, 2001, Flotek changed the corporate domicile to the state of Delaware.

Basis of Presentation

The accompanying Unaudited Condensed Consolidated Financial Statements (the Financial Statements) reflect all adjustments, in the opinion of management, necessary for fair presentation of the financial condition and results of operations for the periods presented. All such adjustments are normal and recurring in nature. The Financial Statements, including selected notes, are prepared in accordance with applicable rules and regulations of the Securities and Exchange Commission (the SEC) regarding interim financial reporting and do not include all information and disclosures required by accounting principles generally accepted in the United States of America (GAAP) for comprehensive financial statement reporting. These interim Financial Statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 (the Annual Report). A copy of the Annual Report is available on the SEC's website, www.sec.gov, under the Company's ticker symbol (FTK) or alternatively by visiting Flotek's website, www.flotekind.com. The results of operations for the six months ended June 30, 2012, are not necessarily indicative of the results to be expected for the year ending December 31, 2012.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect amounts reported in the Financial Statements and accompanying notes. Actual results could differ materially from these estimates.

Reclassifications

Certain reclassifications have been made to prior year balances in order to conform to the current year presentation. These reclassifications had no impact on net income.

Note 2 Recent Accounting Pronouncements

Application of New Accounting Standards

Effective January 1, 2012, the Company adopted the accounting guidance in Accounting Standards Update (ASU) No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs* and is providing additional disclosures relating to unobservable inputs used for Level 3 measurements and about transfers between Level 1 and Level 2 of the fair value hierarchy. Implementation of this guidance required additional disclosures related to fair value measurements beginning for interim periods in 2012.

Effective January 1, 2012, the Company adopted the accounting guidance in ASU No. 2011-5, *Presentation of Comprehensive Income* and has elected to present components of net income and comprehensive income in two separate, but consecutive statements. Implementation of this

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guidance did not change the components of net income or other comprehensive income and only changed the presentation of the financial statements. The new guidance is required to be applied retrospectively to all periods presented.

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In December 2011, the Financial Accounting Standards Board (FASB) issued ASU No. 2011-12, *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU No. 2011- 05*. ASU No. 2011-12 defers changes required in ASU No. 2011-05 related to the presentation of reclassification adjustments and allows time for re-deliberation by the FASB.

Note 3 Supplemental Cash Flow Information

Supplemental cash flow information is as follows (in thousands):

	Six Months Ended June 30,	
	2012	2011
Supplemental non-cash investing and financing activities:		
Fair value of warrant liability reclassified to additional paid-in-capital	\$ 13,973	\$
Value of preferred stock exchanged in conversion to common stock		11,205
Value of common stock issued in payment of convertible notes		5,165
Value of common stock issued in payment of preferred stock dividends		3,254
Value of common stock issued in payment of term loan debt		1,398
Property and equipment acquired through capital leases	873	365
Supplemental cash payment information:		
Interest paid	\$ 2,950	\$ 4,732
Income taxes paid, net	8,574	617

Note 4 Revenue

The Company differentiates revenue and cost of revenue dependent upon whether the source of revenue is attributable to Products, Rentals or Services. Revenue by source is as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Revenue:				
Product	\$ 55,156	\$ 37,040	\$ 110,924	\$ 72,012
Rental	16,981	14,823	35,047	28,958
Service	6,166	4,055	11,527	7,853
	\$ 78,303	\$ 55,918	\$ 157,498	\$ 108,823
Cost of revenue:				
Product	32,030	23,438	64,427	45,105
Rental	7,784	6,401	16,359	12,882
Service	3,650	2,355	6,732	4,520
Depreciation	1,814	1,480	3,504	2,927
	\$ 45,278	\$ 33,674	\$ 91,022	\$ 65,434

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Inventory is as follows (in thousands):

	June 30, 2012	December 31, 2011
Raw materials	\$ 11,493	\$ 12,490
Work-in-process	375	160
Finished goods	31,676	27,917