Primoris Services CORP
Form 10-Q
November 14, 2008
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**
	For the quarterly period ended September 30, 2008
OR	
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.**
	For the transition period from to .

Commission file number 0001-34145

Primoris Services Corporation

(Exact name of registrant as specified in its charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**20-4743916** (I.R.S. Employer Identification No.)
26000 Commercentre Drive, Lake Forest, California (Address of Principal Executive Offices)	**92630** (Zip Code)

Registrant s telephone number, including area code: **(949) 598-9242**

Former Name, Former Address and Former Fiscal Year, if changed since last report.

Former Name: Rhapsody Acquisition Corp.

Former Address: 825 Third Avenue, 40th Floor New York, NY 10022

Former Fiscal Year: March 31

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 x No o

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 o Accelerated filer o Non-accelerated filer x Smaller reporting company o
(Do not check if a 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 o No x

As of October 31, 2008, 29,977,339 shares of the registrant s common stock were outstanding.

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PRIMORIS SERVICES CORPORATION

PART 1. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONDENSED CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS, EXCEPT SHARE AMOUNTS)

		September 30, 2008 (Unaudited)		December 31, 2007
ASSETS				
Current assets:				
Cash and cash equivalents	$	76,695	$	62,966
Restricted cash		13,022		9,984
Accounts receivable, net		83,485		113,307
Costs and estimated earnings in excess of billings		22,837		11,085
Deferred income taxes		4,528		
Inventory, prepaid expenses and other current assets		3,585		4,251
Total current assets		204,152		201,593
Property and equipment, net		27,300		16,143
Other assets		364		922
Investment in non-consolidated joint ventures		531		
Goodwill and other intangible assets		2,932		2,315
Total assets	$	235,279	$	220,973
LIABILITIES AND STOCKHOLDERS EQUITY				
Current liabilities:				
Accounts payable	$	50,384	$	66,792
Billings in excess of costs and estimated earnings		72,743		54,143
Accrued expenses and other current liabilities		25,202		18,215
Distributions payable		7,025		6,115
Current portion of capital leases		1,915		892
Current portion of long-term debt		4,756		3,966
Total current liabilities		162,025		150,123
Long-term debt, net of current portion		22,024		21,433
Long-term capital leases, net of current portion		1,092		1,208
Deferred tax liabilities		1,759		
Other long-term liabilities				1,286
Total liabilities		186,900		174,050
Stockholders equity				
Preferred stock - $.0001 par value, 1,000,000 shares authorized, 0 outstanding				

Common stock - $.0001 par value; authorized: 60,000,000 shares; 29,977,339 and 23,587,200 issued and outstanding at September 30, 2008 and December 31, 2007		3		2
Additional paid-in capital		36,121		1,305
Retained earnings		12,152		45,513
Accumulated other comprehensive income		103		103
Total stockholders equity		48,379		46,923
Total liabilities and stockholders equity	$	235,279	$	220,973

See Accompanying Notes to Condensed Consolidated Financial Statements

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PRIMORIS SERVICES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007
	(Unaudited)		(Unaudited)	
Revenues	$ 146,737	$ 158,054	$ 458,572	$ 382,102
Cost of revenues	125,634	137,489	406,622	339,406
Gross profit	21,103	20,565	51,950	42,696
Selling, general and administrative expenses	7,039	8,531	21,662	21,930
Merger related stock expense	3,675		3,675	
Operating income	10,389	12,034	26,613	20,766
Other income (expense):				
Income from non-consolidated entities	1,474	313	4,501	1,083
Foreign exchange gain (loss)	89	(399)	67	(439)
Interest income (expense) net	(132)	(115)	(356)	(216)
Income before provision for income taxes	11,820	11,833	30,825	21,194
Provision for income taxes	(1,734)	(339)	(2,188)	(713)
Net income	$ 10,086	$ 11,494	$ 28,637	$ 20,481
Dividends per common share	$ 0.025	$	$ 0.025	$
Basic earnings per share	$ 0.36	$ 0.49	$ 1.15	$ 0.87
Diluted earnings per share	$ 0.32	$ 0.49	$ 1.10	$ 0.87
Weighted average common shares outstanding				
Basic	27,824	23,587	25,010	23,415
Diluted	31,063	23,587	26,093	23,415
Pro forma net income data:				
Income before provision for income tax, as reported	$ 11,820	$ 11,833	30,825	$ 21,194
Adjustments for provision for income tax	(4,706)	(4,711)	(12,271)	(8,437)
Pro forma adjusted net income	$ 7,114	$ 7,122	$ 18,554	$ 12,757
Pro forma earnings per share				
Basic	$ 0.26	$ 0.30	$ 0.74	$ 0.54
Diluted	$ 0.23	$ 0.30	$ 0.71	$ 0.54

See Accompanying Notes to Condensed Consolidated Financial Statements

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PRIMORIS SERVICES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(IN THOUSANDS)

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007
	(Unaudited)		(Unaudited)	
Cash flows from operating activities:				
Net income	$ 10,086	$ 11,494	$ 28,637	$ 20,481
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	1,796	1,177	4,763	3,529
Amortization of other intangible assets	9	33	27	98
Merger related stock expense	3,675		3,675	
Gain on sale of property and equipment	(344)	(21)	(724)	(173)
Income from non-consolidated joint ventures	(1,474)	(313)	(4,502)	(1,083)
Changes in assets and liabilities:				
Restricted cash	(3,819)	1,821	(3,038)	(1,279)
Accounts receivable	(210)	(11,216)	29,822	(3,198)
Costs and estimated earnings in excess of billings	(3,923)	3,112	(11,752)	(149)
Inventory, prepaid expenses and other current assets	597	(597)	667	(718)
Other assets	(320)	(405)	564	(940)
Accounts payable	(2,880)	9,163	(16,408)	9,301
Billings in excess of costs and estimated earnings	6,520	7,495	18,600	12,068
Accrued expenses and other current liabilities	6,713	2,388	6,986	840
Deferred income taxes	(2,769)		(2,769)	
Other long-term liabilities	(1,315)	187	(1,286)	331
Net cash provided by operating activities	12,342	24,318	53,262	39,108
Cash flows from investing activities:				
Purchase of property and equipment	(5,576)	(365)	(9,241)	(871)
Proceeds from sale of property and equipment	437	46	1,120	253
Non-consolidated entity distributions	2,754		3,320	
Net cash used in investing activities	(2,385)	(319)	(4,801)	(618)
Cash flows from financing activities:				
Repayment of long-term debt	(1,607)	(939)	(4,787)	(2,438)
Repurchase of common stock	(3,331)	(1,064)	(3,331)	(1,064)
Proceeds from issuance of common stock	34,472	1,567	34,472	1,567
Cash distributions to stockholders	(43,068)	(7,143)	(61,086)	(14,032)
Net cash used in financing activities	(13,534)	(7,579)	(34,732)	(15,967)
Net change in cash and cash equivalents	(3,577)	16,420	13,729	22,523
Cash and cash equivalents at beginning of period	80,272	19,218	62,966	13,115
Cash and cash equivalents at end of the period	$ 76,695	$ 35,638	$ 76,695	$ 35,638

See Accompanying Notes to Condensed Consolidated Financial Statements

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PRIMORIS SERVICES CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
(IN THOUSANDS)

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007
	(Unaudited)		(Unaudited)	
Non-Cash Activities				
Obligations incurred for the acquisition of property and equipment	$	$	$ 7,075	$ 4,470

See Accompanying Notes to Condensed Consolidated Financial Statements

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except share amounts)

(Unaudited)

Note 1 Nature of Business

Organization and operations

Primoris Services Corporation and its wholly-owned subsidiaries ARB, Inc., ARB Structures, Inc., Onquest, Inc., Born Heaters Canada, ULC, Cardinal Contractors, Inc., Cardinal Mechanical, L.P., Pipeline Trenching LLC, Stellaris, LLC and ARB Ecuador, Ltda., collectively Primoris or the Company is engaged in various construction and engineering activities. The Company s underground and directional drilling operations install, replace and repair natural gas, petroleum, telecommunications and water pipeline systems. The Company s industrial, civil and engineering operations construct and provide maintenance services to industrial facilities including power plants, petrochemical facilities, and other processing plants, and construct multi-level parking structures. The Company is incorporated in the State of Delaware and has its corporate headquarters in Lake Forest, California.

On February 19, 2008, Primoris Corporation (the Former Primoris), a privately held company, entered into an Agreement and Plan of Merger (Merger Agreement) with Rhapsody Acquisition Corp. (Rhapsody), a publicly held company trading on the OTC Bulletin Board under the symbols RPSD , RPSDW and RPSDU for its common stock, warrants to purchase common stock (Warrants) and Un (each unit consisting of one share of common stock and one Warrant), respectively. On July 31, 2008, with the approval of the stockholders of each of Former Primoris and Rhapsody, the merger was completed. While Rhapsody was the surviving legal entity, Former Primoris was deemed the acquiring entity for accounting purposes (See Note 4, *Completed Merger*). As part of the merger, Rhapsody changed its name to Primoris Services Corporation. The Company s common stock, Warrants and units now trade on the Nasdaq Global Market under the symbols PRIM , PRIMW and PRIMU , respectively. The audited financial statements of Rhapsody for the period ended March 31, 2007 and the year ended March 31, 2008, and the audited financial statements for Former Primoris for each of the three years ended December 31, 2005, 2006 and 2007 are included in Rhapsody s Form S-4/A filed with the Securities and Exchange Commission (the SEC) on July 9, 2008. The unaudited financial statements for Former Primoris for the three and six months ended June 30, 2008, are included in Rhapsody s Current Report on Form 8-K/A filed with the SEC on August 11, 2008.

Unless specifically noted otherwise, as used throughout these Condensed Consolidated Financial Statements, Primoris or, the Company or we, our, us or its refers to the business, operations and financial results of Former Primoris prior to; and Primoris Services Corporation and its wholly-owned subsidiaries subsequent to; the closing of the merger between Rhapsody and Former Primoris; as the context requires. Rhapsody refers to the operations or financial results of Rhapsody Acquisition Corp. prior to the closing of the merger transaction.

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PRIMORIS CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

Seasonality - Primoris results of operations can be subject to seasonal variations. Weather, particularly rain, can impact Primoris ability to work off backlog. In addition, demand for new projects is generally lower during the early part of the year due to reduced construction activity based on weather concerns. Since the majority of the Company s work is in California, these seasonal impacts are not as dramatic for the Company as may be experienced by companies in some other states or countries. However, as a result, there is a possibility that the Company may experience higher revenues and earnings in the third and fourth quarters of the year as compared to the first two quarters. Additionally, because of the cyclical nature of its business, the financial results for any period may fluctuate depending on whether and when the Company is awarded projects. The Company s clients budget cycles can have an impact on the timing of these awards. Accordingly, the Company s financial condition and operating results may vary from quarter-to-quarter and may not be indicative of its financial condition or operating results for any other quarter or for an entire year.

Note 2 - Basis of Presentation and Significant Accounting Policies

The accompanying unaudited interim Condensed Consolidated Financial Statements were prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and the interim financial statement rules and regulations of the SEC. In the opinion of management, these statements include all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the Condensed Consolidated Financial Statements. The interim operating results are not necessarily indicative of the results for a full year or for any other interim period.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations relating to interim financial statements. The Consolidated Condensed Financial Statements should be read in conjunction with the audited consolidated financial statements and related notes included in Rhapsody s Form S-4/A, filed with the SEC on July 9, 2008.

Principles of consolidation - The Condensed Consolidated Financial Statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates - The preparation of the Company s Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could materially differ from those estimates. Significant estimates used in preparing these consolidated financial statements include estimated costs to complete contracts, which have a direct effect on gross profit.

Goodwill - During 2005, the Company acquired the net assets of Born Heaters Canada Ltd. and Born Canada Services Ltd (the Born Acquisition). The Born Acquisition was recorded pursuant to the purchase method of accounting in accordance with Statement of Financial Accounting Standards, (SFAS) No. 141 *Business Combinations* . The seller is entitled to earn-out payments of up to $2,481 over a five year term, the determination of which is based on the acquired company exceeding pre-established hurdle rates. Amounts paid to the seller under the earn-out agreement increase the total cost of the Born Acquisition. The excess of the Born Acquisition cost over the fair value of the net identifiable tangible assets acquired has been assigned to goodwill, and other intangible assets as appropriate. Additional earn-out payments accrued or paid are recorded as an increase to goodwill. During the period ended September 30, 2008 an additional

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

$644 was payable under the earn-out agreement, which increased the balance of goodwill to $2,871 as of September 30, 2008 from $2,227 as of December 31, 2007. There was $80 remaining of potential additional earn-out for the seller as of September 30, 2008.

Foreign operations - Through its subsidiaries, the Company maintains foreign operations in Canada and Ecuador. In addition, the Company has an investment in ARB Arendal (see Note 8 *Equity Method Investments*), which has operations in Mexico. At September 30, 2008, the Company had operations with assets aggregating approximately $9,200 and $14,100 in Ecuador and Canada, respectively. At December 31, 2007, the Company had operations with assets aggregating $3,100 and $14,800 in Ecuador and Canada, respectively.

Worker s compensation insurance - The Company self-insures worker s compensation claims to a certain level. The Company maintained a self-insurance reserve totaling approximately $4,800 and $4,400 at September 30, 2008 and December 31, 2007, respectively. The amount is included in accrued expenses and other current liabilities on the accompanying consolidated balance sheets. Actual payments that may be made in the future could materially differ from such reserves.

Functional currencies and foreign currency translation - The United States dollar is the functional currency in Canada and Ecuador, as substantially all monetary transactions are made in that currency, and other significant economic facts and circumstances currently support that position. As these factors may change in the future, the Company periodically assesses its position with respect to the functional currency of foreign subsidiaries. Included in other income is a foreign exchange gain of $67 for the nine months ended September 30, 2008 and losses of $439 for the nine months ended September 30, 2007.

***Fixed-price contracts* -** Historically, substantial portions of the Company s revenues have been generated under fixed-price contracts. Fixed-price contracts carry certain inherent risks, including underestimation of costs, problems with new technologies and economic and other changes that may occur over the contract period. The Company recognizes revenues using the percentage-of-completion method for fixed-price contracts, which may result in uneven and irregular results. Unforeseen events and circumstances can alter the estimate of the costs and potential profit associated with a particular contract. To the extent that original cost estimates are modified, estimated costs to complete increase, delivery schedules are delayed, or progress under a contract is otherwise impeded, cash flow, revenue recognition and profitability from a particular contract may be adversely affected.

***Revenue recognition* -** A number of factors relating to the business of the Company affect the recognition of contract revenue. The Company typically structures contracts as unit-price, time and material, fixed-price or cost plus fixed fee. Revenue is recognized on the percentage-of-completion method for all of the types of contracts described in the paragraph above. Under the percentage-of-completion method, estimated contract income and resulting revenue is generally accrued based on costs incurred to date as a percentage of total estimated costs. Total estimated costs, and thus contract income, are impacted by changes in productivity, scheduling, and the unit cost of labor, subcontracts, materials and equipment. Additionally, external factors such as weather, client needs, client delays in providing permits and approvals, labor availability, governmental regulation and politics may affect the progress of a project s completion and thus the timing of revenue recognition. If a current estimate of total contract cost indicates a loss on a contract, the projected loss is recognized in full when determined.

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

The Company considers unapproved change orders to be contract variations on which Primoris has customer approval for scope change but not for price changes associated with such scope change. Costs associated with unapproved change orders are included in the estimated cost to complete the contracts and are expensed as incurred. The Company recognizes revenue equal to costs incurred on unapproved change orders when realization of price approval is probable and the estimated amount is equal to or greater than its costs related to the unapproved change order. Revenue recognized on unapproved change orders is included in costs and estimated earnings in excess of billings on the consolidated balance sheets.

Unapproved change orders involve the use of estimates, and it is reasonably possible that revisions to the estimated costs and recoverable amounts may be required in future reporting periods to reflect changes in estimates or final agreements with customers.

The Company considers claims to be amounts Primoris seeks or will seek to collect from customers or others for customer-caused changes in contract specifications or design, or other customer-related causes of unanticipated additional contract costs on which there is no agreement with customers on both scope and price changes. Revenue from claims is recognized when agreement is reached with customers as to the value of the claims, which in some instances may not occur until after completion of work under the contract. Costs associated with claims are included in the estimated costs to complete the contracts and are expensed when incurred.

Merger related stock expense In connection with the Merger Agreement, Rhapsody, the Former Primoris and two foreign managers of Former Primoris entered into termination agreements related to the fulfillment of obligations under a Put/Call Agreement and a Phantom Stock Agreement (collectively the Deferred Compensation Agreements) discussed in Note 17, *Deferred Compensation Agreements* . Upon consummation of the merger, (see Note 4 *Completed Merger*), the termination agreements cancelled the obligations of the parties under the Deferred Compensation Agreements and called for the issuance to the foreign managers of an aggregate of 507,600 shares of the Company s common stock and for the cash payment of the amounts already accrued under the Deferred Compensation Agreements.

As a result of the issuance of the shares and in accordance with SFAS No 123 (revised 2004) *Share-based Payments* the Company recognized a one-time charge of $3,675 of non-cash expenses related to the termination of the Deferred Compensation Agreements. The same amounts were recorded as an increase to additional paid-in capital and, therefore, had no effect on the Company s net asset value. The issuance of the shares was a one-time, non-recurring event directly related to the consummation of the merger, therefore the entire value of the shares was taken as a charge to earnings at the time of issuance, which was the closing of the merger.

Derivative instruments and hedging activities - From time to time the Company utilizes foreign currency hedge agreements to manage foreign currency exchange exposures, which is accounted for in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* and SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities - an Amendment of SFAS No. 133.*

In January 2008, the Company purchased two derivative financial instruments for the purpose of hedging future currency exchange in Canadian dollars. The contracts enabled the Company to purchase Canadian dollars before certain dates in 2008 at certain exchange rates. The fair values of these contracts were $3,000 and $2,000 in U.S. dollars, respectively, and the related Canadian dollars sold were $3,005CAD and $2,004CAD, respectively. These contracts expired in March and June 2008, respectively. The related gain or loss on these contracts was not significant. At September 30, 2008 the Company had no foreign currency hedge agreements outstanding.

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

Note 3 - Recent Accounting Pronouncements

In March, 2008, the Financial Accounting Standards Board (FASB) issued SFAS No. 161 *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133.* This statement requires enhanced disclosures about an entity s derivative and hedging activities in an effort to improve the transparency of financial reporting. It also changes the disclosure requirements for derivative instruments and hedging activities. Under the statement, entities will be required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity s financial position, financial performance, and cash flows. This statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. The statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. The Company will adopt the provisions of SFAS No. 161 in the fourth quarter of 2008 as required.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations,* (SFAS No. 141R) and SFAS No. 160, *Accounting and Reporting Non-controlling Interest in Consolidated Financial Statements, an amendment of ARB No. 51.* These new standards significantly change the accounting for and reporting of business combination transactions and non-controlling interests (previously referred to as minority interests) in consolidated financial statements. Both standards are effective for the Company beginning January 1, 2009 and are applicable only to transactions occurring after the effective date. Therefore, the adoption of these standards will not affect the accounting for the merger between Rhapsody and Former Primoris. (See Note 4 *Completed Merger*). Management does not expect the adoption of SFAS No. 141R or SFAS No. 160 to have a material effect on its operations, financial position or cash flows.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities.* This statement permits entities to choose to measure many financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. Primoris has adopted SFAS No. 159 as of January 1, 2008, and the adoption did not have a material effect on its results of operations, financial position or cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measures*. This statement defines fair value, establishes a framework for measuring fair value in GAAP, expands disclosures about fair value measurements, and applies under other accounting pronouncements that require or permit fair value measurements. SFAS No. 157 does not require any new fair value measurements. However, the FASB anticipates that for some entities, the application of SFAS No. 157 will change current practices. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. Primoris has adopted SFAS No. 157 as of January 1, 2008, and the adoption did not have a material effect on its results of operations, financial position or cash flows.

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

Note 4 Completed Merger

Rhapsody was founded as a blank check company on April 24, 2006, to effect a merger, capital stock exchange, asset acquisition or other similar business combination with an operating business no later than October 3, 2008. As discussed above, on July 31, 2008 the merger was completed. In the merger, Rhapsody was the surviving legal entity; however, the merger was accounted for as a reverse acquisition and recapitalization. Under this method of accounting, Rhapsody was treated as the acquired company for financial reporting purposes. This determination was primarily based on the Former Primoris comprising the ongoing operations and management of the combined company. In accordance with guidance applicable to these circumstances, the merger was considered to be a capital transaction in substance. Accordingly, for accounting purposes, the merger was treated as the equivalent of Former Primoris issuing stock for the net assets of Rhapsody, accompanied by a recapitalization. The net assets of Rhapsody are stated at historical cost, with no goodwill or other intangible assets recorded. Operations prior to the merger are for those of Former Primoris.

The Former Primoris stockholders and two foreign managers of Former Primoris (collectively, the Former Primoris Holders), pursuant to certain termination agreements, and in exchange for all of their shares of common stock of Former Primoris that were outstanding immediately prior to the merger, received in the aggregate 24,094,800 shares of the Company s common stock. To secure the indemnity rights of Rhapsody under the Merger Agreement, 1,807,110 of the 24,094,800 shares of the Company s common stock issued to the Former Primoris Holders at the time of the merger were placed into escrow and are governed by the terms of an Escrow Agreement. The Merger Agreement also provided that the Former Primoris Holders would receive up to an additional 5,000,000 shares of the Company s common stock, contingent upon the combined company attaining certain defined performance targets in 2008 and 2009.

In connection with the merger, certain Rhapsody stockholders elected to convert their Rhapsody shares into cash as permitted by Rhapsody s certificate of incorporation. Holders of 417,461 shares of Rhapsody s common stock who voted against the merger with Former Primoris elected to exercise their conversion rights with respect to their shares. Each of the holders of those 417,461 shares received $7.98 per share, or an aggregate of $3,331 from the funds that had been placed in Rhapsody s trust by Rhapsody.

As a result of the closing of the merger, the Former Primoris Holders owned approximately 80.4% of the outstanding shares of the Company s common stock at the closing of the merger, and the remaining Rhapsody stockholders owned the remaining approximately 19.6% of the Company s outstanding shares of common stock.

At the closing of the merger, the Chief Executive Officer of the Company and eight other executives of the Company entered into employment agreements with either the Company or one of its subsidiaries.

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

Pursuant to the Merger Agreement, prior to the merger, Former Primoris distributed approximately $48,947 to its stockholders as a distribution of prior earnings of Former Primoris and for payment of their individual income tax liabilities. As a result of the merger, approximately $39,660 of cash and investments held in trust for Rhapsody was released and became part of the assets of the Company upon consummation of the merger. No other assets were contributed by Rhapsody to the post-merger entity. Expenses paid by the Company in connection with the merger amounted to $5,234.

Note 5 - Change in Tax Status

Through July 31, 2008 (the date of the merger), Former Primoris had elected to be taxed in accordance with Subchapter S of the Internal Revenue Code (S-Corporation) and similar codes in states in which the Company was subject to taxation. While this election was in effect, the income (whether distributed or not) was taxed for federal income tax purposes to the Former Primoris stockholders. Accordingly, no provision for federal income tax was required. The provision for income taxes for Former Primoris in 2007 was primarily related to Canadian income taxes.

As of the date of the merger, the Company effectively became taxable in accordance with Subchapter C of the Internal Revenue Code (C-Corporation), which changed the level of taxation from the stockholders to the Company. With the change in tax status, the Company completed an analysis of the effect of the provisions of SFAS No. 109 and FIN 48 (See Note 12 *Income Taxes*).

The unaudited pro forma net income taxes and the pro forma net income reflect federal and state income taxes assuming a combined federal and state statutory rate of 39.8%, as if the Company had been taxed as a C-Corporation for the three and nine months ended September 30, 2008 and 2007. This rate is higher than our 2008 effective tax rate for the three months ended September 30, 2008 as discussed in Note 12 *Income Taxes*, because the pro forma numbers do not consider the reduction in tax rate due to the Company s S-Corporation status through July 31, 2008.

As of September 30, 2008, the Company had $7,025 of undistributed Former Primoris S-Corporation earnings as provided for in the Merger Agreement based on the estimated 2008 S-Corporation tax liability of the Former Primoris stockholders. These amounts will be distributed to the stockholders of Former Primoris and are reflected as a liability on the balance sheet as of September 30, 2008.

Note 6 - Accounts Receivable

The following is a summary of accounts receivable:

	September 30, 2008 (Unaudited)	December 31, 2007
	(in thousands)	
Contracts receivable, net of allowance for doubtful accounts of $200	$ 69,813	$ 96,576
Retention	13,151	14,872
	82,964	111,448
Due from affiliates	34	502
Other accounts receivable	487	1,357
	$ 83,485	$ 113,307

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

Amounts due from affiliates primarily relate to amounts due from related parties (Note 8 *Equity Method Investments* and Note 11 *Related Party Transactions*) for the performance of construction contracts. Contract revenues earned from related parties were $15,144 and $5,918 for the nine months ended September 30, 2008 and 2007, respectively. Contract revenues earned from related parties for the three months ended September 30, 2008 and 2007 were $5,803 and $4,650, respectively. At September 30, 2008 and December 31, 2007 amounts due from OMPP totaling $5,708 and $535, respectively, are included in contracts receivable (see Note 8, *Equity Method Investments*).

Note 7 - Costs and Estimated Earnings on Uncompleted Contracts

Costs and estimated earnings on uncompleted contracts consist of the following at:

		September 30, 2008 (Unaudited)		December 31, 2007
Costs incurred on uncompleted contracts	$	1,136,111	$	988,472
Provision for estimated loss on uncompleted contracts		1,097		632
Gross profit recognized		79,070		84,606
		1,216,278		1,073,710
Less: billings to date		(1,266,184)		(1,116,768)
	$	(49,906)	$	(43,058)

This net amount is included in the accompanying Condensed Consolidated Balance Sheet under the following captions:

		September 30, 2008 (Unaudited)		December 31, 2007
Costs and estimated earnings in excess of billings	$	22,837	$	11,085
Billings in excess of cost and estimated earnings		(72,743)		(54,143)
	$	(49,906)	$	(43,058)

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PRIMORIS SERVICES CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

(Dollars in thousands, except per share amounts)

(Unaudited)

Note 8 - Equity Method Investments

During 2007, the Company established a joint-venture, Otay Mesa Power Partners (OMPP), for the sole purpose of constructing a power plant near San Diego, California. The Company has a 40% interest in OMPP and accounts for its investment in OMPP using the equity method. ARB, Inc. (ARB), the Company s wholly-owned subsidiary, acts as one of OMPP s primary subcontractors. ARB has contracts totaling $25,114 with OMPP and recognized $5,501 and $14,842, respectively, in related revenues for the three and nine months ended September 30, 2008 and $4,064 and $5,332, respectively, for the three and nine months ended September 30, 2007, which is included in the contract revenues earned from related parties as stated in Note 6 *Accounts Receivable* . At September 30, 2008 and December 31, 2007, $535 and $5,708, respectively, was due from OMPP under these contracts and is included in accounts receivable. The following is a summary of the financial position of OMPP as of September 30, 2008 and December 31, 2007 and results of operations for the nine months ended September 30, 2008 and September 30, 2007:

	September 30, 2008 (Unaudited)	December 31, 2007
Otay Mesa Power Partners		
Balance sheet data		
Assets	$ 51,258	$ 37,143
Liabilities		