CORE LABORATORIES N V
Form 10-Q
November 04, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
(Mark One)

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

For the quarterly period ended September 30, 2014
OR

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

For the transition period from ________________ to ______________

Commission File Number: 001-14273

CORE LABORATORIES N.V.
(Exact name of registrant as specified in its charter)

The Netherlands (State or other jurisdiction of incorporation or organization)	Not Applicable (I.R.S. Employer Identification No.)
Strawinskylaan 913 Tower A, Level 9 1077 XX Amsterdam The Netherlands (Address of principal executive offices)	Not Applicable (Zip Code)

(31-20) 420-3191
(Registrant's telephone number, including area code)

None
(Former name, former address and former fiscal year, if changed since last report)

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 Q 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 Q 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 Q Accelerated filer o Non-accelerated filer o 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 ¨ No Q

The number of common shares of the registrant, par value EUR 0.02 per share, outstanding at November 3, 2014 was 43,796,660.

CORE LABORATORIES N.V.
FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 30, 2014

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PART II - OTHER INFORMATION

PART I - FINANCIAL INFORMATION
Item 1. Financial Statements
CORE LABORATORIES N.V.
CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share data)

	September 30, 2014 (Unaudited)	December 31, 2013
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$25,307	$25,088
Accounts receivable, net of allowance for doubtful accounts of $3,526 and $2,872 at 2014 and 2013, respectively	201,769	201,322
Inventories	49,451	46,821
Prepaid expenses	14,398	13,128
Income taxes receivable	9,041	5,294
Other current assets	11,302	12,215
TOTAL CURRENT ASSETS	311,268	303,868
PROPERTY, PLANT AND EQUIPMENT, net	146,951	138,824
INTANGIBLES, net	10,867	10,949
GOODWILL	164,472	163,337
DEFERRED TAX ASSETS, net	7,167	4,452
OTHER ASSETS	44,407	39,580
TOTAL ASSETS	$685,132	$661,010
LIABILITIES AND EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$49,648	$50,821
Accrued payroll and related costs	34,096	38,969
Taxes other than payroll and income	11,308	6,979
Unearned revenue	11,045	10,887
Income taxes payable	5,746	14,462
Other accrued expenses	15,194	13,657
TOTAL CURRENT LIABILITIES	127,037	135,775
LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS	370,000	267,002
DEFERRED COMPENSATION	41,681	38,014
DEFERRED TAX LIABILITIES, net	5,685	8,870
OTHER LONG-TERM LIABILITIES	38,954	41,960
COMMITMENTS AND CONTINGENCIES (Note 6)		
EQUITY:		
Preference shares, EUR 0.02 par value; 6,000,000 shares authorized, none issued or outstanding	—	—
Common shares, EUR 0.02 par value; 200,000,000 shares authorized, 45,600,002 issued and 43,934,396 outstanding at 2014 and 46,750,002 issued and 45,101,389 outstanding at 2013	1,174	1,203
Additional paid-in capital	2,013	—
Retained earnings	384,335	415,930
Accumulated other comprehensive income (loss)	(8,368)	(8,626)
Treasury shares (at cost), 1,665,606 at 2014 and 1,648,613 at 2013	(283,656)	(245,184)
Total Core Laboratories N.V. shareholders' equity	95,498	163,323
Non-controlling interest	6,277	6,066

TOTAL EQUITY	101,775	169,389
TOTAL LIABILITIES AND EQUITY	$685,132	$661,010

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

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CORE LABORATORIES N.V.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Three Months Ended September 30,	
	2014	2013
	(Unaudited)	
REVENUE:		
Services	$203,578	$194,267
Product sales	72,557	78,896
Total revenue	276,135	273,163
OPERATING EXPENSES:		
Cost of services, exclusive of depreciation expense shown below	113,917	110,087
Cost of product sales, exclusive of depreciation expense shown below	53,010	57,340
General and administrative expense, exclusive of depreciation expense shown below	12,316	14,346
Depreciation	6,362	6,396
Amortization	483	357
Other (income) expense, net	927	41
OPERATING INCOME	89,120	84,596
Interest expense	2,561	2,302
Income before income tax expense	86,559	82,294
Income tax expense	19,909	20,490
Net income	66,650	61,804
Net income (loss) attributable to non-controlling interest	153	(91)
Net income attributable to Core Laboratories N.V.	$66,497	$61,895
EARNINGS PER SHARE INFORMATION:		
Basic earnings per share attributable to Core Laboratories N.V.	$1.51	$1.36
Diluted earnings per share attributable to Core Laboratories N.V.	$1.50	$1.35
Cash dividends per share	$0.50	$0.32
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:		
Basic	44,152	45,526
Diluted	44,381	45,828

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

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CORE LABORATORIES N.V.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Nine Months Ended September 30,	
	2014	2013
	(Unaudited)	
REVENUE:		
Services	$580,612	$564,424
Product sales	225,988	232,805
Total revenue	806,600	797,229
OPERATING EXPENSES:		
Cost of services, exclusive of depreciation expense shown below	336,194	329,901
Cost of product sales, exclusive of depreciation expense shown below	160,560	164,674
General and administrative expense, exclusive of depreciation expense shown below	33,983	38,328
Depreciation	18,731	17,775
Amortization	1,065	967
Other (income) expense, net	(14)	82
OPERATING INCOME	256,081	245,502
Interest expense	7,718	6,834
Income before income tax expense	248,363	238,668
Income tax expense	56,464	60,190
Net income	191,899	178,478
Net income (loss) attributable to non-controlling interest	604	391
Net income attributable to Core Laboratories N.V.	$191,295	$178,087
EARNINGS PER SHARE INFORMATION:		
Basic earnings per share attributable to Core Laboratories N.V.	$4.29	$3.88
Diluted earnings per share attributable to Core Laboratories N.V.	$4.27	$3.86
Cash dividends per share	$1.50	$0.96
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:		
Basic	44,571	45,854
Diluted	44,823	46,150

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

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CORE LABORATORIES N.V.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(Unaudited)		(Unaudited)	
Net income	$66,650	$61,804	$191,899	$178,478
Pension and other postretirement benefit plans				
Prior service cost				
Amortization to net income of transition asset	(21)	(21)	(65)	(65)
Amortization to net income of prior service cost	2	39	5	119
Amortization to net income of actuarial loss	135	117	405	351
Income taxes on pension and other postretirement benefit plans	(29)	(33)	(86)	(101)
Comprehensive income	66,737	61,906	192,158	178,782
Comprehensive income (loss) attributable to non-controlling interest	153	(91)	604	391
Comprehensive income attributable to Core Laboratories N.V.	$66,584	$61,997	$191,554	$178,391

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

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CORE LABORATORIES N.V.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Nine Months Ended September 30,	
	2014	2013
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$191,899	$178,478
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock-based compensation	15,497	15,408
Depreciation and amortization	19,796	18,742
Debt issuance costs	341	360
(Increase) decrease in value of life insurance policies	(724)	(3,194)
Deferred income taxes	(190)	6,212
Other non-cash items	728	316
Changes in assets and liabilities:		
Accounts receivable	(959)	(20,425)
Inventories	(3,053)	(5,143)
Prepaid expenses and other current assets	(7,041)	14,595
Other assets	1,529	(414)
Accounts payable	(2,171)	(1,506)
Accrued expenses	(10,604)	1,788
Unearned revenue	158	(1,361)
Other long-term liabilities	453	6,792
Net cash provided by operating activities	205,659	210,648
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(27,624)	(26,988)
Patents and other intangibles	(753)	(3,083)
Business acquisition, net of cash acquired	(1,200)	—
Investment in non-consolidated affiliates	—	(50)
Proceeds from sale of assets	1,098	852
Premiums on life insurance	(3,482)	(2,553)
Net cash used in investing activities	(31,961)	(31,822)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment of debt borrowings	(57,157)	(51,035)
Proceeds from debt borrowings	160,000	73,000
Stock options exercised	—	83
Excess tax benefits from stock-based compensation	2,680	2,500
Debt financing costs	(1,054)	—
Non-controlling interest - dividend	(393)	—
Dividends paid	(67,153)	(44,125)
Repurchase of common shares	(210,402)	(156,271)
Net cash used in financing activities	(173,479)	(175,848)
NET CHANGE IN CASH AND CASH EQUIVALENTS	219	2,978
CASH AND CASH EQUIVALENTS, beginning of period	25,088	19,226
CASH AND CASH EQUIVALENTS, end of period	$25,307	$22,204

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

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CORE LABORATORIES N.V.
NOTES TO THE UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements include the accounts of Core Laboratories N.V. and its subsidiaries for which we have a controlling voting interest and/or a controlling financial interest. These financial statements have been prepared in accordance with United States ("U.S.") generally accepted accounting principles ("GAAP") for interim financial information using the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, these financial statements do not include all of the information and footnote disclosures required by U.S. GAAP and should be read in conjunction with the audited financial statements and the summary of significant accounting policies and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013 (the "2013 Annual Report").

Core Laboratories N.V. uses the equity method of accounting for investments in which it has less than a majority interest and over which it does not exercise control but does exert significant influence. We use the cost method to record certain other investments in which we own less than 20% of the outstanding equity and do not exercise control or exert significant influence. Non-controlling interests have been recorded to reflect outside ownership attributable to consolidated subsidiaries that are less than 100% owned. In the opinion of management, all adjustments considered necessary for a fair statement of the results for the interim periods presented have been included in these financial statements. Furthermore, the operating results presented for the three and nine months ended September 30, 2014 may not necessarily be indicative of the results that may be expected for the year ended December 31, 2014.

Core Laboratories N.V.'s balance sheet information for the year ended December 31, 2013 was derived from the 2013 audited consolidated financial statements but does not include all disclosures in accordance with U.S. GAAP.

Certain reclassifications were made to prior period amounts in order to conform to the current period presentation. These reclassifications had no impact on the reported net income or cash flows for the three and nine months ended September 30, 2013.

References to "Core Lab", the "Company", "we", "our" and similar phrases are used throughout this Quarterly Report on Form 10-Q and relate collectively to Core Laboratories N.V. and its consolidated subsidiaries.

2. INVENTORIES

Inventories consist of the following (in thousands):

	September 30, 2014 (Unaudited)	December 31, 2013
Finished goods	$36,119	$37,143
Parts and materials	10,720	8,323
Work in progress	2,612	1,355
Total inventories	$49,451	$46,821

We include freight costs incurred for shipping inventory to customers in the Cost of product sales line of the Consolidated Statements of Operations.

3. GOODWILL AND INTANGIBLES

We account for intangible assets with indefinite lives, including goodwill, in accordance with the applicable accounting guidance, which requires us to evaluate these assets for impairment annually or more frequently if an indication of impairment is possible. Based upon our most recent evaluation at the end of 2013, we determined that intangible assets, including goodwill, are not impaired. We amortize intangible assets with a finite life on a straight-line basis over their respective useful lives.

4. DEBT AND CAPITAL LEASE OBLIGATIONS

Debt is summarized in the following table (in thousands):

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	September 30, 2014 (Unaudited)	December 31, 2013
Senior notes	$150,000	$150,000
Credit facility	220,000	117,000
Capital lease obligations	5	28
Total debt	370,005	267,028
Less - current maturities of long-term debt and capital lease obligations	5	26
Long-term debt and capital lease obligations, net	$370,000	$267,002

In 2011, we issued two series of senior notes with an aggregate principal amount of $150 million ("Senior Notes") in a private placement transaction. Series A consists of $75 million in aggregate principal amount of notes that bear interest at a fixed rate of 4.01% and are due in full on September 30, 2021. Series B consists of $75 million in aggregate principal amount of notes that bear interest at a fixed rate of 4.11% and are due in full on September 30, 2023. Interest on each series of the Senior Notes is payable semi-annually on March 30 and September 30.

On August 29, 2014, we entered into an agreement to amend our revolving credit facility (the "Credit Facility") to increase the aggregate borrowing capacity from $300 million to $350 million and to increase the uncommitted availability an additional $50 million to bring the total borrowings available to $400 million if certain prescribed conditions are met by the Company. The variable rate was reduced from LIBOR plus 1.5% to LIBOR plus 1.25%. The maturity date was extended from September 28, 2016 to August 29, 2019.

The Credit Facility carries an aggregate borrowing capacity of $350 million and provides an option to increase the commitment to $400 million, if certain conditions are met. The Credit Facility bears interest at variable rates from LIBOR plus 1.25% to a maximum of LIBOR plus 2.00%. Any outstanding balance under the Credit Facility is due August 29, 2019, when the Credit Facility matures. Interest payment terms are variable depending upon the specific type of borrowing under this facility. Our available capacity at any point in time is reduced by borrowings outstanding at the time and outstanding letters of credit which totaled $25.5 million at September 30, 2014, resulting in an available borrowing capacity under the Credit Facility of $104.5 million. In addition to those items under the Credit Facility, we had $19.5 million of outstanding letters of credit and performance guarantees and bonds from other sources as of September 30, 2014.

The terms of the Credit Facility and the Senior Notes require us to meet certain covenants, including, but not limited to, certain minimum equity and cash flow ratios. We believe that we are in compliance with all such covenants contained in our credit agreements. Certain of our material, wholly-owned subsidiaries are guarantors or co-borrowers under the Credit Facility and Senior Notes.

In October 2014, we entered into two interest rate swap agreements for a total notional amount of $50 million to hedge changes in the variable rate interest expense on $50 million of our existing or replacement LIBOR-priced debt. Under the first swap agreement of $25 million, which is effective through August 29, 2024, we will receive interest at one-month LIBOR and will pay interest at a fixed rate of 2.50%, resulting in a total fixed rate of 3.75% for this amount of debt. Under the second swap agreement of $25 million, which is effective through August 29, 2019, we will receive interest at one-month LIBOR and will pay interest at a fixed rate of 1.73%, resulting in a total fixed rate of 2.98% for this amount of debt. Both of these swaps are designated and qualify as cash flow hedging instruments, resulting in no effect to the Consolidated Statements of Operations or earnings per share.

The estimated fair value of total debt at September 30, 2014 and December 31, 2013 approximated the book value of total debt. The fair value was estimated using Level 2 inputs by calculating the sum of the discounted future interest and principal payments through the date of maturity.

5. PENSIONS AND OTHER POSTRETIREMENT BENEFITS

Defined Benefit Plan

We provide a non-contributory defined benefit pension plan for substantially all of our Dutch employees ("Dutch Plan") who were hired prior to 2007 based on years of service and final pay or career average pay, depending on when the employee began participating. The benefits earned by the employees are immediately vested. We fund the future obligations of the Dutch Plan by purchasing insurance contracts from a large multi-national insurance company. The insurance contracts are purchased annually and renew after five years at which time they are replaced with new contracts that are adjusted to include changes in the benefit obligation for the current year and redemption of the expired contracts. We make annual premium payments to the insurance company based on each employee's age and current salary, and the contractual growth rate. We determine the fair value of these plan assets with the assistance of an actuary using observable inputs (Level 2), which approximates the contract value of the investments.

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The following table summarizes the components of net periodic pension cost under the Dutch Plan for the three and nine months ended September 30, 2014 and 2013 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(Unaudited)		(Unaudited)	
Service cost	$361	$394	$1,103	$1,178
Interest cost	439	417	1,341	1,248
Expected return on plan assets	(326)	(321)	(995)	(961)
Amortization of transition asset	(21)	(21)	(65)	(65)
Amortization of prior service cost	2	39	5	119
Amortization of actuarial loss	135	117	405	351
Net periodic pension cost	$590	$625	$1,794	$1,870

During the nine months ended September 30, 2014, we contributed approximately $1.7 million to fund the estimated 2014 premiums on investment contracts held by the Dutch Plan.

Defined Contribution Plans

We maintain defined contribution plans (the "Defined Contribution Plans") for the benefit of eligible employees in certain countries, including Canada, The Netherlands, the United Kingdom and the United States. In accordance with the terms of each plan, we and our participating employees contribute up to specified limits, and under certain plans, we may make discretionary contributions in accordance with the terms of the Defined Contribution Plans.

Deferred Compensation Arrangements

We have entered into deferred compensation contracts for certain key employees. The benefits under these contracts are fully vested and benefits are paid when the participants attain 65 years of age. Life insurance policies with cash surrender values have been purchased for the purpose of assisting in the funding of the deferred compensation contracts.

We have adopted a non-qualified deferred compensation plan that allows certain highly compensated employees to defer a portion of their salary, commission and bonus, as well as the amount of any reductions in their deferrals under the deferred compensation plan for employees in the United States (the "Deferred Compensation Plan"), due to certain limitations imposed by the U.S. Internal Revenue Code of 1986, as amended (the "Internal Revenue Code"). The Deferred Compensation Plan also provides for employer contributions to be made on behalf of participants equal in amount to certain forfeitures of, and/or reductions in, employer contributions that participants could have otherwise received under the Defined Contribution Plan for U.S. employees qualified under Internal Revenue Code Section 401(k) had there not been certain limitations imposed by the Internal Revenue Code. Employer contributions to the Deferred Compensation Plan vest ratably over a period of five years. Contributions to the plan are invested in equity and other investment fund assets within life insurance policies, and carried on the balance sheet at fair value. A participant's plan benefits include the participant's deferrals, the vested portion of the employer's contributions, and deemed investment gains and losses on such amounts. The benefits under these contracts are fully vested and payment of benefits generally commences as of the last day of the month following the termination of services except that the payment of benefits for select executives generally commences on the first working day following a six month waiting period following the date of termination.

The Company's only financial assets and liabilities which involve fair value measures relate to certain aspects of the Company's benefit plans. On a recurring basis, we use the market approach to value certain assets and liabilities at fair value at quoted prices in an active market (Level 1) and certain assets and liabilities using significant other observable inputs (Level 2) with the assistance of a third party specialist. We do not have any assets or liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3). Gains and losses related to the fair value changes in the deferred compensation assets and liabilities are recorded in General and Administrative Expense in the Consolidated Statements of Operations. The following table summarizes the fair value balances (in thousands):

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(Unaudited)		Fair Value Measurement at September 30, 2014		
	Total	Level 1	Level 2	Level 3
Assets:				
Deferred compensation trust assets [1]	$23,316	$—	$23,316	$—
Liabilities:				
Deferred compensation plan	$28,322	$—	$28,322	$—