ENGLOBAL CORP
Form 10-Q
November 05, 2010
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 September 30, 2010

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

Commission File No. 001-14217
ENGlobal Corporation
(Exact name of registrant as specified in its charter)

Nevada
(State or other jurisdiction of
incorporation or organization)

88-0322261
(I.R.S Employer Identification No.)

654 N. Sam Houston Parkway E., Suite 400, Houston, TX	77060-5914
(Address of principal executive offices)	(Zip code)

(281) 878-1000
(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 shortened 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	

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 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	X
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	X

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the close of business on November 2, 2010.

$0.001 Par Value Common Stock	26,676,279 shares

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QUARTERLY REPORT ON FORM 10-Q
FOR THE PERIOD ENDED SEPTEMBER 30, 2010

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PART I. - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ENGlobal Corporation
Condensed Consolidated Statements of Operations
(Unaudited)
(dollars in thousands, except earnings per share)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenues	$85,752	$ 87,271	$227,441	$260,639
Operating costs	79,288	80,103	212,074	235,940
Gross profit	6,464	7,168	15,367	24,699
Selling, general and administrative	14,531	6,980	32,187	20,838
Operating income (loss)	(8,067)	188	(16,820)	3,861
Other income (expense):				
Other income (expense)	(34)	31	114	182
Interest income (expense), net	(101)	(148)	(255)	(479)
Income (loss) before income taxes	(8,202)	71	(16,961)	3,564
Provision for federal and state income taxes	(3,001)	140	(5,705)	1,570
Net income (loss)	$(5,201)	$ (69)	$(11,256)	$1,994
Earnings (loss) per common share:				
Basic	$(0.19)	$ 0.00	$(0.41)	$0.07
Diluted	$(0.19)	$ 0.00	$(0.41)	$0.07
Weighted average shares used in computing earnings (loss) per share (in thousands):				
Basic	27,073	27,305	27,309	27,299
Diluted	27,073	27,305	27,309	27,573

See accompanying notes to interim condensed consolidated financial statements.

ENGlobal Corporation
Condensed Consolidated Balance Sheets
(Unaudited)
(dollars in thousands)

ASSETS

	September 30, 2010	December 31, 2009
Current Assets:		
Cash and cash equivalents	$357	$143
Trade receivables, net of allowances of $1,430 and $1,868	51,337	47,715
Prepaid expenses and other current assets	715	2,182
Current portion of notes receivable	—	15
Costs and estimated earnings in excess of billings on uncompleted contracts	4,559	6,557
Federal and state income taxes receivable	6,462	2,221
Deferred tax asset	3,250	3,250
Total Current Assets	$66,680	$62,083
Property and equipment, net	4,910	5,983
Goodwill	23,003	22,291
Other intangible assets, net	5,481	4,238
Long-term trade and notes receivable, net of current portion and allowances	4,374	14,621
Deferred tax asset, non-current	603	607
Other assets	733	812
Total Assets	$105,784	$110,635

LIABILITIES AND STOCKHOLDERS' EQUITY

	September 30, 2010	December 31, 2009
Current Liabilities:		
Accounts payable	$8,782	$8,252
Accrued compensation and benefits	14,033	11,511
Current portion of long-term debt and leases	11,490	1,064
Deferred rent	632	613
Billings in excess of costs and estimated earnings on uncompleted contracts	1,958	3,601
Other current liabilities	2,097	734
Total Current Liabilities	$38,992	$25,775
Long-Term Debt and Leases, net of current portion	1,317	6,149
Total Liabilities	$40,309	$31,924
Commitments and Contingencies (Note 10)		
Stockholders' Equity:		
Common stock - $0.001 par value; 75,000,000 shares authorized; 26,676,279 and 27,407,159 shares outstanding and 27,657,378 and 27,407,159 shares issued at September 30, 2010 and December 31, 2009, respectively	$28	$27
Additional paid-in capital	37,486	37,108
Retained earnings	30,417	41,672
Treasury stock at cost - 981,099 and 0 shares at September 30, 2010 and December 31, 2009, respectively	(2,363)	—
Accumulated other comprehensive income (loss)	(93)	(96)
Total Stockholders' Equity	$65,475	$78,711
Total Liabilities and Stockholders' Equity	$105,784	$110,635

See accompanying notes to interim condensed consolidated financial statements.

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ENGlobal Corporation
Condensed Consolidated Statements of Cash Flows
(Unaudited)
(dollars in thousands)

	For the Nine Months Ended September 30, 2010	2009
Cash Flows from Operating Activities:		
Net income (loss)	$(11,256)	$1,994
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	3,432	3,713
Share-based compensation expense	316	514
(Gain)/Loss on disposal of property, plant and equipment	75	45
Changes in current assets and liabilities, net of acquisitions:		
Trade accounts and other receivables	6,921	30,341
Costs and estimated earnings in excess of billings on uncompleted contracts	2,002	911
Prepaid expenses and other assets	1,451	(467)
Accounts payable	2,356	(7,679)
Accrued compensation and benefits	2,079	(8,321)
Billings in excess of costs and estimated earnings on uncompleted contracts	(1,648)	3,315
Other liabilities	712	(1,978)
Income taxes receivable/payable	(4,241)	(3,863)
Net cash provided by operating activities	$2,199	$18,525
Cash Flows from Investing Activities:		
Property and equipment acquired	(880)	(3,165)
Proceeds from note receivable	15	44
Business acquisitions, net of cash acquired	(1,896)	(1,050)
Proceeds from sale of other assets	13	3
Net cash used in investing activities	$(2,748)	$(4,168)
Cash Flows from Financing Activities:		
Net borrowings (payments) on line of credit	3,736	(12,530)
Purchase of treasury stock	(2,363)	—
Proceeds from issuance of common stock	63	—
Borrowing (repayments) under capital lease	(142)	(130)
Other long-term debt repayments	(534)	(2,258)
Net cash provided by (used in) financing activities	$760	$(14,918)
Effect of Exchange Rate Changes on Cash	3	10
Net change in cash	214	(551)
Cash, at beginning of period	143	1,000
Cash, at end of period	$357	$449

See accompanying notes to interim condensed consolidated financial statements.

Notes to Condensed Consolidated Financial Statements

NOTE 1 – BASIS OF PRESENTATION

Our condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The Company consolidates all of its subsidiaries and all significant inter-company accounts and transactions have been eliminated in the consolidation.

The condensed consolidated financial statements of ENGlobal Corporation (which may be referred to as "ENGlobal," the "Company," "we," "us," or "our") included herein are unaudited for the three month and nine month periods ended September 30, 2010 and 2009, have been prepared from the books and records of the Company pursuant to the rules and regulations of the Securities and Exchange Commission, and in the case of the condensed balance sheet as of December 31, 2009, have been derived from the audited financial statements. These financial statements reflect all adjustments (consisting of normal recurring adjustments), which are, in the opinion of management, necessary to fairly present the results for the periods presented. Certain information and note disclosures, normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted pursuant to rules and regulations of the Securities and Exchange Commission. It is suggested that these condensed financial statements be read in conjunction with the Company's audited financial statements for the year ended December 31, 2009, included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission. The Company has assessed subsequent events through the date of filing these condensed consolidated financial statements with the Securities and Exchange Commission and believes that the disclosures made herein are adequate to make the information presented not misleading.

NOTE 2 – CRITICAL ACCOUNTING POLICIES AND NEW ACCOUNTING PRONOUNCEMENTS

A summary of critical accounting policies is disclosed in Note 2 to the consolidated financial statements included in our 2009 Annual Report on Form 10-K. Our critical accounting policies are further described under the caption "Critical Accounting Policies" in Management's Discussion and Analysis of Financial Condition and Results of Operations in our 2009 Annual Report on Form 10-K.

NOTE 3 – SHARE-BASED COMPENSATION

The Company's 1998 Incentive Plan ("Option Plan") that provided for the issuance of options to acquire up to 3,250,000 shares of common stock expired in June 2008. The Option Plan provided for grants of non-statutory options, incentive stock options, restricted stock awards and stock appreciation rights. All stock option grants were for a ten-year term. Stock options issued to executives and management generally vested over a four-year period, one-fifth at grant date and one-fifth at December 31 of each year until they are fully vested. Stock options issued to directors under the Option Plan vested quarterly over a one-year period. As of November 2, 2010, 983,336 shares of common stock remained subject to outstanding awards previously granted under the Option Plan.

In June 2009, the Company's stockholders approved a new 2009 Equity Incentive Plan ("Equity Plan") that provides for the issuance of up to 480,000 shares of common stock. The Equity Plan provides for grants of non-statutory options, incentive stock options, restricted stock awards, performance shares, performance units, restricted stock units and other stock-based awards. Grants to employees will generally vest over a four-year period, one-fourth at December 31 of each year until they are fully vested. Grants to non-employee directors will vest quarterly over a one-year period coinciding with their service term. As of November 2, 2010, 242,480 shares of restricted stock have been granted under the Equity Plan, of which 171,410 remain subject to outstanding awards.

Total share-based compensation expense in the amount of $116,000 and $169,000 was recognized during the three months ended September 30, 2010 and 2009, respectively. Total share-based compensation expense in the amount of $316,000 and $514,000 was recognized during the nine months ended September 30, 2010 and 2009, respectively. Share-based compensation expense is reported in selling, general and administrative expense.

Notes to Condensed Consolidated Financial Statements

Stock Options

Compensation expense related to outstanding non-vested stock option awards under the Option Plan of $164,000 had not been recognized at September 30, 2010. This compensation expense is expected to be recognized over a weighted-average period of approximately 15 months.

The following table summarizes stock option activity through the third quarter of 2010:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (000's)*
Balance at December 31, 2009	1,091,104	$7.12	3.6	$737
Granted	—	—	—	—
Exercised	(54,614)	1.07	—	—
Canceled or expired	(53,154)	11.32	—	—
Balance at September 30, 2010	983,336	$7.23	5.3	$153
Exercisable at September 30, 2010	935,336	$7.11	5.2	$153

*Based on average stock price through the third quarter of 2010 of $2.72 per share. The average stock price for the same period in 2009 was $4.43 per share. The total fair value of vested options outstanding as of September 30, 2010 and 2009 was $0.2 million and $1.1 million, respectively.

The total intrinsic value of options exercised was $76,000 for the nine months ended September 30, 2010. There were no options exercised during the nine months ended September 30, 2009.

Restricted Stock Awards

Restricted stock awards granted to directors are intended to compensate and retain the director over the one-year service period commencing July 1 of the year of service. These awards will vest in quarterly installments beginning September 30 of the year of service, so long as the grantee continues to serve as a director of the Company. Restricted stock awards granted to employees will vest in four equal annual installments beginning December 31 in the year granted, so long as the grantee remains employed full-time with the Company as of each vesting date. During 2010, the Company granted restricted stock awards per the following table.

Date Issued	Issued to	Number of Individuals	Number of Shares	Market Price	Fair Value
January 27, 2010	Employee	2	37,500	$3.09	$115,875
June 17, 2010	Employee	1	40,323	$2.48	$100,000
June 17, 2010	Director	3	96,774	$2.48	$240,000
September 10, 2010	Employee	2	21,008	$2.38	$50,000

The amount of compensation expense related to all restricted stock awards that had not been recognized at September 30, 2010, totaled $409,000. This compensation expense is expected to be recognized over a weighted-average period of approximately 26 months.

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Notes to Condensed Consolidated Financial Statements

NOTE 4 – CONTRACTS

Costs, estimated earnings and billings on uncompleted contracts consisted of the following at September 30, 2010 and December 31, 2009:

	September 30, 2010	December 31, 2009
	(dollars in thousands)	
Costs incurred on uncompleted contracts	$51,345	$32,984
Estimated earnings on uncompleted contracts	7,460	5,784
Earned revenues	58,805	38,768
Less: billings to date	56,204	35,812
Net costs and estimated earnings in excess of billings on uncompleted contracts	$2,601	$2,956
Costs and estimated earnings in excess of billings on uncompleted contracts	$4,559	$6,557
Billings in excess of costs and estimated earnings on uncompleted contracts	(1,958)	(3,601)
Net costs and estimated earnings in excess of billings on uncompleted contracts	$2,601	$2,956

Revenue on fixed-price contracts is recorded primarily using the percentage-of-completion (cost-to-cost) method. Under this method, revenue on long-term contracts is recognized in the ratio that contract costs incurred bear to total estimated contract costs. Revenue and gross margin on fixed-price contracts are subject to revision throughout the lives of the contracts and any required adjustments are made in the period in which the revisions become known. To manage unknown risks, management may use contingency amounts to increase the estimated costs, therefore, lowering the earned revenues until the risks are better identified and quantified or have been mitigated. We currently have $0.8 million in contingency as of September 30, 2010 compared to $1.8 million as of December 31, 2009. Losses on contracts are recorded in full as they are identified.

The Company recognizes service revenue as soon as the services are performed. For clients that we consider higher risk, due to past payment history or history of not providing written work authorizations, we have deferred revenue recognition until we receive either a written authorization or a payment. The current amount of revenue deferred for these reasons is $0.3 million as of September 30, 2010 compared to $0.5 million as of December 31, 2009.

We expect a majority of the contingency amount and the deferred revenue to be realized by year end.

Notes to Condensed Consolidated Financial Statements

NOTE 5 – LINE OF CREDIT AND DEBT

	September 30, 2010	December 31, 2009
	(dollars in thousands)	
Schedule of Long-Term Debt and Leases:		
Wells Fargo Credit Facility	$9,736	$6,000
Watco Management, Inc.	—	132
FH McIlwain, PC; JA Walters, PC; WM Bosarge, PC; MR Burton, PC	663	651
ICP Transco, Inc.	94	187
Westech Engineering, Inc.	1,714	—
Control Dynamics International, L.P.	500	—
Total long-term debt	12,707	6,970
Less: current maturities of long-term debt	(11,390)	(872)
Long-term debt, net of current portion	1,317	6,098
Borrowings under capital lease	100	243
Less: current maturities of capital lease	(100)	(192)
Total long-term debt and leases, net of current portion	$1,317	$6,149

On April 1, 2010, a subsidiary of the Company acquired selected assets of Control Dynamics International, LP ("CDI"). Consideration for the acquisition included unsecured, interest bearing deferred payments in the aggregate principal amount of $500,000. The note bears interest at 5% per annum and is payable in two equal installments on April 6, 2011 and 2012.

On April 29, 2010, the Company delivered a promissory note in the principal amount of $2.0 million to Westech Engineering, Inc. providing for payment of outstanding accounts payable. The amount owed is the amount of the subcontractor obligation incurred in connection with the Alon USA, LP project referenced in Note 10. The note bears interest at 5% per annum and is payable in equal monthly installments through March 15, 2013.

The Company's Fixed Charge Coverage Ratio for the quarterly period ended September 30, 2010 was not in compliance with the Wells Fargo Credit Facility covenant; however, Wells Fargo waived its default rights with respect to the breach for the third quarter of 2010 only. Anticipating a covenant breach in the fourth quarter, the $9.7 million line of credit outstanding was classified as current long-term debt on the balance sheet as of September 30, 2010.

NOTE 6 – SEGMENT INFORMATION

During the first two quarters of 2010, the Company managed and reported through four business segments: Engineering, Construction, Automation and Land. In May 2010, the Company hired a new CEO. Since his hiring, the CEO has assessed the Company's business organization and management structure. This assessment led to management changes, a new focus on specific types of work and reorganization of integrated functions within the Company. In response to these changes, we reevaluated our reportable segments under ASC 280, Segment Reporting. As a result, we have elected to realign our reporting into three business segments: Engineering, Automation and Land. Our services that were offered under the previous Construction segment were merged into our current reporting segments.

The total amounts reported for prior periods will remain the same, but amounts reported on a segment basis are reported in the three segments that the Company now operates in, rather than the four segments the Company previously operated and reported in.

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Notes to Condensed Consolidated Financial Statements

The Engineering segment provides consulting services relating to the development, management and execution of projects requiring professional engineering and related project services primarily to the midstream and downstream sectors. Services provided by the Engineering segment include feasibility studies, engineering, design, procurement and construction management. The Engineering segment includes the technical services group, which provides engineering, design, installation, and operation and maintenance of various government, public sector, and international facilities.

The Automation segment provides services related to the design, fabrication and implementation of process distributed control and analyzer systems, advanced automation, information technology, electrical and heat tracing projects primarily to the upstream and downstream sectors.

The Land segment provides land management, right-of-way, inspection, environmental compliance, legislative affairs support and governmental regulatory compliance services primarily to the midstream sector, including pipeline, utility and telecom companies and other owner/operators of infrastructure facilities throughout the United States.

The accounting policies of each of the segments are the same as those described in the summary of critical accounting policies referenced in Note 2 above. The Company evaluates performance based on profit or loss from operations before interest, income taxes and other income or loss, but after selling, general and administrative expenses attributable to the reportable segments. Transactions between reportable segments are at market rates comparable to terms available from unrelated parties.

If any component of our operating results in one of our segments is adversely affected, an impairment of goodwill could result in a write down. Although the Company has made changes to its reportable segments and senior management team, management does not believe there are any indicators of triggering events that would require it to conduct an interim impairment test; however, there is a possibility the Company may have an impairment of goodwill during our annual goodwill testing performed as of the fourth quarter.

Notes to Condensed Consolidated Financial Statements

For the three months ended September 30, 2010 (dollars in thousands)	Engineering	Automation	Land	All Other	Consolidated
Revenue before eliminations	$44,737	$15,201	$26,024	$—	$85,962
Inter-segment eliminations	(9)	(201)	—	—	(210)
Revenue	44,728	15,000	26,024	—	85,752
Gross profit	4,672	(149)	1,941	—	6,464
SG&A	8,955	977	951	3,648	14,531
Operating income (expense)	(4,283)	(1,126)	990	(3,648)	(8,067)
Other income (expense)					(34)
Interest income (expense)					(101)
Tax provision					3,001
Net loss					$(5,201)

For the three months ended September 30, 2009 (dollars in thousands)					
Revenue before eliminations	$35,720	$19,551	$32,072	$—	$87,343
Inter-segment eliminations	(61)	(11)	—	—	(72)
Revenue	35,659	19,540	32,072	—	87,271
Gross profit	1,684	2,747	2,737	—	7,168
SG&A	1,785	1,065	827	3,303	6,980
Operating income (expense)	(101)	1,682	1,910	(3,303)	188
Other income (expense)					31
Interest income (expense)					(148)
Tax provision					(140)
Net loss					$(69)

Notes to Condensed Consolidated Financial Statements

For the nine months ended September 30, 2010 (dollars in thousands)	Engineering	Automation	Land	All Other	Consolidated
Revenue before eliminations	$113,870	$46,222	$67,612	$—	$227,704
Inter-segment eliminations	(48)	(215)	—	—	(263)
Revenue	113,822	46,007	67,612	—	227,441
Gross profit	8,270	1,977	5,120	—	15,367
SG&A	16,082	3,179	2,558	10,368	32,187
Operating income (expense)	(7,812)	(1,202)	2,562	(10,368)	(16,820)
Other income (expense)					114
Interest income (expense)					(255)
Tax provision					5,705
Net loss					$(11,256)

For the nine months ended September 30, 2009 (dollars in thousands)	Engineering	Automation	Land	All Other	Consolidated
Revenue before eliminations	$120,117	$55,808	$86,787	$—	$262,712
Inter-segment eliminations	(1,108)	(100)	(865)	—	(2,073)
Revenue	119,009	55,708	85,922	—	260,639
Gross profit	9,645	6,822	8,232	—	24,699
SG&A	4,959	3,284	2,513	10,082	20,838
Operating income (expense)	4,686	3,538	5,719	(10,082)	3,861
Other income (expense)					182
Interest income (expense)					(479)
Tax provision					(1,570)
Net income					$1,994

Notes to Condensed Consolidated Financial Statements

Total Assets by Segment	As of September 30, 2010	As of December 31, 2009
	(dollars in thousands)	
Engineering	$51,246	$55,006
Automation	23,656	23,523
Land	19,160	23,392
All Other	11,722	8,714
Consolidated	$105,784	$110,635

Financial information about geographic areas
Revenue from the Company's non-U.S. operations is not material. Long-lived assets (principally leasehold improvements and computer equipment) formerly located in Canada were transferred to a U.S. office or disposed of during the three months ended September 30, 2010.

NOTE 7 – FEDERAL AND STATE INCOME TAXES

The components of income tax expense (benefit) for the three months and nine months ended September 30, 2010 and 2009 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(dollars in thousands)			
Current	$200	$64	$461	$1,321
Deferred	(3,201)	76	(6,166)	249
Total tax provision (benefit)	$(3,001)	$140	$(5,705)	$1,570
Effective tax rate	36.6%	197.2%	33.6%	44.1%

As required by ASC 740, the Company makes its interim tax allocation by applying estimated fiscal year effective tax rates to estimated fiscal year ordinary income together with unusual or infrequently occurring activity for the year-to-date period. The effective rate for the nine month period ended September 30, 2010 is lower due to the majority of the Company's work being completed in a state that calculates taxes based on gross margin rather than net income. The computed effective tax rate for the three month period ended September 30, 2009 was higher than the customary relationship between income tax expense and pretax accounting income because we revised our estimate of fiscal year effective tax rates upward to reflect estimated proportionate changes in components of fiscal year pretax income.

Notes to Condensed Consolidated Financial Statements

NOTE 8 – EARNINGS PER SHARE

The following table reconciles the number of shares used to compute basic earnings per share to the number of shares used to compute diluted earnings per share (“EPS”).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(shares in thousands)			
Weighted average shares outstanding used to compute basic EPS	27,073	27,305	27,309	27,299
Effect of share-based compensation plans	—	—	—	274
Shares used to compute diluted EPS	27,073	27,305	27,309	27,573

The Company excluded potentially issuable shares of 813,000 and 638,000 from the computation of diluted EPS, as the effect of including the shares would have been anti-dilutive for the three and nine month periods ended September 30, 2010 and 2009, respectively.

NOTE 9 – STOCK REPURCHASE PROGRAM

Effective May 14, 2010, our Board of Directors authorized a total expenditure of $2.5 million to repurchase shares of the Company's common stock. Through open market purchases under this authorization, we purchased 651,470 and 981,099 shares at an average cost of $2.40 and $2.41 per share during the three months and nine months ended September 30, 2010, respectively. At September 30, 2010, approximately $0.1 million remains authorized in the stock repurchase program. The program does not have an expiration date. However, in accordance with amendments to the loan agreement with Wells Fargo described in Management's Discussion and Analysis - Liquidity and Capital Resources section, the Company does not currently intend to purchase additional shares under this program.

NOTE 10 – COMMITMENTS AND CONTINGENCIES

Employment Agreements

The Company has employment agreements with certain of its executive and other officers, the terms of which expire on or before May 2013, with the severance terms ranging from six to twelve months. Such agreements provide for minimum salary levels. If employment is terminated for any reason other than (1) termination for cause, (2) voluntary resignation or (3) the employee's death, the Company is obligated to provide a severance benefit equal to between six and twelve months of the employee's salary, and, at its option, an additional six months at 50% to 100% of the employee's salary in exchange for an extension of a non-competition agreement. Some of these agreements are renewable for an additional one-year at the Company's option. No liability is recorded for the Company's obligations under employment agreements as the amounts that will ultimately be paid cannot be reasonably estimated, if any.

Notes to Condensed Consolidated Financial Statements

Long-term Trade and Note Receivable

In the first quarter of 2007, ENGlobal Engineering, Inc. (“EEI”) and South Louisiana Ethanol, LLC (“SLE”) executed an agreement for engineering, procurement and construction (“EPC”) services relating to the retro-fit of an ethanol plant in southern Louisiana (the “SLE project”). In October 2007, SLE executed a promissory note, or “Hand Note,” payable to the Company and having a principal balance of approximately $12.3 million, constituting amounts then due to the Company for its work performed in connection with the project. The history of the SLE Project is described in Note 12 to the Company's condensed consolidated financial statements included in its Quarterly Report on Form 10-Q for the quarter ended September 30, 2007, is discussed further in the Company's Annual Reports on Form 10-K for the years ended December 31, 2007, 2008 and 2009, and under Litigation, below, of this Quarterly Report on Form 10-Q. In the current quarter, the Company has elected to take an additional reserve of $7.2 million against the SLE note receivable (discussed further in Litigation below).

On March 13, 2009, the Company entered into a letter agreement (the “letter agreement”) with Alon USA, LP (“Alon”) resolving the payment of accounts receivable invoices in the aggregate amount of $6.8 million, payable in monthly installments with the final payment due in December 2009. The $6.8 million payment plan included $4.6 million in subcontractor obligations which were included in our Accounts Payable balances until April 2010 when they were then reclassified to a long-term note payable (See Note 5). Alon made timely payments under the letter agreement until October 2009, when it failed to pay the full amount due. The parties are now in litigation (discussed further in Litigation below).

The Company had reclassified the accounts receivable balance of $3.0 million related to the Bigler, L.P. litigation and subsequent bankruptcy filing to long-term claims receivable. In June 2010, the Company wrote off the long-term claims receivable. (See Litigation below for more details).

Litigation

Due to past due payments on accounts receivable invoices for services provided to Bigler, LP (“Bigler”) in the amount of $3.0 million, the Company, in February 2009, filed a materialman's and mechanic's lien on the property on which the services were performed. In response, Bigler filed a petition entitled Bigler, L.P. f/k/a Bigler Trading Company, Inc. and Bigler Land, LLC vs. ENGlobal Engineering, Inc. in the 234th District Court of Harris County, Case Number 2009-15676, asking for declaratory relief clearing title of the lien and seeking unspecified monetary damages. ENGlobal has filed a counterclaim for collection of the fees due, and foreclosure of its lien. On October 30, 2009, Bigler filed for bankruptcy in U.S. Bankruptcy Court for the Southern District of Texas (Houston), Bankruptcy Petition #09-38188. The bankruptcy stayed ENGlobal's collection proceedings. The Company believed that, given its lien position and what it believed to be the value of the collateral, it would collect the entire amount due. However, in June 2010, the Bigler assets were sold for significantly less than the amount due to creditors senior to ENGlobal. Thus, in June 2010, ENGlobal wrote off the amount due in its entirety. In October 2010, we executed a mutual release with Bigler and all related entities.

In June 2008, ENGlobal filed an action in the United States District Court for the Eastern District of Louisiana; Case Number 08-3601, against South Louisiana Ethanol LLC (“SLE”) entitled ENGlobal Engineering, Inc. and ENGlobal Construction Resources, Inc. vs. South Louisiana Ethanol, LLC. The lawsuit seeks to enforce collection of $15.8 million owed to ENGlobal and its affiliates for services performed on an ethanol plant in Louisiana. In August 2009, SLE filed for Chapter 11 protection in the United States Bankruptcy Court for the Eastern District of Louisiana, Case number 09-12676. On October 26, 2010, the Bankruptcy Court issued an order setting forth the manner in which proceeds of a sale of the SLE property will be allocated among the debtors in the Bankruptcy proceeding. As a result of this Order, ENGlobal will not receive as much of the proceeds from a sale as it believes it is entitled to. ENGlobal is considering an appeal of the Order. However, given the time this matter has been pending, together with other factors, such as the time it would take to prosecute an appeal, ENGlobal has elected to take an additional reserve of $7.2 million against the SLE note receivable.

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Notes to Condensed Consolidated Financial Statements

On April 23, 2010, ENGlobal filed an action in the United States District Court for the Southern District of Texas, Case Number 4:10-cv-10352 entitled ENGlobal Engineering, Inc. and ENGlobal Construction Resources, Inc. vs. Kennett F. Stewart, John Paul, and William A. Hurst. The lawsuit seeks to enforce collection of $18.75 million owed to ENGlobal and its affiliates for services performed on the South Louisiana ethanol plant, allege fraud by the owners of South Louisiana Ethanol, LLC and seek to recover damages from them in their individual capacities.

In November 2009, the Company filed a petition entitled ENGlobal Engineering, Inc. vs. Alon USA, L.P., Alon USA GP, LLC and Alon USA Refining, Inc. in the 162nd District Court of Dallas County, Case Number 09-15915-I. The lawsuit seeks to enforce the collection of the $3.0 million owed to ENGlobal for services performed for a refinery rebuild project that is remaining as amounts due on a letter payment agreement between ENGlobal and Alon USA, LP (“Alon”) and to foreclose on its lien. Alon counterclaimed and is currently seeking damages of $17.4 million. Mediation is scheduled for November 17, 2010 and trial is currently scheduled for January 3, 2011. The Company has established a reserve for $0.5 million to cover the insurance deductible. We believe these claims are without merit and intend to vigorously defend ourselves against them.

ENGlobal was named as a defendant in a lawsuit entitled Ecoproduct Solutions, L.P. vs. ENGlobal Engineering and Swenson Technology, Inc. The lawsuit was filed on October 8, 2009 in the 270th Judicial District Court of Harris County, Texas, Case Number 2009-64881, and was based on a contract for engineering services performed between November 2004 and August 2005 and for which ENGlobal received approximately $700,000. Ecoproduct claimed that it incurred actual damages of $45 million and sought to recover actual, consequential and punitive damages. On January 28, 2010, the court granted ENGlobal's Motion for Summary Judgment. Ecoproduct has appealed and, barring a reversal of the summary judgment, ENGlobal appears to face little to no further exposure in this matter.

As of the date of these interim financial statements, we are party to several legal proceedings arising in the ordinary course of business that we believe have been reserved for, are covered by insurance or if determined adversely to us, whether individually or in the aggregate, would not have a material adverse effect on our results of operations or financial position. However, we cannot predict the ultimate outcomes of these matters with certainty. In addition, the Company has filed suit against a number of its clients for payment of accounts receivable. Although the Company believes it will receive favorable judgments in these collection matters, due to impact of the downturn of the business and credit climate on its clients' businesses, it may not be able to fully collect on judgments it receives.

Insurance

The Company carries a broad range of insurance coverage, including general and business automobile liability, commercial property, professional errors and omissions, workers' compensation insurance, director's and officer's liability insurance and a general umbrella policy. The Company is not aware of any claims in excess of insurance recoveries. ENGlobal is partially self-funded for health insurance claims. Provisions for expected future payments are accrued based on the Company's experience. Specific stop loss levels provide protection for the Company with $200,000 per occurrence and approximately $15.7 million in the aggregate for each policy year being covered by a separate insurance policy. The self-insurance liability, which is included in the Accrued Compensation and Benefits line of the balance sheet, was $1.2 million as of September 30, 2010 and $0.9 million as of December 31, 2009.

Notes to Condensed Consolidated Financial Statements

NOTE 11 – ACQUISITIONS

In April 2010, a subsidiary of the Company acquired selected assets of Control Dynamics International, LP (“CDI”) a privately-held automation firm based in Houston, Texas. The initial fair value assessment of this acquisition was reported during the period ending June 30, 2010.

As of September 30, 2010 the Company performed fair value assessments of the contingent liabilities as directed per ASC 805, Business Combinations. It was determined that the contingent liability that was based on earnings performance had no fair value as the minimum levels would not be reached. The Company has reversed the contingent liability for $0.3 million as a credit against amortization expense in the Automation segment during the three and nine months ended September 30, 2010.

NOTE 12 – SUBSEQUENT EVENTS

On October 26, 2010, the Bankruptcy Court issued an order setting forth the manner in which proceeds of a sale of the SLE property will be allocated among the debtors in the Bankruptcy proceeding. As a result of this Order, ENGlobal will not receive as much of the proceeds from a sale as it believes it is entitled to. ENGlobal is considering an appeal of the Order. However, given the time this matter has been pending, together with other factors, such as the time it would take to prosecute an appeal, ENGlobal has elected to take an additional reserve of $7.2 million against the SLE note receivable.

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

Forward-Looking Statements

Certain information contained in this Quarterly Report on Form 10-Q, the Company's Annual Report on Form 10-K, as well as other written and oral statements made or incorporated by reference from time to time by the Company and its representatives in other reports, filings with the Securities and Exchange Commission, press releases, conferences or otherwise, may be deemed to be forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. This information includes, without limitation, statements concerning the Company's future financial position and results of operations, planned capital expenditures, business strategy and other plans for future operations, the future mix of revenues and business, customer retention, project reversals, commitments and contingent liabilities, future demand and industry conditions. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Generally, the words “anticipate,” “believe,” “estimate,” “expect,” “may” and similar expressions, identify forward-looking statements, which generally are not historical in nature. Actual results could differ materially from the results described in the forward-looking statements due to the risks and uncertainties set forth in this Quarterly Report on Form 10-Q, the specific risk factors identified in the Company's Annual Report on Form 10-K for the year ended December 31, 2009, and those described from time to time in our future reports filed with the Securities and Exchange Commission.

The following discussion is qualified in its entirety by, and should be read in conjunction with, the Company's condensed consolidated financial statements, including the notes thereto, included in this Quarterly Report on Form 10-Q and the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

MD&A Overview

During the first two quarters of 2010, the Company managed and reported through four business segments: Engineering, Construction, Automation and Land. In May 2010, the Company hired a new CEO. Since his hiring, the CEO has assessed the Company's business organization and management structure. This assessment led to management changes, a new focus on specific types of work and reorganization of integrated functions within the Company. In response to these changes, we reevaluated our reportable segments under ASC 280, Segment Reporting. As a result, we have elected to realign our reporting into three business segments: Engineering, Automation and Land. Our services that were offered under the previous Construction segment were merged into our current reporting segments.

The total amounts reported for prior periods will remain the same, but amounts reported on a segment basis are reported in the three segments that the Company now operates in, rather than the four segments the Company previously operated and reported in.

Management's Discussion and Analysis (continued)

The following list sets forth a general overview of certain significant changes in the Company's financial condition and results of operations for the three months and nine months ended September 30, 2010, compared to the corresponding periods in 2009.

	During the three months ended September 30, 2010	During the nine months ended September 30, 2010
Revenues	Decreased 1.7 %	Decreased 12.7%
Gross profit	Decreased 9.8%	Decreased 37.8%
Operating income	Decreased 4,391.0%	Decreased 535.6%
SG&A expense	Increased 108.2%	Increased 54.5%
Net income	Decreased 7,437.7%	Decreased 664.5%

Selected Balance Sheet Comparisons	As of September 30, 2010	As of December 31, 2009	As of September 30, 2009
	(dollars in thousands)		
Working capital	$27,688	$36,308	$37,193
Total assets	$105,784	$110,635	$123,477
Long-term debt and capital leases, net of current portion	$1,317	$6,149	$1,001
Stockholders' equity	$65,475	$78,711	$79,222
Days sales outstanding	55	55	65

Long-term debt and capital leases, net of current portion, decreased 78.7%, or $4.8 million, from $6.1 million as of December 31, 2009 to $1.3 million as of September 30, 2010. As a percentage of stockholders' equity, long-term debt decreased to 2.0% from 7.8% over this nine-month period primarily due to a pay down on the December 31, 2009 balance and the September 30, 2010 line of credit balance being classified as current portion of long-term debt due to the anticipated debt covenant breach in the fourth quarter. The Company manages its billing and client collection processes toward reducing days sales outstanding to the extent practicable. We believe that our allowance for bad debt is adequate to cover any potential non-payment by our customers.

Total stockholders' equity decreased 16.8%, or $13.2 million, from $78.7 million as of December 31, 2009 to $65.5 million as of September 30, 2010. The decrease in stockholders' equity compared to September 30, 2009 was 17.3%, or $13.7 million.

Management's Discussion and Analysis (continued)

Consolidated Results of Operations for the Three Months Ended September 30, 2010 and 2009
(Unaudited)

For the three months ended September 30, 2010 (dollars in thousands)	Engineering	Automation	Land	All Other	Consolidated	
Revenue before eliminations	$44,737	$15,201	$26,024	$—	$ 85,962	
Inter-segment eliminations	(9)	(201)	—	—	(210)	
Revenue	44,728	15,000	26,024	—	85,752	100.0 %
Gross profit	4,672	(149)	1,941	—	6,464	7.5 %
SG&A	8,955	977	951	3,648	14,531	16.9 %
Operating income (loss)	(4,283)	(1,126)	990	(3,648)	(8,067)	(9.4)%
Other income (expense)					(34)	(0.1)%
Interest income (expense)					(101)	(0.1)%
Tax provision					3,001	3.5 %
Net loss					$ (5,201)	(6.1)%
Diluted earnings per share					$ (0.19)	

For the three months ended September 30, 2009 (dollars in thousands)	Engineering	Automation	Land	All Other	Consolidated	
Revenue before eliminations	$35,720	$19,551	$32,072	$—	$ 87,343	
Inter-segment eliminations	(61)	(11)	—	—	(72)	
Revenue	35,659	19,540	32,072	—	87,271	100.0 %
Gross profit	1,684	2,747	2,737	—	7,168	8.2 %
SG&A	1,785	1,065	827	3,303	6,980	8.0 %
Operating income (loss)	(101)	1,682	1,910	(3,303)	188	0.2 %
Other income (expense)					31	0.1 %
Interest income (expense)					(148)	(0.2)%
Tax provision					(140)	(0.2)%
Net loss					$ (69)	(0.1)%
Diluted earnings per share					$ 0.00	

Increase/(Decrease) in Operating Results (dollars in thousands)	Engineering	Automation	Land	All Other	Consolidated	
Revenue before eliminations	$9,017	$(4,350)	$(6,048)	$—	$ (1,381)	
Inter-segment eliminations	52	(190)	—	—	(138)	
Revenue	9,069	(4,540)	(6,048)	—	(1,519)	(1.7)%
Gross profit	2,988	(2,896)	(796)	—	(704)	(9.8)%
SG&A	7,170	(88)	124	345	7,551	108.2 %
Operating income (loss)	(4,182)	(2,808)	(920)	(345)	(8,255)	(4,391.0)%
Other income (expense)					(65)	(209.7)%
Interest income (expense)					47	31.8 %
Tax provision					3,141	2,243.6 %
Net loss					$ (5,132)	(7,437.7)%

Diluted earnings per share	$ (0.19)

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Management's Discussion and Analysis (continued)

Consolidated Results of Operations for the Nine Months Ended September 30, 2010 and 2009 (Unaudited)

For the nine months ended September 30, 2010 (dollars in thousands)	Engineering	Automation	Land	All Other	Consolidated		
Revenue before eliminations	$113,870	$46,222	$67,612	$—	$227,704		
Inter-segment eliminations	(48)	(215)	—	—	(263)		
Revenue	113,822	46,007	67,612	—	227,441	100.0	%
Gross profit	8,270	1,977	5,120	—	15,367	6.8	%
SG&A	16,082	3,179	2,558	10,368	32,187	14.2	%
Operating income (loss)	(7,812)	(1,202)	2,562	(10,368)	(16,820)	(7.4)	%
Other income (expense)					114	0.1	%
Interest income (expense)					(255)	(0.1)	%
Tax provision					5,705	2.5	%
Net loss					$(11,256)	(4.9)	%
Diluted earnings per share					$(0.41)		

For the nine months ended September 30, 2009 (dollars in thousands)							
Revenue before eliminations	$120,117	$55,808	$86,787	$—	$262,712		
Inter-segment eliminations	(1,108)	(100)	(865)	—	(2,073)		
Revenue	119,009	55,708	85,922	—	260,639	100.0	%
Gross profit	9,645	6,822	8,232	—	24,699	9.5	%
SG&A	4,959	3,284	2,513	10,082	20,838	8.0	%
Operating income (loss)	4,686	3,538	5,719	(10,082)	3,861	1.5	%
Other income (expense)					182	0.1	%
Interest income (expense)					(479)	(0.2)	%
Tax provision					(1,570)	(0.6)	%
Net income					$1,994	0.8	%
Diluted earnings per share					$0.07		

Increase/(Decrease) in Operating Results (dollars in thousands)							
Revenue before eliminations	$(6,247)	$(9,586)	$(19,175)	$—	$(35,008)		
Inter-segment eliminations							