

QUANTA SERVICES INC
Form 10-Q
August 08, 2017
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark

One)

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

For the quarterly period ended June 30, 2017.

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 no. 001-13831

Quanta Services, Inc.

(Exact name of registrant as specified in its charter)

Delaware 74-2851603

(State or other jurisdiction of (I.R.S. Employer incorporation or organization) Identification No.)

2800 Post Oak Boulevard, Suite 2600

Houston, Texas 77056

(Address of principal executive offices, including zip code)

(713) 629-7600

(Registrant's telephone number, including area code)

N/A

(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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T

(§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer

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

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of August 2, 2017, the number of outstanding shares of Common Stock of the Registrant was 151,184,065. As of the same date, 3,500,000 exchangeable shares of a Canadian subsidiary of the Registrant associated with one share of Series F Preferred Stock of the Registrant were outstanding, 449,929 exchangeable shares of a Canadian subsidiary of the Registrant associated with one share of Series G Preferred Stock of the Registrant were outstanding and an additional 36,183 exchangeable shares of certain other Canadian subsidiaries of the Registrant were outstanding.

QUANTA SERVICES, INC. AND SUBSIDIARIES
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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements.

QUANTA SERVICES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share information)

(Unaudited)

	June 30, 2017	December 31, 2016
ASSETS		
Current Assets:		
Cash and cash equivalents	\$99,565	\$ 112,183
Accounts receivable, net of allowances of \$5,279 and \$2,752	1,614,113	1,500,115
Costs and estimated earnings in excess of billings on uncompleted contracts	630,880	473,308
Inventories	94,152	88,548
Prepaid expenses and other current assets	178,489	114,591
Total current assets	2,617,199	2,288,745
Property and equipment, net of accumulated depreciation of \$929,318 and \$862,825	1,190,333	1,174,094
Other assets, net	145,120	101,028
Other intangible assets, net of accumulated amortization of \$313,486 and \$297,313	184,375	187,023
Goodwill	1,616,317	1,603,169
Total assets	\$5,753,344	\$ 5,354,059
LIABILITIES AND EQUITY		
Current Liabilities:		
Current maturities of long-term debt and short-term debt	\$1,375	\$ 7,563
Accounts payable and accrued expenses	969,654	922,819
Billings in excess of costs and estimated earnings on uncompleted contracts	314,987	274,846
Total current liabilities	1,286,016	1,205,228
Long-term debt and notes payable, net of current maturities	483,638	353,562
Deferred income taxes	206,868	192,834
Insurance and other non-current liabilities	267,491	259,733
Total liabilities	2,244,013	2,011,357
Commitments and Contingencies		
Equity:		
Common stock, \$.00001 par value, 600,000,000 shares authorized, 148,964,532 and 144,710,773 shares issued, and 148,490,467 and 144,710,773 shares outstanding	1	1
Exchangeable Shares, no par value, 3,986,112 and 6,515,453 shares issued and outstanding	—	—
Series F Preferred Stock, \$.00001 par value, 1 share authorized, issued and outstanding	—	—
Series G Preferred Stock, \$.00001 par value, 1 share authorized, issued and outstanding	—	—
Additional paid-in capital	1,785,194	1,749,306
Retained earnings	1,988,185	1,876,081
Accumulated other comprehensive loss	(231,167)	(271,673)
Treasury stock, 474,065 and 0 common shares	(35,490)	(14,288)
Total stockholders' equity	3,506,723	3,339,427

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Non-controlling interests	2,608	3,275
Total equity	3,509,331	3,342,702
Total liabilities and equity	\$5,753,344	\$ 5,354,059

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

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QUANTA SERVICES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share information)

(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2017	2016	June 30, 2017	2016
Revenues	\$2,200,374	\$1,792,430	\$4,378,544	\$3,506,167
Cost of services (including depreciation)	1,898,209	1,592,213	3,810,191	3,102,637
Gross profit	302,165	200,217	568,353	403,530
Selling, general and administrative expenses	185,880	156,607	370,432	315,131
Amortization of intangible assets	6,494	8,141	13,056	15,636
Operating income	109,791	35,469	184,865	72,763
Interest expense	(4,271)	(3,583)	(8,236)	(7,172)
Interest income	164	641	451	1,157
Other income (expense), net	(1,079)	(1,103)	(1,443)	(1,022)
Income before income taxes	104,605	31,424	175,637	65,726
Provision for income taxes	40,245	14,695	62,837	28,138
Net income	64,360	16,729	112,800	37,588
Less: Net income attributable to non-controlling interests	523	167	696	530
Net income attributable to common stock	\$63,837	\$16,562	\$112,104	\$37,058
Earnings per share attributable to common stock - basic and diluted	\$0.41	\$0.11	\$0.72	\$0.23
Shares used in computing earnings per share attributable to common stock:				
Weighted average basic shares outstanding	155,090	156,128	154,859	159,577
Weighted average diluted shares outstanding	156,165	156,130	155,745	159,579

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

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QUANTA SERVICES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net income	\$64,360	\$16,729	\$112,800	\$37,588
Other comprehensive income, net of tax provision:				
Foreign currency translation adjustment, net of tax of \$0, \$0, \$0 and \$0	26,685	3,083	40,506	63,669
Other comprehensive income	26,685	3,083	40,506	63,669
Comprehensive income	91,045	19,812	153,306	101,257
Less: Comprehensive income attributable to non-controlling interests	523	167	696	530
Total comprehensive income attributable to Quanta stockholders	\$90,522	\$19,645	\$152,610	\$100,727

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

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QUANTA SERVICES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
	2017	2016	2017	2016
Cash Flows from Operating Activities of Continuing Operations:				
Net income	\$64,360	\$16,729	\$112,800	\$37,588
Adjustments to reconcile net income to net cash provided by (used in) operating activities of continuing operations—				
Depreciation	44,650	42,759	87,343	83,929
Amortization of intangible assets	6,494	8,141	13,056	15,636
Equity in (earnings) losses of unconsolidated affiliates	2,148	378	2,751	559
Amortization of debt issuance costs	338	338	678	678
(Gain) loss on sale of property and equipment	(2,007)	654	(166)	547
Foreign currency loss	641	558	862	668
Provision for (recovery of) doubtful accounts	61	56	926	(927)
Deferred income tax provision (benefit)	3,666	(7,858)	3,630	(5,142)
Non-cash stock-based compensation	11,557	9,503	23,423	23,222
Changes in operating assets and liabilities, net of non-cash transactions	(126,963)	(3,448)	(244,169)	116,863
Net cash provided by operating activities of continuing operations	4,945	67,810	1,134	273,621
Cash Flows from Investing Activities of Continuing Operations:				
Proceeds from sale of property and equipment	7,543	5,165	12,344	10,254
Additions of property and equipment	(58,257)	(60,855)	(105,281)	(108,550)
Cash paid for acquisitions, net of cash acquired	(6,108)	(35)	(7,635)	(39,710)
Investments in and return of equity from unconsolidated affiliates	(9,229)	(3,163)	(12,954)	(5,388)
Cash received from (paid for) other investments, net	615	503	(1,086)	1,080
Cash withdrawn from (deposited to) restricted cash	(2,031)	42	(119)	42
Net cash used in investing activities of continuing operations	(67,467)	(58,343)	(114,731)	(142,272)
Cash Flows from Financing Activities of Continuing Operations:				
Borrowings under credit facility	550,883	696,572	1,248,094	1,350,988
Payments under credit facility	(491,943)	(696,668)	(1,123,384)	(1,426,271)
Payments on other long-term debt	(1,354)	(692)	(2,883)	(5,547)
Payments on short-term debt	—	—	(2,783)	(4,711)
Distributions to non-controlling interests	(383)	—	(1,363)	—
Payments related to tax withholding for share-based compensation	(1,613)	(1,160)	(17,805)	(7,232)
Exercise of stock options	—	163	25	214
Net cash provided by (used in) financing activities of continuing operations	55,590	(1,785)	99,901	(92,559)
Discontinued operations:				
Net cash used in investing activities	—	(437)	—	(6,080)
Net cash used in discontinued operations	—	(437)	—	(6,080)
Effect of foreign exchange rate changes on cash and cash equivalents	(17)	(216)	1,078	863

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Net increase (decrease) in cash and cash equivalents	(6,949)	7,029	(12,618)	33,573
Cash and cash equivalents, beginning of period	106,514	155,315	112,183	128,771
Cash and cash equivalents, end of period	\$99,565	\$162,344	\$99,565	\$162,344

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

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QUANTA SERVICES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. BUSINESS AND ORGANIZATION:

Quanta Services, Inc. (Quanta) is a leading provider of specialty contracting services, offering infrastructure solutions primarily to the electric power, oil and gas and communications industries in the United States, Canada and Australia and select other international markets. Quanta reports its results under two reportable segments: (1) Electric Power Infrastructure Services and (2) Oil and Gas Infrastructure Services.

Electric Power Infrastructure Services Segment

The Electric Power Infrastructure Services segment provides comprehensive network solutions to customers in the electric power industry. Services performed by the Electric Power Infrastructure Services segment generally include the design, installation, upgrade, repair and maintenance of electric power transmission and distribution infrastructure and substation facilities along with other engineering and technical services. This segment also provides emergency restoration services, including the repair of infrastructure damaged by inclement weather, the energized installation, maintenance and upgrade of electric power infrastructure utilizing unique bare hand and hot stick methods and Quanta's proprietary robotic arm technologies, and the installation of "smart grid" technologies on electric power networks. In addition, this segment designs, installs and maintains renewable energy generation facilities, consisting of solar, wind and certain types of natural gas generation facilities, and related switchyards and transmission infrastructure. To a lesser extent, the segment also provides comprehensive communications infrastructure services to wireline, fiber and wireless carrier customers within the communications industry, and services in connection with the construction of electric power generation facilities, the design, installation, maintenance and repair of commercial and industrial wiring, and the installation of traffic networks and cable and control systems for light rail lines.

Oil and Gas Infrastructure Services Segment

The Oil and Gas Infrastructure Services segment provides comprehensive network solutions to customers involved in the development and transportation of natural gas, oil and other pipeline products. Services performed by the Oil and Gas Infrastructure Services segment generally include the design, installation, repair and maintenance of pipeline transmission and distribution systems, gathering systems, production systems, storage systems and compressor and pump stations, as well as related trenching, directional boring and mechanized welding services. In addition, this segment's services include pipeline protection, integrity testing, rehabilitation and replacement, and fabrication of pipeline support systems and related structures and facilities. Quanta also serves the offshore and inland water energy markets, primarily providing services to oil and gas exploration platforms, including mechanical installation (or "hook-ups"), electrical and instrumentation, pre-commissioning and commissioning, coatings, fabrication and marine asset repair. To a lesser extent, this segment designs, installs and maintains fueling systems, as well as water and sewer infrastructure.

Acquisitions

During the second quarter of 2017, Quanta acquired a communications infrastructure services contractor located in the United States, the results of which are generally included in Quanta's Electric Power Infrastructure Services segment. The results of the acquired business have been included in Quanta's consolidated financial statements beginning on the date of acquisition. This acquisition should enhance Quanta's communications service offerings in the United States. During 2016, Quanta completed five acquisitions. The results have been included in Quanta's consolidated financial statements beginning on the respective dates of acquisition. See further discussion in Note 4. See Note 13 for information on an acquisition that occurred subsequent to June 30, 2017.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Principles of Consolidation

The condensed consolidated financial statements of Quanta include the accounts of Quanta Services, Inc. and its wholly owned subsidiaries, which are also referred to as its operating units. The condensed consolidated financial statements also include the accounts of certain of Quanta's investments in joint ventures, which are either consolidated or proportionately consolidated, as discussed in the following summary of significant accounting policies. Investments in affiliated entities in which Quanta does not have a controlling financial interest, but over which Quanta has significant influence, usually because Quanta holds a voting interest of between 20% and 50%, are accounted for

using the equity method. All significant intercompany accounts and transactions

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QUANTA SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

(Unaudited)

have been eliminated in consolidation. Unless the context requires otherwise, references to Quanta include Quanta Services, Inc. and its consolidated subsidiaries.

Interim Condensed Consolidated Financial Information

These unaudited condensed consolidated financial statements have been prepared pursuant to the rules of the U.S. Securities and Exchange Commission (SEC). Certain information and footnote disclosures, normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States (US GAAP), have been condensed or omitted pursuant to those rules and regulations. Quanta believes that the disclosures made are adequate to make the information presented not misleading. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to fairly state the financial position, results of operations, comprehensive income and cash flows with respect to the interim condensed consolidated financial statements have been included. The results of operations and comprehensive income for the interim periods are not necessarily indicative of the results for the entire fiscal year. The results of Quanta have historically been subject to significant seasonal fluctuations.

Quanta recommends that these unaudited condensed consolidated financial statements be read in conjunction with the audited consolidated financial statements and notes thereto of Quanta and its consolidated subsidiaries included in Quanta's Annual Report on Form 10-K for the year ended December 31, 2016, which was filed with the SEC on March 1, 2017.

Reclassifications

Quanta reclassified certain prior period amounts related to stock-based compensation on the condensed consolidated statements of cash flows to conform to the current period presentation under a recently adopted accounting update. Additionally, certain reclassifications have been made to the prior year's condensed consolidated statements of operations to conform to classifications in the current year.

Use of Estimates and Assumptions

The preparation of financial statements in conformity with US GAAP requires the use of estimates and assumptions by management in determining the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities known to exist as of the date the financial statements are published, and the reported amounts of revenues and expenses recognized during the periods presented. Quanta reviews all significant estimates affecting its consolidated financial statements on a recurring basis and records the effect of any necessary adjustments prior to their publication. Judgments and estimates are based on Quanta's beliefs and assumptions derived from information available at the time such judgments and estimates are made. Uncertainties with respect to such estimates and assumptions are inherent in the preparation of financial statements. Estimates are primarily used in Quanta's assessment of the allowance for doubtful accounts, valuation of inventory, useful lives of assets, fair value assumptions in analyzing goodwill, other intangibles and long-lived asset impairments, equity and other investments, loan receivables, purchase price allocations, liabilities for self-insured and other claims and guarantees, multiemployer pension plan withdrawal liabilities, revenue recognition for construction contracts inclusive of contractual change orders and claims, share-based compensation, operating results of reportable segments, as well as the provision for income taxes and the calculation of uncertain tax positions.

Cash and Cash Equivalents

Quanta had cash and cash equivalents of \$99.6 million and \$112.2 million as of June 30, 2017 and December 31, 2016. Cash consisting of interest-bearing demand deposits is carried at cost, which approximates fair value. Quanta considers all highly liquid investments with an original maturity of three months or less at the time of purchase to be cash equivalents, which are carried at fair value. At June 30, 2017 and December 31, 2016, cash equivalents were \$8.4 million and \$8.8 million, and consisted primarily of money market investments and money market mutual funds and are discussed further in Fair Value Measurements below. As of June 30, 2017 and December 31, 2016, cash and cash equivalents held in domestic bank accounts were \$31.4 million and \$19.5 million, and cash and cash equivalents held in foreign bank accounts were \$68.2 million and \$92.7 million. As of June 30, 2017 and December 31, 2016, cash and

cash equivalents held by Quanta's investments in joint ventures, which are either consolidated or proportionately consolidated, were \$13.4 million and \$11.5 million, of which \$10.5 million and \$10.0 million related to domestic joint ventures. Cash and cash equivalents held by the joint ventures are available to support joint venture operations, but Quanta cannot utilize those assets to support its other operations. Quanta generally has no right to the joint ventures' cash and cash equivalents other than participating in distributions and in the event of dissolution.

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QUANTA SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

(Unaudited)

Current and Long-Term Accounts and Notes Receivable and Allowance for Doubtful Accounts

Quanta provides an allowance for doubtful accounts when collection of an account or note receivable is considered doubtful, and receivables are written off against the allowance when deemed uncollectible. Inherent in the assessment of the allowance for doubtful accounts are certain judgments and estimates regarding, among other factors, the customer's access to capital, the customer's willingness or ability to pay, general economic and market conditions, the ongoing relationship with the customer and uncertainties related to the resolution of disputed matters. Quanta considers accounts receivable delinquent after 30 days but does not generally include delinquent accounts in its analysis of the allowance for doubtful accounts unless the accounts receivable have been outstanding for at least 90 days. In addition to balances that have been outstanding for 90 days or more, Quanta also includes accounts receivable balances that relate to customers in bankruptcy or with other known difficulties in its analysis of the allowance for doubtful accounts. Material changes in customers' business or cash flows, which may be impacted by negative economic and market conditions, could affect Quanta's ability to collect amounts due from them. As of June 30, 2017 and December 31, 2016, Quanta had allowances for doubtful accounts on current receivables of \$5.3 million and \$2.8 million. Long-term accounts receivable are included within other assets.

Should customers experience financial difficulties or file for bankruptcy, or should anticipated recoveries relating to receivables in existing bankruptcies or other workout situations fail to materialize, Quanta could experience reduced cash flows and losses in excess of current allowances provided.

The balances billed but not paid by customers pursuant to retainage provisions in certain contracts are generally due upon completion of the contracts and acceptance by the customer. Based on Quanta's experience with similar contracts in recent years, the majority of the retainage balances at each balance sheet date are expected to be collected within the next twelve months. Current retainage balances as of June 30, 2017 and December 31, 2016 were \$239.8 million and \$231.0 million and were included in "Accounts receivable". Retainage balances with settlement dates beyond the next twelve months were included in "Other assets, net", and as of June 30, 2017 and December 31, 2016 were \$31.0 million and \$5.2 million.

Within accounts receivable, Quanta recognizes unbilled receivables in circumstances such as when revenues have been earned and recorded but the amount cannot be billed under the terms of the contract until a later date; costs have been incurred but are yet to be billed under cost-reimbursement type contracts; or amounts arise from routine lags in billing (for example, work completed one month but not billed until the next month). These balances do not include revenues accrued for work performed under fixed-price contracts as these amounts are recorded as costs and estimated earnings in excess of billings on uncompleted contracts. At June 30, 2017 and December 31, 2016, the balances of unbilled receivables included in accounts receivable were \$247.4 million and \$206.8 million.

Goodwill and Other Intangibles

Quanta has recorded goodwill in connection with its historical acquisitions of companies. Upon acquisition, these companies were either combined into one of Quanta's existing operating units or managed on a stand-alone basis as an individual operating unit. Goodwill recorded in connection with these acquisitions is subject to an annual assessment for impairment, which Quanta performs at the operating unit level for each operating unit that carries a balance of goodwill. Each of Quanta's operating units is organized into one of two internal divisions: the Electric Power Infrastructure Services Division and the Oil and Gas Infrastructure Services Division. As most of the companies acquired by Quanta provide multiple types of services for multiple types of customers, these divisional designations are based on the predominant type of work performed by each operating unit at the point in time the divisional designation is made. Goodwill is required to be measured for impairment at the reporting unit level, which represents the operating segment level or one level below the operating segment level for which discrete financial information is available. Quanta has determined that its individual operating units represent its reporting units for the purpose of assessing goodwill impairments.

Quanta has the option to first assess qualitative factors to determine whether it is necessary to perform the two-step fair value-based impairment test described below. If Quanta believes that, as a result of its qualitative assessment, it is

more likely than not that the fair value of a reporting unit is less than its carrying amount, the quantitative impairment test is required. Quanta can choose to perform the qualitative assessment on none, some or all of its reporting units. Quanta can also bypass the qualitative assessment for any reporting unit in any period and proceed directly to step one of the impairment test, and then resume the qualitative assessment in any subsequent period. Qualitative indicators including deterioration in macroeconomic conditions, declining financial performance, or a sustained decrease in share price, among other things, may trigger the need for annual or interim impairment testing of goodwill associated with one or all of the reporting units.

Quanta's goodwill impairment assessment is performed at year-end, or more frequently if events or circumstances arise which indicate that goodwill may be impaired. For instance, a decrease in Quanta's market capitalization below book value, a

QUANTA SERVICES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

(Unaudited)

significant change in business climate or loss of a significant customer, as well as the qualitative indicators referenced above, may trigger the need for interim impairment testing of goodwill for one or all of its reporting units. The first step of the two-step fair value based test involves comparing the fair value of each of Quanta's reporting units with its carrying value, including goodwill. If the carrying value of the reporting unit exceeds its fair value, the second step is performed. The second step compares the carrying amount of the reporting unit's goodwill to the implied fair value of its goodwill. If the implied fair value of goodwill is less than the carrying amount, an impairment loss would be recorded as a reduction to goodwill with a corresponding charge to operating expense.

Quanta determines the fair value of its reporting units using a weighted combination of the discounted cash flow, market multiple and market capitalization valuation approaches, with heavier weighting on the discounted cash flow method, as in management's opinion, this method currently results in the most accurate calculation of a reporting unit's fair value. Determining the fair value of a reporting unit requires judgment and the use of significant estimates and assumptions. Such estimates and assumptions include, among others, revenue growth rates, operating margins, discount rates, weighted average costs of capital and future market conditions. Quanta believes the estimates and assumptions used in its impairment assessments are reasonable and based on available market information, but variations in any of the assumptions could result in materially different calculations of fair value and determinations of whether or not an impairment is indicated.

Under the discounted cash flow method, Quanta determines fair value based on the estimated future cash flows of each reporting unit, discounted to present value using risk-adjusted industry discount rates, which reflect the overall level of inherent risk of a reporting unit and the rate of return an outside investor would expect to earn. Cash flow projections are derived from budgeted amounts and operating forecasts (typically a one-year model) plus an estimate of later period cash flows, all of which are evaluated by management. Subsequent period cash flows are developed for each reporting unit using growth rates that management believes are reasonably likely to occur, along with a terminal value derived from the reporting unit's earnings before interest, taxes, depreciation and amortization (EBITDA). The EBITDA multiples for each reporting unit are based on trailing twelve-month comparable industry data.

Under the market multiple and market capitalization approaches, Quanta determines the estimated fair value of each of its reporting units by applying transaction multiples to each reporting unit's projected EBITDA and then averaging that estimate with similar historical calculations using either a one, two or three year average. For the market capitalization approach, Quanta adds a reasonable control premium, which is estimated as the premium that would be received in a sale of the reporting unit in an orderly transaction between market participants.

For recently acquired reporting units, a step one impairment test may indicate an implied fair value that is substantially similar to the reporting unit's carrying value. Such similarities in value are generally an indication that management's estimates of future cash flows associated with the recently acquired reporting unit remain relatively consistent with the assumptions that were used to derive its initial fair value.

During the fourth quarter of 2016, a two-step fair-value based goodwill impairment analysis was performed for each of Quanta's reporting units, and no reporting units were evaluated solely on a qualitative basis. Step one of the analysis indicated that the implied fair value of each of Quanta's reporting units, other than recently acquired reporting units and the reporting units that recorded goodwill impairment charges in 2015, was substantially in excess of its carrying value.

As discussed generally above, when evaluating the 2016 step one impairment test results, management considered many factors in determining whether or not an impairment of goodwill for any reporting unit was reasonably likely to occur in future periods, including future market conditions and the economic environment in which Quanta's reporting units were operating. Additionally, management considered the sensitivity of its fair value estimates to changes in certain valuation assumptions. After taking into account a 10% decrease in the fair value of each of Quanta's reporting units, two reporting units within Quanta's Oil and Gas Infrastructure Division had fair values below their respective carrying values. Quanta recorded asset impairment charges for these reporting units in 2015. The fair values determined in 2016 for these reporting units were consistent with the fair values determined in 2015 and approximated

their current carrying values, and therefore no impairment was required. Circumstances such as market declines, unfavorable economic conditions, loss of a major customer or other factors could increase the risk of impairment of goodwill for these reporting units in future periods.

If an operating unit experiences prolonged periods of declining revenues, operating margins or both, it may be at risk of failing step one of the goodwill impairment test. Certain operating units have experienced declines over the short-term due to challenging macroeconomic conditions in certain geographic areas and low oil and natural gas prices, which have negatively impacted customer spending and resulted in project cancellations and delays.

Additionally, customer capital spending has been constrained as a result of an increasingly complex regulatory and permitting environment. Certain operating units within Quanta's

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Oil and Gas Infrastructure Services Division that primarily operate within the midstream and smaller-scale transmission market have continued to be negatively impacted by these factors. Goodwill and intangible assets associated with the operating units within Quanta's Oil and Gas Infrastructure Services Division that have been significantly impacted by the factors mentioned above were \$70.7 million and \$11.5 million at June 30, 2017. Quanta monitors these conditions and others to determine if it is necessary to perform step one of the fair-value based impairment test for one or more operating units prior to the annual impairment assessment. No interim impairment charges were recorded during the six months ended June 30, 2017. Although Quanta is not aware of circumstances that would lead to a goodwill impairment at a reporting unit currently, circumstances such as a continued market decline, the loss of a major customer or other factors could impact the valuation of goodwill in the future.

Quanta's intangible assets include customer relationships, backlog, trade names, non-compete agreements, patented rights and developed technology, all subject to amortization. The value of customer relationships is estimated as of the date a business is acquired based on the value-in-use concept utilizing the income approach, specifically the excess earnings method. This analysis consists of discounting to present value the projected cash flows attributable to the customer relationships, with consideration given to customer contract renewals and estimated customer attrition rates, the importance of existing customer relationships to Quanta's business plan, income taxes and required rates of return. Quanta values backlog for acquired businesses as of the acquisition date based upon the contractual nature of the backlog within each service line, discounted to present value. The value of trade names is estimated using the relief-from-royalty method of the income approach. This approach is based on the assumption that in lieu of ownership, a company would be willing to pay a royalty for use of the trade name.

Quanta amortizes intangible assets based upon the estimated consumption of their economic benefits, or on a straight-line basis if the pattern of economic benefit cannot otherwise be reliably estimated. Intangible assets subject to amortization are reviewed for impairment and are tested for recoverability whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. For instance, a significant change in business climate or a loss of a significant customer, among other things, may trigger the need for interim impairment testing of intangible assets. An impairment loss would be recognized if the carrying amount of an intangible asset is not recoverable and its carrying amount exceeds its fair value.

Investments in Affiliates and Other Entities

In the normal course of business, Quanta enters into various types of investment arrangements, each having unique terms and conditions. These investments may include equity interests held by Quanta in business entities, including general or limited partnerships, contractual joint ventures, or other forms of equity or profit participation. These investments may also include Quanta's participation in different financing structures such as the extension of loans to project specific entities, the acquisition of convertible notes issued by project specific entities, or other strategic financing arrangements. Quanta also enters into strategic partnerships with customers and infrastructure investors to provide fully integrated infrastructure services on certain projects, including planning and feasibility analyses, engineering, design, procurement, construction financing, and investment and project operation and maintenance. These projects include public-private partnerships, private infrastructure projects and concessions, along with build, own, operate and transfer and build to suit arrangements. As part of this strategy, Quanta formed a partnership with select infrastructure investors that provides \$750.0 million of capital, including \$60.0 million from Quanta, available to invest in certain of these infrastructure projects. Wholly owned subsidiaries of Quanta serve as the general partner of this partnership and as a separately operating registered investment adviser that manages the invested capital. Quanta determines whether such investments involve a variable interest entity (VIE) based on the characteristics of the subject entity. If the entity is determined to be a VIE, then management determines if Quanta is the primary beneficiary of the entity and whether or not consolidation of the VIE is required. The primary beneficiary consolidating the VIE must normally have both (i) the power to direct the activities that most significantly affect the VIE's economic performance and (ii) the obligation to absorb significant losses of, or the right to receive significant benefits from, the VIE. When Quanta is deemed to be the primary beneficiary, the VIE is consolidated and the other

party's equity interest in the VIE is accounted for as a non-controlling interest. In cases where Quanta determines that it has an undivided interest in the assets, liabilities, revenues and profits of an unincorporated VIE (e.g., a general partnership interest), such amounts are consolidated on a basis proportional to Quanta's ownership interest in the unincorporated entity.

Investments in entities of which Quanta is not the primary beneficiary, but over which Quanta has the ability to exercise significant influence, are accounted for using the equity method of accounting. Quanta's share of net income or losses from unconsolidated equity investments is reported as equity in earnings (losses) of unconsolidated affiliates, which is included in "Other income (expense)" in the condensed consolidated statements of operations. Equity investments are reviewed for impairment by assessing whether any decline in the fair value of the investment below the carrying value is other than temporary. In making this determination, factors such as the ability to recover the carrying amount of the investment and the inability of the investee to sustain an earnings capacity are evaluated in determining whether a loss in value should be recognized. Any impairment losses

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related to investments would be recognized in equity in earnings (losses) of unconsolidated affiliates. Equity method investments are carried at original cost and are included in "Other assets, net" in the condensed consolidated balance sheets and are adjusted for Quanta's proportionate share of the investees' income, losses and distributions.

Under the investment structure described above, Quanta has a minority ownership interest in a limited partnership that was selected during 2014 to build, own and operate a new electric transmission line and two substations in Alberta, Canada. The limited partnership contracted with a Quanta subsidiary to perform the engineering, procurement and construction (EPC) services for the project, and the Quanta subsidiary recognizes revenue and related cost of services as performance progresses on the project. However, due to Quanta's ownership interest, a proportional amount of the EPC profit is deferred until the electric transmission line and related substations are constructed and ownership of the assets is deemed to be transferred to the third party customer. The profit deferral has been recorded as a decrease to the equity method investment included in "Other assets, net" in the accompanying condensed consolidated balance sheets and as a component of equity in earnings (losses) of unconsolidated affiliates, which is included in "Other income (expense)" in the condensed consolidated statements of operations.

Revenue Recognition

Quanta provides its services pursuant to master service agreements, repair and maintenance contracts and fixed price and non-fixed price installation contracts. Pricing under these contracts may be competitive unit price, cost-plus/hourly (or time and materials basis) or fixed price (or lump sum basis), and the final terms and prices of these contracts are frequently negotiated with the customer. Under unit-based contracts, the utilization of an output-based measurement is appropriate for revenue recognition, and Quanta recognizes revenue as units are completed based on pricing established with the customer for each delivered unit, which best reflects the pattern in which the obligation to the customer is fulfilled. Under cost-plus/hourly and time and materials type contracts, Quanta recognizes revenue on an input basis, as labor hours are incurred and services are performed.

Revenues from fixed price contracts are recognized using the percentage-of-completion method, measured by the percentage of costs incurred to date to total estimated costs for each contract. Such contracts provide that the customer accept completion of progress to date and compensate Quanta for services rendered, which may be measured in terms of units installed, hours expended, costs incurred to date compared to total estimated contract costs or some other measure of progress. Contract costs include all direct materials, labor and subcontract costs and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and depreciation costs. Much of the material associated with Quanta's work is owner-furnished and is therefore not included in contract revenues and costs. The cost estimation process is based on professional knowledge and experience of Quanta's engineers, project managers and financial professionals. Changes in job performance, job conditions and final contract settlements are factors that influence management's assessment of contract value and estimated costs, and as a result, the profit recognized.

Actual revenues and project costs can vary, sometimes substantially, from previous estimates due to changes in a variety of factors including unforeseen circumstances not included in Quanta's cost estimates or covered by its contracts for which it cannot obtain adequate compensation, including concealed or unknown environmental conditions; changes in the cost of equipment, commodities, materials or labor; unanticipated costs or claims due to customer-caused delays, customer failure to provide required materials or equipment, errors in engineering, specifications or designs, project modifications, or contract termination and Quanta's inability to obtain reimbursement for such costs or recover on such claims; weather conditions; and quality issues requiring rework or replacement. These factors, along with other risks inherent in performing fixed price contracts may cause actual revenues and gross profits for a project to differ from previous estimates and could result in reduced profitability or losses on projects. Changes in these factors may result in revisions to costs and income, and their effects are recognized in the period in which the revisions are determined. These factors are routinely evaluated on a project-by-project basis throughout the project term, and the impact of corresponding revisions in management's estimates of contract value, contract cost and contract profit are recorded as necessary in the period in which the revisions are determined. Provisions for losses on

uncompleted contracts are made in the period in which such losses are determined to be probable and the amount can be reasonably estimated.

Quanta's operating results for the three months ended June 30, 2017 were positively impacted by 10.2% as a result of aggregate changes in contract estimates related to projects that were in progress at March 31, 2017. Included within the operating results for the three months ended June 30, 2017 were positive changes in estimates of \$24.6 million primarily related to favorable mitigation of project risks and the release of related cost contingencies on two natural gas pipeline projects nearing completion in the quarter. Quanta's operating results for the six months ended June 30, 2017 were impacted by less than 5% as a result of aggregate changes in contract estimates related to projects that were in progress at December 31, 2016.

Quanta's operating results for the three months ended June 30, 2016 were negatively impacted by 9.2% as a result of aggregate changes in contract estimates related to projects that were in progress at March 31, 2016. Quanta's operating results for the six

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months ended June 30, 2016 were negatively impacted by 6.7% as a result of aggregate changes in contract estimates related to projects that were in progress at December 31, 2015. Operating results for the three and six months ended June 30, 2016 included losses on a power plant construction project in Alaska due to performance issues that resulted in an increase of the estimated total costs necessary to complete the project. During the three and six months ended June 30, 2016, Quanta recognized project losses of \$30.5 million and \$51.8 million related to this project. This project was substantially completed during the fourth quarter of 2016. The losses on this project were partially offset by the aggregate positive impact of numerous individually immaterial changes in profitability generally due to better than expected performance on projects that were in progress at December 31, 2015.

The current asset "Costs and estimated earnings in excess of billings on uncompleted contracts" represents revenues recognized in excess of amounts billed for fixed price contracts. The current liability "Billings in excess of costs and estimated earnings on uncompleted contracts" represents billings in excess of revenues recognized for fixed price contracts.

Quanta may incur costs subject to change orders, whether approved or unapproved by the customer, and/or claims related to certain contracts. Quanta determines the probability that such costs will be recovered based upon evidence such as past practices with the customer, specific discussions or preliminary negotiations with the customer or verbal approvals. Quanta treats items as costs of contract performance in the period incurred if it is not probable that the costs will be recovered or will recognize revenue if it is probable that the contract price will be adjusted and can be reliably estimated.

As of June 30, 2017 and December 31, 2016, Quanta recognized revenues of \$118.9 million and \$137.8 million related to change orders and/or claims that were in the process of being negotiated in the normal course of business. These aggregate contract price adjustments represent management's best estimate of additional contract revenues which have been earned and which management believes are probable of collection. The amounts ultimately realized by Quanta upon final acceptance by its customers could be higher or lower than such estimated amounts; however, such amounts cannot currently be estimated.

Income Taxes

Quanta follows the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recorded for future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that are expected to be in effect when the underlying assets or liabilities are recovered or settled.

Quanta regularly evaluates valuation allowances established for deferred tax assets for which future realization is uncertain. The estimation of required valuation allowances includes estimates of future taxable income. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Quanta considers projected future taxable income and tax planning strategies in making this assessment. If actual future taxable income differs from these estimates, Quanta may not realize deferred tax assets to the extent estimated.

Quanta records reserves for income taxes related to certain tax positions in those instances where Quanta considers it more likely than not that additional taxes may be due in excess of amounts reflected on income tax returns filed. When recording reserves for expected tax consequences of uncertain positions, Quanta assumes that taxing authorities have full knowledge of the position and all relevant facts. Quanta continually reviews exposure to additional tax obligations, and as further information is known or events occur, changes in tax reserves may be recorded. To the extent interest and penalties may be assessed by taxing authorities on any underpayment of income tax, such amounts have been accrued and included in the provision for income taxes.

As of June 30, 2017, the total amount of unrecognized tax benefits relating to uncertain tax positions was \$36.3 million, an increase from December 31, 2016 of \$1.1 million. This increase in unrecognized tax benefits resulted primarily from tax positions to be taken for 2017. Although the Internal Revenue Service completed its examination related to tax years 2010, 2011 and 2012 during the year ended December 31, 2016, certain subsidiaries remain under

examination by various U.S. state, Canadian and other foreign tax authorities for multiple periods. Quanta believes it is reasonably possible that within the next 12 months unrecognized tax benefits may decrease by up to \$13.4 million as a result of settlement of these examinations or as a result of the expiration of certain statute of limitations periods. U.S. federal and state and foreign income tax laws and regulations are voluminous and are often ambiguous. As such, Quanta is required to make many subjective assumptions and judgments regarding its tax positions that could materially affect amounts recognized in its future consolidated balance sheets, consolidated statements of operations and consolidated statements of comprehensive income.

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Earnings Per Share

Basic and diluted earnings per share attributable to common stock are computed using the weighted average number of common shares outstanding during the periods. Exchangeable shares that were issued pursuant to certain of Quanta's historical acquisitions (as further discussed in Note 8), which are exchangeable on a one-for-one basis with shares of Quanta common stock, have been included in the calculation of weighted average shares outstanding for basic and diluted earnings per share attributable to common stock for the portion of the periods that they were outstanding. Additionally, unvested stock-based awards that contain non-forfeitable rights to dividends or dividend equivalents (participating) have been included in the calculation of basic and diluted earnings per share attributable to common stock for the portion of the periods that they were outstanding. Diluted earnings per share attributable to common stock is computed using the weighted average number of common shares outstanding during the period adjusted for all potentially dilutive common stock equivalents, except in cases where the effect of the common stock equivalents would be antidilutive.

Self-Insurance

Quanta is insured for employer's liability, workers' compensation, auto liability and general liability claims. Under these programs, the deductible for employer's liability is \$1.0 million per occurrence, the deductible for workers' compensation is \$5.0 million per occurrence, and the deductibles for auto liability and general liability are \$10.0 million per occurrence. Quanta is generally self-insured for all claims that do not exceed the amount of the applicable deductible. Quanta also has employee health care benefit plans for most employees not subject to collective bargaining agreements, of which the primary plan is subject to a deductible of \$0.4 million per claimant per year. Losses under all of these insurance programs are accrued based upon Quanta's estimate of the ultimate liability for claims reported and an estimate of claims incurred but not reported, with assistance from third-party actuaries. These insurance liabilities are difficult to assess and estimate due to unknown factors, including the severity of an injury, the extent of damage, the determination of Quanta's liability in proportion to other parties and the number of incidents not reported. The accruals are based upon known facts and historical trends, and management believes such accruals are adequate.

Collective Bargaining Agreements

Some of Quanta's operating units are parties to various collective bargaining agreements with unions that represent certain of their employees. The collective bargaining agreements expire at various times and have typically been renegotiated and renewed on terms similar to those in the expiring agreements. The agreements require the operating units to pay specified wages, provide certain benefits to their union employees and contribute certain amounts to multiemployer pension plans and employee benefit trusts. Quanta's multiemployer pension plan contribution rates generally are specified in the collective bargaining agreements (usually on an annual basis), and contributions are made to the plans on a "pay-as-you-go" basis based on its union employee payrolls. The location and number of union employees that Quanta employs at any given time and the plans in which they may participate vary depending on the projects Quanta has ongoing at that time and the need for union resources in connection with those projects. Therefore, Quanta is unable to accurately predict the union employee payroll and the amount of the resulting multiemployer pension plan contribution obligation for future periods.

Stock-Based Compensation

Quanta recognizes compensation expense for restricted stock, restricted stock units (RSUs) and performance units to be settled in common stock based on the fair value of the awards at the date of grant, net of estimated forfeitures. The fair value of restricted stock awards, RSUs and performance units to be settled in common stock is determined based on the number of shares or units granted and the closing price of Quanta's common stock on the date of grant or the fair value as determined using a Monte Carlo simulation for performance units with market-based metrics. An estimate of future forfeitures is utilized to determine the period expense. Quanta uses historical data to estimate the forfeiture rate; however, these estimates are subject to change and may impact the value that will ultimately be recognized as compensation expense. The resulting compensation expense from performance unit and time-based

RSU awards is recognized on a straight-line basis over the requisite service period, which is generally the vesting period, while compensation expense from performance-based RSU awards is recognized using the graded vesting method over the requisite service period. However, compensation expense related to performance units can vary from period to period based on changes in the total number of performance units that Quanta anticipates will vest. Payments made by Quanta to satisfy employees' tax withholding obligations associated with awards settled in common stock are classified as financing cash flows.

Compensation expense associated with liability based awards, such as RSUs that are expected to or may settle in cash, is recognized based on a remeasurement of the fair value of the award at the end of each reporting period. Upon settlement, the

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holders receive for each RSU an amount in cash equal to the fair market value on the settlement date of one share of Quanta common stock, as specified in the applicable award agreement. For additional information on Quanta's restricted stock, RSU and performance unit awards, see Note 9.

Functional Currency and Translation of Financial Statements

The U.S. dollar is the functional currency for the majority of Quanta's operations, which are primarily located within the United States. The functional currency for Quanta's foreign operations, which are primarily located in Canada and Australia, is typically the currency of the country in which