

QUANTA SERVICES INC  
Form 10-Q  
August 09, 2007

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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, 2007**
- 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**

*(State or other jurisdiction of  
incorporation or organization)*

**74-2851603**

*(I.R.S. Employer  
Identification No.)*

**1360 Post Oak Blvd.**

**Suite 2100**

**Houston, Texas 77056**

*(Address of principal executive offices, including zip code)*

**(713) 629-7600**

*(Registrant's telephone number, including area code)*

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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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

119,176,424 shares of common stock were outstanding as of August 7, 2007. As of the same date, 760,171 shares of limited vote common stock were outstanding.

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**QUANTA SERVICES, INC. AND SUBSIDIARIES**

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**Table of Contents****QUANTA SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands, except share information)

(Unaudited)

	<b>December 31, 2006</b>	<b>June 30, 2007</b>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 383,687	\$ 405,792
Accounts receivable, net of allowances of \$5,419 and \$4,277	507,761	474,171
Costs and estimated earnings in excess of billings on uncompleted contracts	36,113	49,788
Inventories	28,768	23,394
Prepaid expenses and other current assets	34,300	33,860
<b>Total current assets</b>	<b>990,629</b>	<b>987,005</b>
Property and equipment, net of accumulated depreciation of \$296,903 and \$308,221	276,789	293,713
Accounts and notes receivable, net of allowances of \$42,953, respectively	7,815	6,376
Other assets, net	31,981	33,821
Other intangible assets, net of accumulated amortization of \$2,156 and \$3,620	1,448	7,808
Goodwill	330,495	353,707
<b>Total assets</b>	<b>\$ 1,639,157</b>	<b>\$ 1,682,430</b>

**LIABILITIES AND STOCKHOLDERS EQUITY**

Current Liabilities:		
Current maturities of long-term debt	\$ 34,845	\$ 33,380
Accounts payable and accrued expenses	270,897	220,339
Billings in excess of costs and estimated earnings on uncompleted contracts	28,714	24,485
<b>Total current liabilities</b>	<b>334,456</b>	<b>278,204</b>
Convertible subordinated notes	413,750	413,750
Deferred income taxes and other non-current liabilities	161,868	181,665
<b>Total liabilities</b>	<b>910,074</b>	<b>873,619</b>
Commitments and Contingencies		
Stockholders Equity:		
Common Stock, \$.00001 par value, 300,000,000 shares authorized, 119,605,047 and 121,323,104 shares issued and 117,618,130 and 119,147,044 shares outstanding		

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Limited Vote Common Stock, \$.00001 par value, 3,345,333 shares authorized, 915,805 and 760,171 shares issued and outstanding		
Additional paid-in capital	1,103,332	1,132,846
Accumulated deficit	(351,639)	(297,098)
Treasury stock, 1,986,917 and 2,176,060 common shares, at cost	(22,610)	(26,937)
Total stockholders' equity	729,083	808,811
Total liabilities and stockholders' equity	\$ 1,639,157	\$ 1,682,430

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

**Table of Contents****QUANTA SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except per share information)****(Unaudited)**

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2006</b>	<b>2007</b>	<b>2006</b>	<b>2007</b>
Revenues	\$ 514,048	\$ 557,600	\$ 1,010,542	\$ 1,132,480
Cost of services (including depreciation)	433,693	471,931	870,739	968,405
Gross profit	80,355	85,669	139,803	164,075
Selling, general and administrative expenses	46,550	47,310	88,734	96,542
Amortization of intangible assets	90	692	181	1,464
Income from operations	33,715	37,667	50,888	66,069
Interest expense	(9,794)	(5,544)	(15,678)	(11,096)
Interest income	3,036	5,654	6,015	9,952
Gain on early extinguishment of debt, net	1,598		1,598	
Other income (expense), net	180	82	328	111
Income before income tax provision	28,735	37,859	43,151	65,036
Provision for income taxes	11,075	15,993	17,633	11,966
Net income	\$ 17,660	\$ 21,866	\$ 25,518	\$ 53,070
Earnings per share:				
Basic	\$ 0.15	\$ 0.18	\$ 0.22	\$ 0.45
Diluted	\$ 0.14	\$ 0.17	\$ 0.21	\$ 0.40
Shares used in computing earnings per share:				
Basic	117,152	118,578	116,840	118,306
Diluted	142,014	149,964	141,827	149,736

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

**Table of Contents****QUANTA SERVICES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2006</b>	<b>2007</b>	<b>2006</b>	<b>2007</b>
<b>Cash Flows from Operating Activities:</b>				
Net income	\$ 17,660	\$ 21,866	\$ 25,518	\$ 53,070
Adjustments to reconcile net income to net cash provided by operating activities				
Depreciation and amortization	12,886	13,214	25,566	26,333
Amortization of debt issuance costs	4,253	675	5,167	1,350
Loss (gain) on sale of property and equipment	(124)	(93)	(587)	231
Gain on early extinguishment of debt	(2,088)		(2,088)	
Provision for doubtful accounts	757	(28)	855	373
Deferred income tax provision (benefit)	(1,877)	1,543	26	1,487
Non-cash stock-based compensation	1,568	1,771	3,017	3,620
Tax impact of stock-based equity awards	(285)	(3,525)	(4,643)	(5,587)
Changes in operating assets and liabilities, net of non-cash transactions				
(Increase) decrease in				
Accounts and notes receivable	2,021	(5,589)	(14,282)	39,684
Costs and estimated earnings in excess of billings on uncompleted contracts	1,770	(8,680)	(7,202)	(13,006)
Inventories	614	2,039	(1,809)	5,374
Prepaid expenses and other current assets	1,170	(2,743)	1,229	(223)
Increase (decrease) in				
Accounts payable and accrued expenses and other non-current liabilities	144	(12,810)	(3,707)	(34,304)
Billings in excess of costs and estimated earnings on uncompleted contracts	1,098	897	4,376	(4,713)
Other, net	2,362	(108)	1,051	(1,211)
Net cash provided by operating activities	41,929	8,429	32,487	72,478
<b>Cash Flows from Investing Activities:</b>				
Proceeds from sale of property and equipment	3,016	3,419	4,622	4,274
Additions of property and equipment	(15,716)	(16,671)	(29,307)	(42,065)
Cash paid for acquisition, net of cash acquired		(1,998)		(19,734)
Purchases of short-term investments	(233,525)		(294,040)	(309,055)
Proceeds from the sale of short-term investments	21,875		21,875	309,055
Net cash used in investing activities	(224,350)	(15,250)	(296,850)	(57,525)



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Cash Flows from Financing Activities:

Payments under credit facility	(4,500)		(7,500)	
Proceeds from other long-term debt	144,098	378	145,576	4,875
Payments on other long-term debt	(138,856)	(466)	(140,386)	(6,531)
Debt issuance and amendment costs	(5,671)		(5,671)	
Tax impact of stock-based equity awards	285	3,525	4,643	5,587
Exercise of stock options	173	2,744	790	3,221
Net cash provided by (used in) financing activities	(4,471)	6,181	(2,548)	7,152
Net increase (decrease) in cash and cash equivalents	(186,892)	(640)	(266,911)	22,105
Cash and cash equivalents, beginning of period	224,248	406,432	304,267	383,687
Cash and cash equivalents, end of period	\$ 37,356	\$ 405,792	\$ 37,356	\$ 405,792
Supplemental disclosure of cash flow information				
Cash (paid) received during the period for				
Interest paid	\$ (8,790)	\$ (8,903)	\$ (12,452)	\$ (9,736)
Income taxes paid	\$ (4,143)	\$ (17,770)	\$ (5,390)	\$ (28,593)
Income tax refunds	\$ 90	\$ 35	\$ 195	\$ 156

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 specialized contracting services, offering end-to-end network solutions to the electric power, gas, telecommunications and cable television industries. Quanta's comprehensive services include designing, installing, repairing and maintaining network infrastructure.

*Interim Condensed Consolidated Financial Information*

These unaudited condensed consolidated financial statements have been prepared pursuant to the rules of the 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, 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 and cash flows with respect to the interim consolidated financial statements have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year. The results of Quanta historically have 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 subsidiaries included in Quanta's Annual Report on Form 10-K for the year ended December 31, 2006, which was filed with the SEC on February 28, 2007.

*Use of Estimates and Assumptions*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 amount 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 property and equipment, fair value assumptions in analyzing goodwill and long-lived asset impairments, self-insured claims liabilities, revenue recognition under percentage-of-completion accounting and provision for income taxes.

*Reclassifications*

Certain reclassifications have been made in prior years' financial statements to conform to classifications used in the current year.

*Short-Term Investments*

Quanta held no short-term investments as of December 31, 2006 or June 30, 2007; however during the first quarter of 2007, Quanta invested from time to time in variable rate demand notes (VRDNs), which are classified as short-term investments available for sale when held. The income from VRDNs is tax exempt to Quanta.

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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. Inherent in the assessment of the allowance for doubtful accounts are certain judgments and estimates including, among others, the customer's access to capital, the customer's willingness or ability to pay, general economic conditions and the ongoing relationship with the customer. Under certain circumstances such as foreclosures or negotiated settlements, Quanta may take title to the underlying assets in lieu of cash in settlement of receivables. As of June 30, 2007, Quanta had total allowances for doubtful accounts of approximately \$47.2 million. 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. In addition, material changes in Quanta's customers' revenues or cash flows could affect its ability to collect amounts due from them.

Included in accounts and notes receivable are amounts due from a customer relating to the construction of independent power plants. During 2006, the underlying assets which had secured these notes receivable were sold pursuant to liquidation proceedings and the net proceeds are being held by a trustee. The final collection of amounts owed Quanta are subject to further legal proceedings. Quanta recorded allowances for a significant portion of these notes receivable in prior periods. Also included in accounts and notes receivable as of June 30, 2007 are \$1.0 million in retainage balances with settlement dates beyond the next twelve months.

*Concentration of Credit Risk*

Quanta grants credit under normal payment terms, generally without collateral, to its customers, which include electric power and gas companies, telecommunications and cable television system operators, governmental entities, general contractors and builders, owners and managers of commercial and industrial properties located primarily in the United States. Consequently, Quanta is subject to potential credit risk related to changes in business and economic factors throughout the United States; however, Quanta generally has certain statutory lien rights with respect to services provided. No customer accounted for more than 10% of accounts receivable as of December 31, 2006 and June 30, 2007 or revenues for the three and six months ended June 30, 2006 and June 30, 2007.

*Goodwill*

In accordance with Statement of Financial Accounting Standards (SFAS) No. 142 Goodwill and Other Intangible Assets, goodwill attributable to each of Quanta's reporting units is tested for impairment by comparing the fair value of each reporting unit with its carrying value. Fair value is determined using a combination of the discounted cash flow, market multiple and market capitalization valuation approaches. Significant estimates used in the above methodologies include estimates of future cash flows, future short-term and long-term growth rates, weighted average cost of capital and estimates of market multiples for each of the reportable units. On an ongoing basis, absent impairment indicators, Quanta performs impairment tests annually during the fourth quarter. SFAS No. 142 does not allow increases in the carrying value of reporting units that may result from Quanta's impairment test, therefore Quanta may record goodwill impairments in the future, even when the aggregate fair value of Quanta's reporting units and Quanta as a whole may increase.

*Intangible Assets*

During the first six months of 2007, Quanta recorded approximately \$7.8 million in other intangible assets associated with two acquisitions closed during that period of time.

**Table of Contents****QUANTA SERVICES INC. AND SUBSIDIARIES****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(Unaudited)**

Intangible assets are comprised of (in thousands):

	<b>December 31, 2006</b>	<b>June 30, 2007</b>
Intangible assets:		
Customer relationships	\$ 2,100	\$ 7,420
Backlog		1,810
Non-compete agreements		694
Patent	1,504	1,504
Total intangible assets	3,604	11,428
Accumulated amortization:		
Customer relationships	(1,313)	(1,591)
Backlog		(1,091)
Non-compete agreements		(45)
Patent	(843)	(893)
Total accumulated amortization	(2,156)	(3,620)
Intangible assets, net	\$ 1,448	\$ 7,808

Quanta amortizes intangible assets as these assets are utilized or on a straight line basis over the life of these assets, as appropriate. Expenses for the amortization of intangible assets were \$0.1 million and \$0.7 million for the three months ended June 30, 2006 and 2007, and \$0.2 million and \$1.5 million for the six months ended June 30, 2006 and 2007. The weighted average amortization period for all intangible assets as of June 30, 2007 is 10.8 years, while the weighted average amortization periods for customer relationships, backlog, non-compete agreements and the patent are 13.2 years, 7.3 months, 4.7 years and 6.1 years. The estimated aggregate amortization expense of intangible assets is set forth below (in thousands):

**For the Fiscal Year Ended December 31,**

2007 (excludes six months ended June 30, 2007)	\$ 1,064
2008	939
2009	856
2010	594
2011	594
Thereafter	3,761

Total

\$ 7,808

*Income Taxes*

Quanta follows the liability method of accounting for income taxes in accordance with SFAS No. 109, 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

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**QUANTA SERVICES INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(Unaudited)**

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 adopted Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 (FIN No. 48) on January 1, 2007. As a result of the implementation of FIN No. 48, Quanta recognized a \$1.5 million decrease in the reserve for uncertain tax positions, which was accounted for as an adjustment to the accumulated deficit as of January 1, 2007. Including the effect of the \$1.5 million decrease, the total amount of unrecognized tax benefits as of the date of adoption was \$72.5 million. Of this total, \$60.6 million, net of the federal benefit on state issues, represents the amount of unrecognized tax benefits that, if recognized, would favorably impact the effective income tax rate in future periods. Also, as of January 1, 2007, Quanta had accrued \$14.0 million of interest and penalties relating to unrecognized tax benefits. Quanta's continuing practice is to recognize within the provision for income taxes any interest and/or penalties related to income tax matters.

In the first half of 2007, Quanta recorded a decrease in the total amount of unrecognized tax benefits of \$7.0 million, consisting of a \$11.5 million decrease in unrecognized tax benefits due to the completion of Internal Revenue Service (IRS) audits for tax years 2000 to 2004 partially offset by a \$4.5 million increase in unrecognized tax benefits as a result of tax positions expected to be taken in the current year. The total amount of unrecognized tax benefits as of June 30, 2007 was \$65.5 million. Quanta believes that it is reasonably possible that within the next 12 months the total unrecognized tax benefits will decrease by an additional \$22.8 million to \$33.9 million due to the expiration of certain statutes of limitations.

Quanta is subject to income tax in the United States, multiple state jurisdictions and a few foreign jurisdictions. Quanta remains open to examination by the Internal Revenue Services (IRS) for tax years 2000 through 2006 as these statutes of limitations have not yet expired. Quanta does not consider any state in which it does business to be a major tax jurisdiction under FIN No. 48.

*New Accounting Pronouncements*

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes methods used to measure fair value and expands disclosure requirements about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal periods. Quanta is currently evaluating the impact of this statement, if any, on its consolidated financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115. SFAS No. 159 permits entities to choose to measure at fair value many financial instruments and certain other items at fair value that are not currently required to be measured. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. Quanta is currently evaluating the impact of this statement, if any, on its consolidated financial position, results of operations or cash flows.



**2. PENDING MERGER WITH INFRASOURCE SERVICES, INC.**

On March 18, 2007, Quanta entered into a definitive agreement to acquire, through a merger transaction (the Merger), InfraSource Services, Inc. (InfraSource). InfraSource is a leading specialty contractor servicing electric, natural gas and telecommunications infrastructure in the United States. InfraSource's services include design, engineering, procurement, construction, testing and maintenance services for electric, natural gas and telecommunications infrastructure. Pursuant to the merger agreement, Quanta will issue to InfraSource's stockholders

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**QUANTA SERVICES INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**  
**(Unaudited)**

1.223 shares of Quanta common stock for each share of InfraSource common stock. The boards of directors of Quanta and InfraSource have each unanimously approved the transaction. The Merger is subject to various customary closing conditions, including approval of the Merger by both Quanta and InfraSource stockholders. Quanta and InfraSource have scheduled their respective special stockholders meetings for August 30, 2007. Quanta's management and board of directors will continue in their current positions following the completion of the Merger. The Merger is expected to close on or about August 30, 2007, as soon as practicable following the approval of Quanta's and InfraSource's stockholders and satisfaction of any other remaining closing conditions.

Under the terms of the merger agreement, Quanta will issue approximately 51 million shares of common stock to holders of InfraSource's common stock (based on the number of outstanding shares of InfraSource on July 26, 2007 and assuming the exercise of all outstanding options to purchase shares of InfraSource common stock that are vested, as well as an updated number of options to purchase 370,219 shares of InfraSource common stock that will vest as a result of the consummation of the Merger). Concurrent with the closing of the Merger, Quanta expects to repay InfraSource's outstanding borrowings under its credit agreement to the extent InfraSource does not have sufficient funds to pay such amount. The amount outstanding under InfraSource's credit agreement as of June 30, 2007 was approximately \$60.0 million.

The accompanying Consolidated Financial Statements do not reflect any adjustments or disclosures that may be required upon consummation of the pending Merger.

**3. STOCK-BASED COMPENSATION:**

On May 24, 2007, Quanta stockholders approved the Quanta Services, Inc. 2007 Stock Incentive Plan (the 2007 Plan). The 2007 Plan provides for the award of incentive stock options, non-qualified stock options and restricted common stock. Quanta's 2001 Stock Incentive Plan (as amended and restated March 13, 2003) (the 2001 Plan) was terminated effective May 24, 2007, and no further awards or grants under the 2001 Plan will occur. Outstanding awards and grants made under the 2001 Plan, however, will continue to be governed by its terms.

Quanta issues restricted common stock at the fair market value of the common stock as of the date of issuance. The shares of restricted common stock issued are subject to forfeiture, restrictions on transfer and certain other conditions until they vest, which generally occurs over three years in equal annual installments. During the restriction period, the plan participants are entitled to vote and receive dividends on such shares. During the three months ended June 30, 2006 and 2007, Quanta granted 48,846 and 28,866 shares of restricted common stock with a weighted average grant date price of \$15.97 and \$28.96. During the six months ended June 30, 2006 and 2007, Quanta granted approximately 0.7 million and 0.4 million shares of restricted common stock with a weighted average grant price of \$13.89 and \$25.67.

During the three months ended June 30, 2006 and 2007, Quanta recorded non-cash compensation expense with respect to restricted stock in the amount of \$1.6 million and \$1.8 million and a related income tax benefit of \$0.6 million and \$0.7 million. During the six months ended June 30, 2006 and 2007, Quanta recorded non-cash compensation expense with respect to restricted stock in the amount of \$3.0 million and \$3.6 million and a related income tax benefit of \$1.2 million and \$1.4 million. During the three months ended June 30, 2006 and 2007, the actual tax benefit realized for the tax deductions from vested restricted stock totaled approximately \$0.2 million and

\$0.7 million. During the six months ended June 30, 2006 and 2007, the actual tax benefit realized for the tax deductions from vested restricted stock totaled approximately \$4.2 million and \$2.3 million.

The actual tax benefit realized for the tax deductions from options exercised totaled approximately \$0.1 million and \$2.8 million for the three months ended June 30, 2006 and 2007. The actual tax benefit realized for the tax deduction from options exercised totaled approximately \$0.3 million and \$3.2 million for the six months ended June 30, 2006 and 2007. Additionally, the actual tax benefit related to the 1999 Employee Stock Purchase Plan,

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**(Unaudited)**

which was terminated in 2005, was none and \$0.1 million for the three and six months ended June 30, 2006, with no effect on the three and six months ended June 30, 2007.

**4. PER SHARE INFORMATION:**

Basic earnings per share is computed using the weighted average number of common shares outstanding during the period, and diluted earnings per share 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 equivalent would be antidilutive. The weighted average number of shares used to compute the basic and diluted earnings per share for the three and six months ended June 30, 2006 and 2007 is illustrated below (in thousands):

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2006</b>	<b>2007</b>	<b>2006</b>	<b>2007</b>
<b>NET INCOME:</b>				
Net income	\$ 17,660	\$ 21,866	\$ 25,518	\$ 53,070
Effect of convertible subordinated notes under the if-converted method interest expense addback, net of taxes	2,230	3,199	4,460	6,398
Net income for diluted earnings per share	\$ 19,890	\$ 25,065	\$ 29,978	\$ 59,468
<b>WEIGHTED AVERAGE SHARES:</b>				
Weighted average shares outstanding for basic earnings per share	117,152	118,578	116,840	118,306
Effect of dilutive stock options and restricted stock	625	734	750	778
Effect of convertible subordinated notes under the if-converted method weighted convertible shares issuable	24,237	30,652	24,237	30,652
Weighted average shares outstanding for diluted earnings per share	142,014	149,964	141,827	149,736

For the three months and six months ended June 30, 2007, stock options for approximately 0.1 million shares were excluded from the computation of diluted earnings per share because the options' exercise prices were greater than the average market prices of Quanta's common stock. For the three and six months ended June 30, 2006, stock options for approximately 0.2 million shares were excluded from the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of Quanta's common stock. For the three and six months ended June 30, 2006, the effect of assuming conversion of the 4.0% and 3.75% convertible subordinated notes

would be antidilutive, so they were excluded from the calculation of diluted earnings per share. For the three and six months ended June 30, 2007, the effect of assuming the conversion of the 4.0% convertible subordinated notes would be antidilutive, so they were excluded from the calculation of diluted earnings per share.

## **5. BUSINESS COMBINATIONS**

In May 2007, Quanta acquired a telecommunications company for a purchase price (including the estimated post-closing purchase price adjustment for net working capital) of \$4.3 million, consisting of \$2.6 million in cash and 54,560 shares of Quanta common stock valued at \$1.7 million at the date of acquisition. The acquisition allows Quanta to further expand its telecommunications business in the western United States. The estimated fair value of the tangible assets was \$1.8 million and consisted of current assets of \$1.5 million and property and equipment of

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\$0.3 million. Net tangible assets acquired were \$1.5 million after considering liabilities of \$0.3 million. The excess of the purchase price over net tangible assets acquired was recorded as goodwill in the amount of \$1.2 million and intangible assets, consisting of customer relationships, backlog and a non-compete agreement, in the amount of \$1.6 million.

In January 2007, Quanta acquired a foundation drilling company for a purchase price of \$33.6 million, consisting of \$20.4 million in cash and 693,784 shares of Quanta common stock valued at \$13.2 million at the date of acquisition. The acquisition allows Quanta to have in-house capabilities to construct drilled pier foundations for electric transmission towers and wireless telecommunication towers. The estimated fair value of the tangible assets was \$11.3 million and consisted of current assets of \$7.3 million and property and equipment of \$4.0 million. Net tangible assets acquired were \$5.4 million after considering liabilities of \$5.9 million. The excess of the purchase price over net tangible assets acquired was recorded as goodwill in the amount of \$22.0 million and intangible assets, consisting of customer relationships, backlog and a non-compete agreement, in the amount of \$6.2 million.

**6. DEBT:**

*Credit Facility*

As of June 30, 2007, Quanta had a credit facility with various lenders which provides for a \$300.0 million senior secured revolving credit facility maturing on June 12, 2011 (the credit facility). Subject to the conditions specified in the credit facility, Quanta has the option to increase the revolving commitments under the credit facility by up to an additional \$125.0 million from time to time upon receipt of additional commitments from new or existing lenders. Borrowings under the credit facility are to be used for working capital, capital expenditures and other general corporate purposes. The entire amount of the credit facility is available for the issuance of letters of credit.

As of June 30, 2007, Quanta had approximately \$140.3 million of letters of credit issued under the credit facility and no outstanding revolving loans. The remaining \$159.7 million was available for revolving loans or issuing new letters of credit. Amounts borrowed under the credit facility bear interest, at Quanta's option, at a rate equal to either (a) the Eurodollar Rate (as defined in the credit facility) plus 1.25% to 1.875%, as determined by the ratio of Quanta's total funded debt to consolidated EBITDA (as defined in the credit facility), or (b) the base rate (as described below) plus 0.25% to 0.875%, as determined by the ratio of Quanta's total funded debt to consolidated EBITDA. Letters of credit issued under the credit facility are subject to a letter of credit fee of 1.25% to 1.875%, based on the ratio of Quanta's total funded debt to consolidated EBITDA. Quanta is also subject to a commitment fee of 0.25% to 0.35%, based on the ratio of its total funded debt to consolidated EBITDA, on any unused availability under the credit facility. The base rate equals the higher of (i) the Federal Funds Rate (as defined in the credit facility) plus 1/2 of 1% and (ii) the bank's prime rate.

The credit facility contains certain covenants, including covenants with respect to maximum funded debt to consolidated EBITDA, maximum senior debt to consolidated EBITDA, minimum interest coverage and minimum consolidated net worth, in each case as specified in the credit facility. For purposes of calculating the maximum funded debt to consolidated EBITDA ratio and the maximum senior debt to consolidated EBITDA ratio, Quanta's maximum funded debt and maximum senior debt are reduced by all cash and cash equivalents (as defined in the credit facility) held by Quanta in excess of \$25.0 million. As of June 30, 2007, Quanta was in compliance with all of its

covenants. The credit facility limits certain acquisitions, mergers and consolidations, capital expenditures, asset sales and prepayments of indebtedness and, subject to certain exceptions, prohibits liens on material assets. The credit facility also limits the payment of dividends and stock repurchase programs in any fiscal year to an annual aggregate amount of up to 25% of Quanta's consolidated net income (plus the amount of non-cash charges that reduced such consolidated net income) for the prior fiscal year. The credit facility does not limit dividend payments or other distributions payable solely in capital stock. The credit facility provides for customary events of default and carries cross-default provisions with all of Quanta's existing subordinated notes, its continuing indemnity and

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security agreement with its surety and all of its other debt instruments exceeding \$10.0 million in borrowings. If an event of default (as defined in the credit facility) occurs and is continuing, on the terms and subject to the conditions set forth in the credit facility, amounts outstanding under the credit facility may be accelerated and may become or be declared immediately due and payable.

The credit facility is secured by a pledge of all of the capital stock of Quanta's U.S. subsidiaries, 65% of the capital stock of its foreign subsidiaries and substantially all of Quanta's assets. Quanta's U.S. subsidiaries guarantee the repayment of all amounts due under the credit facility. Quanta's obligations under the credit facility constitute designated senior indebtedness under its 3.75%, 4.0% and 4.5% convertible subordinated notes.

Quanta is currently in the process of amending the credit facility in connection with the consummation of the Merger, including an exception to the timing of the requirement to pledge certain regulated assets and interests that Quanta will acquire in the Merger that Quanta will not be able to pledge prior to the receipt of certain government approvals. Following the consummation of the Merger, Quanta will pledge the stock and assets of InfraSource and its subsidiaries in accordance with the terms of the credit facility, except as otherwise provided in the proposed amendment.

*4.0% Convertible Subordinated Notes*

As of June 30, 2007, Quanta had \$33.3 million aggregate principal amount of 4.0% convertible subordinated notes (4.0% Notes) outstanding, which was classified as a current obligation as these 4.0% Notes matured on July 1, 2007. The outstanding principal balance of the 4.0% Notes plus accrued interest were repaid on July 2, 2007, the first business day after the maturity date.

*4.5% Convertible Subordinated Notes*

As of June 30, 2007, Quanta had \$270.0 million aggregate principal amount of 4.5% convertible subordinated notes due 2023 (4.5% Notes) outstanding. The resale of the notes and the shares issuable upon conversion thereof was registered for the benefit of the holders in a shelf registration statement filed with the SEC. The 4.5% Notes require semi-annual interest payments on April 1 and October 1, until the notes mature on October 1, 2023.

The 4.5% Notes are convertible into shares of Quanta's common stock based on an initial conversion rate of 89.7989 shares of Quanta's common stock per \$1,000 principal amount of 4.5% Notes (which is equal to an initial conversion price of approximately \$11.14 per share), subject to adjustment as a result of certain events. The 4.5% Notes are convertible by the holder (i) during any fiscal quarter if the last reported sale price of Quanta's common stock is greater than or equal to 120% of the conversion price for at least 20 trading days in the period of 30 consecutive trading days ending on the first trading day of such fiscal quarter, (ii) during the five business day period after any five consecutive trading day period in which the trading price per note for each day of that period was less than 98% of the product of the last reported sale price of Quanta's common stock and the conversion rate, (iii) upon Quanta calling the notes for redemption or (iv) upon the occurrence of specified corporate transactions. If the notes become convertible under any of these circumstances, Quanta has the option to deliver cash, shares of Quanta's common stock or a combination thereof, with the amount of cash determined in accordance with the terms of the indenture under which the notes were issued. During each quarter of 2006, and in the first two quarters of 2007, the market price condition described in clause (i) above was satisfied, and the notes were convertible at the option of the



holder, although no holders exercised their right to convert. The notes are presently convertible at the option of each holder, and the conversion period will expire on September 30, 2007, but may continue or resume in future periods upon the satisfaction of the market price condition or other conditions.

Beginning October 8, 2008, Quanta may redeem for cash some or all of the 4.5% Notes at the principal amount thereof plus accrued and unpaid interest. The holders of the 4.5% Notes may require Quanta to repurchase all or some of their notes at the principal amount thereof plus accrued and unpaid interest on October 1, 2008, 2013 or

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2018, or upon the occurrence of a fundamental change, as defined by the indenture under which Quanta issued the notes. Quanta must pay any required repurchases on October 1, 2008 in cash. For all other required repurchases, Quanta has the option to deliver cash, shares of its common stock or a combination thereof to satisfy its repurchase obligation. If Quanta were to satisfy any required repurchase obligation with shares of its common stock, the number of shares delivered will equal the dollar amount to be paid in common stock divided by 98.5% of the market price of Quanta's common stock, as defined by the indenture. The right to settle for shares of common stock can be surrendered by Quanta. The 4.5% Notes carry cross-default provisions with Quanta's other debt instruments exceeding \$10.0 million in borrowings, which includes Quanta's existing credit facility.

*3.75% Convertible Subordinated Notes*

As of June 30, 2007, Quanta had \$143.8 million aggregate principal amount of 3.75% convertible subordinated notes due 2026 (3.75% Notes) outstanding. The resale of the notes and the shares issuable upon conversion thereof was registered for the benefit of the holders in a shelf registration statement filed with the SEC. The 3.75% Notes mature on April 30, 2026 and bear interest at the annual rate of 3.75%, payable semi-annually on April 30 and October 30, until maturity.

The 3.75% Notes are convertible into Quanta's common stock, based on an initial conversion rate of 44.6229 shares of Quanta's common stock per \$1,000 principal amount of 3.75% Notes (which is equal to an initial conversion price of approximately \$22.41 per share), subject to adjustment as a result of certain events. The 3.75% Notes are convertible by the holder (i) during any fiscal quarter if the closing price of Quanta's common stock is greater than 130% of the conversion price for at least 20 trading days in the period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter, (ii) upon Quanta calling the 3.75% Notes for redemption, (iii) upon the occurrence of specified distributions to holders of Quanta's common stock or specified corporate transactions or (iv) at any time on or after March 1, 2026 until the business day immediately preceding the maturity date of the 3.75% Notes. If the 3.75% Notes become convertible under any of these circumstances, Quanta has the option to deliver cash, shares of Quanta's common stock or a combination thereof, with the amount of cash determined in accordance with the terms of the indenture under which the notes were issued. The holders of the 3.75% Notes who convert their notes in connection with certain change in control transactions, as defined in the indenture, may be entitled to a make whole premium in the form of an increase in the conversion rate. In the event of a change in control, in lieu of paying holders a make whole premium, if applicable, Quanta may elect, in some circumstances, to adjust the conversion rate and related conversion obligations so that the 3.75% Notes are convertible into shares of the acquiring or surviving company. During the three months ended June 30, 2007, the market price condition described in clause (i) above was satisfied, and the notes are presently convertible at the option of each holder. The conversion period will expire on September 30, 2007, but may continue or resume in future periods upon the satisfaction of the market price condition or other conditions.

Beginning on April 30, 2010 until April 30, 2013, Quanta may redeem for cash all or part of the 3.75% Notes at a price equal to 100% of the principal amount plus accrued and unpaid interest, if the closing price of Quanta's common stock is equal to or greater than 130% of the conversion price then in effect for the 3.75% Notes for at least 20 trading days in the 30 consecutive trading day period ending on the trading day immediately prior to the date of mailing of the notice of redemption. In addition, Quanta may redeem for cash all or part of the 3.75% Notes at any time on or after April 30, 2010 at certain redemption prices, plus accrued and unpaid interest. Beginning with the six-month interest period commencing on April 30, 2010, and for each six-month interest period thereafter, Quanta will be required to

pay contingent interest on any outstanding 3.75% Notes during the applicable interest period if the average trading price of the 3.75% Notes reaches a specified threshold. The contingent interest payable within any applicable interest period will equal an annual rate of 0.25% of the average trading price of the 3.75% Notes during a five trading day reference period.

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The holders of the 3.75% Notes may require Quanta to repurchase all or a part of the notes in cash on each of April 30, 2013, April 30, 2016 and April 30, 2021, and in the event of a change in control of Quanta, as defined in the indenture, at a purchase price equal to 100% of the principal amount of the 3.75% Notes plus accrued and unpaid interest. The 3.75% Notes carry cross-default provisions with Quanta's other debt instruments exceeding \$20.0 million in borrowings, which includes Quanta's existing credit facility.

**7. STOCKHOLDERS' EQUITY:***Treasury Stock*

Pursuant to Quanta's stock-based compensation plans, employees may elect to satisfy their tax withholding obligations upon vesting of restricted stock by having Quanta make such tax payments and withhold a number of vested shares having a value on the date of vesting equal to their tax withholding obligation. As a result of such employee elections, during the first six months of 2007, Quanta withheld 189,143 shares of Quanta common stock with a total market value of \$4.3 million to satisfy the tax withholding obligations, and these shares were accounted for as treasury stock.

**8. SEGMENT INFORMATION:**

Quanta has aggregated each of its individual operating units into one reportable segment as a specialty contractor. Quanta provides comprehensive network solutions to the electric power, gas, telecommunications and cable television industries, including designing, installing, repairing and maintaining network infrastructure. In addition, Quanta provides ancillary services such as inside electrical wiring, intelligent traffic networks, cable and control systems for light rail lines, airports and highways, and specialty rock trenching, directional boring and road milling for industrial and commercial customers. Each of these services is provided by various Quanta subsidiaries and discrete financial information is not provided to management at the service level. The following table presents information regarding revenues derived from the various industries in which we operate (in thousands):

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2006</b>	<b>2007</b>	<b>2006</b>	<b>2007</b>
Electric power and gas network services	\$ 340,758	\$ 385,316	\$ 670,443	\$ 788,486
Telecommunications and cable television network services	85,936	82,349	154,537	160,850
Ancillary services	87,354	89,935	185,562	183,144
	\$ 514,048	\$ 557,600	\$ 1,010,542	\$ 1,132,480

Quanta does not have significant operations or long-lived assets in countries outside of the United States. Quanta derived \$8.1 million and \$26.8 million of its revenues from foreign operations during the three and six months ended June 30, 2006 and \$13.4 million and \$29.1 million of its revenues from foreign operations during the three and six

months ended June 30, 2007. The majority of revenues from foreign operations was earned in Canada during the three and six months ended June 30, 2006 and 2007.

**9. COMMITMENTS AND CONTINGENCIES:**

*Litigation*

Quanta is from time to time party to various lawsuits, claims and other legal proceedings that arise in the ordinary course of business. These actions typically seek, among other things, compensation for alleged personal injury, breach of contract and/or property damages, punitive damages, civil penalties or other losses, or injunctive or declaratory relief. With respect to all such lawsuits, claims and proceedings, Quanta records reserves when it is

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probable that a liability has been incurred and the amount of loss can be reasonably estimated. Quanta does not believe that any of these proceedings, separately or in the aggregate, would be expected to have a material adverse effect on Quanta's financial position, results of operations or cash flows.

*Self-Insurance*

As of June 30, 2007, Quanta was insured for employer's liability and general liability claims, subject to a deductible of \$1.0 million per occurrence, and for auto liability and workers' compensation claims, subject to a deductible of \$2.0 million per occurrence. Quanta is also subject to an additional cumulative aggregate liability of up to \$2.0 million on workers' compensation claims in excess of \$2.0 million per occurrence per policy year. Quanta also has an employee health care benefits plan for employees not subject to collective bargaining agreements, which is subject to a deductible of \$250,000 per claimant per year. Losses are accrued based upon Quanta's estimates of the ultimate liability for claims reported and an estimate of claims incurred but not reported, with assistance from a third-party actuary. The accruals are based upon known facts and historical trends and management believes such accruals to be adequate. As of December 31, 2006 and June 30, 2007, the gross amount accrued for self-insurance claims totaled \$117.2 million and \$118.7 million, with \$73.4 million and \$79.9 million considered to be long-term and included in other non-current liabilities. Related insurance recoveries/receivables as of December 31, 2006 and June 30, 2007 were \$10.7 million and \$10.7 million, of which \$5.0 million and \$1.0 million are included in prepaid expenses and other current assets and \$5.7 million and \$9.7 million are included in other assets, net.

Quanta's casualty insurance carrier for the policy periods from August 1, 2000 to February 28, 2003 is experiencing financial distress but is currently paying valid claims. In the event that this insurer's financial situation deteriorates, Quanta may be required to pay certain obligations that otherwise would have been paid by this insurer. Quanta estimates that the total future claim amount that this insurer is currently obligated to pay on Quanta's behalf for the above-mentioned policy periods is approximately \$4.7 million, and Quanta has recorded a receivable and corresponding liability for such amount as of June 30, 2007. However, Quanta's estimate of the potential range of these future claim amounts is between \$2.1 million and \$7.5 million. The actual amounts ultimately paid by Quanta related to these claims, if any, may vary materially from the above range and could be impacted by further claims development and the extent to which the insurer could not honor its obligations. Quanta continues to monitor the financial situation of this insurer and analyze any alternative actions that could be pursued. In any event, Quanta does not expect any failure by this insurer to honor its obligations to Quanta, or any alternative actions Quanta may pursue, to have a material adverse impact on Quanta's financial condition; however, the impact could be material to Quanta's results of operations or cash flows in a given period.

*Performance Bonds*

In certain circumstances, Quanta is required to provide performance bonds in connection with its contractual commitments. Quanta has indemnified the surety for any expenses paid out under these performance bonds. As of June 30, 2007, the total amount of outstanding performance bonds was approximately \$630.7 million and the estimated cost to complete these bonded projects was approximately \$120.3 million.

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(Unaudited)***Leases*

Quanta leases certain land, buildings and equipment under non-cancelable lease agreements, including related party leases. The terms of these agreements vary from lease to lease, including some with renewal options and escalation clauses. The following schedule shows the future minimum lease payments under these leases as of June 30, 2007 (in thousands):

	<b>Operating Leases</b>
Year Ending December 31	
2007 (excludes six months ended June 30, 2007)	\$ 19,699
2008	31,450
2009	25,387
2010	21,602
2011	18,330
Thereafter	21,704
Total minimum lease payments	\$ 138,172

Quanta has guaranteed the residual value on certain of its equipment operating leases. Quanta guarantees the difference between this residual value and the fair market value of the underlying asset at the date of termination of the leases. At June 30, 2007, the maximum guaranteed residual value was approximately \$118.3 million. Quanta believes that no significant payments will be made as a result of the difference between the fair market value of the leased equipment and the guaranteed residual value. However, there can be no assurance that significant payments will not be required in the future.

*Employment Agreements*

Quanta has entered into various employment agreements with certain executives which provide for compensation and certain other benefits and for severance payments under certain circumstances. In addition, certain employment agreements contain clauses that become effective upon a change of control of Quanta. Upon the occurrence of any of the defined events in the various employment agreements, Quanta will pay certain amounts to the employee, which vary with the level of the employee's responsibility.

*Collective Bargaining Agreements*

Certain of Quanta's subsidiaries are party to various collective bargaining agreements with certain of their employees. The agreements require such subsidiaries to pay specified wages and provide certain benefits to their union employees. These agreements expire at various times.

*Indemnities*

Quanta has indemnified various parties against specified liabilities that those parties might incur in the future in connection with Quanta's previous acquisitions of certain companies. These indemnities usually are contingent upon the other party incurring liabilities that reach specified thresholds. As of June 30, 2007, Quanta is not aware of circumstances that would lead to future indemnity claims against it for material amounts in connection with these transactions.



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**Item 2. *Management's Discussion and Analysis of Financial Condition and Results of Operations.***

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and with our Annual Report on Form 10-K for the year ended December 31, 2006, which was filed with the SEC on February 28, 2007 and is available on the SEC's website at [www.sec.gov](http://www.sec.gov). The discussion below contains forward-looking statements that are based upon our current expectations and are subject to uncertainty and changes in circumstances. Actual results may differ materially from these expectations due to inaccurate assumptions and known or unknown risks and uncertainties, including those identified under the headings

Uncertainty of Forward-Looking Statements and Information below in this Item 2 and Risk Factors in Item 1A of Part II of this Quarterly Report.

**Introduction**

We are a leading national provider of specialty contracting services, offering end-to-end network solutions to the electric power, gas, telecommunications, cable television and specialty services industries. We believe that we are the largest contractor servicing the transmission and distribution sector of the North American electric utility industry. We derive our revenues from one reportable segment. Our customers include electric power, gas, telecommunications and cable television companies, as well as commercial, industrial and governmental entities. We had consolidated revenues for the six months ended June 30, 2007 of approximately \$1.13 billion, of which 70% was attributable to electric power and gas customers, 14% to telecommunications and cable television customers and 16% to ancillary services, such as inside electrical wiring, intelligent traffic networks, cable and control systems for light rail lines, airports and highways, and specialty rock trenching, directional boring and road milling for industrial and commercial customers.

Our customers include many of the leading companies in the industries we serve. We have developed strong strategic alliances with numerous customers and strive to develop and maintain our status as a preferred vendor to our customers. We enter into various types of contracts, including competitive unit price, hourly rate, cost-plus (or time and materials basis), and fixed price (or lump sum basis), the final terms and prices of which we frequently negotiate with the customer. Although the terms of our contracts vary considerably, most are made on either a unit price or fixed price basis in which we agree to do the work for a price per unit of work performed (unit price) or for a fixed amount for the entire project (fixed price). We complete a substantial majority of our fixed price projects within one year, while we frequently provide maintenance and repair work under open-ended unit price or cost-plus master service agreements that are renewable annually. Some of our customers require us to post performance and payment bonds upon execution of the contract, depending upon the nature of the work to be performed.

We generally recognize revenue on our unit price and cost-plus contracts when units are completed or services are performed. For our fixed price contracts, we typically record revenues as work on the contract progresses on a percentage-of-completion basis. Under this valuation method, revenue is recognized based on the percentage of total costs incurred to date in proportion to total estimated costs to complete the contract. Fixed price contracts generally include retainage provisions under which a percentage of the contract price is withheld until the project is complete and has been accepted by our customer.

**Pending Merger with InfraSource Services, Inc.**

On March 18, 2007, we entered into a definitive agreement to acquire, through a merger transaction (the Merger), InfraSource Services, Inc. (InfraSource). Pursuant to the merger agreement, we will issue to InfraSource's stockholders

1.223 shares of our common stock for each share of InfraSource common stock, or approximately 51 million shares in the aggregate (based on the number of outstanding shares of InfraSource common stock on July 26, 2007 and assuming the exercise of all outstanding options to purchase shares of InfraSource common stock that are vested as well as an updated number of options to purchase 370,219 shares of InfraSource common stock that will vest as a result of the consummation of the Merger). Based upon our common stock outstanding as of July 26, 2007 and the assumptions described above, we expect to have 170,133,510 shares of common stock outstanding immediately following the closing of the Merger. In the merger agreement, we and InfraSource have made customary representations, warranties and covenants, including, among others, covenants (a) to conduct their

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respective businesses in the ordinary course consistent with past practice during the interim period between the execution of the merger agreement and the consummation of the Merger, (b) not to engage in certain transactions during such period and (c) that, subject to certain exceptions and conditions, the boards of directors of Quanta and InfraSource will each recommend that their respective stockholders approve the Merger. The boards of directors of Quanta and InfraSource have each unanimously approved the transaction. The Merger is subject to various customary closing conditions, including approval of the Merger by both our and InfraSource's stockholders. We and InfraSource have scheduled our respective special stockholders meetings for August 30, 2007. The Merger is expected to be completed on or about August 30, 2007, as soon as practicable following the approval of Quanta's and InfraSource's stockholders and satisfaction of any other remaining closing conditions.

InfraSource is a leading specialty contractor servicing electric, natural gas and telecommunications infrastructure in the United States. InfraSource's services include design, engineering, procurement, construction, testing and maintenance services for electric, natural gas and telecommunications infrastructure. InfraSource was formed in 2003 as a Delaware corporation, and it operates in two business segments. The Infrastructure Construction Services (ICS) segment provides design, engineering, procurement, construction, testing, maintenance and repair services for utility infrastructure. ICS customers include electric power utilities, natural gas utilities, telecommunication customers, government entities and heavy industrial companies, such as petrochemical, processing and refining businesses. The Telecommunication Services (TS) segment leases point-to-point telecommunications infrastructure in select markets and provides design, procurement, construction and maintenance services for telecommunications infrastructure. TS customers include communication service providers, large industrial and financial services customers, school districts and other entities with high bandwidth telecommunication needs. The companies in the TS segment are regulated as public telecommunication utilities in various states. InfraSource operates in multiple service territories throughout the United States but does not have significant operations or assets outside the United States.

## **Seasonality; Fluctuations of Results**

Our revenues and results of operations can be subject to seasonal variations. These variations are influenced by weather, customer spending patterns, bidding seasons and holidays. Typically, our revenues are lowest in the first quarter of the year because cold, snowy or wet conditions cause delays. The second quarter is typically better than the first, as some projects begin, but continued cold and wet weather can often impact second quarter productivity. The third quarter is typically the best of the year, as a greater number of projects are underway and weather is more accommodating to work on projects. Revenues during the fourth quarter of the year are typically lower than the third quarter but higher than the second quarter. Many projects are completed in the fourth quarter and revenues often are impacted positively by customers seeking to spend their capital budget before the end of the year; however, the holiday season and inclement weather sometimes can cause delays and thereby reduce revenues and increase costs.

Additionally, our industry can be highly cyclical. As a result, our volume of business may be adversely affected by declines in new projects in various geographic regions in the United States. The financial condition of our customers and their access to capital, variations in the margins of projects performed during any particular quarter, regional economic conditions, timing of acquisitions and the timing and magnitude of acquisition assimilation costs may also materially affect quarterly results. Accordingly, our operating results in any particular quarter or year may not be indicative of the results that can be expected for any other quarter or for any other year. You should read *Outlook* and *Understanding Gross Margins* for additional discussion of trends and challenges that may affect our financial condition and results of operations.

## **Understanding Gross Margins**

Our gross margin is gross profit expressed as a percentage of revenues. Cost of services, which is subtracted from revenues to obtain gross profit, consists primarily of salaries, wages and benefits to employees, depreciation, fuel and

other equipment expenses, equipment rentals, subcontracted services, insurance, facilities expenses, materials and parts and supplies. To enable management to analyze revenue and gross profit, we aggregate operating units by predominant type of work into the following categories: electric power and gas, telecommunications and cable and ancillary. Adjustments are made to this analysis for large, known customers whose work varies from an operating unit's predominant type of work. These reports provide directional guidance based on the

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predominant type of work each operating unit provides but do not quantify revenues or gross profit by type of customer or type of work. Various factors – some controllable, some not – impact our gross margins on a quarterly or annual basis.

*Seasonal and Geographical.* As discussed above, seasonal patterns can have a significant impact on gross margins. Generally, business is slower in the winter months versus the warmer months of the year. This can be offset somewhat by increased demand for electrical service and repair work resulting from severe weather. In addition, the mix of business conducted in different parts of the country will affect margins, as some parts of the country offer the opportunity for higher gross margins than others.

*Weather.* Adverse or favorable weather conditions can impact gross margins in a given period. For example, it is typical in the first quarter of any fiscal year that parts of the country may experience snow or rainfall that may negatively impact our revenues and gross margin due to reduced productivity. In many cases, projects may be delayed or temporarily placed on hold. Conversely, in periods when weather remains dry and temperatures are accommodating, more work can be done, sometimes with less cost, which would have a favorable impact on gross margins. In some cases, strong storms or hurricanes can provide us with high margin emergency service restoration work, which generally has a positive impact on margins.

*Revenue Mix.* The mix of revenues derived from the industries we serve will impact gross margins. Changes in our customers' spending patterns in each of the industries we serve can cause an imbalance in supply and demand and, therefore, affect margins and mix of revenues by industry served.

*Service and Maintenance versus Installation.* Installation work is often obtained on a fixed-price basis, while maintenance work is often performed under pre-established or negotiated prices or cost-plus pricing arrangements. Gross margins for installation work may vary from project to project, and are often higher than maintenance work, because work obtained on a fixed-price basis has higher risk than other types of pricing arrangements. We typically derive approximately 50% of our annual revenues from maintenance work, but a higher portion of installation work in any given quarter may affect our gross margins for that quarter.

*Subcontract Work.* Work that is subcontracted to other service providers generally has lower gross margins. An increase in subcontract work in a given period may contribute to a decrease in gross margin. We typically subcontract approximately 10% to 15% of our work to other service providers.

*Materials versus Labor.* Margins may be lower on projects on which we furnish materials as material prices are generally more predictable than labor costs. Consequently, we generally are not able to mark up materials as much as labor costs. In a given period, a higher percentage of work that has a higher materials component may decrease overall gross margin.

*Depreciation.* We include depreciation in cost of services. This is common practice in our industry, but can make comparability to other companies difficult. This must be taken into consideration when comparing us to other companies.

*Insurance.* Gross margins could be impacted by fluctuations in insurance accruals related to our deductibles in the period in which such adjustments are made. As of June 30, 2007, we had a deductible of \$1.0 million per occurrence related to employer's and general liability insurance and a deductible of \$2.0 million per occurrence for automobile liability and workers' compensation insurance. We are also subject to an additional cumulative aggregate liability of up to \$2.0 million on workers' compensation claims in excess of \$2.0 million per occurrence per policy year. We also have an employee health care benefit plan for employees not subject to collective bargaining agreements, which is subject to a deductible of \$250,000 per claimant per year.

**Selling, General and Administrative Expenses**

Selling, general and administrative expenses consist primarily of compensation and related benefits to management, administrative salaries and benefits, marketing, office rent and utilities, communications, professional fees, bad debt expense, letter of credit fees and gains and losses on the sale of property and equipment.

**Table of Contents****Results of Operations**

The following table sets forth selected statements of operations data and such data as a percentage of revenues for the three and six months indicated (dollars in thousands):

	<b>Three Months Ended June 30,</b>				<b>Six Months Ended June 30,</b>			
	<b>2006</b>		<b>2007</b>		<b>2006</b>		<b>2007</b>	
Revenues	\$ 514,048	100.0%	\$ 557,600	100.0%	\$ 1,010,542	100.0%	\$ 1,132,480	100.0%
Cost of services (including depreciation)	433,693	84.4	471,931	84.6	870,739	86.2	968,405	85.5
Gross profit	80,355	15.6	85,669	15.4	139,803	13.8	164,075	14.5
Selling, general and administrative expenses	46,550	9.0	47,310	8.5	88,734	8.8	96,542	8.6
Amortization of intangible assets	90		692	0.1	181		1,464	0.1
Income from operations	33,715	6.6	37,667	6.8	50,888	5.0	66,069	5.8
Interest expense	(9,794)	(1.9)	(5,544)	(1.0)	(15,678)	(1.6)	(11,096)	(1.0)
Interest income	3,036	0.6	5,654	1.0	6,015	0.6	9,952	0.9
Gain on early extinguishment of debt	1,598	0.3			1,598	0.2		
Other income (expense), net	180		82		328	0.1	111	
Income before income taxes	28,735	5.6	37,859	6.8	43,151	4.3	65,036	5.7
Provision for income taxes	11,075	2.2	15,993	2.9	17,633	1.8	11,966	1.0
Net income	\$ 17,660	3.4%	\$ 21,866	3.9%	\$ 25,518	2.5%	\$ 53,070	4.7%

**Three months ended June 30, 2007 compared to the three months ended June 30, 2006**

**Revenues.** Revenues increased \$43.6 million, or 8.5%, to \$557.6 million for three months ended June 30, 2007, with revenues derived from the electric power and gas network services industry increasing by approximately \$44.6 million. This increase in revenues is a result of the increased number and size of projects as a result of larger capital budgets for our customers, as well as improved pricing. Revenues derived from the telecommunications and cable television network services industry decreased slightly due to delays in spending from certain wireless customers. Revenues derived from ancillary services remained relatively constant.

*Gross profit.* Gross profit increased \$5.3 million, or 6.6%, to \$85.7 million for the three months ended June 30, 2007. As a percentage of revenues, gross margin decreased from 15.6% for the three months ended June 30, 2006 to 15.4% for the three months ended June 30, 2007. This decrease in gross margin resulted primarily from the negative impact on productivity due to significant rainfall in the south central United States, as compared to higher margins achieved in the second quarter of 2006 which were positively impacted by better productivity and cost control on certain jobs.

*Selling, general and administrative expenses.* Selling, general and administrative expenses increased \$0.8 million or 1.6% to \$47.3 million for the three months ended June 30, 2007 compared to the three months ended June 30, 2006. As a percentage of revenues, selling, general and administrative expenses decreased from 9.0% in the second quarter of 2006 to 8.5% in the second quarter of 2007. The slight increase of \$0.8 million is primarily due to \$0.7 million in integration planning costs incurred in the second quarter of 2007 as part of the pending Merger. Although selling, general and administrative expenses remained relatively constant, the amount as a percentage of revenues declined due to improved cost absorption as a result of higher revenues.



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*Amortization of intangible assets.* Amortization of intangible assets increased \$0.6 million to \$0.7 million for the three months ended June 30, 2007. This increase is due to the amortization of intangible assets associated with two acquisitions completed during the first six months of 2007.

*Interest expense.* Interest expense for the three months ended June 30, 2007 decreased \$4.3 million as compared to the three months ended June 30, 2006, primarily due to the expensing of unamortized debt issuance costs of \$3.3 million during the three months ended June 30, 2006 as a result of replacing our prior credit facility in June 2006 and repurchasing 80.7% of our 4.0% convertible subordinated notes during the quarter. The remaining decrease is due to the lower interest rate associated with our 3.75% convertible subordinated notes that were issued in the second quarter of 2006, the proceeds of which were used to repurchase a substantial portion of the 4.0% convertible subordinated notes.

*Interest income.* Interest income was \$5.7 million for the quarter ended June 30, 2007, compared to \$3.0 million for the quarter ended June 30, 2006. The increase is primarily due to higher interest rates and a higher average cash balance for the quarter ended June 30, 2007 as compared to the quarter ended June 30, 2006.

*Provision for income taxes.* The provision for income taxes was \$16.0 million for the three months ended June 30, 2007, with an effective tax rate of 42.2%, compared to a provision of \$11.1 million for the three months ended June 30, 2006, with an effective tax rate of 38.5%. The lower effective tax rate for the three months ended June 30, 2006 included the impact of recording a \$1.6 million refund related to the settlement of a multi-year state tax claim.

***Six months ended June 30, 2007 compared to the six months ended June 30, 2006***

*Revenues.* Revenues increased \$121.9 million, or 12.1%, to \$1.13 billion for the six months ended June 30, 2007, with revenues derived from the electric power and gas network services industry increasing by approximately \$118 million and revenues from the telecommunications and cable television network services industry increasing by approximately \$6 million. These increases in revenues are a result of a higher volume of emergency restoration services performed during the first quarter of 2007 as compared to the first quarter of 2006, coupled with an increased number and size of projects as a result of larger capital budgets for our customers, as well as improved pricing. Revenues derived from the ancillary services customers decreased by approximately \$2 million primarily due to the timing of projects.

*Gross profit.* Gross profit increased \$24.3 million, or 17.4%, to \$164.1 million for the six months ended June 30, 2007. As a percentage of revenues, gross margin increased from 13.8% for the six months ended June 30, 2006 to 14.5% for the six months ended June 30, 2007. This increase in gross margin resulted primarily from a higher volume of higher margin emergency restoration services in the first quarter of 2007, better fixed cost absorption as a result of higher revenues and improved pricing, partially offset by the second quarter effects discussed above.

*Selling, general and administrative expenses.* Selling, general and administrative expenses increased \$7.8 million or 8.8% to \$96.5 million for the six months ended June 30, 2007. As a percentage of revenues, selling, general and administrative expenses decreased from 8.8% to 8.6%. The \$7.8 million increase was primarily due to \$2.4 million in increased salaries and benefits costs associated with additional personnel, salary increases and higher performance bonuses, \$1.6 million in increased professional fees and \$1.0 million in integration planning costs incurred during 2007 as part of the pending Merger with InfraSource. This increase was also due to \$0.9 million in higher facility costs and \$0.2 million in net losses on sales of equipment during 2007, as compared to \$0.6 million in net gains on sales of equipment in 2006.

*Amortization of intangible assets.* Amortization of intangible assets increased \$1.3 million to \$1.5 million for the six months ended June 30, 2007. This increase is due to the amortization of intangible assets associated with two

acquisitions completed during the first six months of 2007.

*Interest expense.* Interest expense for the six months ended June 30, 2007 decreased \$4.6 million to \$11.1 million as compared to the six months ended June 30, 2006, primarily due to the expensing of unamortized debt issuance costs of \$3.3 million during the three months ended June 30, 2006 as a result of replacing our prior credit facility in June 2006 and repurchasing 80.7% of our 4.0% convertible subordinated notes during the quarter.

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The remaining decrease is due to the lower interest rate associated with our 3.75% convertible subordinated notes that were issued in the second quarter of 2006, the proceeds of which were used to repurchase a substantial portion of the 4.0% convertible subordinated notes.

*Interest income.* Interest income was \$10.0 million for the six months ended June 30, 2007, compared to \$6.0 million for the six months ended June 30, 2006. The increase is primarily due to higher interest rates and a higher average cash balance for the six months ended June 30, 2007 as compared to the six months ended June 30, 2006.

*Provision for income taxes.* The provision for income taxes was \$12.0 million for the six months ended June 30, 2007, with an effective tax rate of 18.4%, compared to a provision of \$17.6 million for the six months ended June 30, 2006, with an effective tax rate of 40.9%. The lower effective tax rate for 2007 results from a \$15.3 million tax benefit recorded in the first quarter of 2007 primarily due to a decrease in reserves for uncertain tax positions resulting from the settlement of a multi-year Internal Revenue Service audit.

## **Liquidity and Capital Resources**

### ***Cash Requirements***

We anticipate that our cash and cash equivalents on hand, which totaled \$405.8 million as of June 30, 2007, our credit facility, short term investments, if any, and our future cash flow from operations will provide sufficient funds to enable us to meet our future operating needs, debt service requirements and planned capital expenditures and to facilitate our future ability to grow. Initiatives to rebuild the United States electric power grid or momentum in deployment of fiber to the premises may require a significant amount of additional working capital. We also evaluate opportunities for strategic acquisitions from time to time that may require cash. We had \$33.3 million aggregate principal amount of 4.0% convertible subordinated notes (4.0% Notes) outstanding at June 30, 2007, which was classified as a current obligation as these 4.0% Notes matured on July 1, 2007. The outstanding principal balance of the 4.0% Notes plus accrued interest were repaid on July 2, 2007, the first business day after the maturity date. Additionally, concurrent with the anticipated closing of the pending Merger, we expect to use cash on hand to repay InfraSource's outstanding borrowings under its credit agreement, which were approximately \$60.0 million at June 30, 2007, to the extent InfraSource does not have sufficient funds to pay such amount, as well as to pay for any costs associated with the pending Merger. We believe that we have adequate cash and availability under our credit facility to meet all such needs.

### ***Sources and Uses of Cash***

As of June 30, 2007, we had cash and cash equivalents of \$405.8 million, working capital of \$708.8 million and long-term debt of \$413.8 million, net of current maturities. We also had \$140.3 million of letters of credit outstanding under our credit facility and \$159.7 million was available for revolving loans or issuing new letters of credit.

### ***Operating Activities***

Cash flow from operations is primarily influenced by demand for our services, operating margins and the type of services we provide. Operating activities provided net cash to us of \$8.4 million during the three months ended June 30, 2007 as compared to \$41.9 million during the three months ended June 30, 2006. This decrease in operating cash flows is primarily due to the working capital requirements associated with a large project on going during the second quarter of 2007. No project of similar magnitude was in progress during the second quarter of 2006. In addition, we had larger estimated tax payments in 2007 as compared to the second quarter of 2006, as certain NOL carryforwards reduced cash tax requirements for the second quarter of 2006. Operating activities provided net cash to us of \$72.5 million during the six months ended June 30, 2007 as compared to \$32.5 million during the six months

ended June 30, 2006. The first quarter of 2007 had substantial operating cash flows due to a significant amount of emergency restoration services performed during December 2006 and the first quarter of 2007, which were collected as of the end of the first quarter of 2007.

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### *Investing Activities*

During the six months ended June 30, 2007, we used net cash in investing activities of \$57.5 million as compared to \$296.9 million in the first six months of 2006. Investing activities in 2006 and the first quarter of 2007 included purchases of short-term investments. We invest from time to time in variable rate demand notes (VRDNs), which are classified as short-term investments, available for sale when held. We did not invest in VRDNs in the second quarter of 2007. Other investing activities for the first six months of 2007 include \$42.1 million used for capital expenditures, coupled with \$19.7 million in net cash outlays for acquisitions that closed during the first half of 2007, offset by \$4.3 million of proceeds from the sale of equipment. The \$12.8 million increase in capital expenditures for the six months ended June 30, 2007 compared to the six months ended June 30, 2006 is consistent with our estimated \$21.5 million increase in capital expenditures for the year ended December 31, 2007 compared to actual capital expenditures of \$48.5 million for the year ended December 31, 2006. This increase is related primarily to the growth in our business.

### *Financing Activities*

For the six months ended June 30, 2007, financing activities provided net cash flow of \$7.2 million as compared to \$2.5 million used in financing activities for the six months ended June 30, 2006. For the six months ended June 30, 2007, cash provided resulted primarily from a \$5.6 million tax benefit from stock-based equity awards and \$3.2 million received from the exercise of stock options. Contributing to a net use of cash for the six months ended June 30, 2006 was a payment of \$5.7 million in debt issuance costs related to our second quarter 2006 issuance of our 3.75% convertible subordinated notes, coupled with \$2.3 million in net debt repayments resulting primarily from the repurchase of a portion of our 4.0% convertible subordinated notes and net repayment of other long-term debt, partially offset by the issuance of our 3.75% convertible subordinated notes.

### *Debt Instruments*

#### *Credit Facility*

As of June 30, 2007, we had a credit facility with various lenders which provides for a \$300.0 million senior secured revolving credit facility maturing on June 12, 2011 (the credit facility). Subject to the conditions specified in the credit facility, we have the option to increase the revolving commitments under the credit facility by up to an additional \$125.0 million from time to time upon receipt of additional commitments from new or existing lenders. Borrowings under the credit facility are to be used for working capital, capital expenditures and other general corporate purposes. The entire amount of the credit facility is available for the issuance of letters of credit.

As of June 30, 2007, we had approximately \$140.3 million of letters of credit issued under the credit facility and no outstanding revolving loans. The remaining \$159.7 million was available for revolving loans or issuing new letters of credit. Amounts borrowed under the credit facility bear interest, at our option, at a rate equal to either (a) the Eurodollar Rate (as defined in the credit facility) plus 1.25% to 1.875%, as determined by the ratio of our total funded debt to consolidated EBITDA (as defined in the credit facility), or (b) the base rate (as described below) plus 0.25% to 0.875%, as determined by the ratio of our total funded debt to consolidated EBITDA. Letters of credit issued under the credit facility are subject to a letter of credit fee of 1.25% to 1.875%, based on the ratio of our total funded debt to consolidated EBITDA. We are also subject to a commitment fee of 0.25% to 0.35%, based on the ratio of our total funded debt to consolidated EBITDA, on any unused availability under the credit facility. The base rate equals the higher of (i) the Federal Funds Rate (as defined in the credit facility) plus 1/2 of 1% and (ii) the bank's prime rate.

The credit facility contains certain covenants, including covenants with respect to maximum funded debt to consolidated EBITDA, maximum senior debt to consolidated EBITDA, minimum interest coverage and minimum

consolidated net worth, in each case as specified in the credit facility. For purposes of calculating the maximum funded debt to consolidated EBITDA ratio and the maximum senior debt to consolidated EBITDA ratio, our maximum funded debt and maximum senior debt are reduced by all cash and cash equivalents (as defined in the credit facility) held by us in excess of \$25.0 million. As of June 30, 2007, we were in compliance with all of our covenants. The credit facility limits certain acquisitions, mergers and consolidations, capital expenditures, asset sales and prepayments of indebtedness and, subject to certain exceptions, prohibits liens on material assets. The

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credit facility also limits the payment of dividends and stock repurchase programs in any fiscal year to an annual aggregate amount of up to 25% of our consolidated net income (plus the amount of non-cash charges that reduced such consolidated net income) for the prior fiscal year. The credit facility does not limit dividend payments or other distributions payable solely in capital stock. The credit facility provides for customary events of default and carries cross-default provisions with all of our existing subordinated notes, our continuing indemnity and security agreement with our surety and all of our other debt instruments exceeding \$10.0 million in borrowings. If an event of default (as defined in the credit facility) occurs and is continuing, on the terms and subject to the conditions set forth in the credit facility, amounts outstanding under the credit facility may be accelerated and may become or be declared immediately due and payable.

The credit facility is secured by a pledge of all of the capital stock of our U.S. subsidiaries, 65% of the capital stock of our foreign subsidiaries and substantially all of our assets. Our U.S. subsidiaries guarantee the repayment of all amounts due under the credit facility. Our obligations under the credit facility constitute designated senior indebtedness under our 3.75%, 4.0% and 4.5% convertible subordinated notes.

We are currently in the process of amending the credit facility in connection with the consummation of the Merger, including an exception to the timing of the requirement to pledge certain regulated assets and interests that we will acquire in the Merger that we will not be able to pledge prior to the receipt of certain government approvals. Following the consummation of the Merger, we will pledge the stock and assets of InfraSource and its subsidiaries in accordance with the terms of the credit facility, except as otherwise provided in the amendment.

*4.0% Convertible Subordinated Notes*

As of June 30, 2007, we had \$33.3 million aggregate principal amount of 4.0% Notes outstanding, which was classified as a current obligation as these 4.0% Notes matured on July 1, 2007. The outstanding principal balance of the 4.0% Notes plus accrued interest were repaid on July 2, 2007, the first business day after the maturity date.

*4.5% Convertible Subordinated Notes*

As of June 30, 2007, we had \$270.0 million aggregate principal amount of 4.5% convertible subordinated notes due 2023 (4.5% Notes) outstanding. The resale of the notes and the shares issuable upon conversion thereof was registered for the benefit of the holders in a shelf registration statement filed with the SEC. The 4.5% Notes require semi-annual interest payments on April 1 and October 1 until the notes mature on October 1, 2023.

The 4.5% Notes are convertible into shares of our common stock based on an initial conversion rate of 89.7989 shares of Quanta's common stock per \$1,000 principal amount of 4.5% Notes (which is equal to an initial conversion price of approximately \$11.14 per share), subject to adjustment as a result of certain events. The 4.5% Notes are convertible by the holder (i) during any fiscal quarter if the last reported sale price of our common stock is greater than or equal to 120% of the conversion price for at least 20 trading days in the period of 30 consecutive trading days ending on the first trading day of such fiscal quarter, (ii) during the five business day period after any five consecutive trading day period in which the trading price per note for each day of that period was less than 98% of the product of the last reported sale price of our common stock and the conversion rate, (iii) upon us calling the notes for redemption or (iv) upon the occurrence of specified corporate transactions. If the notes become convertible under any of these circumstances, we have the option to deliver cash, shares of our common stock or a combination thereof, with the amount of cash determined in accordance with the terms of the indenture under which the notes were issued. During each quarter of 2006 and in the first and second quarters of 2007, the market price condition described in clause (i) above was satisfied, and the notes were convertible at the option of the holder, although no holders exercised their right to convert. The notes are presently convertible at the option of each holder, and the conversion period will expire on September 30, 2007, but may continue or resume in future periods upon the satisfaction of the market price

condition or other conditions.

Beginning October 8, 2008, we may redeem for cash some or all of the 4.5% Notes at the principal amount thereof plus accrued and unpaid interest. The holders of the 4.5% Notes may require us to repurchase all or some of their notes at the principal amount thereof plus accrued and unpaid interest on October 1, 2008, 2013 or 2018, or upon the occurrence of a fundamental change, as defined by the indenture under which we issued the notes. We must pay any required repurchases on October 1, 2008 in cash. For all other required repurchases, we have the option to



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deliver cash, shares of our common stock or a combination thereof to satisfy our repurchase obligation. If we were to satisfy any required repurchase obligation with shares of our common stock, the number of shares delivered will equal the dollar amount to be paid in common stock divided by 98.5% of the market price of our common stock, as defined by the indenture. The right to settle for shares of common stock can be surrendered by us. The 4.5% Notes carry cross-default provisions with our other debt instruments exceeding \$10.0 million in borrowings, which includes our existing credit facility.

*3.75% Convertible Subordinated Notes*

As of June 30, 2007, we had \$143.8 million aggregate principal amount of 3.75% Notes outstanding. The resale of the notes and the shares issuable upon conversion thereof was registered for the benefit of the holders in a shelf registration statement filed with the SEC. The 3.75% Notes mature on April 30, 2026 and bear interest at the annual rate of 3.75%, payable semi-annually on April 30 and October 30, until maturity.

The 3.75% Notes are convertible into our common stock, based on an initial conversion rate of 44.6229 shares of our common stock per \$1,000 principal amount of 3.75% Notes (which is equal to an initial conversion price of approximately \$22.41 per share), subject to adjustment as a result of certain events. The 3.75% Notes are convertible by the holder (i) during any fiscal quarter if the closing price of our common stock is greater than 130% of the conversion price for at least 20 trading days in the period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter, (ii) upon our calling the 3.75% Notes for redemption, (iii) upon the occurrence of specified distributions to holders of our common stock or specified corporate transactions or (iv) at any time on or after March 1, 2026 until the business day immediately preceding the maturity date of the 3.75% Notes. If the 3.75% Notes become convertible under any of these circumstances, we have the option to deliver cash, shares of our common stock or a combination thereof, with the amount of cash determined in accordance with the terms of the indenture under which the notes were issued. The holders of the 3.75% Notes who convert their notes in connection with certain change in control transactions, as defined in the indenture, may be entitled to a make whole premium in the form of an increase in the conversion rate. In the event of a change in control, in lieu of paying holders a make whole premium, if applicable, we may elect, in some circumstances, to adjust the conversion rate and related conversion obligations so that the 3.75% Notes are convertible into shares of the acquiring or surviving company. During the three months ended June 30, 2007, the market price condition described in clause (i) above was satisfied, and the notes are presently convertible at the option of each holder. The conversion period will expire on September 30, 2007, but may continue or resume in future periods upon satisfaction of the market price condition or other conditions.

Beginning on April 30, 2010 until April 30, 2013, we may redeem for cash all or part of the 3.75% Notes at a price equal to 100% of the principal amount plus accrued and unpaid interest, if the closing price of our common stock is equal to or greater than 130% of the conversion price then in effect for the 3.75% Notes for at least 20 trading days in the 30 consecutive trading day period ending on the trading day immediately prior to the date of mailing of the notice of redemption. In addition, we may redeem for cash all or part of the 3.75% Notes at any time on or after April 30, 2010 at certain redemption prices, plus accrued and unpaid interest. Beginning with the six-month interest period commencing on April 30, 2010, and for each six-month interest period thereafter, we will be required to pay contingent interest on any outstanding 3.75% Notes during the applicable interest period if the average trading price of the 3.75% Notes reaches a specified threshold. The contingent interest payable within any applicable interest period will equal an annual rate of 0.25% of the average trading price of the 3.75% Notes during a five trading day reference period.

The holders of the 3.75% Notes may require us to repurchase all or a part of the notes in cash on each of April 30, 2013, April 30, 2016 and April 30, 2021, and in the event of a change in control, as defined in the indenture, at a purchase price equal to 100% of the principal amount of the 3.75% Notes plus accrued and unpaid interest. The

3.75% Notes carry cross-default provisions with our other debt instruments exceeding \$20.0 million in borrowings, which includes our existing credit facility.

**Off-Balance Sheet Transactions**

As is common in our industry, we have entered into certain off-balance sheet arrangements in the ordinary course of business that result in risks not directly reflected in our balance sheets. Our significant off-balance sheet

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transactions include liabilities associated with non-cancelable operating leases, letter of credit obligations and surety guarantees. We have not engaged in any off-balance sheet financing arrangements through special purpose entities.

### ***Leases***

We enter into non-cancelable operating leases for many of our facility, vehicle and equipment needs. These leases allow us to conserve cash by paying a monthly lease rental fee for use of facilities, vehicles and equipment rather than purchasing them. We may decide to cancel or terminate a lease before the end of its term, in which case we are typically liable to the lessor for the remaining lease payments under the term of the lease.

We have guaranteed the residual value of the underlying assets under certain of our equipment operating leases at the date of termination of such leases. We have agreed to pay any difference between this residual value and the fair market value of each underlying asset as of the lease termination date. As of June 30, 2007, the maximum guaranteed residual value was approximately \$118.3 million. We believe that no significant payments will be made as a result of the difference between the fair market value of the leased equipment and the guaranteed residual value. However, there can be no assurance that future significant payments will not be required.

### ***Letters of Credit***

Certain of our vendors require letters of credit to ensure reimbursement for amounts they are disbursing on our behalf, such as to beneficiaries under our self-funded insurance programs. In addition, from time to time some customers require us to post letters of credit to ensure payment to our subcontractors and vendors under those contracts and to guarantee performance under our contracts. Such letters of credit are generally issued by a bank or similar financial institution. The letter of credit commits the issuer to pay specified amounts to the holder of the letter of credit if the holder demonstrates that we have failed to perform specified actions. If this were to occur, we would be required to reimburse the issuer of the letter of credit. Depending on the circumstances of such a reimbursement, we may also have to record a charge to earnings for the reimbursement. We do not believe that it is likely that any claims will be made under a letter of credit in the foreseeable future.

As of June 30, 2007, we had \$140.3 million in letters of credit outstanding under our credit facility primarily to secure obligations under our casualty insurance program. These are irrevocable stand-by letters of credit with maturities expiring at various times throughout 2007 and 2008. Upon maturity, it is expected that the majority of these letters of credit will be renewed for subsequent one-year periods.

### ***Performance Bonds***

Many customers, particularly in connection with new construction, require us to post performance and payment bonds issued by a financial institution known as a surety. These bonds provide a guarantee to the customer that we will perform under the terms of a contract and that we will pay subcontractors and vendors. If we fail to perform under a contract or to pay subcontractors and vendors, the customer may demand that the surety make payments or provide services under the bond. We must reimburse the surety for any expenses or outlays it incurs. Under our continuing indemnity and security agreement with the surety and with the consent of our lenders under our credit facility, we have granted security interests in certain of our assets to collateralize our obligations to the surety. We may be required to post letters of credit or other collateral in favor of the surety or our customers in the future. Posting letters of credit in favor of the surety or our customers would reduce the borrowing availability under our credit facility. To date, we have not been required to make any reimbursements to the surety for bond-related costs. We believe that it is unlikely that we will have to fund significant claims under our surety arrangements in the foreseeable future. As of June 30, 2007, an aggregate of approximately \$630.7 million in original face amount of bonds issued by the surety were outstanding. Our estimated cost to complete these bonded projects was approximately \$120.3 million as of

June 30, 2007.

**Table of Contents****Contractual Obligations**

As of June 30, 2007, our future contractual obligations are as follows (in thousands):

	<b>Total</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>Thereafter</b>
Long-term debt principal	\$ 447,130	\$ 33,380	\$ 270,000	\$	\$	\$	\$ 143,750
Long-term debt interest	46,408	8,770	14,503	5,391	5,391	5,391	6,962
Operating lease obligations	138,172	19,699	31,450	25,387	21,602	18,330	21,704
Total	\$ 631,710	\$ 61,849	\$ 315,953	\$ 30,778	\$ 26,993	\$ 23,721	\$ 172,416

As of June 30, 2007, we had no borrowings under our credit facility. In addition, our multi-employer pension plan contributions are determined annually based on our union employee payrolls, which cannot be determined for future periods in advance. As of June 30, 2007, the total unrecognized tax benefit related to uncertain tax positions was \$65.5 million. We estimate that \$0.1 million of this will be paid within the next twelve months. We also believe that it is reasonably possible that within the next twelve months the total unrecognized tax benefits will decrease by \$22.8 million to \$33.9 million due to the expiration of certain statutes of limitations. We are unable to make reasonably reliable estimates regarding the timing of future cash outflows, if any, associated with the remaining unrecognized tax benefits.

**Concentration of Credit Risk**

We grant credit under normal payment terms, generally without collateral, to our customers, which include electric power and gas companies, telecommunications and cable television system operators, governmental entities, general contractors, and builders, owners and managers of commercial and industrial properties located primarily in the United States. Consequently, we are subject to potential credit risk related to changes in business and economic factors throughout the United States. However, we generally have certain statutory lien rights with respect to services provided. Under certain circumstances such as foreclosures or negotiated settlements, we may take title to the underlying assets in lieu of cash in settlement of receivables. As previously discussed herein, our customers have experienced significant financial difficulties. These economic conditions expose us to increased risk related to collectibility of receivables for services we have performed. No customer accounted for more than 10% of accounts receivable as of June 30, 2007 or revenues for the three or six months ended June 30, 2007.

**Litigation**

We are from time to time party to various lawsuits, claims and other legal proceedings that arise in the ordinary course of business. These actions typically seek, among other things, compensation for alleged personal injury, breach of contract and/or property damages, punitive damages, civil penalties or other losses, or injunctive or declaratory relief. With respect to all such lawsuits, claims and proceedings, we record reserves when it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. We do not believe that any of these proceedings, separately or in the aggregate, would be expected to have a material adverse effect on our financial position, results of operations or cash flows.

### **Related Party Transactions**

In the normal course of business, we enter into transactions from time to time with related parties. These transactions typically take the form of facility leases with prior owners of certain acquired companies.

### **New Accounting Pronouncements**

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes methods used to measure fair value and expands disclosure requirements about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal periods. We are currently evaluating the impact of this statement, if any, on our consolidated financial position, results of operations or cash flows.

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In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115. SFAS No. 159 permits entities to choose to measure at fair value many financial instruments and certain other items at fair value that are not currently required to be measured. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of this statement, if any, on our consolidated financial position, results of operations or cash flows.

## **Critical Accounting Policies**

The discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities known to exist at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. We evaluate our estimates on an ongoing basis, based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. There can be no assurance that actual results will not differ from those estimates. Management has reviewed its development and selection of critical accounting estimates with the audit committee of our Board of Directors. We believe the following accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements:

*Revenue Recognition.* Quanta designs, installs and maintains networks for the electric power, gas, telecommunications and cable television industries, as well as provides various ancillary services to commercial, industrial and governmental entities. These services may be provided 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 our unit-based contracts, the utilization of an output-based measurement is appropriate for revenue recognition. Under these contracts, we recognize revenue when units are completed based on pricing established between us and the customer for each unit of delivery, which best reflects the pattern in which the obligation to the customer is fulfilled. Under our cost-plus/hourly or time and materials type contracts, we recognize 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. These contracts provide for a fixed amount of revenues for the entire project. Such contracts provide that the customer accept completion of progress to date and compensate us for services rendered, measured in terms of units installed, hours expended or some other measure of progress. Contract costs include all direct material, 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 materials associated with our work are owner-furnished and are therefore not included in contract revenues and costs. The cost estimation process is based on the professional knowledge and experience of our engineers, project managers and financial professionals. Changes in job performance, job conditions and final contract settlements are factors that influence management's assessment of the total estimated costs to complete those contracts and therefore, our profit recognition. 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. Provisions for the total estimated losses on uncompleted contracts are made in the period in which such losses are determined. If actual results significantly differ from our estimates used for revenue recognition and claim assessments, our financial condition and results of operations could be materially impacted.

We may incur costs related to change orders, whether approved or unapproved by the customer, and/or claims related to certain contracts. We determine whether there is a probability that the costs will be recovered based upon evidence such as past practices with the customer, specific discussions or preliminary negotiations



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with the customer or verbal approvals. We treat items as a cost 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.

*Self-Insurance.* We are insured for employer's liability and general liability claims, subject to a deductible of \$1.0 million per occurrence, and for auto liability and workers' compensation subject to a deductible of \$2.0 million per occurrence. We are also subject to an additional cumulative aggregate liability of up to \$2.0 million on workers' compensation claims in excess of \$2.0 million per occurrence per policy year. We also have an employee health care benefits plan for employees not subject to collective bargaining agreements that is subject to a deductible of \$250,000 per claimant per year. Losses are accrued based upon our estimates of the ultimate liability for claims reported and an estimate of claims incurred but not reported, with assistance from a third-party actuary. However, insurance liabilities are difficult to assess and estimate due to unknown factors, including the severity of an injury, the determination of our liability in proportion to other parties, the number of incidents not reported and the effectiveness of our safety program. The accruals are based upon known facts and historical trends and management believes such accruals to be adequate.

Our casualty insurance carrier for the policy periods from August 1, 2000 to February 28, 2003 has been experiencing financial distress but is currently paying valid claims. In the event that this insurer's financial situation further deteriorates, we may be required to pay certain obligations that otherwise would have been paid by this insurer. We estimate that the total future claim amount that this insurer is currently obligated to pay on our behalf for the above mentioned policy periods is approximately \$4.7 million; however, our estimate of the potential range of these future claim amounts is between \$2.1 million and \$7.5 million. The actual amounts ultimately paid by us in connection with such claims, if any, may vary materially from the above range and could be impacted by further claims development and the extent to which the insurer could not honor its obligations. We continue to monitor the financial situation of this insurer and analyze any alternative actions that could be pursued. In any event, we do not expect any failure by this insurer to honor its obligations to us, or any alternative actions that we may pursue, to have a material adverse impact on our financial condition; however, the impact could be material to our results of operations or cash flow in a given period.

*Valuation of Intangibles and Long-Lived Assets.* SFAS No. 142 provides that goodwill and other intangible assets that have indefinite useful lives not be amortized but, instead, must be tested at least annually for impairment, and intangible assets that have finite useful lives should continue to be amortized over their useful lives. SFAS No. 142 also provides specific guidance for testing goodwill and other nonamortized intangible assets for impairment. SFAS No. 142 does not allow increases in the carrying value of reporting units that may result from our impairment test; therefore, we may record goodwill impairments in the future, even when the aggregate fair value of our reporting units and the company as a whole may increase. Goodwill of a reporting unit will be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. Examples of such events or circumstances may include a significant change in business climate or a loss of key personnel, among others. SFAS No. 142 requires that management make certain estimates and assumptions in order to allocate goodwill to reporting units and to determine the fair value of reporting unit net assets and liabilities, including, among other things, an assessment of market conditions, projected cash flows, cost of capital and growth rates, which could significantly impact the reported value of goodwill and other intangible assets. Estimating future cash flows requires significant judgment, and our projections may vary from cash flows eventually realized. A provision for impairment could be required in a future period if future operating results and residual values differ from our estimates. Intangible assets with definite lives are also reviewed for impairment if events or changes in circumstances indicate that the carrying amount may not be realizable.

We review long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be realizable. If an evaluation is required, the estimated future undiscounted cash flows associated

with the asset are compared to the asset's carrying amount to determine if an impairment of such asset is necessary. This requires us to make long-term forecasts of the future revenues and costs related to the assets subject to review. Forecasts require assumptions about demand for our products and future market conditions. Since estimating future cash flows requires significant judgment, our projections may vary from cash flows eventually realized. Future events and unanticipated changes to assumptions could require a

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provision for impairment in a future period. The effect of any impairment would be to expense the difference between the fair value of such asset and its carrying value. In addition, we estimate the useful lives of our long-lived assets and other intangibles. We periodically review factors to determine whether these lives are appropriate.

*Current and Non-Current Accounts and Notes Receivable and Provision for Doubtful Accounts.* We provide an allowance for doubtful accounts when collection of an account or note receivable is considered doubtful. Inherent in the assessment of the allowance for doubtful accounts are certain judgments and estimates relating to, among others, our customer's access to capital, our customer's willingness or ability to pay, general economic conditions and the ongoing relationship with the customer. Certain of our customers, several of them large public telecommunications carriers and utility customers, have experienced financial difficulties in the past. Should any major customers experience difficulties or file for bankruptcy, or should anticipated recoveries relating to the receivables in existing bankruptcies and other workout situations fail to materialize, we could experience reduced cash flows and losses in excess of current reserves. In addition, material changes in our customers' revenues or cash flows could affect our ability to collect amounts due from them.

*Income Taxes.* We follow the liability method of accounting for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes. Under this method, deferred 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.

We regularly evaluate 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. We consider projected future taxable income and tax planning strategies in making this assessment. If actual future taxable income differs from our estimates, we may not realize deferred tax assets to the extent we have estimated.

We account for uncertain tax positions in accordance with FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes, as interpretation of SFAS No. 109, Accounting for Income Taxes (FIN No. 48). FIN No. 48 prescribes a comprehensive model for how companies should recognize, measure, present and disclose in their financial statements uncertain tax positions taken or to be taken on a tax return. The income tax laws and regulations are voluminous and are often ambiguous. As such, we are required to make many subjective assumptions and judgments regarding our tax positions that can materially affect amounts recognized in our consolidated balance sheets and statements of income.

## **Outlook**

The following statements are based on current expectations. These statements are forward-looking, and actual results may differ materially.

Many utilities across the country have regained their financial health and have increased spending on their transmission and distribution systems. As a result, we are seeing new construction, extensive pole change outs, line upgrades and maintenance projects on many systems and expect this trend to continue over the next several quarters.

We also anticipate increased spending as a result of the Energy Policy Act of 2005 (the Energy Act), which requires the power industry to meet federal reliability standards for its transmission and distribution systems and provides further incentives to the industry to invest in and improve maintenance on its systems.

Several industry and market trends are prompting customers in the electric power industry to seek outsourcing partners, such as Quanta. These trends include an aging utility workforce, increased spending, increasing costs such as salaries and benefits, and labor issues.

There are several telecommunications initiatives currently in discussion and underway by several wireline carriers and government organizations that provide us with pockets of opportunity, particularly from fiber to the

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premises (FTTP) and fiber to the node (FTTN) initiatives. Such initiatives are underway by Verizon and AT&T, and municipalities and other government jurisdictions have also become active in these initiatives. We are anticipating increased spending by wireless telecommunications customers on their networks, as the impact of mergers within the wireless industry has begun to lessen. In addition, several wireless companies have announced plans to increase their cell site deployment plans over the next year, including the expansion of next generation technology.

Spending in the cable television industry is beginning to improve. Several telecommunications companies are increasing the pace of their FTTP and FTTN projects that will enable them to offer TV services via fiber to their customers. These initiatives serve as a catalyst for the cable industry to begin a new network upgrade cycle to expand its service offerings in an effort to retain and attract customers.

We continue to evaluate potential strategic acquisitions of companies to broaden our customer base, expand our geographic area of operation and grow our portfolio of services. On March 18, 2007, we entered into the merger agreement with InfraSource, pursuant to which InfraSource will become a wholly owned subsidiary upon closing of the Merger, subject to the satisfaction of various closing conditions including approval by stockholders of both companies. We expect the proposed transaction to enhance our resources and expand our service portfolio through InfraSource's complementary businesses, strategic geographic footprint and skilled workforce. We believe that additional attractive acquisition candidates exist primarily as a result of the highly fragmented nature of the industry, the inability of many companies to expand and modernize due to capital constraints and the desire of owners of acquisition candidates for liquidity. We also believe that our financial strength and experienced management team will be attractive to acquisition candidates.

With the growth in several of our markets and our margin enhancement initiatives, we continue to see our gross margins generally improve. We continue to focus on the elements of the business we can control, including cost control, the margins we accept on projects, collecting receivables, ensuring quality service and rightsizing initiatives to match the markets we serve. These initiatives include aligning our workforce with our current revenue base, evaluating opportunities to reduce the number of field offices and evaluating our non-core assets for potential sale. Such initiatives, together with realignments associated with the planned integration of InfraSource operations and any other future acquisitions, could result in future charges related to, among other things, severance, retention, facilities shutdown and consolidation, property disposal and other exit costs.

Capital expenditures in 2007 are expected to be approximately \$70.0 million, without giving effect to the pending Merger with InfraSource. A majority of the expenditures will be for operating equipment. We expect expenditures for 2007 to be funded substantially through internal cash flows or to the extent necessary, from cash on hand.

We believe that we are adequately positioned to capitalize upon opportunities in the industries we serve because of our proven full-service operating units with broad geographic reach, financial capability and technical expertise. Additionally, we believe that these industry opportunities and trends will increase the demand for our services; however, we cannot predict the actual timing or magnitude of the impact on us of these opportunities and trends.

## **Uncertainty of Forward-Looking Statements and Information**

This Quarterly Report on Form 10-Q includes statements reflecting assumptions, expectations, projections, intentions or beliefs about future events that are intended as forward-looking statements under the Private Securities Litigation Reform Act of 1995. You can identify these statements by the fact that they do not relate strictly to historical or current facts. They use words such as anticipate, estimate, project, forecast, may, will, should, could, and other words of similar meaning. In particular, these include, but are not limited to, statements relating to:

Projected operating or financial results;

The effects of any acquisitions and divestitures we may make, including the pending acquisition of InfraSource;

Expectations regarding our business outlook and capital expenditures;

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The effects of competition in our markets;

The benefits of the Energy Policy Act of 2005;

The current economic conditions and trends in the industries we serve; and

Our ability to achieve cost savings.

These forward-looking statements are not guarantees of future performance and involve or rely on a number of risks, uncertainties, and assumptions that are difficult to predict or beyond our control. We have based our forward-looking statements on our management's beliefs and assumptions based on information available to our management at the time the statements are made. We caution you that actual outcomes and results may differ materially from what is expressed, implied or forecast by our forward-looking statements and that any or all of our forward-looking statements may turn out to be wrong. They can be affected by inaccurate assumptions and by known or unknown risks and uncertainties, including:

Quarterly variations in our operating results;

Adverse changes in economic conditions and trends in the markets served by us or by our customers;

Our ability to effectively compete for new projects;

Our ability to generate internal growth;

Our ability to consummate the Merger with InfraSource and the timing thereof, including difficulties and delays in obtaining stockholder and regulatory approvals and other difficulties in satisfying other closing conditions set forth in the Merger Agreement;

Potential failure of the Energy Policy Act of 2005 to result in increased spending on the electrical power transmission infrastructure;

Our ability to successfully identify, complete and integrate acquisitions, including the pending acquisition of InfraSource;

Estimates and assumptions in determining our financial results;

The financial distress of our casualty insurance carrier that may require payment for losses that would otherwise be insured;

Estimates relating to our use of percentage-of-completion accounting;

Our dependence on fixed price contracts and the potential to incur losses with respect to those contracts;

Liabilities for claims that are not self-insured or for claims that our casualty insurance carrier fails to pay;

Potential liabilities relating to occupational health and safety matters;

Realization of certain unrecognized tax benefits;

The adverse impact of goodwill or other intangible asset impairments;

Our ability to effectively integrate the operations of businesses we acquire, including InfraSource;

The inability of our customers to pay for services following a bankruptcy or other financial difficulty;

Rapid technological and structural changes that could reduce the demand for the services we provide;

Our ability to obtain performance bonds;

Cancellation provisions within our contracts and the risk that contracts expire and are not renewed or are replaced on less favorable terms;

Retention of key personnel and qualified employees;

The impact of our unionized workforce on our operations and on our ability to complete future acquisitions;



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Our ability to attract skilled labor and the potential shortage of skilled employees;

Our growth outpacing our infrastructure;

Potential exposure to environmental liabilities;

Risks associated with expanding our business in international markets;

Requirements relating to governmental regulation and changes thereto;

Our ability to continue to meet the requirements of the Sarbanes-Oxley Act of 2002;

The cost of borrowing, availability of credit, debt covenant compliance and other factors affecting our financing activities;

The potential conversion of our outstanding 4.5% Notes or 3.75% Notes into cash and/or common stock; and

The other risks and uncertainties as are described under the heading *Risk Factors* in Item 1A of Part II of this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2006 and as may be detailed from time to time in our other public filings with the SEC.

All of our forward-looking statements, whether written or oral, are expressly qualified by these cautionary statements and any other cautionary statements that may accompany such forward-looking statements or that are otherwise included in this report. In addition, we do not undertake any obligation to update any forward-looking statements to reflect events or circumstances after the date of this report or otherwise.

**Item 3. *Quantitative and Qualitative Disclosures About Market Risk.***

The information in this section should be read in connection with the information on financial market risk related to changes in interest rates in Part II, Item 7A, *Quantitative and Qualitative Disclosures About Market Risk*, in our Annual Report on Form 10-K for the year ended December 31, 2006. Our primary exposure to market risk relates to unfavorable changes in interest rates and changes in equity investment prices.

As of December 31, 2006, the fair value of our fixed-rate debt of \$447.0 million aggregate principal amount was approximately \$692.2 million based upon current market prices and, as of June 30, 2007, the fair value of our fixed-rate debt of \$447.0 million aggregate principal amount was approximately \$1.0 billion based upon current market prices.

**Item 4. *Controls and Procedures.***

Attached as exhibits to this quarterly report on Form 10-Q are certifications of Quanta's Chief Executive Officer and Chief Financial Officer that are required in accordance with Rule 13a-14 of the Securities Exchange Act of 1934, as amended (the Exchange Act). This *Controls and Procedures* section includes information concerning the controls and controls evaluation referred to in the certifications, and it should be read in conjunction with the certifications for a more complete understanding of the topics presented.

***Evaluation of Disclosure Controls and Procedures***

Our management has established and maintains a system of disclosure controls and procedures that are designed to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act, such as this quarterly report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. The disclosure controls and procedures are also designed to provide reasonable assurance that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

As of the end of the period covered by this quarterly report, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15(b) of the Exchange Act. This evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer. Based on this evaluation, these officers have concluded that, as of

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June 30, 2007, our disclosure controls and procedures were effective to provide reasonable assurance of achieving their objectives.

***Internal Control over Financial Reporting***

There has been no change in our internal control over financial reporting during the quarter ended June 30, 2007, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

***Design and Operation of Control Systems***

Our management, including the Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and breakdowns can occur because of simple errors or mistakes. Controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

**PART II OTHER INFORMATION**

**QUANTA SERVICES, INC. AND SUBSIDIARIES**

**Item 1. *Legal Proceedings.***

We are from time to time a party to various lawsuits, claims and other legal proceedings that arise in the ordinary course of business. These actions typically seek, among other things, compensation for alleged personal injury, breach of contract and/or property damages, punitive damages, civil penalties or other losses, or injunctive or declaratory relief. With respect to all such lawsuits, claims and proceedings, we accrue reserves when it is probable a liability has been incurred and the amount of loss can be reasonably estimated. We do not believe that any of these proceedings, separately or in the aggregate, would be expected to have a material adverse effect on our results of operations, cash flow or financial position.

**Item 1A. *Risk Factors.***

Except as provided below, as of the date of this filing, there have been no material changes from the risk factors previously disclosed in Item 1A to Part I of our Annual Report on Form 10-K for the year ended December 31, 2006 (2006 Annual Report). An investment in our common stock involves various risks. When considering an investment in our company, you should carefully consider all of the risk factors described in our 2006 Annual Report as well as the risk factors below. These risks and uncertainties are not the only ones facing us and there may be additional matters that are not known to us or that we currently consider immaterial. All of these risks and uncertainties could adversely affect our business, financial condition or future results and, thus, the value of an investment in our company.



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***Failure to complete the Merger with InfraSource could negatively impact the stock price and our future business and financial results.***

Completion of the Merger with InfraSource is not assured and is subject to risks, including the risks that approval of the transaction by stockholders of both Quanta and InfraSource or by regulatory agencies is not obtained or that certain other closing conditions are not satisfied. If the merger is not completed, our ongoing business may be adversely affected, and we will be subject to several risks, including the following:

having to pay certain significant costs relating to the Merger without receiving the benefits of the Merger;

the attention of our management will have been diverted to the Merger instead of on our operations and pursuit of other opportunities that may have been beneficial to us; and

resulting negative customer perception could adversely affect our ability to compete for, or to win, new and renewal business in the marketplace.

***We will incur substantial transaction and Merger-related costs in connection with the Merger and our stockholders will be diluted by the Merger.***

We expect to incur a number of non-recurring transaction and Merger-related costs associated with completing the Merger with InfraSource, combining the operations of the two companies and achieving desired synergies. These fees and costs will be substantial. Additional unanticipated costs may be incurred in the integration of the businesses of Quanta and InfraSource. Although we expect that the elimination of duplicative costs, as well as the realization of other efficiencies related to the integration of the two businesses will offset the incremental transaction and Merger-related costs over time, this net benefit may not be achieved in the near term, or at all.

The Merger will dilute the ownership of our current stockholders who are expected to hold approximately 75% of the combined company's common stock on a fully diluted basis immediately following completion of the Merger.

***In certain circumstances, the merger agreement pursuant to which we will acquire InfraSource requires payment of a termination fee of \$43 million by us to InfraSource.***

Under the merger agreement, we may be required to pay InfraSource a termination fee of \$43 million if the merger agreement is terminated under certain circumstances. Should the merger agreement be terminated in circumstances under which such a termination fee is payable by us, the payment of this fee could have material and adverse consequences to our financial condition and operations.

***If the Merger with InfraSource is completed, we will be subject to additional risks.***

The success of the Merger will depend, in part, on our ability to realize the synergies and other benefits from acquiring InfraSource. To realize these synergies and benefits, however, we must successfully integrate the operations and personnel of InfraSource into our business. If the integration process is unsuccessful, the anticipated benefits of the Merger may not be realized fully or at all or may take longer or cost more to realize than expected. Because we and InfraSource have operated as independent companies and will continue to do so during the pendency of the Merger, it is possible that the integration process will result in the loss of valuable employees, the disruption of both Quanta's and InfraSource's businesses or inconsistencies in standards, controls, procedures, practices, policies and compensation arrangements and that the combined company's results of operations could be adversely affected by any issues attributable to either company's operations that arise prior to the closing of the Merger. Further, the size of the Merger may make integration difficult, expensive and disruptive, adversely affecting our revenues and earnings.

After the Merger, we may be affected to a greater extent by the skilled labor shortages of certain types of qualified personnel, including engineers, project managers, field supervisors and linemen, that both Quanta and InfraSource have from time-to-time experienced. These shortages have also negatively impacted, and may continue to negatively impact, the productivity and profitability of certain projects. Our inability to bid on new and attractive

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projects, or maintain productivity and profitability on existing projects, due to the limited supply of skilled workers, may negatively affect our profitability and results of operations.

We will also be acquiring InfraSource's dark fiber business, which is subject to regulations of the Federal Communications Commission (the FCC) and of various state regulatory agencies. Changes in federal or state regulations could reduce the profitability of InfraSource's telecommunications business, and InfraSource could be subject to fines if the FCC or a state regulatory agency were to determine that any of its activities or positions is not in compliance with certain regulations. If InfraSource's profitability in the telecommunications business were to decline, or if InfraSource were to become subject to fines, our profitability could also be adversely affected.

In connection with the Merger, we expect to record approximately \$800 to \$900 million in goodwill based on the application of purchase accounting. Statement of Financial Accounting Standards (SFAS) No. 142 requires that goodwill and other intangible assets that have indefinite useful lives not be amortized, but instead be tested at least annually for impairment, and that intangible assets that have finite useful lives continue to be amortized over their useful lives. Any future impairments of the goodwill recognized in connection with the Merger would negatively impact Quanta's results of operations for the period in which the impairment is recognized.

InfraSource, certain of its officers and directors and various other parties are defendants in pending litigation, which if not favorably resolved, could adversely affect us following the completion of the Merger.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.****Unregistered Sales of Securities**

Between April 1, 2007 and June 30, 2007, Quanta completed one acquisition of a telecommunications company in which some of the purchase price consideration consisted of the issuance of unregistered securities of Quanta. The aggregate consideration (including an estimated post-closing purchase price adjustment for net working capital) of \$4.3 million paid in this transaction was \$2.6 million in cash and 54,560 shares of common stock. This acquisition was not affiliated with any prior acquisition. Additionally, Quanta issued 35,008 shares of Quanta common stock as part of a post-closing purchase price adjustment in connection with an acquisition of a foundation drilling company that was consummated in the first quarter of 2007.

All securities listed on the following table were shares of common stock. Quanta relied on Section 4(2) of the Securities Act of 1933, as amended (the Securities Act), as the basis for exemption from registration. For all issuances, the purchasers were accredited investors as defined in Rule 501 of the Securities Act. All issuances were to owners of businesses acquired in privately negotiated transactions and not pursuant to public solicitations.

Period	Number of Shares	Purchaser	Consideration
April 1, 2007 - April 30, 2007	35,008	Stockholders of acquired company	Sale of acquired company
May 1, 2007 - May 31, 2007	54,560	Stockholders of acquired company	Sale of acquired company





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The following table contains information about our purchases of equity securities during the three months ended June 30, 2007:

**Issuer Purchases of Equity Securities**

<b>Period</b>	<b>(a) Total Number of Shares Purchased</b>	<b>(b) Average Price Paid Per Share</b>	<b>(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>(d) Maximum Number of Shares that may yet be Purchased Under the Plans or Programs</b>
June 1, 2007 - June 30, 2007	5,886(i)	\$ 29.00	None	None

(i) Represents shares purchased from employees to satisfy tax withholding obligations in connection with the vesting of restricted stock awards pursuant to our 2001 Stock Incentive Plan (as amended and restated March 13, 2003).

**Item 4. Submission of Matters to a Vote of Security Holders.**

We held our annual meeting of stockholders in Houston, Texas on May 24, 2007. Eleven members were elected to the board of directors, each to serve until our next annual meeting of stockholders and until their respective successors have been elected and qualified.

The following ten individuals were elected to the board of directors by the holders of our common stock:

<b>Nominee</b>	<b>For</b>	<b>Withheld</b>
James R. Ball	103,018,803	3,919,139
John R. Colson	105,959,590	978,352
Ralph R. DiSibio	106,438,456	499,486
Bernard Fried	103,424,795	3,513,147
Louis C. Golm	106,319,107	618,835
Worthing F. Jackman	103,541,653	3,396,289
Bruce Ranck	106,320,512	617,430
Gary A. Tucci	105,869,979	1,068,262
John R. Wilson	106,866,883	1,071,059
Pat Wood, III	106,551,794	386,148

The holders of our limited vote common stock elected Vincent D. Foster to the board of directors by a vote of 473,331 shares of limited vote common stock, with no shares withheld.

The stockholders ratified the appointment of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2007 by a vote of 107,159,760 shares of common stock and limited vote common stock, voting together, with (i) 222,247 shares of common stock and no shares of limited vote common stock voting against and (ii) 29,267 shares of common stock and no shares of limited vote common stock abstaining.

The stockholders also approved our 2007 Stock Incentive Plan by a vote of 88,468,680 shares of common stock and limited vote common stock, voting together, with (i) 1,539,633 shares of common stock and no shares of limited vote common stock voting against and (ii) 89,723 shares of common stock and no shares limited vote common stock abstaining. Broker non-votes on this Plan approval, deemed a non-routine matter in accordance with New York Stock Exchange regulations, were not considered entitled to vote and therefore not counted as a vote for or against the Plan.

**Table of Contents****Item 6. Exhibits.**

Exhibit No.	Description
3.1	Restated Certificate of Incorporation (previously filed as Exhibit 3.3 to the Company's Form 10-Q (No. 001-13831) filed August 14, 2003 and incorporated herein by reference)
3.2	Amended and Restated Bylaws (previously filed as Exhibit 3.2 to the Company's 2000 Form 10-K (No. 001-13831) filed April 2, 2001 and incorporated herein by reference)
10.1+	First Amendment to Quanta Services, Inc. 2001 Stock Incentive Plan, as amended and restated March 13, 2003 (previously filed as Exhibit 99.1 to the Company's Form 8-K (001-13831) filed April 23, 2007 and incorporated herein by reference)
10.2+	Quanta Services, Inc. 2007 Stock Incentive Plan (previously filed as Exhibit 99.1 to the Company's Form 8-K (001-13831) filed May 29, 2007 and incorporated herein by reference)
10.3+	Quanta Services, Inc. 2007 Stock Incentive Plan Form of Employee/Consultant Restricted Stock Agreement (previously filed as Exhibit 99.2 to the Company's Form 8-K (001-13831) filed May 29, 2007 and incorporated herein by reference)
10.4+	Quanta Services, Inc. 2007 Stock Incentive Plan Form of Non-Employee Director Restricted Stock Agreement (previously filed as Exhibit 99.3 to the Company's Form 8-K (001-13831) filed May 29, 2007 and incorporated herein by reference)
31.1*	Certification of Periodic Report by Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) and pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
31.2*	Certification of Periodic Report by Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) and pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)
32.1*	Certification of Periodic Report by Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith)

+ Management contracts or compensatory plans or arrangements

\* Filed or furnished herewith

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**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant, Quanta Services, Inc., has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Quanta Services, Inc.

By: /s/ Derrick A. Jensen  
Derrick A. Jensen  
*Vice President, Controller and  
Chief Accounting Officer*

Dated: August 9, 2007

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