

Orion Group Holdings Inc
Form 10-Q
August 03, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

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

For the transition period from _____ to _____

Commission File Number:

1-33891

ORION GROUP HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE 26-0097459
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification Number)

12000 Aerospace Avenue, Suite 300 77034
Houston, Texas
(Address of principal executive offices) (Zip Code)

713-852-6500
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one)
Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

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

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

As of August 3, 2017, 28,203,490 shares of the Registrant's common stock, \$0.01 par value, were outstanding.

1

ORION GROUP HOLDINGS, INC.

Quarterly Report on Form 10-Q for the period ended June 30, 2017

INDEX

PART I FINANCIAL INFORMATION

| | | |
|--------|--|-----------|
| Item 1 | Financial Statements (Unaudited) | Page |
| | <u>Condensed Consolidated Balance Sheets at June 30, 2017 and December 31, 2016</u> | <u>3</u> |
| | <u>Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2017 and 2016</u> | <u>4</u> |
| | <u>Consolidated Statements of Comprehensive Loss for the Three and Six Months Ended June 30, 2017 and 2016</u> | <u>5</u> |
| | <u>Consolidated Statement of Stockholders' Equity for the Six Months Ended June 30, 2017</u> | <u>6</u> |
| | <u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2017 and 2016</u> | <u>7</u> |
| | <u>Notes to Condensed Consolidated Financial Statements</u> | <u>8</u> |
| Item 2 | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | <u>27</u> |
| Item 3 | <u>Quantitative and Qualitative Disclosures About Market Risk</u> | <u>36</u> |
| Item 4 | <u>Controls and Procedures</u> | <u>36</u> |

PART II

OTHER INFORMATION

| | | |
|---------|---|-----------|
| Item 1 | <u>Legal Proceedings</u> | <u>36</u> |
| Item 1A | <u>Risk Factors</u> | <u>36</u> |
| Item 2 | <u>Unregistered Sale of Equity Securities and Use of Proceeds</u> | <u>37</u> |
| Item 3 | <u>Defaults upon Senior Securities</u> | <u>37</u> |
| Item 4 | <u>Mine Safety Disclosures</u> | <u>37</u> |
| Item 5 | <u>Other Information</u> | <u>37</u> |
| Item 6 | <u>Exhibits</u> | <u>38</u> |

| | | |
|--|-------------------|-----------|
| | <u>SIGNATURES</u> | <u>39</u> |
|--|-------------------|-----------|

Part I - Financial Information

Item 1 Financial Statements

Orion Group Holdings, Inc. and Subsidiaries
 Condensed Consolidated Balance Sheets
 (In Thousands, Except Share and Per Share Information)

| | June 30, 2017 (Unaudited) | December 31, 2016 (Audited) |
|--|---------------------------------|-----------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 920 | \$ 305 |
| Accounts receivable: | | |
| Trade, net of allowance of \$0 and \$0, respectively | 87,619 | 92,202 |
| Retainage | 32,482 | 40,201 |
| Other current | 3,723 | 4,634 |
| Income taxes receivable | 2,335 | 133 |
| Inventory | 5,467 | 5,392 |
| Deferred tax asset | — | 2,013 |
| Costs and estimated earnings in excess of billings on uncompleted contracts | 41,829 | 39,968 |
| Assets held for sale | 1,375 | 6,375 |
| Prepaid expenses and other | 3,170 | 3,885 |
| Total current assets | 178,920 | 195,108 |
| Property and equipment, net | 151,501 | 158,082 |
| Accounts receivable, non-current | 1,304 | 733 |
| Inventory, non-current | 3,927 | 3,998 |
| Goodwill | 68,913 | 66,351 |
| Intangible assets, net of amortization | 20,298 | 22,032 |
| Other noncurrent | 1,609 | 1,372 |
| Total assets | \$ 426,472 | \$ 447,676 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Current debt, net of debt issuance costs | \$ 13,093 | \$ 19,188 |
| Accounts payable: | | |
| Trade | 47,593 | 49,123 |
| Retainage | 1,167 | 893 |
| Accrued liabilities | 17,471 | 19,946 |
| Taxes payable | — | 689 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | 28,951 | 27,681 |
| Total current liabilities | 108,275 | 117,520 |
| Long-term debt, net of debt issuance costs | 72,739 | 82,077 |
| Other long-term liabilities | 3,506 | 2,493 |
| Deferred income taxes | 16,637 | 19,000 |
| Interest rate swap liability | 272 | 382 |
| Total liabilities | 201,429 | 221,472 |
| Stockholders' equity: | | |
| Preferred stock -- \$0.01 par value, 10,000,000 authorized, none issued | — | — |
| Common stock -- \$0.01 par value, 50,000,000 authorized, 28,904,566 and 28,405,850 issued; 28,193,342 and 27,694,626 outstanding at June 30, 2017 and December 31, 2016, | 288 | 283 |

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

respectively

| | | | | |
|--|------------|---|------------|---|
| Treasury stock, 711,231 and 711,231 shares, at cost, as of June 30, 2017 and December 31, 2016, respectively | (6,540 |) | (6,540 |) |
| Accumulated other comprehensive loss | (272 |) | (382 |) |
| Additional paid-in capital | 173,221 | | 171,079 | |
| Retained earnings | 58,346 | | 61,764 | |
| Total stockholders' equity | 225,043 | | 226,204 | |
| Total liabilities and stockholders' equity | \$ 426,472 | | \$ 447,676 | |

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

3

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

Orion Group Holdings, Inc. and Subsidiaries
 Condensed Consolidated Statements of Operations
 (In Thousands, Except Share and Per Share Information)
 (Unaudited)

| | Three months ended June 30, | | Six months ended June 30, | |
|--|--------------------------------|------------|------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Contract revenues | \$137,420 | \$140,301 | \$276,177 | \$269,924 |
| Costs of contract revenues | 122,023 | 123,355 | 247,795 | 238,267 |
| Gross profit | 15,397 | 16,946 | 28,382 | 31,657 |
| Selling, general and administrative expenses | 17,528 | 16,899 | 32,507 | 32,437 |
| Loss (gain) on sale of assets, net | 335 | (234) | (177) | (606) |
| Operating (loss) income from operations | (2,466) | 281 | (3,948) | (174) |
| Other (expense) income | | | | |
| Other income | 11 | 9 | 21 | 22 |
| Interest income | — | — | — | 1 |
| Interest expense | (1,462) | (1,600) | (2,817) | (3,117) |
| Other expense, net | (1,451) | (1,591) | (2,796) | (3,094) |
| Loss before income taxes | (3,917) | (1,310) | (6,744) | (3,268) |
| Income tax benefit | (1,624) | (502) | (2,643) | (1,252) |
| Net loss | \$(2,293) | \$(808) | \$(4,101) | \$(2,016) |
| Basic loss per share | \$(0.08) | \$(0.03) | \$(0.15) | \$(0.07) |
| Diluted loss per share | \$(0.08) | \$(0.03) | \$(0.15) | \$(0.07) |
| Shares used to compute loss per share | | | | |
| Basic | 27,941,814 | 27,464,683 | 27,867,090 | 27,383,748 |
| Diluted | 27,941,814 | 27,464,683 | 27,867,090 | 27,383,748 |

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

Orion Group Holdings, Inc. and Subsidiaries
 Consolidated Statements of Comprehensive Loss
 (In Thousands)
 (Unaudited)

| | Three months ended June 30, | | Six months ended June 30, | |
|--|--------------------------------|-----------|------------------------------|-----------|
| | 2017 | 2016 | 2017 | 2016 |
| Net loss | \$(2,293) | \$(808) | \$(4,101) | \$(2,016) |
| Change in fair value of cash flow hedge, net of tax benefit of \$59 and \$99 for the three and six months ended June 30, 2017, respectively and net of tax benefit of \$195 and \$680 for the three and six months ended June 30, 2016, respectively | (86) | (315) | 110 | (1,097) |
| Total comprehensive loss | \$(2,379) | \$(1,123) | \$(3,991) | \$(3,113) |

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

Orion Group Holdings, Inc. and Subsidiaries
 Consolidated Statement of Stockholders' Equity
 (In Thousands, Except Share Information)
 (Unaudited)

| | Common Stock | | Treasury Stock | | Accumulated Other Comprehensive | Additional Paid-In | Retained | Earnings Total | |
|--------------------------------|--------------|--------|----------------|-----------|---------------------------------|--------------------|------------|----------------|--|
| | Shares | Amount | Shares | Amount | Income (Loss) | Capital | Earnings | Total | |
| Balance, December 31, 2016 | 28,405,850 | \$ 283 | (711,231) | \$(6,540) | \$ (382) | \$171,079 | \$61,764 | \$226,204 | |
| Stock-based compensation | — | \$ — | — | \$— | \$ — | \$1,207 | \$— | \$1,207 | |
| Deferred tax adjustment | — | \$ — | — | \$— | \$ — | \$— | \$683 | \$683 | |
| Exercise of stock options | 159,808 | \$ 2 | — | \$— | \$ — | \$938 | \$— | \$940 | |
| Issuance of restricted stock | 345,913 | \$ 3 | — | \$— | \$ — | \$(3) | \$— | \$— | |
| Cash flow hedge (net of tax) | — | \$ — | — | \$— | \$ 110 | \$— | \$— | \$110 | |
| Forfeiture of restricted stock | (7,005) | \$ — | — | \$— | \$ — | \$— | \$— | \$— | |
| Net income | — | \$ — | — | \$— | \$ — | \$— | \$(4,101) | \$(4,101) | |
| Balance, June 30, 2017 | 28,904,566 | \$ 288 | (711,231) | \$(6,540) | \$ (272) | \$173,221 | \$58,346 | \$225,043 | |

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

Orion Group Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(In Thousands)
(Unaudited)

| | Six months ended June 30, 2017 | 2016 |
|---|-----------------------------------|-------------|
| Cash flows from operating activities: | | |
| Net loss | \$ (4,101) | \$ (2,016) |
| Adjustments to reconcile net loss to net cash provided by Operating activities: | | |
| Depreciation and amortization | 15,119 | 17,203 |
| Deferred financing cost amortization | 631 | 620 |
| Deferred income taxes | (760) | (1,180) |
| Stock-based compensation | 1,207 | 1,302 |
| Gain on sale of property and equipment | (177) | (606) |
| Change in operating assets and liabilities: | | |
| Accounts receivable | 17,742 | 1,037 |
| Income tax receivable | (2,202) | — |
| Inventory | (5) | 779 |
| Prepaid expenses and other | 720 | 861 |
| Costs and estimated earnings in excess of billings on uncompleted contracts | (1,853) | 11,207 |
| Accounts payable | (3,774) | (11,857) |
| Accrued liabilities | (1,989) | (5,469) |
| Income tax payable | (689) | (306) |
| Billings in excess of costs and estimated earnings on uncompleted contracts | 252 | (1,444) |
| Net cash provided by operating activities | 20,121 | 10,131 |
| Cash flows from investing activities: | | |
| Proceeds from sale of property and equipment | 5,547 | 888 |

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

| | | | | |
|---|----------|---|----------|---|
| Contributions to CSV life insurance | (241) |) | (471) |) |
| TAS acquisition adjustment | — | | (369) |) |
| Acquisition of TBC | (6,000) |) | — | |
| Purchase of property and equipment | (3,689) |) | (12,513) |) |
| Net cash used in investing activities | (4,383) |) | (12,465) |) |
| Cash flows from financing activities: | | | | |
| Borrowings from Credit Facility | 37,000 | | 32,000 | |
| Payments made on borrowings from Credit Facility | (53,063) |) | (29,021) |) |
| Loan costs from Credit Facility | — | | (486) |) |
| Exercise of stock options | 940 | | 8 | |
| Net cash (used in) provided by financing activities | (15,123) |) | 2,501 | |
| Net change in cash and cash equivalents | 615 | | 167 | |
| Cash and cash equivalents at beginning of period | 305 | | 1,345 | |
| Cash and cash equivalents at end of period | \$ 920 | | \$ 1,512 | |
| Supplemental disclosures of cash flow information: | | | | |
| Cash paid during the period for: | | | | |
| Interest | \$ 2,193 | | \$ 2,588 | |
| Taxes (net of refunds) | \$ 1,067 | | \$ 235 | |

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

Orion Group Holdings, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements

(Tabular Amounts in thousands, Except for Share and per Share Amounts)

(Unaudited)

1. Description of Business and Basis of Presentation

Description of Business

Orion Group Holdings, Inc., its subsidiaries and affiliates (hereafter collectively referred to as the "Company"), provide a broad range of specialty construction and services in the infrastructure, industrial, and building sectors of the continental United States, Alaska, Canada and the Caribbean Basin. The Company's marine construction segment service the infrastructure sector through its services which include marine transportation facility construction, marine pipeline construction, marine environmental structures, dredging of waterways, channels and ports, environmental dredging, design, and specialty services. Its concrete construction segment services the building sector by providing turnkey concrete construction services including pour and finish, dirt work, layout, forming, rebar, and mesh across the light commercial structural and other associated business areas. The Company is headquartered in Houston, Texas with offices throughout its operating areas.

The tools used by the chief operating decision maker to allocate resources and assess performance are based on two reportable and operating segments: marine construction (formerly heavy civil marine construction), which operates under the Orion Marine Group brand and logo, and concrete construction (formerly commercial concrete construction), which operates under the TAS Commercial Concrete brand and logo.

Although we describe the business in this report in terms of the services the Company provides, the base of customers and the areas in which it operates, the Company has determined that its operations currently comprise two reportable segments pursuant to Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 280 - Segment Reporting.

In making this determination, the Company considered the similar economic characteristics of its operations. For the marine construction segment, the methods used, and the internal processes employed, to deliver marine construction services are similar throughout the segment, including standardized estimating, project controls and project management. This segment has the same customers with similar funding drivers, and it complies with regulatory environments driven through Federal agencies such as the U.S. Army Corps of Engineers, U.S. Fish and Wildlife Service, U.S. Environmental Protection Agency ("EPA") and the U.S. Occupational Safety and Health Administration ("OSHA"), among others. Additionally, the segment is driven by macro-economic considerations including the level of import/export seaborne transportation, development of energy related infrastructure, cruise line expansion and operations, marine bridge infrastructure development, waterway pipeline crossings and the maintenance of waterways. These considerations, and others, are key catalysts for future prospects and are similar across the segment.

For the concrete construction segment, the Company also considered the similar economic characteristics of these operations. The methods used, and the internal processes employed, to deliver concrete construction services are similar throughout the segment, including standardized estimating, project controls and project management. This segment complies with regulatory environments such as OSHA. Additionally, this segment is driven by macro-economic considerations, including movements in population, commercial real estate development, institutional funding and expansion, and recreational development, specifically in metropolitan areas of Texas. These considerations, and others, are key catalysts for future prospects and are similar across the segment.

Basis of Presentation

The accompanying condensed consolidated financial statements and financial information included herein have been prepared pursuant to the interim period reporting requirements of Form 10-Q. Consequently, certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") have been condensed or omitted. Readers of this report should also read our consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

the fiscal year ended December 31, 2016 (“2016 Form 10-K”) as well as Item 7 – Management’s Discussion and Analysis of Financial Condition and Results of Operations also included in our 2016 Form 10-K.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments considered necessary for a fair presentation of the Company’s financial position, results of operations, and cash flows for the periods presented. Such adjustments are of a normal recurring nature. Interim results of operations for the six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017.

2. Summary of Significant Accounting Principles

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management's estimates, judgments and assumptions are continually evaluated based on available information and experience; however, actual amounts could differ from those estimates. Please refer to Note 2 of the Notes to Consolidated Financial Statements included in our 2016 Form 10-K for a discussion of other significant estimates and assumptions affecting our condensed consolidated financial statements which are not discussed below.

On an ongoing basis, the Company evaluates the significant accounting policies used to prepare its condensed consolidated financial statements, including, but not limited to, those related to:

- Revenue recognition from construction contracts;
- Allowance for doubtful accounts;
- Assessing of goodwill and other long-lived assets for indicators of impairment;
- Income taxes;
- Self-insurance; and
- Stock-based compensation.

Revenue Recognition

For financial statement purposes, the Company records revenue on construction contracts using the percentage-of-completion method, measured by the percentage of actual contract costs incurred to date to total estimated costs for each contract. This method is used because management considers contract costs incurred to be the best available measure of progress on these contracts. Contract revenue is derived from the original contract price adjusted for agreed upon change orders. Contract costs include all direct costs, such as material and labor, and those indirect costs incurred that are related to contract performance such as payroll taxes and insurance. General and administrative costs are charged to expense as incurred. Incentive fees, if available, are billed to the customer based on the terms and conditions of the contract. Pending claims are recognized as an increase in contract revenue only when the collection is deemed probable and if the amount can be reasonably estimated for purposes of calculating total profit or loss on long-term contracts. The Company records revenue and the unbilled receivable for project claims to the extent of costs incurred and to the extent management believes related collection is probable and includes no profit on claims recorded. Through the second quarter of 2017, in accordance with ASC 605-35-25-30, the Company has recognized a claim of approximately \$0.5 million with a customer. Additionally, during 2016, the Company recognized claims of approximately \$12.3 million with customers. The Company believes collection of these claims are probable, although the full amount of the recorded claims may not be recognized. Changes in job performance, job conditions and estimated profitability, including those arising from final contract settlements, may result in revisions to costs and revenues and are recognized in the period in which the revisions are determined. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined, without regard to the percentage of completion. Revenue is recorded net of any sales taxes collected and paid on behalf of the customer, if applicable.

The current asset “costs and estimated earnings in excess of billings on uncompleted contracts” represents revenues recognized in excess of amounts billed, which management believes will be billed and collected within one year of the completion of the contract. The liability “billings in excess of costs and estimated earnings on uncompleted contracts” represents billings in excess of revenues recognized.

The Company's projects are typically short in duration, and usually span a period of less than one year. Historically, the Company has not had cause to combine or segment contracts.

Classification of Current Assets and Liabilities

The Company includes in current assets and liabilities amounts realizable and payable in the normal course of contract completion.

Cash and Cash Equivalents

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. At times, cash held by financial institutions may exceed federally insured limits. The Company has not historically sustained losses on its cash balances in excess of federally insured limits. Cash equivalents at June 30, 2017 and December 31, 2016 consisted primarily of overnight bank deposits.

Risk Concentrations

Financial instruments that potentially subject the Company to concentrations of credit risk principally consist of accounts receivable.

The Company depends on its ability to continue to obtain federal, state and local governmental contracts, and indirectly on the amount of funding available to these agencies for new and current governmental projects. Therefore, a portion of the Company's operations is dependent upon the level and timing of government funding. Statutory mechanics liens provide the Company high priority in the event of lien foreclosures following financial difficulties of private owners, thus minimizing credit risk with private customers.

Accounts Receivable

Accounts receivable are stated at the historical carrying value, less allowances for doubtful accounts. The Company has significant investments in billed and unbilled receivables. Billed receivables represent amounts billed upon the completion of small contracts and progress billings on large contracts in accordance with contract terms and milestone achievements. Unbilled receivables on contracts, which are included in costs in excess of billings, arise as revenues are recognized under the percentage-of-completion method. Unbilled amounts on contracts represent recoverable costs and accrued profits not yet billed. Revenue associated with these billings is recorded net of any sales tax, if applicable. Past due balances over 90 days and other higher risk amounts are reviewed individually for collectability. In establishing an allowance for doubtful accounts, the Company evaluates its contract receivables and costs in excess of billings and thoroughly reviews historical collection experience, the financial condition of its customers, billing disputes and other factors. The Company writes off uncollectible accounts receivable against the allowance for doubtful accounts if it is determined that the amounts will not be collected or if a settlement is reached for an amount that is less than the carrying value. As of June 30, 2017 and December 31, 2016, the Company had not recorded an allowance for doubtful accounts.

Balances billed to customers but not paid pursuant to retainage provisions in construction contracts generally become payable upon contract completion and acceptance by the owner. Retainage at June 30, 2017 totaled \$32.5 million, of which \$8.5 million is expected to be collected beyond June 30, 2018. Retainage at December 31, 2016 totaled \$40.2 million.

The Company negotiates change orders and claims with its customers. Unsuccessful negotiations of claims could result in a change to contract revenue that is less than amounts recorded, which could result in the recording of a loss. Successful claims negotiations could result in the recovery of previously recorded losses. Significant losses on receivables could adversely affect the Company's financial position, results of operations and overall liquidity.

Advertising Costs

The Company primarily obtains contracts through an open bid process, and therefore advertising costs are not a significant component of expense. Advertising costs are expensed as incurred.

Environmental Costs

Costs related to environmental remediation are charged to expense. Other environmental costs are also charged to expense unless they increase the value of the property and/or provide future economic benefits, in which event the costs are capitalized. Environmental liabilities, if any, are recognized when the expenditure is considered probable and the amount can be reasonably estimated.

Fair Value Measurements

The Company evaluates and presents certain amounts included in the accompanying condensed consolidated financial statements at “fair value” in accordance with U.S. GAAP, which requires the Company to base its estimates on assumptions that market participants, in an orderly transaction, would use to price an asset or liability, and to establish a hierarchy that prioritizes the information used to determine fair value. Refer to Note 8 for more information regarding fair value determination.

The Company generally applies fair value valuation techniques on a non-recurring basis associated with (1) valuing assets and liabilities acquired in connection with business combinations and other transactions; (2) valuing potential impairment loss related to long-lived assets; and (3) valuing potential impairment loss related to goodwill and indefinite-lived intangible assets.

Inventory

Current inventory consists of parts and small equipment held for use in the ordinary course of business and is valued at the lower of cost (using historical average cost) or net realizable value. Where shipping and handling costs are incurred by the Company, these charges are included in inventory and charged to cost of contract revenue upon use. Non-current inventory consists of spare parts (including engines, cutters and gears) that require special order or long-lead times for manufacture or fabrication, but must be kept on hand to reduce equipment downtime.

Property and Equipment

Property and equipment are recorded at cost. Ordinary maintenance and repairs that do not improve or extend the useful life of the asset are expensed as incurred. Major renewals and betterments of equipment are capitalized and depreciated generally over three to seven years until the next scheduled maintenance.

When property and equipment are retired or otherwise disposed of, the cost and accumulated depreciation are removed from the accounts and any resulting gain or loss is included in results of operations for the respective period. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets for financial statement purposes, as follows:

| | |
|-----------------------------|---------------|
| Automobiles and trucks | 3 to 5 years |
| Buildings and improvements | 5 to 30 years |
| Construction equipment | 3 to 15 years |
| Vessels and other equipment | 1 to 15 years |
| Office equipment | 1 to 5 years |

The Company generally uses accelerated depreciation methods for tax purposes where appropriate.

Dry-docking costs are capitalized and amortized on the straight-line method over a period ranging from three to 15 years. Dry-docking costs include, but are not limited to, the inspection, refurbishment and replacement of steel, engine components, tailshafts, mooring equipment and other parts of the vessel. Amortization related to dry-docking activities is included as a component of depreciation. These costs and the related amortization periods are periodically reviewed to determine if the estimates are accurate. If warranted, a significant upgrade of equipment may result in a revision to the useful life of the asset, in which case the change is accounted for prospectively.

Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are separately presented in the balance sheet and reported at the lower of the carrying amount or the fair value, less the costs to sell, and are no longer depreciated. Assets held for sale at June 30, 2017 and December 31, 2016 are expected to be disposed of within one year.

Goodwill and Other Intangible Assets

Goodwill

The Company has acquired businesses and assets in purchase transactions that resulted in the recognition of goodwill. Goodwill represents the costs in excess of fair values assigned to the identifiable assets acquired and liabilities assumed in the acquisition. In accordance with U.S. GAAP, acquired goodwill is not amortized, but is subject to impairment testing at least annually or more frequently if events or circumstances indicate that the asset more likely than not may be impaired. The Company determined that its operations comprise two reporting units for goodwill impairment testing, which match its two operating segments for financial reporting.

The Company assesses the fair value of its reporting units based on a weighted average of valuations based on market multiples, discounted cash flows, and consideration of its market capitalization. The key assumptions used in the discounted cash flow valuations are discount rates, weighted average cost of capital and perpetual growth rates applied to cash flow projections. Also, inherent in the discounted cash flow valuation models are past performance, projections and assumptions in current operating plans, and revenue growth rates over the next five years. These assumptions contemplate business, market and overall economic conditions. Other considerations are assumptions that market participants may use an analysis of comparable companies. The underlying assumptions used for determining fair value, as discussed above, require significant judgment and are susceptible to change from period to period and could potentially cause a material impact to the income statement. In the future, the Company's estimated fair value could be negatively impacted by extended declines in stock price, changes in macroeconomic indicators, sustained operating losses, and other factors which may affect of assessment of fair value.

See [Note 9](#) for additional discussion of our goodwill and related goodwill impairment testing.

Intangible Assets

Intangible assets that have finite lives are amortized. In addition, the Company evaluates the remaining useful life of intangible assets in each reporting period to determine whether events and circumstances warrant a revision of the remaining period of amortization. If the estimate of an intangible asset's remaining life is changed, the remaining carrying value of such asset is amortized prospectively over that revised remaining useful life. Intangible assets that have indefinite lives are not amortized, but are subject to impairment testing at least annually or more frequently if events or circumstances indicate that the asset more likely than not may be impaired.

The Company has one indefinite-lived intangible asset, a trade name, which is tested for impairment annually on October 31, or whenever events or circumstances indicate that the carrying amount of the trade name may not be recoverable. Impairment is calculated as the excess of the trade name's carrying value over its fair value. The fair value of the trade name is determined using the relief from royalty method, a variation of the income approach. This method assumes that if a company owns intellectual property, it does not have to "rent" the asset and is, therefore, "relieved" from paying a royalty. Once a supportable royalty rate is determined, the rate is then applied to the projected revenues over the expected remaining life of the intangible assets to estimate the royalty savings. This approach is dependent on a number of factors, including estimates of future growth and trends, royalty rates, discount rates and other variables.

See [Note 9](#) for additional discussion of our intangible assets and trade name impairment testing.

Stock-Based Compensation

The Company recognizes compensation expense for equity awards over the vesting period based on the fair value of these awards at the date of grant. The computed fair value of these awards is recognized as a non-cash cost over the period the employee provides services, which is typically the vesting period of the award. The fair value of options granted is estimated on the date of grant using the Black-Scholes option-pricing model. The Black-Scholes model requires the use of highly subjective assumptions in the computation. Changes in these assumptions can cause significant fluctuations in the fair value of the option award. The fair value of restricted stock grants is equivalent to the fair value of the stock issued on the date of grant, and is measured as the mean price of the stock on the date of grant.

Compensation expense is recognized only for share-based payments expected to vest. The Company estimates forfeitures at the date of grant based on historical experience and future expectations and this assessment is updated on a periodic basis. See [Note 14](#) for further discussion of the Company's stock-based compensation plan.

Income Taxes

The Company determines its consolidated income tax provision using the asset and liability method prescribed by U.S. GAAP, which requires the recognition of income tax expense for the amount of taxes payable or refundable for the current period and for deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity's financial statements or tax returns. The Company must make significant assumptions, judgments and estimates to determine its current provision for income taxes, its deferred tax assets and liabilities, and any valuation allowance to be recorded against any deferred tax asset. The current provision for income tax is based upon the current tax laws and the Company's interpretation of these laws, as well as the probable outcomes of any tax audits. The value of any net deferred tax asset depends upon estimates of the amount and category of future taxable income reduced by the amount of any tax benefits that the Company does not expect to realize. Actual operating results and the underlying amount and category of income in future years could render current assumptions, judgments and estimates of recoverable net deferred taxes inaccurate, thus impacting the Company's financial position and results

of operations. The Company computes deferred income taxes using the liability method. Under the liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Under the liability method, the effect on deferred tax assets and liabilities of a change in tax rates is recognized as income in the period that includes the enactment date.

The Company accounts for uncertain tax positions in accordance with the provisions of ASC 740-10 which prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken, or expected to be taken, on its consolidated tax return. The Company evaluates and records any uncertain tax positions based on the amount that management deems is more likely than not to be sustained upon examination and ultimate settlement with the tax authorities in the tax jurisdictions in which it operates.

Insurance Coverage

The Company maintains insurance coverage for its business and operations. Insurance related to property, equipment, automobile, general liability, and a portion of workers' compensation is provided through traditional policies, subject to a deductible or deductibles. A portion of the Company's workers' compensation exposure is covered through a mutual association, which is subject to supplemental calls.

The marine construction segment maintains five levels of excess loss insurance coverage, totaling \$200.0 million in excess of primary coverage. The marine construction segment's excess loss coverage responds to most of its policies when a primary limit of \$1.0 million has been exhausted; provided that the primary limit for Contingent Maritime Employer's Liability is \$10.0 million and the Watercraft Pollution Policy primary limit is \$5.0 million. The concrete construction segment maintains five levels of excess loss insurance coverage, totaling \$200.0 million in excess of primary coverage which excess loss coverage responds to most of its policies when a primary limit of \$1.0 million has been exhausted.

If a claim arises and a potential insurance recovery is probable the impending gain is recognized separately from the related loss. The recovery will only be recognized up to the amount of the loss once the recovery of the claim is deemed probable and any excess gain will fall under contingency accounting and will only be recognized once it is realized. The Company does not net insurance recoveries against the related claim liability as the amount of the claim liability is determined without consideration of the anticipated insurance recoveries from third parties.

Separately, the Company's marine construction segment employee health care is provided through a trust administered by a third party. Funding of the trust is based on current claims. The administrator has purchased appropriate stop-loss coverage. Losses on these policies up to the deductible amounts are accrued based upon known claims incurred and an estimate of claims incurred but not reported. The accruals are derived from known facts, historical trends and industry averages to determine the best estimate of the ultimate expected loss. Actual claims may vary from estimates. Any adjustments to such reserves are included in the consolidated results of operations in the period in which they become known. The Company's concrete construction segment employee health care is provided through two policies. A fully funded policy is offered primarily to salaried employees and their dependents while a partially self-funded plan with an appropriate stop-loss is offered primarily to hourly employees and their dependents. The self-funded plan is funded to the maximum exposure and, as a result, is expected to receive a partial refund after the policy expiration.

The accrued liability for insurance includes incurred but not reported claims of \$5.5 million and \$5.2 million at June 30, 2017 and December 31, 2016, respectively.

Recent Accounting Pronouncements

The FASB issues accounting standards and updates (each, an "ASU") from time to time to its Accounting Standards Codification, which is the primary source of U.S. GAAP. The Company regularly monitors ASUs as they are issued and considers applicability to its business. All ASUs are adopted by their respective due dates and in the manner prescribed by the FASB. The following are those recently issued ASUs most likely to affect the presentation of the Company's condensed consolidated financial statements:

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment. The FASB issued this update to simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. The amendments in this update modify the concept of impairment from the condition that exists when the carrying amount of goodwill exceeds its implied fair value to the condition that exists when the carrying amount of a reporting unit exceeds

its fair value. The guidance should be applied on a prospective basis and is effective for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted and the Company does not anticipate that the changes will materially impact the financial statements unless a goodwill impairment is recognized in the future.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The Board issued this update to increase the transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The Company anticipates the most significant of the amendments to our organization to be the recognition of assets and liabilities by lessees for those leases classified as operating leases under previous U.S. GAAP. Under the new standard the Company will be required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those annual periods. In early 2017, the Company established a steering committee to analyze the potential impact of the new standard and identify potential differences that will result from adopting the standard. The Company is currently assessing the effects of adoption on the Company's financial statements.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This comprehensive new revenue recognition standard will supersede existing revenue guidance under U. S. GAAP. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation.

The guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the cumulative catch-up transition method). The Company currently anticipates adopting the standard using the cumulative catch-up transition method which will involve recognizing in beginning retained earnings an adjustment for the cumulative effect of the change and providing additional disclosures comparing results to previous years.

The Company established a steering committee consisting of representatives from various business segments within the organization. The purpose of this committee is to analyze the impact of the new standard on the Company's business by reviewing the current revenue practices to identify potential differences that would result from applying the requirements of the new standard to revenue contracts. In addition, the Company is analyzing the possibility of any necessary changes to current business processes, systems and controls to support recognition and disclosure under the new standard.

The effective date of this guidance was deferred through the issuance of ASU 2015-14 and is effective for the Company beginning January 1, 2018. The impact of adopting the new standard is not expected to materially impact revenue, net income or the consolidated balance sheet. The Company expects the largest impact from the new standard to be on performance obligations within the contracts and the timing of revenue being recognized. The Company continues to evaluate all areas of the standard and its effect on the Company's financial statements.

During the periods presented in these financial statements, the Company implemented other new accounting pronouncements other than those noted above that are discussed in the notes where applicable.

3. Business Acquisition

On April 9, 2017, T.A.S. Commercial Concrete Construction, LLC, a wholly owned subsidiary of Orion Group Holdings, Inc. ("the Company") entered into a Stock Purchase Agreement ("the Agreement") for the purchase of all the issued and outstanding shares (the "shares") of Tony Bagliore Concrete, Inc., a Texas corporation ("TBC"). The Company and the two sole shareholders of TBC closed the purchase transactions on April 10, 2017 (the "Closing Date"). Upon the terms of and subject to the conditions set forth in the Agreement, the total aggregate consideration paid on the Closing Date by the Company to the Sellers for the shares was \$6 million in cash. In addition however, if certain target considerations are met in future periods, up to an additional cash payment of \$2 million will become payable to the Seller.

The allocation of the estimated acquisition consideration is preliminary because initial accounting for this business combination is incomplete. The preliminary allocation is based on estimates, assumptions, valuations, and other studies which have not progressed to a stage where there is sufficient information to make a definitive allocation. Accordingly, the acquisition consideration allocation unaudited purchase accounting adjustments will remain preliminary until the Company determines the final acquisition consideration allocation. The final amounts allocated to assets acquired and liabilities assumed could differ significantly from the amounts presented in the combined consolidated financial statements.

The purpose of the acquisition was primarily to achieve growth by expanding the Company's current service offerings in addition to expansion into new markets. The tangible assets acquired include accounts receivable, retainage and fixed assets.

Under the acquisition method of accounting, the total acquisition consideration is allocated to the acquired tangible and intangible assets and assumed liabilities of TBC based on their estimated fair values as of the closing of the acquisition. The table below outlines the total actual acquisition consideration allocated to the fair values of TBC's tangible and intangible assets and liabilities as of April 9, 2017:

| | |
|--|----------|
| Accounts receivable | \$3,239 |
| Retainage | 1,860 |
| Fixed assets, net | 2,098 |
| Other | 9 |
| Goodwill | 2,562 |
| Other intangible assets | 878 |
| Accounts payable | (2,017) |
| Accrued expenses and other current liabilities | (1,080) |
| Contingent consideration | (456) |
| Deferred tax liability | (1,093) |
| Total Acquisition Consideration at April 9, 2017 | \$6,000 |

The excess of the acquisition consideration over the fair value of assets acquired and liabilities assumed was allocated to goodwill. The goodwill of \$2.6 million arising from the acquisition consists primarily of synergies and business opportunities expected to be realized from the purchase of the Company. The goodwill is not deductible for income tax purposes.

Finite-lived intangible assets include customer relationships and contractual backlog. (See [Note 9](#)).

The fixed assets acquired include construction equipment and automobiles and trucks and will be depreciated in accordance with Company policy, generally 3 to 15 years.

As stated in the Agreement, the Company has agreed to pay the sellers an earn-out of up to \$2.0 million in cash, if earned, as additional purchase consideration. The seller's right to receive the contingent consideration, if any, shall be based on the Company's achievement of certain future financial targets. The Company measured the fair value of the contingent consideration at the Acquisition Date, and determined that fair value to be approximately \$0.5 million, as shown above. This amount of contingent liability is classified on the Condensed Consolidated Balance Sheets as other long-term liabilities.

Pro Forma Results (unaudited)

The results and operations of TBC have been included in the Consolidated Statements of Operations since the acquisition date of April 9, 2017. The Company has calculated the pro forma impact of the acquisition of TBC on its operating results for the six months ended June 30, 2017 and 2016, respectively.

The Company derived the pro forma results of the acquisition based upon historical financial information obtained from the seller and certain management assumptions. The pro forma adjustments related to incremental amortization expense associated with the acquired finite-lived intangible assets and interest expense on borrowings extinguished by the Company during the purchase, assuming a January 1, 2017 and 2016 effective transaction date. In addition, the tax impact of these adjustments was calculated at a 35% statutory rate.

These pro forma results are not necessarily indicative of the results that would have been obtained had the acquisition of TBC been completed on January 1 of the respective period, or that may be obtained in the future.

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

Unaudited Pro Forma Combined Condensed Consolidated Statements of Operations
 For the Six Month Period Ended June 30, 2017
 (in thousands except per share information)

| | Orion Group Holdings | TBC (through April 9) | Combined Historical | Pro Forma Adjustments | Combined Pro Forma |
|--|----------------------------|-----------------------------|------------------------|--------------------------|-----------------------|
| Contract revenues | \$276,177 | \$5,507 | \$281,684 | \$ — | \$281,684 |
| Costs of contract revenues | 247,795 | 5,325 | 253,120 | — | 253,120 |
| Gross profit | 28,382 | 182 | 28,564 | — | 28,564 |
| Selling, general and administrative expenses | 32,507 | 598 | 33,105 | 146 | 33,251 |
| (Gain) loss on sale of assets, net | (177) |)— | (177) |)— | (177) |
| Operating loss from operations | (3,948) |) (416 |) (4,364 |) (146 |) (4,510) |
| Other (expense) income | | | | | |
| Other income | 21 | 3 | 24 | — | 24 |
| Interest income | — | — | — | — | — |
| Interest expense | (2,817) |) (10 |) (2,827 |) 10 | (2,817) |
| Other expense, net | (2,796) |) (7 |) (2,803 |) 10 | (2,793) |
| Loss before income taxes | (6,744) |) (423 |) (7,167 |) (136 |) (7,303) |
| Income tax benefit | (2,643) |)— | (2,643) |) (196 |) (2,839) |
| Net loss | \$(4,101) |) \$(423 |) \$(4,524 |) \$ 60 | \$(4,464) |
| Basic loss per share | \$ (0.15) | | \$ (0.16) | | \$ (0.16) |
| Diluted loss per share | \$ (0.15) | | \$ (0.16) | | \$ (0.16) |
| Shares used to compute loss per share | | | | | |
| Basic | 27,867,090 | | 27,867,090 | | 27,867,090 |
| Diluted | 27,867,090 | | 27,867,090 | | 27,867,090 |

Unaudited Pro Forma Combined Condensed Consolidated Statements of Operations
 For the Six Month Period Ended June 30, 2016
 (in thousands except per share information)

| | Orion Group Holdings | TBC | Combined Historical | Pro Forma Adjustments | Combined Pro Forma |
|--|----------------------------|----------|------------------------|--------------------------|-----------------------|
| Contract revenues | \$269,924 | \$17,076 | \$287,000 | \$ — | \$287,000 |
| Costs of contract revenues | 238,267 | 15,754 | 254,021 | — | 254,021 |
| Gross profit | 31,657 | 1,322 | 32,979 | — | 32,979 |
| Selling, general and administrative expenses | 32,437 | 525 | 32,962 | 146 | 33,108 |
| (Gain) loss on sale of assets, net | (606) |)— | (606) |)— | (606) |
| Operating loss from operations | (174) |)797 | 623 | (146) |) 477 |
| Other (expense) income | | | | | |
| Other income | 22 | — | 22 | — | 22 |
| Interest income | 1 | — | 1 | — | 1 |
| Interest expense | (3,117) |)(18) |)(3,135) |)18 | (3,117) |
| Other expense, net | (3,094) |)(18) |)(3,112) |)18 | (3,094) |
| Loss before income taxes | (3,268) |)779 | (2,489) |)(128) |) (2,617) |
| Income tax benefit | (1,252) |)— | (1,252) |)228 | (1,024) |
| Net loss | \$(2,016) |)\$779 | \$(1,237) |)\$ (356) |) \$(1,593) |
| Basic loss per share | \$ (0.07) | | \$ (0.05) | | \$ (0.06) |
| Diluted loss per share | \$ (0.07) | | \$ (0.05) | | \$ (0.06) |
| Shares used to compute loss per share | | | | | |
| Basic | 27,383,748 | | 27,383,748 | | 27,383,748 |
| Diluted | 27,383,748 | | 27,383,748 | | 27,383,748 |

4. Concentration of Risk and Enterprise Wide Disclosures

Accounts receivable include amounts billed to governmental agencies and private customers and do not bear interest. Balances billed to customers but not paid pursuant to retainage provisions generally become payable upon contract completion and acceptance by the owner. The table below presents the concentrations of current receivables (trade and retainage) at June 30, 2017 and December 31, 2016, respectively:

| | June 30, 2017 | | December 31, 2016 | |
|--------------------|---------------|-------|-------------------|-------|
| Federal Government | \$5,996 | 5 % | \$5,542 | 4 % |
| State Governments | 4,314 | 4 % | 9,302 | 7 % |
| Local Governments | 20,183 | 17 % | 20,886 | 16 % |
| Private Companies | 89,608 | 74 % | 96,673 | 73 % |
| Total receivables | \$120,101 | 100 % | \$132,403 | 100 % |

At June 30, 2017 and December 31, 2016 no single customer accounted for more than 10% of total current receivables.

Additionally, the table below represents concentrations of contract revenue by type of customer for the three and six months ended June 30, 2017 and 2016, respectively:

| | Three months ended June 30, | | | | Six months ended June 30, | | | |
|-------------------------|-----------------------------|------|-----------|------|---------------------------|------|-----------|------|
| | 2017 | % | 2016 | % | 2017 | % | 2016 | % |
| Federal | \$18,360 | 13 % | \$7,776 | 6 % | \$38,092 | 14 % | \$11,932 | 4 % |
| State | 12,706 | 9 % | 10,462 | 7 % | 24,726 | 9 % | 15,829 | 6 % |
| Local | 20,731 | 15 % | 22,470 | 16 % | 44,556 | 16 % | 42,147 | 16 % |
| Private | 85,623 | 63 % | 99,593 | 71 % | 168,803 | 61 % | 200,016 | 74 % |
| Total contract revenues | \$137,420 | 100% | \$140,301 | 100% | \$276,177 | 100% | \$269,924 | 100% |

In the three and six months ended June 30, 2017 and 2016, no single customer generated more than 10% of total contract revenues.

The Company does not believe that the loss of any one of its customers would have a material adverse effect on the Company or its subsidiaries and affiliates since no single specific customer sustains such a large portion of receivables or contract revenue over time.

In addition, the concrete construction segment primarily purchases concrete from select suppliers. The loss of one of these suppliers could adversely impact short-term operations.

5. Contracts in Progress

Contracts in progress are as follows at June 30, 2017 and December 31, 2016:

| | June 30, 2017 | December 31, 2016 |
|---|------------------|----------------------|
| Costs incurred on uncompleted contracts | \$871,900 | \$ 802,140 |
| Estimated earnings | 140,465 | 143,975 |
| | 1,012,365 | 946,115 |
| Less: Billings to date | (999,487) | (933,828) |
| | \$12,878 | \$ 12,287 |
| Included in the accompanying condensed consolidated balance sheet under the following captions: | | |
| Costs and estimated earnings in excess of billings on uncompleted contracts | \$41,829 | \$ 39,968 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | (28,951) | (27,681) |
| | \$12,878 | \$ 12,287 |

Costs and estimated earnings in excess of billings on completed contracts totaled \$0.4 million at June 30, 2017 and \$0.6 million at December 31, 2016.

6. Property and Equipment

The following is a summary of property and equipment at June 30, 2017 and December 31, 2016:

| | June 30, 2017 | December 31, 2016 |
|--------------------------------------|------------------|----------------------|
| Automobiles and trucks | \$2,219 | \$ 2,525 |
| Building and improvements | 37,277 | 37,269 |
| Construction equipment | 164,373 | 165,023 |
| Vessels and other equipment | 89,313 | 88,659 |
| Office equipment | 7,472 | 7,125 |
| | 300,654 | 300,601 |
| Less: accumulated depreciation | (188,996) | (181,293) |
| Net book value of depreciable assets | 111,658 | 119,308 |
| Construction in progress | 1,612 | 543 |
| Land | 38,231 | 38,231 |
| | \$151,501 | \$ 158,082 |

For the three months ended June 30, 2017 and 2016, depreciation expense was \$6.2 million and \$6.8 million, respectively. For the six months ended June 30, 2017 and 2016, depreciation expense was \$12.5 million and \$13.6 million, respectively. Substantially all depreciation expense is included in the cost of contract revenue in the Company's Condensed Consolidated Statements of Operations. Substantially all of the assets of the Company are pledged as collateral under the Company's Credit Agreement (as defined in [Note 11](#)).

Substantially all of the Company's long-lived assets are located in the United States.

The Company reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. Assets to be disposed of are separately presented in the balance sheet and reported at the lower of the carrying amount or the fair value, less the costs to sell, and are no longer depreciated. During the six months ended June 30, 2017, approximately \$5.0 million of these assets were sold for cash of \$4.5 million. The difference of \$0.5 million is classified as a loss on sale of assets on the Consolidated Statement of Operations. Approximately \$1.4 million remain as held for sale on the Company's Consolidated Balance Sheet at June 30, 2017. The Company expects to dispose of the remaining assets within one year of the balance sheet date.

7. Inventory

Current inventory at June 30, 2017 and December 31, 2016, of \$5.5 million and \$5.4 million, respectively, consisted primarily of spare parts and small equipment held for use in the ordinary course of business.

Non-current inventory at June 30, 2017 and December 31, 2016 of \$3.9 million and \$4.0 million respectively, consisted primarily of spare engine components or items which require longer lead times for sourcing or fabrication for certain of the Company's assets to reduce equipment downtime.

8. Fair Value

The fair value of financial instruments is the amount at which the instrument could be exchanged in a current transaction between willing parties. Due to their short term nature, the Company believes that the carrying value of its accounts receivable, other current assets, accounts payable and other current liabilities approximate their fair values.

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

The Company classifies financial assets and liabilities into the following three levels based on the inputs used to measure fair value in the order of priority indicated:

Level 1- fair values are based on observable inputs such as quoted prices in active markets for identical assets or liabilities;

Level 2 - fair values are based on pricing inputs other than quoted prices in active markets for identical assets and liabilities and are either directly or indirectly observable as of the measurement date; and

Level 3- fair values are based on unobservable inputs in which little or no market data exists.

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input to the fair value requires judgment and may affect the placement of assets and liabilities within the fair value hierarchy levels.

The following table sets forth by level within the fair value hierarchy the Company's recurring financial assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2017 and December 31, 2016:

| | Carrying Value | Fair Value Measurements | |
|---|----------------|-------------------------|--------------------|
| | | Level 1 | Level 2 Level 3 |
| June 30, 2017 | | | |
| Assets: | | | |
| Cash surrender value of life insurance policy | \$ 1,430 | -1,430 | — |
| Liabilities: | | | |
| Derivatives | \$ 436 | -436 | — |
| December 31, 2016 | | | |
| Assets: | | | |
| Cash surrender value of life insurance policy | \$ 1,188 | -1,188 | — |
| Liabilities: | | | |
| Derivatives | \$ 447 | -447 | — |

The Company's derivatives, which are comprised of interest rate swaps, are valued using a discounted cash flow analysis that incorporates observable market parameters, such as interest rate yield curves and credit risk adjustments that are necessary to reflect the probability of default by us or the counterparty. These derivatives are classified as a Level 2 measurement within the fair value hierarchy. See [Note 11](#) for additional information on the Company's derivative instrument.

The Company's concrete segment has life insurance policies covering 4 employees with a combined face value of \$11.1 million. The policies are invested in mutual funds and the fair value measurement of the cash surrender balance associated with these policies is determined using Level 2 inputs within the fair value hierarchy and will vary with investment performance. These assets are included in the "Other noncurrent" asset section in the consolidated balance sheets.

Other Fair Value Measurements

The fair value of the Company's debt at June 30, 2017 and December 31, 2016 approximated its carrying value of \$88.5 million and \$104.6 million, respectively, as interest is based on current market interest rates for debt with similar risk and maturity. If the Company's debt was measured at fair value, it would have been classified as a Level 2 measurement in the fair value hierarchy.

9. Goodwill and Intangible Assets

Goodwill

The table below summarizes changes in goodwill recorded by the Company during the periods ended June 30, 2017 and December 31, 2016, respectively:

| | June 30, 2017 | December 31, 2016 |
|--|---------------|-------------------|
| | | |

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

| | | |
|------------------------------|----------|-----------|
| Beginning balance, January 1 | \$66,351 | \$ 65,982 |
| Additions | 2,562 | 369 |
| Ending balance | \$68,913 | \$ 66,351 |

At June 30, 2017, goodwill totaled \$68.9 million, of which \$33.8 million relates to the marine construction segment and \$35.1 million relates to the concrete construction segment.

As discussed previously in Note 2, goodwill is reviewed at a reporting unit level for impairment annually as of October 31 or when circumstances arise that indicate a possible impairment might exist. Test of impairment requires a two-step process to be performed to analyze whether or not goodwill has been impaired. The first step of this test, used to identify potential impairment,

compares the estimated fair value of a reporting unit with its carrying amount. The second step, if necessary, quantifies the impairment.

During the three months ended June 30, 2017 the Company identified potential indicators of impairment, specifically to goodwill in its marine construction reporting unit. These indicators included having losses for three consecutive quarters within the segment, adjusted forecasted earnings for future quarters, and other negative trends within the reporting unit. As such, the Company performed an interim goodwill impairment analysis as of June 30, 2017. The result of the first step in the two-step process indicated that no impairment existed and, as such, the Company did not progress to the second step.

Intangible assets

The tables below present the activity and amortization of finite-lived intangible assets:

| | Six months ended | |
|--|------------------|------------|
| | June 30, | |
| | 2017 | 2016 |
| Intangible assets, January 1 | \$34,362 | \$34,362 |
| Additions | 878 | — |
| Total intangible assets, end of period | 35,240 | 34,362 |
| Accumulated amortization, January 1 | \$(19,220) | \$(11,933) |
| Current year amortization | (2,613) | (1,822) |
| Total accumulated amortization | (21,833) | (13,755) |
| Net intangible assets, end of period | \$13,407 | \$20,607 |

Finite-lived intangible assets were acquired as part of the purchase of T.A.S. Commercial Concrete Construction ("TAS") which included contractual backlog and customer relationships. Contractual backlog was valued at approximately \$8.7 million and is currently being amortized over two years. Customer relationships were valued at approximately \$18.1 million and is currently being amortized over eight years. In addition, during the second quarter of 2017, the Company acquired finite-lived intangible assets as part of the purchase of TBC, which also included contractual backlog and customer relationships. Contractual backlog was valued at approximately \$0.1 million and will be amortized over seven months. Customer relationships were valued at approximately \$0.7 million and will be amortized over seven years. Both of these assets will be amortized using an accelerated method based on the pattern in which the economic benefits of the assets are consumed. For the six months ended June 30, 2017, \$2.6 million of amortization expense was recognized for these assets. Future expense remaining of approximately \$13.4 million will be amortized as follows:

| | |
|------------|----------|
| 2017 | \$2,124 |
| 2018 | 3,389 |
| 2019 | 2,640 |
| 2020 | 2,069 |
| 2021 | 1,521 |
| Thereafter | 1,664 |
| | \$13,407 |

Additionally, the Company has one indefinite-lived intangible asset, as described in Note 2. At June 30, 2017 the trade name was valued at approximately \$6.9 million and no indicators of impairment existed.

10. Accrued Liabilities

Accrued liabilities at June 30, 2017 and December 31, 2016 consisted of the following:

| | June 30, December | |
|--------------------------------------|-------------------|-----------|
| | 2017 | 31, 2016 |
| Accrued salaries, wages and benefits | \$9,409 | \$ 10,818 |
| Accrual for insurance liabilities | 5,538 | 5,223 |
| Property taxes | 929 | 1,615 |
| Sales taxes | 1,237 | 1,722 |
| Interest | — | 19 |
| Other accrued expenses | 358 | 549 |
| Total accrued liabilities | \$17,471 | \$ 19,946 |

11. Long-term Debt, Line of Credit and Derivatives

The Company entered into a syndicated credit agreement (the "Credit Agreement") on August 5, 2015 with Regions Bank, as administrative agent and collateral agent, and the following co-syndication agents: Bank of America, N.A., BOKF, NA dba Bank of Texas, Branch Banking & Trust Company, Frost Bank, Bank Midwest, a division of NBH Bank, N.A., IBERIABANK, KeyBank NA, Trustmark National Bank, and First Tennessee Bank NA. The primary purpose of the Credit Agreement was to finance the acquisition of TAS, to provide a revolving line of credit, and to provide financing to extinguish all prior indebtedness with Wells Fargo Bank, National Associates, as administrative agent, and Wells Fargo Securities, LLC.

The Credit Agreement, which may be amended from time to time, provides for borrowings under a revolving line of credit and swingline loans with a commitment amount of \$50.0 million and a term loan with a commitment amount of \$135.0 million (together, the "Credit Facility"). The Credit Facility is guaranteed by the subsidiaries of the Company, secured by the assets of the Company, including stock held in its subsidiaries, and may be used to finance general corporate and working capital purposes, to finance capital expenditures, to refinance existing indebtedness, to finance permitted acquisitions and associated fees, and to pay for all related expenses to the Credit Facility. Interest is due and is computed based on the designation of the loan, with the option of a Base Rate Loan (the base rate plus the Applicable Margin), or an Adjusted LIBOR Rate Loan (the adjusted LIBOR rate plus the Applicable Margin). Interest is due on the last day of each quarter end for Base Rate Loans and at the end of the LIBOR rate period for Adjusted LIBOR Rate Loans. The rate for all loans at the time of loan origination was 4.75%. Principal balances drawn under the Credit Facility may be prepaid at any time, in whole or in part, without premium or penalty. Amounts repaid under the revolving line of credit may be re-borrowed. The Credit Facility matures on August 5, 2020.

The quarterly weighted average interest rate for the Credit Facility as of June 30, 2017 was 3.57%.

The Company's obligations under debt arrangements consisted of the following:

| | June 30, 2017 | | | December 31, 2016 | | |
|--------------------------|----------------------|----------|--------|----------------------|----------|---------|
| | Debt | | | Debt | | |
| | Principal | Issuance | Total | Principal | Issuance | Total |
| | Costs ⁽¹⁾ | | | Costs ⁽¹⁾ | | |
| Revolving line of credit | \$— | \$— | \$— | \$8,000 | \$(252) | \$7,748 |
| Term loan - current | 13,500 | (407) | 13,093 | 11,813 | (373) | 11,440 |
| Total current debt | 13,500 | (407) | 13,093 | 19,813 | (625) | 19,188 |
| Term loan - long-term | 75,000 | (2,261) | 72,739 | 84,750 | (2,673) | 82,077 |

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

Total debt \$88,500 \$(2,668) \$85,832 \$104,563 \$(3,298) \$101,265

(1) Total debt issuance costs, include underwriter fees, legal fees and syndication fees and fees related to the execution of the First Amendment to the Credit Agreement.

22

Provisions of the revolving line of credit and accordion

The Company has a maximum borrowing availability under the revolving line of credit and swingline loans (as defined in the Credit Agreement) of \$50.0 million. The letter of credit sublimit is equal to the lesser of \$20.0 million and the aggregate unused amount of the revolving commitments then in effect. The swingline sublimit is equal to the lesser of \$5.0 million and the aggregate unused amount of the revolving commitments then in effect.

Revolving loans may be designated as Base Rate Loan or Adjusted LIBOR Rate Loans, at the Company's request, and must be made in an aggregate minimum amount of \$1.0 million and integral multiples of \$250,000 in excess of that amount. Swingline loans must be made in an aggregate minimum amount of \$250,000 and integral multiples of \$50,000 in excess of that amount. The Company may convert, change, or modify such designations from time to time.

The Company is subject to a Commitment Fee for the unused portion of the maximum available to borrow under the revolving line of credit. The Commitment Fee, which is due quarterly in arrears, is equal to the Applicable Margin of the actual daily amount by which the Aggregate Revolving Commitments exceeds the Total Revolving Outstanding. The revolving line of credit termination date is the earlier of the Credit Facility termination date, August 5, 2020, or the date the outstanding balance is permanently reduced to zero. The Company has the intent and ability to repay the amounts outstanding on the revolving line of credit within one year, therefore, the outstanding balance as of June 30, 2017 has been classified as current.

As of June 30, 2017, there was no outstanding balance on the revolving line of credit. There was \$0.9 million in outstanding letters of credit as of June 30, 2017, which reduced the maximum borrowing availability on the revolving line of credit to \$49.1 million as of June 30, 2017. The Company made payments of \$28.5 million on the outstanding revolving balance during the second quarter of 2017. Subsequent to the second quarter, the Company drew \$15.0 million on the revolving line of credit.

Provisions of the term loan

The original principal amount of \$135.0 million for the term loan commitment is paid off in quarterly installment payments (as stated in the Credit Agreement). At June 30, 2017, the outstanding term loan component of the Credit Facility totaled \$88.5 million and was secured by specific assets of the Company. The table below outlines the total remaining payment amounts annually for the term loan through maturity of the Credit Facility:

| | |
|------|----------|
| 2017 | \$6,750 |
| 2018 | 13,500 |
| 2019 | 15,188 |
| 2020 | 53,062 |
| | \$88,500 |

During the three months ended June 30, 2017, the Company made the scheduled quarterly principal payment of \$2.5 million, and an additional principal paydown of \$3.0 million, which reduced the outstanding principal balance to \$88.5 million at June 30, 2017. The current portion of debt is \$13.5 million and the non-current portion is \$75.0 million. As of June 30, 2017, the term loan was designated as an Adjusted LIBOR Rate Loan with an interest rate of 3.56%.

Financial covenants

Restrictive financial covenants under the Credit Facility include:

▲ consolidated Fixed Charge Coverage Ratio as of the end of any fiscal quarter to not be less than 1.25 to 1.00.

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

▲ consolidated Leverage Ratio to not exceed the following during each noted period:

- Closing Date through and including December 31, 2015, to not exceed 3.25 to 1.00;
- Fiscal Quarter Ending March 31, 2016, to not exceed 4.00 to 1.00;
- Fiscal Quarter Ending June 30, 2016, to not exceed 3.75 to 1.00;
- Fiscal Quarter Ending September 30, 2016, to not exceed 3.25 to 1.00;
- Fiscal Quarter Ending December 31, 2016, to not exceed 3.00 to 1.00;
- Fiscal Quarter Ending March 31, 2017, to not exceed 2.75 to 1.00;
- Fiscal Quarter Ending June 30, 2017, to not exceed 2.75 to 1.00;
- Fiscal Quarter Ending September 30, 2017, to not exceed 2.75 to 1.00;
- Fiscal Quarter Ending December 31, 2017 and each Fiscal Quarter thereafter, to not exceed 2.50 to 1.00.

In addition, the Credit Facility contains events of default that are usual and customary for similar arrangements, including non-payment of principal, interest or fees; breaches of representations and warranties that are not timely cured; violation of covenants; bankruptcy and insolvency events; and events constituting a change of control.

During the second quarter of 2017, the Company initiated discussions with the lead bank in an effort to explore available options given the step down of the Leverage Ratio covenant and concerns the Company would not be in compliance with financial covenants. A second amendment to the Credit Agreement was executed during July 2017, which was effective as of June 30, 2017. The Leverage Ratio was adjusted beginning with the quarter ended June 30, 2017 through September 30, 2017, as reflected above. The Fixed Charge Coverage Ratio was unchanged. This amendment to the Credit Agreement will increase the cost of the Company's borrowings if the Leverage Ratio exceeds 2.75 to 1.00 and will impose additional limitations on certain types of activities, such as acquisitions. With the execution of the aforementioned amendment, the Company was in compliance with all financial covenants as of June 30, 2017.

Derivative Financial Instruments

On September 16, 2015, the Company entered into a series of receive-variable, pay-fixed interest rate swaps to hedge the variability in the interest payments on 50% of the aggregate principal amount of the Regions Term Loan outstanding, beginning with a notional amount of \$67.5 million. There are a total of five sequential interest rate swaps to achieve the hedged position and each year on August 31, with the exception of the final swap, the existing interest rate swap is scheduled to expire and will be immediately replaced with a new interest rate swap until the expiration of the final swap on July 31, 2020. At inception, these interest rate swaps were designated as a cash flow hedge for hedge accounting, and as such, the effective portion of unrealized changes in market value are recorded in accumulated other comprehensive income (loss) and reclassified into earnings during the period in which the hedged forecasted transaction affects earnings. Gains and losses from hedge ineffectiveness are recognized in current earnings. The change in fair market value of the swaps as of June 30, 2017 is \$0.3 million, which is reflected in the balance sheet as a liability. The fair market value of the swaps as of June 30, 2017 is \$0.4 million. See [Note 8](#) for more information regarding the fair value of the Company's derivative instruments.

12. Income Taxes

The Company's effective tax rate is based on expected income, statutory rates and tax planning opportunities available to it. For interim financial reporting, the Company estimates its annual tax rate based on projected taxable income (or loss) for the full year and records a quarterly tax provision in accordance with the anticipated annual rate. The effective rate for the six months ended June 30, 2017 and 2016 was 39.2% and 38.3%, respectively. For both 2016 and 2017 the effective tax rate differed from the Company's statutory rate of 35.0% primarily due to state income taxes, the non-deductibility of certain permanent items, such as incentive stock compensation expense, a movement in the valuation allowance related to state attributes, as discussed below, and a benefit related to the domestic production gross receipts deduction.

The Company assessed the realizability of its deferred tax assets at June 30, 2017, and considered whether it was more likely than not that some portion or all of the deferred tax assets will not be realized. The realization of deferred tax assets depends upon the generation of future taxable income, which includes the reversal of deferred tax liabilities related to depreciation, during the periods in which these temporary differences become deductible.

The Company has a tax effected net operating loss carryforward ("NOL") of approximately \$4.2 million for state income tax reporting purposes due to the losses sustained in various states. The Company believes it will be able to partially utilize these NOLs against future income primarily with reversing of temporary differences attributable to

depreciation and due to expiration dates well into the future. However, the Company determined that a portion of the NOLs related to certain jurisdictions will more likely than not be able to be fully utilized. Therefore, the Company has an existing valuation allowance of \$3.4 million for this portion of the NOLs. For federal tax reporting purposes, the Company has utilized its ability to carry losses back prior to 2016. Approximately \$11.2 million remains as a federal tax carryforward. The Company expects it will be able to fully utilize these NOLs before the end of 2017.

The Company has adopted ASU 2016-09, Improvements to Employee Share-Based Payment Accounting. As part of this adoption, certain federal NOLs that were previously classified off balance sheet must now be recognized as deferred tax assets through an adjustment to opening retained earnings. The Company chose to prospectively adopt this guidance during the first quarter of 2017 and as such the balance sheet includes an adjustment of approximately \$0.7 million as an addition to the "Retained earnings" and a reduction to the "Deferred income taxes" lines on the Condensed Consolidated Balance Sheet to true up the tax effected portion of the NOLs mentioned above. Due to the prospective adoption, no prior year adjustments were made.

The Company does not believe that its tax positions will significantly change due to any settlement and/or expiration of statutes of limitations prior to December 31, 2017.

13. Earnings (Loss) Per Share

Basic earnings (loss) per share are based on the weighted average number of common shares outstanding during each period. Diluted earnings per share are based on the weighted average number of common shares outstanding and the effect of all dilutive common stock equivalents during each period. The exercise price for certain stock options awarded by the Company exceeds the average market price of the Company's common stock. Such stock options are antidilutive and are not included in the computation of earnings (loss) per share. In the three months ended June 30, 2017 and June 30, 2016, no potential common stock equivalents were included as the effect of such would be anti-dilutive. For the three month periods ended June 30, 2017 and June 30, 2016, the Company had 2,251,034 and 2,358,684 securities, respectively, that were potentially dilutive in future earnings per share calculations. For the six months ended June 30, 2017 and June 30, 2016, the Company had 2,243,763 and 2,239,139 securities, respectively, that were potentially dilutive in future earnings calculations. Such dilution will be dependent on the excess of the market price of our stock over the exercise price and other components of the treasury stock method.

The following table reconciles the denominators used in the computations of both basic and diluted earnings (loss) per share:

| | Three months ended | | Six months ended | |
|--|--------------------|------------|------------------|------------|
| | June 30, | | June 30, | |
| | 2017 | 2016 | 2017 | 2016 |
| Basic: | | | | |
| Weighted average shares outstanding | 27,941,814 | 27,464,683 | 27,867,090 | 27,383,748 |
| Diluted: | | | | |
| Total basic weighted average shares outstanding | 27,941,814 | 27,464,683 | 27,867,090 | 27,383,748 |
| Effect of dilutive securities: | | | | |
| Common stock options | — | — | — | — |
| Total weighted average shares outstanding assuming dilution | 27,941,814 | 27,464,683 | 27,867,090 | 27,383,748 |
| Anti-dilutive stock options | — | 2,317,572 | — | 2,237,217 |
| Shares of common stock issued from the exercise of stock options | 55,953 | — | 159,808 | 3,924 |

14. Stock-Based Compensation

The Compensation Committee of the Company's Board of Directors is responsible for the administration of the Company's stock incentive plans, which include the 2017 Long Term Incentive Plan, or the "2017 LTIP", which was approved by shareholders in May 2017 and authorized the maximum aggregate number of shares of common stock to be issued at 2,400,000. In general, the Company's 2017 LTIP provides for grants of restricted stock and stock options to be issued with a per-share price equal to the fair market value of a share of common stock on the date of grant. Option terms are specified at each grant date, but are generally 10 years from the date of issuance. Options generally vest over a three to five year period.

The Company applies a 3.2% and a 5.5% forfeiture rate, which gets compounded over the vesting terms of the individual award, to its restricted stock and option grants, respectively, based on historical analysis.

In the three months ended June 30, 2017 and 2016, compensation expense related to stock based awards outstanding was \$858,000 and \$869,000, respectively. In the six months ended June 30, 2017 and 2016, compensation expense

related to stock based awards
outstanding was \$1.2 million and \$1.3 million, respectively.

In May 2017, the Company granted certain executives options to purchase 425,204 shares of common stock and used the Black Scholes option pricing model to estimate the fair value of these options using the following assumptions:

| | |
|-------------------------------------|--------|
| Grant-date fair value | \$2.44 |
| Risk-free interest rate | 1.46 % |
| Expected volatility | 48.2 % |
| Expected term of options (in years) | 3.0 |
| Dividend yield | — % |

The risk-free interest rate is based on interest rates on U.S. Treasury zero-coupon issues that match the contractual terms of the stock option grants. The expected term represents the period in which the Company's equity awards are expected to be outstanding.

Also, in May 2017, certain officers and executives of the Company were awarded 345,913 shares of restricted common stock. The fair value on the date of the grant was \$7.22 per share.

In May 2017, the Company awarded certain executives 69,945 shares of performance based stock options, with 100% of shares to be earned based on the achievement of an objective return on invested capital measured over a two-year performance period. The fair value on the date of the grant of \$7.22 per share.

In the three months ended June 30, 2017, 55,953 options were exercised, generating proceeds to the Company of \$316,000. In the three months ended June 30, 2016, no options were exercised, generating no proceeds to the Company. In the six months ended June 30, 2017, 159,808 options were exercised, generating proceeds to the Company of approximately \$940,000. In the six months ended June 30, 2016, 3,924 options were exercised, generating proceeds to the Company of approximately \$8,000.

At June 30, 2017, total unrecognized compensation expense related to unvested stock and options was approximately \$4.9 million, which is expected to be recognized over a period of approximately two years.

15. Commitments and Contingencies

From time to time the Company is 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, property damage, punitive damages, civil penalties or other losses, or injunctive or declaratory relief. With respect to such lawsuits, the Company accrues reserves when it is probable a liability has been incurred and the amount of loss can be reasonably estimated. The Company does not believe any other proceedings, individually or in the aggregate, would be expected to have a material adverse effect on results of operations, cash flows or financial condition.

16. Segment Information

The Company currently operates in two reportable segments: marine construction and concrete construction. The Company's financial reporting systems present various data for management to run the business, including profit and loss statements prepared according to the segments presented. Management uses operating income to evaluate performance between the two segments. Segment information for the periods presented is provided as follows:

| | Three months ended June 30, 2017 | Three months ended June 30, 2016 | Six months ended June 30, 2017 | Six months ended June 30, 2016 |
|---------------------------------------|--|--|--|--|
| Marine Construction | | | | |
| Contract revenues | \$62,003 | \$79,966 | \$129,183 | \$142,381 |
| Operating loss | (8,617) | (1,212) | (16,323) | (4,354) |
| Depreciation and amortization expense | (5,087) | (5,176) | (10,342) | (10,243) |
| | | | | |
| Total Assets | \$252,348 | \$297,207 | \$252,348 | \$297,207 |
| Property, Plant and Equipment, net | 135,492 | 149,912 | 135,492 | \$149,912 |
| | | | | |
| Concrete Construction | | | | |
| Contract revenues | \$75,417 | \$60,335 | \$146,994 | \$127,543 |
| Operating income | 6,150 | 1,493 | 12,375 | 4,180 |
| Depreciation and amortization expense | (2,505) | (3,477) | (4,777) | (6,960) |
| | | | | |
| Total Assets | \$174,124 | \$146,127 | \$174,124 | \$146,127 |
| Property, Plant and Equipment, net | 16,009 | 14,472 | 16,009 | 14,472 |

There were no intersegment revenues between the Company's two reportable segments for the three and six months ended June 30, 2017 and 2016. The marine construction segment had foreign revenues of approximately \$0.8 million and \$3.7 million for the three months ended June 30, 2017 and 2016, respectively, and \$0.9 million and \$6.1 million for the six months ended June 30, 2017 and 2016, respectively. These revenues are derived from projects in Mexico and the Caribbean and are paid in U.S. dollars. There was no foreign revenue for the concrete construction segment.

17. Related Party Transactions

Upon the completion of the acquisition of TAS, the Company entered into a lease arrangement with an entity in which an employee owns an interest. This lease is for office space and yard facilities used by the concrete construction segment. Annual lease expense will be approximately \$820,000, of which approximately \$205,000 and \$410,000 represented lease expense during the three and six months ended June 30, 2017, respectively.

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

CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS

Unless the context otherwise indicates, all references in this quarterly report to "Orion," "the Company," "we," "our," or "us" refer to Orion Group Holdings, Inc. and its subsidiaries taken as a whole.

Certain information in this Quarterly Report on Form 10-Q, including but not limited to Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), may constitute forward-looking statements as such term is defined within the meaning of the "safe harbor" provisions of Section 27A of the Securities Exchange Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended.

All statements other than statements of historical facts, including those that express a belief, expectation, or intention are forward-looking statements. The forward-looking statements may include projections and estimates concerning the timing and success of specific projects and our future production, revenues, income and capital spending. Our forward-looking statements are generally accompanied by words such as "estimate," "project," "predict," "believe," "expect," "anticipate," "potential," "plan," "goal" or other words that convey the uncertainty of future events or outcomes.

We have based these forward-looking statements on our current expectations and assumptions about future events. While our management considers these expectations and assumptions to be reasonable, they are inherently subject to significant business, economic, competitive, regulatory and other risks, contingencies and uncertainties, most of which are difficult to predict and many of which are beyond our control, including unforeseen productivity delays and other difficulties encountered in project execution, levels of government funding or other governmental budgetary constraints, and contract cancellation at the discretion of the customer. These and other important factors, including those described under "Risk Factors" in Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2016 ("2016 Form 10-K") may cause our actual results, performance or achievements to differ materially from any future results, performance or achievements expressed or implied by these forward-looking statements. The forward-looking statements in this quarterly report on Form 10-Q speak only as of the date of this report; we disclaim any obligation to update these statements unless required by securities law, and we caution you not to rely on them unduly.

MD&A provides a narrative analysis explaining the reasons for material changes in the Company's (i) financial condition since the most recent fiscal year-end, and (ii) results of operations during the current fiscal year-to-date period and current fiscal quarter as compared to the corresponding periods of the preceding fiscal year. In order to better understand such changes, this MD&A should be read in conjunction with the Company's fiscal 2016 audited consolidated financial statements and notes thereto included in its 2016 Form 10-K, Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations included in our 2016 Form 10-K and with our unaudited condensed consolidated financial statements and related notes appearing elsewhere in this quarterly report.

Overview

Orion Group Holdings, Inc., its subsidiaries and affiliates (hereafter collectively referred to as the "Company"), provide a broad range of specialty construction and services in the infrastructure, industrial, and building sectors of the continental United States, Alaska, Canada and the Caribbean Basin. The Company's marine construction segment service the infrastructure sector through its services which include marine transportation facility construction, marine pipeline construction, marine environmental structures, dredging of waterways, channels and ports, environmental dredging, design, and specialty services. Its concrete construction segment services the building sector by providing turnkey concrete construction services including pour and finish, dirt work, layout, forming, rebar, and mesh across

the light commercial structural and other associated business areas. The Company is headquartered in Houston, Texas with offices throughout its operating areas.

Our contracts are obtained primarily through competitive bidding in response to “requests for proposals” by federal, state and local agencies and through negotiation and competitive bidding with private parties and general contractors. Our bidding activity and strategies are affected by such factors as our backlog, current utilization of equipment and other resources, job location, our ability to obtain necessary surety bonds and competitive considerations. The timing and location of awarded contracts may result in unpredictable fluctuations in the results of our operations.

Most of our revenue is derived from fixed-price contracts. We record revenue on construction contracts using the percentage-of-completion method, measured by the percentage of contract costs incurred to date to total estimated costs for each contract. There

are a number of factors that can create variability in contract performance and therefore impact the results of our operations. The most significant of these include the following:

- completeness and accuracy of the original bid;
- increases in commodity prices such as concrete, steel and fuel;
- customer delays, work stoppages, and other costs due to weather and environmental restrictions;
- availability and skill level of workers; and
- a change in availability and proximity of equipment and materials.

All of these factors can have a negative impact on our contract performance, which can adversely affect the timing of revenue recognition and ultimate contract profitability. We plan our operations and bidding activity with these factors in mind and they have not had a material adverse impact on the results of our operations in the past.

Second quarter 2017 recap and 2017 Outlook

During the second quarter, the Company experienced continued delays in certain customers' ability to obtain necessary permits on certain marine construction projects. These permitting delays, resulted in a resequencing of work on a couple of large projects, which led to increased costs as a result of idle crews and equipment. Without these delays, the results for the second quarter were forecasted to have been above the market consensus due to solid job execution and continued strong demand for services across both segments. The Company is pleased with progress in the second quarter, and believes that there will be strong financial improvements in the back half of this year. Additionally, the Company continues to focus on developing opportunities across the infrastructure, industrial, and building sectors through organic growth, greenfield expansion, and strategic acquisition opportunities. Looking at the second half of 2017, the Company expects a solid volume of high-quality bid opportunities to continue as each of the operating markets maintain market share expansion efforts while also pursuing new business avenues in certain sectors. The peak backlog level at quarter end, in addition to solid operational performance and continuous improvement and training across the business provides long-term visibility to support future success.

Marine Construction Segment

Demand for our marine construction services remains strong. We continue to see solid demand to help maintain and expand the infrastructure that facilitates the movement of goods and people on and over waterways. Specifically, we continue to see bid opportunities from our private sector energy related customers as they expand their marine facilities related to the storage, transportation and refining of domestically produced energy. Over the long term, we expect further opportunities in this sector from petrochemical related customers, energy exporters, and liquefied natural gas facilities. Opportunities from local port authorities also remain solid, many of which are related to the completion of the Panama Canal expansion project. Additionally, we expect to see some bid opportunities related to coastal restoration funded through the Resources and Ecosystems Sustainability, Tourism Opportunities and Revived Economy of the Gulf Coast Act of 2011 (the "RESTORE Act") towards the end of 2017. We believe the adjustments we have made to our capital assets will allow us to better meet market demand for projects from both our public and private customers in the future.

In the long-term, we see positive trends in demands for our services in our end markets, including:

- General demand to repair and improve degrading U. S. marine infrastructure;
- Improving economic conditions and increased activity in the petrochemical industry and energy related companies will necessitate capital expenditures, including larger projects, as well as maintenance call-out work;
- Expected increases in cargo volume and future demands from larger ships transiting the Panama Canal that will require ports along the Gulf Coast and Atlantic Seaboard to expand port infrastructure as well as perform additional dredging services;

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

The Water Resources Reform and Development Act (the "WRRDA Act") authorizing expenditures for the conservation and development of the nation's waterways, as well as addressing funding deficiencies within the Harbor Maintenance Trust Fund;

Renewed focus on coastal rehabilitation along the Gulf Coast, particularly through the use of RESTORE Act funds based on fines collected related to the 2010 Gulf of Mexico oil spill; and

Funding for highways and transportation under the FAST Act, which provides authority through 2020.

Concrete Construction Segment

Our concrete construction segment's demand for services also remains strong. The Texas building sector is in solid shape as its three major metropolitan areas, and expanding suburbs, continuously retain their positions as leading destinations for families and businesses to reside. Population growth throughout our markets continues to drive new distribution centers, office expansion, retail and grocery establishments and new multi-family housing units. In Houston, warehouse construction and new education facilities comprised nearly half of the second quarter sales mix. To the north, the Dallas-Fort Worth office has begun efforts to expand their distribution channels beyond light commercial and will be targeting structural construction opportunities going forward. As anticipated, our Central Texas operations are off to a great start, as we are seeing solid project execution and expanding market share along the I-35 corridor. Sustained demand for concrete services in Houston and Dallas/Fort Worth markets coupled with the early progress being made in Central Texas, indicate the concrete segment should continue providing meaningful contribution to EBITDA during the second half of the year,

Consolidated Results of Operations

Backlog Information

Our contract backlog represents our estimate of the revenues we expect to realize under the portion of contracts remaining to be performed. Given the typical duration of our contracts, which is generally less than a year, our backlog at any point in time usually represents only a portion of the revenue that we expect to realize during a twelve month period. Many projects that make up our backlog may be canceled at any time without penalty; however, we can generally recover actual committed costs and profit on work performed up to the date of cancellation. Although we have not been adversely affected by contract cancellations or modifications in the past, we may be in the future, especially in economically uncertain periods. Consequently, backlog is not necessarily indicative of future results. In addition to our backlog under contract, we also have a substantial number of projects in negotiation or pending award at any time.

Backlog for our marine construction segment at June 30, 2017 was \$210.0 million, as compared with \$166.4 million at June 30, 2016.

Backlog for our concrete construction segment at June 30, 2017 was \$218.1 million, as compared with \$201.2 million at June 30, 2016.

Three months ended June 30, 2017 compared with three months ended June 30, 2016

| | Three months ended June 30, | | | |
|--|-------------------------------|---------|-----------|---------|
| | 2017 | | 2016 | |
| | Amount | Percent | Amount | Percent |
| | (dollar amounts in thousands) | | | |
| Contract revenues | \$137,420 | 100.0 % | \$140,301 | 100.0 % |
| Cost of contract revenues | 122,023 | 88.8 % | 123,355 | 87.9 % |
| Gross profit | 15,397 | 11.2 % | 16,946 | 12.1 % |
| Selling, general and administrative expenses | 17,528 | 12.8 % | 16,899 | 12.0 % |
| Loss (gain) on sale of assets, net | 335 | 0.2 % | (234) | (0.2)% |
| Operating (loss) income from operations | (2,466) | (1.8)% | 281 | 0.2 % |
| Other (expense) income | | | | |
| Other income | 11 | — % | 9 | — % |
| Interest income | — | — % | — | — % |

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

| | | | | |
|--------------------------|------------|---------|----------|---------|
| Interest expense | (1,462) | (1.1)% | (1,600) | (1.1)% |
| Other expense, net | (1,451) | (1.1)% | (1,591) | (1.1)% |
| Loss before income taxes | (3,917) | (2.9)% | (1,310) | (0.9)% |
| Income tax benefit | (1,624) | (1.2)% | (502) | (0.4)% |
| Net loss | \$(2,293) | (1.7)% | \$(808) | (0.5)% |

Contract Revenues. Consolidated contract revenues for the three months ended June 30, 2017 were \$137.4 million as compared with \$140.3 million in the comparable prior year period, which was a decrease of \$2.9 million, or 2.1%. This decrease is primarily attributable to permitting delays in the marine construction segment that were partially offset by solid operation execution and continued demand for services, particularly in the Dallas market, for our concrete construction segment.

Contract revenues generated from private sector customers for the marine construction segment represented 36.0% of segment contract revenues in the second quarter of 2017, or approximately \$22.3 million as compared with \$45.8 million or 57.3% for the comparable prior year period. The decrease in revenue is due to a shift in timing of projects as well as completion of certain projects prior to the current quarter.

Contract revenues generated from public sector customers for the marine construction segment represented 64.0% of segment contract revenues in the second quarter of 2017, or approximately \$39.7 million, as compared with \$34.1 million or 42.7%, in the comparable prior year period. The increase in revenue is due to a shift in timing of projects as well as the addition of significant projects.

Contract revenues in the concrete construction segment are primarily derived from private sector customers. Private sector customers represent \$63.3 million, or 84.0%, of total contract revenues for the concrete construction segment in the second quarter of 2017, compared to \$53.8 million, or 89.1% in the comparable prior year period.

Gross Profit. Gross profit was \$15.4 million in the three months ended June 30, 2017, as compared with \$16.9 million in the comparable prior year period. Gross margin in the second quarter was 11.2%, as compared with 12.1% in the comparable prior year period. Gross profit decreased primarily due to permitting delays which caused interruptions in the anticipated commencement of certain projects within the marine construction segment.

Selling, General and Administrative Expense. Selling, general and administrative ("SG&A") expenses in the second quarter of 2017 were \$17.5 million as compared with \$16.9 million in the comparable prior year period, which was an increase of \$0.6 million, or 3.7%. The increase is mainly attributable to increases in payroll and payroll related expenses partially offset by decreases for depreciation and amortization expenses for the period.

Other income, net of expense. Other expense primarily reflects interest on our borrowings.

Income Tax Benefit. We have estimated our annual effective tax rate at 39.2% for 2017. This differs from the statutory rate of 35%, primarily due to state income taxes, the non-deductibility of certain permanent items, such as incentive stock compensation expense, and a change in the valuation allowance.

Six months ended June 30, 2017 compared with six months ended June 30, 2016

| | Six months ended June 30, | | Six months ended June 30, | |
|--|-------------------------------|---------|---------------------------|---------|
| | 2017 | Percent | 2016 | Percent |
| | Amount | | Amount | |
| | (dollar amounts in thousands) | | | |
| Contract revenues | \$276,177 | 100.0% | \$269,924 | 100.0% |
| Cost of contract revenues | 247,795 | 89.7% | 238,267 | 88.3% |
| Gross profit | 28,382 | 10.3% | 31,657 | 11.7% |
| Selling, general and administrative expenses | 32,507 | 11.8% | 32,437 | 12.0% |
| (Gain) loss on sale of assets, net | (177) | (0.1)% | (606) | (0.3)% |
| Operating loss from operations | (3,948) | (1.4)% | (174) | —% |
| Other (expense) income | | | | |
| Other income | 21 | —% | 22 | —% |
| Interest income | — | —% | 1 | —% |
| Interest expense | (2,817) | (1.0)% | (3,117) | (1.2)% |
| Other expense, net | (2,796) | (1.0)% | (3,094) | (1.2)% |
| Loss before income taxes | (6,744) | (2.4)% | (3,268) | (1.2)% |

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

| | | | | |
|--------------------|------------|--------|------------|--------|
| Income tax benefit | (2,643) | (1.0)% | (1,252) | (0.5)% |
| Net loss | \$(4,101) | (1.4)% | \$(2,016) | (0.7)% |

Contract Revenues. Consolidated contract revenues for the six months ended June 30, 2017 were \$276.2 million as compared with \$269.9 million in the comparable prior year period, which was an increase of \$6.3 million, or 2.3%. This increase is primarily attributable to the result of solid operation execution and continued demand for services, particularly in the Dallas market, for our concrete construction segment.

Contract revenues generated from private sector customers for the marine construction segment represented 36.7% of segment contract revenues in the second quarter of 2017, or approximately \$47.4 million as compared with \$86.7 million or 61% for the comparable prior year period. The decrease in revenue is due to a shift in timing of projects as well as completion of certain projects prior to the current quarter.

Contract revenues generated from public sector customers for the marine construction segment represented 63.3% of segment contract revenues in the second quarter of 2017, or approximately \$81.8 million, as compared with \$55.7 million or 39.1%, in the comparable prior year period. The increase in revenue is due to a shift in timing of projects as well as the addition of significant projects.

Contract revenues in the concrete construction segment are primarily derived from private sector customers. Private sector customers represent \$121.4 million, or 82.6%, of total contract revenues for the concrete construction segment in the second quarter of 2017, compared to \$113.3 million, or 88.9% in the comparable prior year period.

Gross Profit. Gross profit was \$28.4 million in the six months ended June 30, 2017, as compared with \$31.7 million in the comparable prior year period. Gross margin in the second quarter was 10.3%, as compared with 11.7% in the comparable prior year period. Gross profit decreased primarily as a result of permitting delays in the marine construction segment.

Selling, General and Administrative Expense. Selling, general and administrative ("SG&A") expenses in the second quarter of 2017 were \$32.5 million as compared with \$32.4 million in the comparable prior year period, which was an increase of \$0.1 million, or 0.2%. The increase is mainly attributable to increases in payroll and payroll related expenses partially offset by decreases for depreciation and amortization expenses for the period.

Other income, net of expense. Other expense primarily reflects interest on our borrowings.

Income Tax Benefit. We have estimated our annual effective tax rate at 39.2% for 2017. This differs from the statutory rate of 35%, primarily due to state income taxes, the non-deductibility of certain permanent items, such as incentive stock compensation expense, and a change in the valuation allowance.

Segment Results

The following table sets forth, for the periods indicated, statements of operations data by segment, segment revenues as a percentage of consolidated revenues and segment operating income as a percentage of segment revenues:

Three months ended June 30, 2017 compared with three months ended June 30, 2016

| | Three months ended June 30, | | 2016 | | |
|-------------------------------|-------------------------------|---------|-----------|---------|--|
| | 2017 | | Amount | Percent | |
| | Amount | Percent | Amount | Percent | |
| | (dollar amounts in thousands) | | | | |
| Contract revenues | | | | | |
| Marine Construction Segment | \$62,003 | 45.1 % | \$79,966 | 57.0 % | |
| Concrete Construction Segment | 75,417 | 54.9 % | 60,335 | 43.0 % | |
| Total | \$137,420 | 100.0 % | \$140,301 | 100.0 % | |
| Operating income (loss) | | | | | |
| Marine Construction Segment | \$(8,617) | (13.9)% | \$(1,212) | (1.5)% | |
| Concrete Construction Segment | 6,150 | 8.2 % | 1,493 | 2.5 % | |

| | | |
|-------|------------|-------|
| Total | \$(2,467) | \$281 |
|-------|------------|-------|

Marine Construction Segment

Revenues for our marine construction segment for the three months ended June 30, 2017 were \$62.0 million compared to \$80.0 million for the three months ended June 30, 2016, a decrease of \$18.0 million, or 22.5%. The decrease is primarily attributable to permitting delays which caused interruptions in the anticipated commencement of certain projects within the marine construction segment.

Operating loss for our marine construction segment for the three months ended June 30, 2017 was \$8.6 million, compared to a \$1.2 million loss, a decrease of \$7.4 million from the three months ended June 30, 2016. The decrease is primarily due to permitting delays that caused interruptions on certain jobs. As a percentage of revenues, operating income for our marine construction segment was (13.9)% for the three months ended June 30, 2017 compared to (1.5)% for the three months ended June 30, 2016.

Concrete Construction Segment

Revenues for our concrete construction segment for the three months ended June 30, 2017 were \$75.4 million compared to \$60.3 million for the three months ended June 30, 2016, an increase of \$15.1 million, or 25.0%. This increase in revenue was primarily due to growth in the Dallas market.

Operating income for our concrete construction segment for the three months ended June 30, 2017 was \$6.2 million, compared to \$1.5 million, an increase of \$4.7 million from the three months ended June 30, 2016. The margin improvement was primarily due to solid execution of operations in the segment. As a percentage of revenues, operating income for our concrete construction segment was 8.2% for the three months ended June 30, 2017 compared to 2.5% for the three months ended June 30, 2016.

Six months ended June 30, 2017 compared with six months ended June 30, 2016

| | Six months ended June 30, 2017 | | 2016 | | |
|-------------------------------|-----------------------------------|----------|-----------|---------|--|
| | Amount | Percent | Amount | Percent | |
| | (dollar amounts in thousands) | | | | |
| Contract revenues | | | | | |
| Marine Construction Segment | \$129,183 | 46.8 % | \$142,381 | 52.7 % | |
| Concrete Construction Segment | \$146,994 | 53.2 % | \$127,543 | 47.3 % | |
| Total | \$276,177 | 100.0 % | \$269,924 | 100.0 % | |
| Operating income (loss) | | | | | |
| Marine Construction Segment | (16,323) | (12.6)% | (4,354) | (3.1)% | |
| Concrete Construction Segment | 12,375 | 8.4 % | 4,180 | 3.3 % | |
| Total | \$(3,948) | | \$(174) | | |

Marine Construction Segment

Revenues for our marine construction segment for the six months ended June 30, 2017 were \$129.2 million compared to \$142.4 million for the six months ended June 30, 2016, a decrease of \$13.2 million, or 9.3%. The decrease is primarily attributable to permitting delays which caused delays in the anticipated commencement of certain projects within the marine construction segment.

Operating loss for our marine construction segment for the six months ended June 30, 2017 was \$16.3 million, compared to a \$4.4 million loss, a decrease of \$12.0 million from the six months ended June 30, 2016. The decrease is primarily due to permitting delays that caused interruptions on certain jobs. As a percentage of revenues, operating income for our marine construction segment was (12.6)% for the six months ended June 30, 2017 compared to (3.1)% for the six months ended June 30, 2016.

Concrete Construction Segment

Revenues for our concrete construction segment for the six months ended June 30, 2017 were \$147.0 million compared to \$127.5 million for the six months ended June 30, 2016, an increase of \$19.5 million, or 15.3%. This increase in revenue was primarily due to growth in the Dallas market.

Operating income for our concrete construction segment for the six months ended June 30, 2017 was \$12.4 million, compared to \$4.2 million, an increase of \$8.2 million from the six months ended June 30, 2016. The margin improvement was primarily due to solid execution of operations in the segment. As a percentage of revenues, operating income for our concrete construction segment was 8.4% for the six months ended June 30, 2017 compared to 3.3% for the six months ended June 30, 2016.

Liquidity and Capital Resources

Our primary liquidity needs are to finance our working capital, fund capital expenditures, and pursue strategic acquisitions. Historically, our source of liquidity has been cash provided by our operating activities and borrowings under our Credit Facility (as defined below).

Our working capital position fluctuates from period to period due to normal increases and decreases in operational activity. At June 30, 2017, our working capital was \$70.6 million, as compared with \$77.6 million at December 31, 2016. As of June 30, 2017, we had cash on hand of \$0.9 million. Due to the outstanding amount on our revolver and outstanding letters of credit, our borrowing capacity at June 30, 2017 was approximately \$49.1 million.

We expect to meet our future internal liquidity and working capital needs, and maintain or replace our equipment fleet through capital expenditure purchases and major repairs, from funds generated by our operating activities for at least the next 12 months. We believe our cash position is adequate for our general business requirements discussed above and to service our debt.

The following table provides information regarding our cash flows and our capital expenditures for the six months ended June 30, 2017 and 2016:

| | Six months ended June 30, | |
|---|------------------------------|------------|
| | 2017 | 2016 |
| Cash flows provided by (used in) operating activities | \$20,121 | \$10,131 |
| Cash flows used in investing activities | \$(4,383) | \$(12,465) |
| Cash flows (used in) provided by financing activities | \$(15,123) | \$2,501 |
| Capital expenditures (included in investing activities above) | \$(3,689) | \$(12,513) |

Operating Activities. In the six months of 2017, our operations provided approximately \$20.1 million of cash, as compared with cash used in operations in the comparable prior year period of \$10.1 million. The change in cash between periods was \$10.0 million and was primarily attributable to changes in working capital of \$13.4 million, offset by an increased net loss of \$2.1 million, changes in depreciation and amortization expense and deferred income taxes, gain on sale of property and equipment and stock compensation of approximately \$1.3 million.

Changes in working capital are normal within our business and are not necessarily indicative of any fundamental change within working capital components or trend in the underlying business.

Investing Activities. Capital asset additions and betterments to our fleet were \$3.7 million in the six months ended June 30, 2017, as compared with \$12.5 million in the comparable prior year period. The decrease is primarily a result of timing of purchase of capital assets. The Company is on track to meet its projected capital expenditures budget for the current fiscal year.

Financing Activities. Through the six months ended June 30, 2017, we drew down \$37.0 million from our revolving line of credit. Additionally, we repaid \$45.0 million on the revolver, as well as made our regularly scheduled debt payments and an additional payment on the term loan of \$8.1 million for a total of \$53.1 million in debt payments. In the comparable prior year period, we drew down \$32.0 million from our revolving line of credit. Additionally we repaid \$24.0 million on the revolver, as well as made our regularly scheduled debt payments and an additional payment on the term loan of \$5.0 million, for a total of \$29.0 million in debt payments.

Sources of Capital

The Company entered into a syndicated credit agreement (the "Credit Agreement") on August 5, 2015 with Regions Bank, as administrative agent and collateral agent, and the following co-syndication agents: Bank of America, N.A., BOKF, NA dba Bank of Texas, Branch Banking & Trust Company, Frost Bank, Bank Midwest, a division of NBH Bank, N.A., IBERIABANK, KeyBank NA, Trustmark National Bank, and First Tennessee Bank NA. The primary purpose of the Credit Agreement was to finance the acquisition of TAS, to provide a revolving line of credit, and to provide financing to extinguish all prior indebtedness with Wells Fargo Bank, National Associates, as administrative agent, and Wells Fargo Securities, LLC.

The Credit Agreement, which may be amended from time to time, provides for borrowings under a revolving line of credit and swingline loans with a commitment amount of \$50.0 million and a term loan with a commitment amount of \$135.0 million (together, the "Credit Facility"). The Credit Facility is guaranteed by the subsidiaries of the Company, secured by the assets of the Company,

including stock held in its subsidiaries, and may be used to finance general corporate and working capital purposes, to finance capital expenditures, to refinance existing indebtedness, to finance permitted acquisitions and associated fees, and to pay for all related expenses to the Credit Facility. Interest is due and is computed based on the designation of the loan, with the option of a Base Rate Loan (the base rate plus the Applicable Margin), or an Adjusted LIBOR Rate Loan (the adjusted LIBOR rate plus the Applicable Margin). Interest is due on the last day of each quarter end for Base Rate Loans and at the end of the LIBOR rate period for Adjusted LIBOR Rate Loans. The rate for all loans at the time of loan origination was 4.75%. Principal balances drawn under the Credit Facility may be prepaid at any time, in whole or in part, without premium or penalty. Amounts repaid under the revolving line of credit may be re-borrowed. The Credit Facility matures on August 5, 2020.

See Note 11 in the Notes to the Financial Statements (of this Form 10-Q) for further discussion on the Company's Debt.

Financial covenants

Restrictive financial covenants under the Credit Facility include:

- ▲ consolidated Fixed Charge Coverage Ratio as of the end of any fiscal quarter to be less than 1.25 to 1.00.
- ▲ consolidated Leverage Ratio to not exceed the following during each noted period:
 - Closing Date through and including December 31, 2015, to not exceed 3.25 to 1.00;
 - Fiscal Quarter Ending March 31, 2016, to not exceed 4.00 to 1.00;
 - Fiscal Quarter Ending June 30, 2016, to not exceed 3.75 to 1.00;
 - Fiscal Quarter Ending September 30, 2016, to not exceed 3.25 to 1.00;
 - Fiscal Quarter Ending December 31, 2016, to not exceed 3.00 to 1.00;
 - Fiscal Quarter Ending March 31, 2017, to not exceed 2.75 to 1.00;
 - Fiscal Quarter Ending June 30, 2017, to not exceed 2.75 to 1.00;
 - Fiscal Quarter Ending September 30, 2017, to not exceed 2.75 to 1.00;
 - Fiscal Quarter Ending December 31, 2017 and each Fiscal Quarter thereafter, to not exceed 2.50 to 1.00.

In addition, the Credit Facility contains events of default that are usual and customary for similar arrangements, including non-payment of principal, interest or fees; breaches of representations and warranties that are not timely cured; violation of covenants; bankruptcy and insolvency events; and events constituting a change of control.

During the second quarter of 2017, the Company initiated discussions with the lead bank in an effort to explore available options given the step down of the Leverage Ratio covenant and concerns the Company would not be in compliance with financial covenants. A second amendment to the Credit Agreement was executed during July 2017, which was effective as of June 30, 2017. The Leverage Ratio was adjusted beginning with the quarter ended June 30, 2017 through September 30, 2017, as reflected above. The Fixed Charge Coverage Ratio was unchanged. This amendment to the Credit Agreement will increase the cost of the Company's borrowings if the Leverage Ratio exceeds 2.75 to 1.00 and will impose additional limitations on certain types of activities, such as acquisitions. With the execution of the aforementioned amendment, the Company was in compliance with all financial covenants as of June 30, 2017.

The Company expects to meet its future internal liquidity and working capital needs, and maintain or replace its equipment fleet through capital expenditure purchases and major repairs, from funds generated by our operating activities for at least the next 12 months. The Company believes that our cash position and available borrowings together with cash flow from our operations is adequate for general business requirements and to service its debt.

Derivative Financial Instruments

On September 16, 2015, the Company entered into a series of receive-variable, pay-fixed interest rate swaps to hedge the variability in the interest payments on 50% of the aggregate principal amount of the Regions Term Loan outstanding, beginning with a notional amount of \$67.5 million. There are a total of five sequential interest rate swaps to achieve the hedged position and each year on August 31, with the exception of the final swap, the existing interest rate swap is scheduled to expire and will be immediately replaced with a new interest rate swap until the expiration of the final swap on July 31, 2020. At inception, these interest rate swaps were designated as a cash flow hedge for hedge accounting, and as such, the effective portion of unrealized changes in market value are recorded in accumulated other comprehensive income (loss) and reclassified into earnings during the period in which the hedged forecasted transaction affects earnings. Gains and losses from hedge ineffectiveness are recognized in current earnings. The change in fair market value of the swaps as of June 30, 2017 is \$0.3 million which is reflected in the balance sheet as a liability. The fair market value of the swaps as of June 30, 2017 is \$0.4 million.

Bonding Capacity

We are generally required to provide various types of surety bonds that provide additional security to our customers for our performance under certain government and private sector contracts. Our ability to obtain surety bonds depends on our capitalization, working capital, past performance and external factors, including the capacity of the overall surety market. At June 30, 2017, our capacity under our current bonding arrangement was in excess of \$400 million, of which we had approximately \$197 million in surety bonds outstanding. We believe our strong balance sheet and working capital position will allow us to continue to access our bonding capacity.

Effect of Inflation

We are subject to the effects of inflation through increases in the cost of raw materials and other items, such as fuel, concrete, and steel. Due to the relative short-term duration of our projects, we are generally able to include anticipated price increases in the cost of our bids.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

In the normal course of business, our results of operations are subject to risks related to fluctuation in commodity prices and fluctuations in interest rates. Historically, our exposure to foreign currency fluctuations has not been material and has been limited to temporary field accounts located in foreign countries where we perform work. Foreign currency fluctuations were immaterial in this reporting period.

Commodity price risk

We are subject to fluctuations in commodity prices for concrete, steel products and fuel. Although we routinely attempt to secure firm quotes from our suppliers, we generally do not hedge against increases in prices for concrete, steel and fuel. Commodity price risks may have an impact on our results of operations due to the fixed-price nature of many of our contracts, although the short-term duration of our projects may allow us to include price increases in the costs of our bids.

Interest rate risk

At June 30, 2017, we had \$88.5 million in outstanding borrowings under our credit facility, with a weighted average interest rate over the three month period of 3.57%. Also we have entered into a series of receive-variable, pay-fixed interest rate swaps to hedge the variability in the interest payments on 50% of the aggregate principal amount of the term loan component of the credit facility outstanding, beginning with a notional amount of \$67.5 million. At inception, these interest rate swaps were designated as a cash flow hedge for hedge accounting. Our objectives in managing interest rate risk are to lower our overall borrowing costs and limit interest rate changes on our earnings and cash flows. To achieve this, we closely monitor changes in interest rates and we utilize cash from operations to reduce our debt position, if warranted.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. As required, the Company's management, with the participation of its Chief Executive Officer and Chief Financial Officer, have conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this quarterly report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective.

Changes in Internal Controls. There have been no changes in our internal controls over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal

controls over financial reporting.

PART II - Other Information

Item 1. Legal Proceedings

For information about litigation involving us, see Note 15 to the condensed consolidated financial statements in Part I of this report, which we incorporate by reference into this Item 1 of Part II.

Item 1A. Risk Factors

There have been no material changes to the risk factors previously disclosed in our 2016 Form 10-K.

36

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

There were no sales of equity securities in the period ended June 30, 2017.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

37

Item 6. Exhibits

Exhibit

Number Description

- 2.1 Membership Interests Purchase Agreement dated August 5, 2015 by and among T.A.S. Holdings, LLC and Orion Concrete Construction, LLC (Schedules, exhibits and similar attachments to the Purchase Agreement that are not material have been omitted pursuant to Item 601(b)(2) of Regulation S-K. The Company will furnish supplementally a copy of any omitted schedule, exhibit or similar attachment to the SEC upon request) (incorporated herein by reference to Exhibit 2.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, filed with the Securities and Exchange Commission on August 7, 2015 (File No. 1-33892)).
- 2.2 First Amendment, effective June 17, 2016, to the Membership Interests Purchase Agreement dated August 5, 2015 (incorporated herein by reference to Exhibit 2.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016, filed with the Securities and Exchange Commission on August 5, 2016 (File No. 1-33891)).
- 2.3 Post Closing Supplemental Agreement Amendment, effective June 17, 2016, as a supplement to the Membership Interests Purchase Agreement dated August 5, 2015 (incorporated herein by reference to Exhibit 2.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016, filed with the Securities and Exchange Commission on August 5, 2016 (File No. 1-33891)).
- 2.4 Stock Purchase Agreement dated April 9 2017 by and among Anthony James Bagliore III and Lorie Sue Bagliore and T.A.S. Commercial Concrete Construction, LLC (Schedules, exhibits and similar attachments to the Agreement that are not material have been omitted pursuant to Item 601(b)(2) of Regulation S-K. The Company will furnish supplementally a copy of any omitted schedule, exhibit or similar attachment to the SEC upon request) (incorporated herein by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on April 13, 2017 (File No. 1-33891)).
- 3.1 Amended and Restated Certificate of Incorporation of Orion Group Holdings, Inc. (incorporated herein by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016, filed with the Securities and Exchange Commission on August 5, 2016 (File No. 1-33891)).
- 3.2 Amended and Restated Bylaws of Orion Group Holdings, Inc. (incorporated herein by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016, filed with the Securities and Exchange Commission on August 5, 2016 (File No. 1-33891)).
- 4.1 Registration Rights Agreement by and between Friedman, Billings, Ramsey & Co., Inc. and Orion Marine Group, Inc. dated May 17, 2007 (incorporated herein by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-1 filed with the Securities and Exchange Commission on August 20, 2007 (File No. 333-145588)).
- 10.1 Credit Agreement dated as of August 5, 2015 among Orion Marine Group, Inc. as Borrower, Certain Subsidiaries of the Borrower Party Hereto From Time to Time, as Guarantors, The Lenders Party Hereto, Regions Bank, as Administrative Agent and Collateral Agent, and Bank of America, N.A., BOKF, NA DBA Bank of Texas, and Branch Banking and Trust Company, as Co-Syndication Agents, Regions Capital Markets, a division of Regions Bank, as Lead Arranger and Book Manager (incorporated herein by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, filed with the Securities and Exchange Commission on August 7, 2015 (File No. 1-33982)).
- 10.2 First amendment, effective March 31, 2016, to the Credit Agreement dated as of August 5, 2015 among Orion Marine Group, Inc. as Borrower, Certain Subsidiaries of the Borrower Party Hereto From Time to Time, as Guarantors, The Lenders Party Hereto, Regions Bank, as Administrative Agent and Collateral Agent, and Bank of America, N.A., BOKF, NA DBA Bank of Texas, and Branch Banking and Trust Company, as Co-Syndication Agents, Regions Capital Markets, a division of Regions Bank, as Lead Arranger and Book Manager (incorporated herein by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for

Edgar Filing: Orion Group Holdings Inc - Form 10-Q

the quarter ended March 31, 2016, filed with the Securities and Exchange Commission on May 6, 2016 (File No. 1-33892)).

- *
10.3 Second amendment, effective June 30, 2016, to the Credit Agreement dated as of August 5, 2015 among Orion Marine Group, Inc. as Borrower, Certain Subsidiaries of the Borrower Party Hereto From Time to Time, as Guarantors, the Lenders Party Hereto, Regions Bank, as Administrative Agent and Collateral Agent, and Bank of America, N.A., BOKF, NA DBA Bank of Texas, and Branch Banking and Trust Company, as Co-syndication Agents, Regions Capital Markets, a division of Regions Bank, as Lead Arranger and Book Manager
- 10.4 Orion Group Holdings, In. 2017 Long-Term Incentive Plan (incorporated herein by reference to Appendix A to the Company's Definitive Proxy Statement on Schedule 14A, filed with the Securities and Exchange Commission on April 11, 2017 (File No. 1-33891)).
- 10.5 Amendment to Employment Agreement by and between Orion Group Holdings, Inc. and Peter R. Buchler, effective April 1, 2017 (incorporated herein by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K, filed with the Securities and Exchange Commission on April 5, 2017 (File No. 1-33891)).
- *
31.1 Certification of the Chief Executive Officer Pursuant to Rules 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

- * Certification of the Chief Financial Officer Pursuant to Rules 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- * Certification of the Chief Executive Officer and the Chief Financial Officer pursuant to Title 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101.~~IN~~BRL Instance Document.
101.~~SC~~BRL Taxonomy Extension Schema Document.
101.~~CA~~BRL Taxonomy Extension Calculation Linkbase Document.
101.~~DE~~BRL Taxonomy Extension Definition Linkbase Document.
101.~~LA~~BRL Taxonomy Extension Label Linkbase Document.
101.~~PR~~BRL Taxonomy Extension Presentation Linkbase Document.

* filed herewith

† management or compensatory arrangement

SIGNATURES

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

ORION GROUP HOLDINGS, INC.

By: /s/ Mark R. Stauffer
August 3, 2017 Mark R. Stauffer
President and Chief Executive Officer

By: /s/ Christopher J. DeAlmeida
August 3, 2017 Christopher J. DeAlmeida
Executive Vice President and Chief Financial Officer