

BOOTS & COOTS INTERNATIONAL WELL CONTROL INC  
Form 10-Q  
May 15, 2003

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

FORM 10-Q

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

FOR THE QUARTER ENDED MARCH 31, 2003

COMMISSION FILE NUMBER 1-13817

BOOTS & COOTS INTERNATIONAL  
WELL CONTROL, INC.  
(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

11-2908692  
(I.R.S. Employer  
Identification No.)

11615 N. HOUSTON ROSSYLN  
HOUSTON, TEXAS  
(Address of principal executive offices)

77086  
(Zip Code)

(281) 931-8884  
Registrant's telephone number, including area code

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act)  
Yes  No

The number of shares of the Registrant's Common Stock, par value \$.00001 per share, outstanding at May 13, 2003, was 82,767,293.

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BOOTS & COOTS INTERNATIONAL WELL CONTROL, INC.

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(UNAUDITED)

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BOOTS & COOTS INTERNATIONAL WELL CONTROL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

	ASSETS	DECEMBER 31, 2002	
		-----	-----
CURRENT ASSETS:			
Cash and cash equivalents. . . . .	\$	261,000	\$
Receivables - net . . . . .		2,868,000	
Restricted assets . . . . .		69,000	
Assets of discontinued operations . . . . .		212,000	
Prepaid expenses and other current assets . . . . .		620,000	
Total current assets. . . . .		4,030,000	
		-----	
PROPERTY AND EQUIPMENT - net. . . . .		3,000,000	
OTHER ASSETS. . . . .		6,000	
Total assets. . . . .	\$	7,036,000	\$
		=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)

CURRENT LIABILITIES:

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Short term debt and current maturities of long-term debt and notes payable.	\$	15,000,000	\$
Accounts payable. . . . .		2,939,000	
Accrued liabilities . . . . .		1,897,000	
Liabilities of discontinued operations. . . . .		1,188,000	
		-----	
Total current liabilities . . . . .		21,024,000	
		-----	
Total liabilities . . . . .		21,024,000	
		-----	
COMMITMENTS AND CONTINGENCIES . . . . .			-
STOCKHOLDERS' EQUITY (DEFICIT):			
Preferred stock (\$.00001 par, 5,000,000 shares authorized, 331,000 and 129,000 shares issued and outstanding at December 31, 2002 and March 31, 2003, respectively) . . . . .			-
Common stock (\$.00001 par, 125,000,000 shares authorized, 44,862,000 and 73,074,000 shares issued and outstanding at December 31, 2002 and March 31, 2003, respectively) . . . . .			-
Additional paid-in capital. . . . .		59,832,000	
Accumulated other comprehensive loss. . . . .		(438,000)	
Accumulated deficit . . . . .		(73,382,000)	
		-----	
Total stockholders' equity (deficit). . . . .		(13,988,000)	
		-----	
Total liabilities and stockholders' equity (deficit). . . . .	\$	7,036,000	\$
		=====	=====

See accompanying notes to condensed consolidated financial statements.

BOOTS & COOTS INTERNATIONAL WELL CONTROL, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

	THREE MONTHS ENDED MARCH 31,	
	2002	2003
	-----	-----
REVENUES		
Service. . . . .	\$ 4,010,000	\$ 4,302,000
Equipment sales. . . . .	-	6,629,000
	-----	-----
Total Revenues. . . . .	4,010,000	10,931,000
COSTS OF SALES		
Service. . . . .	1,369,000	881,000
Equipment sales. . . . .	-	3,082,000
	-----	-----
Total Costs of Sales. . . . .	1,369,000	3,963,000
Gross Margin. . . . .	2,641,000	6,968,000

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Operating expenses . . . . .	1,626,000	1,859,000
Selling, general and administrative. . . . .	679,000	837,000
Depreciation and amortization. . . . .	286,000	245,000
	-----	-----
OPERATING INCOME . . . . .	50,000	4,027,000
INTEREST EXPENSE (INCOME) AND OTHER. . . . .	100,000	425,000
	-----	-----
	(50,000)	3,602,000
INCOME (LOSS) FROM CONTINUING OPERATIONS, before income taxes		
INCOME TAX EXPENSE . . . . .	15,000	304,000
	-----	-----
INCOME (LOSS) FROM CONTINUING OPERATIONS . . . . .	(65,000)	3,298,000
LOSS (INCOME) FROM DISCONTINUED OPERATIONS, net of income taxes.	(1,765,000)	15,000
	-----	-----
NET INCOME (LOSS). . . . .	(1,830,000)	3,313,000
PREFERRED DIVIDEND REQUIREMENTS & ACCRETIONS . . . . .	830,000	732,000
	-----	-----
NET INCOME (LOSS) ATTRIBUTABLE TO COMMON STOCKHOLDERS. . . . .	\$ (2,660,000)	\$ 2,581,000
	=====	=====
Basic Earnings (Loss) per Common Share:		
Continuing Operations . . . . .	\$ (0.02)	\$ 0.05
	=====	=====
Discontinued Operations . . . . .	\$ (0.04)	\$ 0.00
	=====	=====
Net Income (Loss) . . . . .	\$ (0.06)	\$ 0.05
	=====	=====
Weighted Average Common Shares Outstanding - Basic . . . . .	41,442,000	53,978,000
	=====	=====
Diluted Earnings (Loss) per Common Share:		
Continuing Operations . . . . .	\$ (0.02)	\$ 0.04
	=====	=====
Discontinued Operations . . . . .	\$ (0.04)	\$ 0.00
	=====	=====
Net Income (Loss) . . . . .	\$ (0.06)	\$ 0.04
	=====	=====
Weighted Average Common Shares Outstanding - Diluted . . . . .	41,442,000	72,245,000
	=====	=====

See accompanying notes to condensed consolidated financial statements.

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CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)  
THREE MONTHS ENDED MARCH 31, 2003  
(UNAUDITED)

	PREFERRED STOCK		COMMON STOCK		PAID-IN CAPITAL
	SHARES	AMOUNT	SHARES	AMOUNT	
BALANCES, December 31, 2002 . . . .	331,000	\$ -	44,862,000	\$ -	\$59,832,000
Warrant discount accretion . . .	-	-	-	-	13,000
Common stock options exercised. .	-	-	1,291,000	-	651,000
Preferred stock conversion to common stock. . . . .	(202,000)	-	26,921,000	-	-
Preferred stock dividends accrued . . . . .	-	-	-	-	719,000
Net income (loss) . . . . .	-	-	-	-	-
Foreign currency translation loss	-	-	-	-	-
Comprehensive income . . . . .	-	-	-	-	-
BALANCES, March 31, 2003	129,000	\$ -	73,074,000	\$ 1,000	\$61,214,000

TOTAL  
STOCKHOLDERS'  
EQUITY  
(DEFICIT)

BALANCES, December 31, 2002 . . . .	\$ (13,988,000)
Warrant discount accretion .	-
Common stock options exercised. .	651,000
Preferred stock conversion to common stock. . . . .	-
Preferred stock dividends accrued . . . . .	-
Net income (loss) . . . . .	3,313,000
Foreign currency translation loss	(76,000)
Comprehensive income . . . . .	3,237,000
BALANCES, March 31, 2003	\$ (10,100,000)

See accompanying notes to condensed consolidated financial statements.

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	THREE MONTHS ENDED MARCH 31,	
	2002	2003
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income (loss) . . . . .	\$ (1,830,000)	\$ 3,313,000
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization . . . . .	286,000	245,000
Bad debt expense . . . . .	15,000	-
Gain on sale of assets . . . . .	(3,000)	-
Other non cash charges . . . . .	-	392,000
Net cash provided by operating activities before changes in operating assets and liabilities: . . . . .	(1,532,000)	3,950,000
Receivables . . . . .	(127,000)	(1,092,000)
Restricted Assets . . . . .	513,000	69,000
Inventories . . . . .	(379,000)	-
Prepaid expenses and other current assets . . . . .	310,000	164,000
Other assets . . . . .	28,000	13,000
Accounts payable and accrued liabilities . . . . .	1,019,000	(224,000)
Change in net assets and liabilities of discontinued operations . . . . .	813,000	(117,000)
Net cash provided by operating activities . . . . .	645,000	2,763,000
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Property and equipment additions . . . . .	(36,000)	(1,032,000)
Proceeds from sale of property and equipment . . . . .	3,000	-
Net cash used in investing activities . . . . .	(33,000)	(1,032,000)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Common stock options exercised . . . . .	-	651,000
Proceeds from short term senior debt financing . . . . .	-	200,000
Payments of short term senior debt financing . . . . .	-	(700,000)
Repayments to pledging arrangements . . . . .	(148,000)	(59,000)
Net cash provided by (used in) financing activities . . . . .	(148,000)	92,000
Impact of foreign currency on cash . . . . .	-	(76,000)
Net increase in cash and cash equivalents . . . . .	464,000	1,747,000
CASH AND CASH EQUIVALENTS, Beginning of Period . . . . .	303,000	261,000
CASH AND CASH EQUIVALENTS, End of Period . . . . .	\$ 767,000	\$ 2,008,000
<b>SUPPLEMENTAL CASH FLOW DISCLOSURES:</b>		
Cash paid for interest . . . . .	\$ 94,000	60,000
Cash paid for income taxes . . . . .	-	262,000
<b>NON-CASH INVESTING AND FINANCING ACTIVITIES:</b>		
Stock and warrant accretions . . . . .	13,000	13,000
Preferred stock dividends accrued . . . . .	817,000	719,000
Preferred stock issued for settlement . . . . .	19,000	-

See accompanying notes to condensed consolidated financial statements.

BOOTS & COOTS INTERNATIONAL WELL CONTROL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
THREE MONTHS ENDED MARCH 31, 2003  
(UNAUDITED)

A. GOING CONCERN

At March 31, 2003, the Company had a working capital deficit of \$13,500,000 and a total stockholders' deficit of \$10,100,000. In addition, the Company is currently in default under its loan agreements with The Prudential Insurance Company of America and Specialty Finance Fund 1, LLC, and, as a consequence, these lenders and the participants in the Specialty Finance credit facility may accelerate the maturity of their obligations at any time. As of the date of this quarterly report on Form 10-Q, the Company has not received notice from any lender of acceleration nor any demand for repayment. All of these obligations have been classified as current liabilities at March 31, 2003 in the accompanying condensed consolidated balance sheet. See Note F for further discussion of the Company's debt. The Company also has significant past due vendor payables at March 31, 2003.

During the quarter ended March 31, 2003, the Company's short term liquidity improved as a consequence of certain asset sales, which resulted in net proceeds (after replacement costs) to the Company of approximately \$2 million. A portion of these proceeds were used to repay \$700,000 plus interest owing under the Company's credit facility with Checkpoint Business, Inc. (See Note F for further discussion). The Company also applied \$400,000 of the proceeds to settle the Calicutt lawsuit (See Note G for further discussion) and to reduce payables owing to certain of the Company's significant vendors.

The Company generates its revenues from prevention services and emergency response activities. Response activities are generally associated with a specific emergency or "event" whereas prevention activities are generally "non-event" related services. Event related services typically produce higher operating margins for the Company, but the frequency of occurrence varies widely and is inherently unpredictable. Non-event services typically have lower operating margins, but the volume and availability of work is more predictable. Historically the Company has relied on event driven revenues as the primary focus of its operating activity, but more recently the Company's strategy has been to achieve greater balance between event and non-event service activities. While the Company has successfully improved this balance, event related services are still the major source of revenues and operating income for the Company.

The majority of the Company's event related revenues are derived from well control events (i.e., blowouts) in the oil and gas industry. Demand for the Company's well control services is impacted by the number and size of drilling and work over projects, which fluctuate as changes in oil and gas prices affect exploration and production activities, forecasts and budgets. The Company's reliance on event driven revenues in general, and well control events in particular, impairs the Company's ability to generate predictable operating cash flows.

During the first quarter of 2003, there was a significant increase in demand for the Company's services and equipment, particularly internationally and specifically in the Middle East in connection with the war in Iraq. Such increase in activity resulted in the Company generating income from operations of \$4,027,000 for the first quarter of 2003. While these developments have positively impacted the Company's near-term liquidity, there can be no assurance

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that the cash flows generated from such activities will be sufficient to meet the Company's near-term liquidity needs. In addition, while the Company has recently been able to pay its critical vendors for current services and materials, there remain significant overdue payables which the Company has been unable to satisfy.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. However, the uncertainties surrounding the sufficiency and timing of its future cash flows, the current defaults of certain debt agreements with its lenders, and the lack of firm commitments for additional capital raises substantial doubt about the ability of the Company to continue as a going concern. The accompanying consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

### B. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form

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10-Q and Rule 10-01 of Regulation S-X. They do not include all information and notes required by generally accepted accounting principles for complete annual financial statements. The accompanying condensed consolidated financial statements include all adjustments, including normal recurring accruals, which, in the opinion of management, are necessary in order to make the condensed consolidated financial statements not be misleading. The unaudited condensed consolidated financial statements and notes thereto and the other financial information contained in this report should be read in conjunction with the audited financial statements and notes in the Company's annual report on Form 10-K for the year ended December 31, 2002, and those reports filed previously with the Securities and Exchange Commission ("SEC"). The results of operations for the three-month periods ended March 31, 2002 and 2003 are not necessarily indicative of the results to be expected for the full year.

### C. STOCK-BASED COMPENSATION

The Company accounts for stock-based compensation granted under its the long-term incentive plan using the intrinsic value method prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. Stock-based compensation expenses associated with option grants were not recognized in the net income (loss) of the three month periods ended March 31, 2003 and 2002, as all options granted had exercise prices equal to the market value of the underlying common stock on the dates of grant. The following table illustrates the effect on net income (loss) and earnings per share if the Company had applied the fair value recognition provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" to stock-based employee compensation:

THREE MONTHS ENDED MARCH 31, 2002	THREE MONTHS ENDED MARCH 31, 2003
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Net income (loss) to common		
stockholders as reported . . . . .	\$ (2,660,000)	\$ 2,581,000
Less total stock based employee compensation expense determined under fair value based method for all awards, net of tax related effects. .	186,000	64,000
	-----	-----
Pro forma net income (loss) to common stockholders . . . . .	\$ (2,846,000)	\$ 2,517,000
	-----	-----
Basic net income (loss) per share		
As reported . . . . .	\$ (0.06)	\$ 0.05
Pro forma . . . . .	\$ (0.07)	\$ 0.05
Diluted net income (loss) per share		
As reported . . . . .	\$ (0.06)	\$ 0.04
Pro forma . . . . .	\$ (0.07)	\$ 0.03

### D. RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations ("SFAS No. 143") which covers all legally enforceable obligations associated with the retirement of tangible long-lived assets and provides the accounting and reporting requirements for such obligations. The Company adopted SFAS No. 143 effective January 1, 2003, as required. The adoption of SFAS No. 143 did not have a material impact on Company's condensed consolidated financial position or results of operations.

In December 2002, the FASB issued Accounting for Stock-Based Compensation ("SFAS No. 148") amending SFAS No. 123, to provide alternative methods of transition to the fair value method of accounting for stock-based employee compensation. The three methods provided in SFAS No. 148 include (1) the prospective method which is the method currently provided for in SFAS No. 123, (2) the retroactive restatement method which would allow companies to restate all periods presented and (3) the modified prospective method which would allow companies to present the recognition provisions of all outstanding stock-based employee compensation instruments as of the beginning of the fiscal year of adoption. In addition, SFAS No. 148 amends the disclosure provisions of SFAS No. 123 to require disclosure in the summary of significant accounting policies of the effects of an entity's accounting policy with respect to stock-based employee compensation on reported net income and earnings per share in annual and interim financial statements. SFAS No. 148 does not amend SFAS No. 123 to require companies to account for their employee stock-based awards using the fair value method. However, the disclosure provisions are required for all

companies with stock-based employee compensation, regardless of whether they utilize the fair method of accounting described in SFAS No. 123 or the intrinsic value method described in APB Opinion No. 25, Accounting for Stock Issued to Employees. The Company does not currently intend to adopt the fair value method of accounting for stock-based compensation, however it has adopted the disclosure provisions of SFAS No. 148.

In January 2003, the FASB issued Interpretation No. 46, Consolidation of Variable Interest Entities (FIN No. 46), which addresses consolidation by business enterprises of variable interest entities. FIN No. 46 clarifies the application of Accounting Research Bulletin No. 51, Consolidated Financial Statements, to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient

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equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN No. 46 applies immediately to variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. It applies in the first fiscal year or interim period beginning after June 15, 2003, to variable interest entities in which an enterprise holds a variable interest that it acquired before February 1, 2003. The Company does not expect to identify any variable interest entities that must be consolidated and thus the Company does not expect the requirements of FIN No. 46 to have a material impact on its financial condition or results of operations.

E. DISCONTINUED OPERATIONS

On June 30, 2002, the Company made the decision and formalized a plan to sell the assets of its Special Services and Abasco operations. The sales proceeds were approximately \$1,041,000. The operations of these two companies are reflected as discontinued operations on the condensed consolidated statements of operations and as assets and liabilities of discontinued operations on the condensed consolidated balance sheets.

The following represents a condensed detail of assets and liabilities for discontinued operations adjusted for write-downs:

	DECEMBER 31, 2002	MARCH 31, 2003
	-----	-----
Cash		
Receivables - net . . . . .	174,000	188,000
Restricted assets . . . . .	38,000	-
	-----	-----
Total assets . . . . .	\$ 212,000	\$ 188,000
	=====	=====
Short term debt and current maturities of long-term debt and notes payable . . . . .	\$ 32,000	\$
Accounts payable . . . . .	801,000	715,000
Accrued liabilities . . . . .	355,000	332,000
	-----	-----
Total liabilities . . . . .	\$ 1,188,000	\$1,047,000
	=====	=====

Reconciliation of change in net asset value of discontinued operations:

Balance of net liability of discontinued operations at December 31, 2002	\$ (976,000)
Income from discontinued operations	15,000
Intercompany transfers	102,000
	-----
Balance of net liability of discontinued operations at March 31, 2003	\$ (859,000)
	=====

F. LONG-TERM DEBT AND NOTES PAYABLE

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As of March 31, 2003, the Company was not in compliance with the ratio tests for the trailing twelve month period under its loan agreement with the Prudential Insurance Company of America and the Company did not receive a waiver from Prudential for this period. Under the Prudential loan agreement, failure to comply with the ratio tests is an event of default and the note holder may, at its option, by notice in writing to the Company, declare all of the Notes to be immediately due and payable together with interest accrued thereon. Accordingly, the Company has classified this obligation as a current liability on its balance sheet. As of May 14, 2003, the Company has not received a written notice of default from Prudential and the Company is in discussion with Prudential to secure a forbearance agreement.

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On April 9, 2002, the Company entered into a loan participation agreement under which it borrowed an additional \$750,000 under its existing Senior Secured Loan Facility with Specialty Finance Fund I, LLC. The effective interest rate of the participation is 11% after taking into account rate adjustment fees. The Company also paid 3% of the borrowed amount in origination fees, paid closing expenses and issued 100,000 shares of common stock to the participation lender at closing. The participation had an initial maturity of 90 days, which was extended for an additional 90 days at the Company's option. The Company issued an additional 100,000 shares of common stock to the participation lender to extend the maturity date. On October 9, 2002, the loan extension period matured. As of May 14, 2003, none of the loan participation has been repaid nor has the Company received formal demand for payment from the loan participant. However, in the loan documentation, the Company has waived the notices which might otherwise be required by law and, as a consequence, the loan participants have the current ability to post the collateral securing their notes for foreclosure.

On May 2, 2002, the Company borrowed \$250,000 under the Senior Secured Loan Facility upon similar terms, except that the Company issued 33,334 shares of common stock to the participating lenders at closing and issued an additional 33,334 shares of common stock to extend the maturity of those notes for an additional 90 days. On October 25, 2002, the loan extension period matured. As of May 14, 2003, none of the loan participations have been repaid nor has the Company received formal demand for payment from the loan participants. However, in the loan documentation the Company has waived the notices which might otherwise be required by law and, as a consequence, the loan participants have the current ability to post the collateral securing their notes for foreclosure.

On July 5, 2002, the Company entered into a loan participation agreement under which it borrowed an additional \$100,000 under its existing Senior Secured Loan Facility. The effective interest rate of the participation is 25% after taking into account rate adjustment fees. The Company also paid 3% of the borrowed amount in origination fees, paid closing expenses and issued 130,000 shares of common stock to the participation lender at closing. The participation had a maturity of 90 days. On September 28, 2002, the loan matured. As of May 14, 2003, none of the loan participation has been repaid nor has the Company received formal demand for payment from the loan participant. However, in the loan documentation the Company has waived the notices which might otherwise be required by law and, as a consequence, the loan participants have the current ability to post the collateral securing their notes for foreclosure.

On July 8, 2002, the Company entered into a loan participation agreement with a certain party under which it borrowed an additional \$200,000 under its existing Senior Secured Loan Facility with Specialty Finance Fund I, LLC. The effective interest rate of the participation is 16% after taking into account rate adjustment fees. The Company also paid 4% of the borrowed amount in origination fees, paid closing expenses and issued 150,000 shares of common

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stock to the participation lender at closing. The participation had a maturity of 90 days. On October 1, 2002, the loan matured. As of May 14, 2003, none of the loan participation has been repaid nor has the Company received formal demand for payment from the loan participant. However, in the loan documentation the Company has waived the notices which might otherwise be required by law and, as a consequence, the loan participants have the current ability to post the collateral securing their notes for foreclosure.

On December 4, 2002, the Company entered into a loan agreement with Checkpoint Business, Inc. ("Checkpoint") providing for short term working capital up to \$1,000,000. The effective interest rate of under the loan agreement was 15% per annum. Checkpoint collateral included substantially all of the assets of the Company, including the stock of the Company's Venezuelan subsidiary. As of December 31, 2002 and March 28, 2003, the Company had borrowed \$500,000 and an additional \$200,000, respectively, under this facility.

On March 28, 2003, the Company paid in full the principal balance of \$700,000 and interest outstanding under its loan agreement with Checkpoint. On May 7, 2003, the Company settled Checkpoint's option to purchase its Venezuelan subsidiary and terminated Checkpoint's exclusivity rights. This settlement consisted of \$300,000 of cash and \$100,000 in notes maturing in six months.

### G. COMMITMENTS AND CONTINGENCIES

In September 1999, a lawsuit styled Jerry Don Calicutt, Jr., et al., v. Larry H. Ramming, et al., was filed against the Company, certain of its subsidiaries, Larry H. Ramming, Charles Phillips, certain other employees of the Company, and several entities affiliated with Larry H. Ramming in the 269th Judicial District Court, Harris County, Texas. The plaintiffs alleged various causes of action, including fraud, breach of contract, breach of fiduciary duty

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and other intentional misconduct relating to the acquisition of stock of a corporation by the name of Emergency Resources International, Inc. ("ERI") by a corporation affiliated with Larry H. Ramming and the circumstances relating to the founding of the Company. In July 2002, the Company agreed to pay \$500,000 in cash in four installments, the last installment being due in January 2003, in partial settlement of the plaintiffs' claims against all of the defendants. As to the remaining claims, the defendants filed motions for summary judgment. On September 24, 2002 the court granted the defendants' motions for summary judgment. The Company had defaulted on the settlement after paying one installment of \$100,000, but has since resettled the case on behalf of all Boots & Coots entities and all employees of the Company (but not on behalf of Larry H. Ramming, Charles Phillips, and the other entities affiliated with Larry H. Ramming) by paying the remaining unpaid \$400,000 in March 2003 in exchange for full and final release by all plaintiffs from any and all claims related to the subject of the case.

The Company is involved in or threatened with various other legal proceedings from time to time arising in the ordinary course of business. The Company does not believe that any liabilities resulting from any such proceedings will have a material adverse effect on its operations or financial position.

### H. EARNINGS PER SHARE

Basic income (loss) per share is computed by dividing net income (loss) attributable to common shareholders by the weighted average number of common shares outstanding for the period. The computation of diluted net income (loss) attributable to common shareholders per share reflects the potential dilution that could occur if securities or other contracts to issue common stock that are

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dilutive to net income attributable to common shareholders were exercised or converted into common stock or resulted in the issuance of common stock that would then share in the earnings of the Company.

The following table is a reconciliation of the basic and diluted weighted average shares outstanding for the three months ended March 31, 2002 and 2003:

	Three Months Ended March 31,	
	2002	2003
Weighted average common shares outstanding:		
Basic. . . . .	41,442,000	53,978,000
Senior convertible debt. . . . .	-	1,333,000
Convertible preferred stock. . . . .	-	16,931,000
Stock purchase warrants (a). . . . .	-	-
Stock options (b). . . . .	-	3,000
	-----	-----
Diluted. . . . .	41,442,000	72,245,000
	-----	-----

(a) Stock purchase warrants to purchase 35,471,000 shares and 31,595,000 shares of common stock were outstanding but not included in the computations of diluted net income (loss) attributable to common shareholders per share for the three months ended March 31, 2002 and 2003, respectively, because the exercise prices of the warrants were greater than the average market price of the common shares and would be anti-dilutive to the computations.

(b) Common stock options to purchase 7,848,000 shares and 1,443,000 shares of common stock were outstanding but not included in the computations of diluted net income (loss) attributable to common shareholders per share for the three months ended March 31, 2002 and 2003, respectively, because the exercise prices of the options were greater than the average market price of the common shares and would be anti-dilutive to the computations.

### I. BUSINESS SEGMENT INFORMATION

On January 1, 2001, the Company redefined the segments in which it operates as a result of the discontinued operations of ITS and Baylor business operations and further redefined the segments during 2002, as a result of the decision to discontinue its Abasco and Special Services business operations. The current segments are Prevention and Response. Intercompany transfers between segments were not material. The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies. For purposes of this presentation, general and corporate expenses have been allocated between segments on a pro rata basis based on revenue. ITS, Baylor, Abasco and Special Services are presented as discontinued operations in the condensed consolidated financial statements and are therefore excluded from the segment information for all periods presented.

The Prevention segment consists of "non-event" services that are designed to reduce the number and severity of critical well events to oil and gas operators. The scope of these services include training, contingency planning, well plan reviews, services associated with the Company's Safeguard programs and

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services in conjunction with the WELLSURE(R) risk management program. All of these services are designed to significantly reduce the risk of a well blowout or other critical response event.

The Response segment consists of personnel and equipment services provided during an emergency response such as a critical well event or a hazardous material response. These services are designed to minimize response time and damage while maximizing safety. Response revenues typically provide high gross profit margins.

Information concerning operations in the two business segments for the three months ended March 31, 2002 and 2003 is presented below.

	PREVENTION -----	RESPONSE -----	CONSOLIDATED -----
Three months Ended March 31, 2002:			
Net Operating Revenues . . . . .	\$ 1,729,000	\$2,281,000	\$ 4,010,000
Operating Income (Loss) . . . . .	105,000	(55,000)	50,000
Identifiable Operating Assets . .	3,034,000	4,002,000	7,036,000
Capital Expenditures . . . . .	16,000	20,000	36,000
Depreciation and Amortization . .	109,000	177,000	286,000
Interest Expense and Other . . . .	45,000	55,000	100,000
Three months Ended March 31, 2003:			
Net Operating Revenues . . . . .	\$ 8,659,000	\$2,272,000	\$ 10,931,000
Operating Income (Loss) . . . . .	2,978,000	1,049,000	4,027,000
Identifiable Operating Assets . .	7,922,000	2,078,000	10,000,000
Capital Expenditures . . . . .	817,000	215,000	1,032,000
Depreciation and Amortization . .	194,000	51,000	245,000
Interest Expense and Other . . . .	337,000	88,000	425,000

For the three-month periods ended March 31, 2002 and 2003, the Company's revenue mix between domestic and foreign sales were (domestic 70%, foreign 30%) and (domestic 80%, foreign 20%), respectively.

### J. SUBSEQUENT EVENTS

From April 1, 2003 through May 13, 2003, the remaining 8,000 shares of the 12,000 total shares issued of the Company's Junior Redeemable Convertible Preferred Stock ("Redeemable Preferred") were converted into 407,842 shares of the Company's common stock.

From April 1, 2003 through May 13, 2003, 1,246 shares of 1,246 total remaining shares of the Company's Series H Cumulative Convertible Preferred Stock ("Series H Preferred Stock") were converted into 166,113 shares of the Company's common stock. The converted Series H Preferred Stock conversion included dividends which were paid in kind of 221 shares of Series H Preferred Stock.

From April 1, 2003 through May 13, 2003, there were 1,598,026 shares of common stock issued under various stock option plans and 7,146,344 shares of common stock issued from the exercise of warrants.

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

### FORWARD-LOOKING STATEMENTS

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The Private Securities Litigation Reform Act of 1995 provides safe harbor provisions for forward-looking information. Forward-looking information is based on projections, assumptions and estimates, not historical information. Some statements in this Form 10 - Q are forward-looking and use words like "may," "may not," "believes," "do not believe," "expects," "do not expect," "do not anticipate," and other similar expressions. We may also provide oral or written forward-looking information on other materials we release to the public. Forward-looking information involves risks and uncertainties and reflects our best judgment based on current information. Our results of operations can be affected by inaccurate assumptions we make or by known or unknown risks and uncertainties. In addition, other factors may affect the accuracy of our forward-looking information. As a result, no forward-looking information can be guaranteed. Actual events and results of operations may vary materially.

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While it is not possible to identify all factors, we face many risks and uncertainties that could cause actual results to differ from our forward-looking statements including those contained in this 10-Q, our press releases and our Forms 10-Q, 8-K and 10-K filed with to the United States Securities and Exchange Commission. We do not assume any responsibility to publicly update any of our forward-looking statements regardless of whether factors change as a result of new information, future events or for any other reason.

### OVERVIEW

On January 1, 2001, the Company redefined the segments in which it operates as a result of the discontinued operations of ITS and Baylor business operations and further redefined the segments during 2002, as a result of the decision to discontinue its Abasco and Special Services business operations. The current segments are Prevention and Response. Intercompany transfers between segments were not material. The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies. For purposes of this presentation, general and corporate expenses have been allocated between segments on a pro rata basis based on revenue. ITS, Baylor, Abasco and Special Services are presented as discontinued operations in the condensed consolidated financial statements and are therefore excluded from the segment information for all periods presented.

The Prevention segment consists of "non-event" services that are designed to reduce the number and severity of critical well events to oil and gas operators. The scope of these services include training, contingency planning, well plan reviews, services associated with the Company's Safeguard programs and services in conjunction with the WELLSURE(R) risk management program. All of these services are designed to significantly reduce the risk of a well blowout or other critical response event.

The Response segment consists of personnel and equipment services provided during an emergency response such as a critical well event or a hazardous material response. These services are designed to minimize response time and damage while maximizing safety. Response revenues typically provide high gross profit margins.

### AMERICAN STOCK EXCHANGE LISTING

The American Stock Exchange ("AMEX") by letter dated March 15, 2002, required the Company to submit a reasonable plan to regain compliance with AMEX's continued listing standards by December 31, 2002. On April 15, 2002, the Company submitted a plan that included interim milestones that the Company would be required to meet to remain listed. AMEX subsequently notified the Company that its plan had been accepted; however, on June 28, 2002, the Company

submitted an amendment to the plan to take into account, among other things, certain restructuring initiatives that the Company had undertaken. The Company has not been advised by AMEX whether or not it approved the June 28, 2002, amended plan. Since submitting the amended plan, the Company has been actively pursuing alternatives that would allow it to fulfill the objectives outline in the amended plan. However, the Company does not, at this time, have any prospects or commitments for new financing or the restructuring of its existing obligations that, if successfully completed, would result in compliance with AMEX's continued listing standards.

AMEX may institute immediate delisting proceedings as a consequence of the Company's failure to achieve compliance its continued listing standards. AMEX recently requested that the Company submit a letter requesting that the AMEX grant the company an additional two quarters to attain compliance as a consequence of recent business improvements. The Company is preparing such a request.

AMEX continued listing standards require that listed companies maintain stockholders' equity of \$2,000,000 or more if the Company has sustained operating losses from continuing operations or net losses in two of its three most recent fiscal years or stockholders equity of \$4,000,000 or more if it has sustained operating losses from continuing operations or net losses in three of its four most recent fiscal years. Further, the AMEX will normally consider delisting companies that have sustained losses from continuing operations or net losses in their five most recent fiscal years or that have sustained losses that are so substantial in relation to their operations or financial resources, or whose financial condition has become so impaired, that it appears questionable, in the opinion of AMEX, as to whether the company will be able to continue operations or meet its obligations as they mature.

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#### CRITICAL ACCOUNTING POLICIES

In response to the SEC's Release No. 33-8040, "Cautionary Advice Regarding Disclosure about Critical Accounting Policies," the Company has identified the accounting principles which it believes are most critical to the reported financial status by considering accounting policies that involve the most complex or subjective decisions or assessment. The Company identified its most critical accounting policies to be those related to revenue recognition, allowance for doubtful accounts and income taxes.

Revenue Recognition - Revenue is recognized on the Company's service contracts primarily on the basis of contractual day rates as the work is completed. On a small number of turnkey contracts, revenue may be recognized on the percentage-of-completion method based upon costs incurred to date and estimated total contract costs. Revenue and cost from equipment sales is recognized upon customer acceptance and contract completion.

Contract costs include all direct material and labor costs and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and depreciation costs. General and administrative costs are charged to expense as incurred. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined.

The Company recognizes revenues under the WELLSURE(R) program as follows: (a) initial deposits for pre-event type services are recognized ratably over the life of the contract period, typically twelve months (b) revenues and billings for pre-event type services provided are recognized when the insurance carrier has billed the operator and the revenues become determinable and (c) revenues



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and billings for contracting and event services are recognized based upon predetermined day rates of the Company and sub-contracted work as incurred.

Allowance for Doubtful Accounts - The Company performs ongoing evaluations of its customers and generally does not require collateral. The Company assesses its credit risk and provides an allowance for doubtful accounts for any accounts which it deems doubtful of collection.

Income Taxes - The Company accounts for income taxes pursuant to the SFAS No. 109 "Accounting For Income Taxes," which requires recognition of deferred income tax liabilities and assets for the expected future tax consequences of events that have been recognized in the Company's financial statements or tax returns. Deferred income tax liabilities and assets are determined based on the temporary differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities and available tax carry forwards.

### RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the unaudited condensed consolidated financial statements and notes thereto and the other financial information included in this report and contained in the Company's periodic reports previously filed with the SEC.

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Information concerning operations in different business segments for the three months ended March 31, 2002 and 2003 is presented below. Certain reclassifications have been made to the prior periods to conform to the current presentation.

	THREE MONTHS ENDED MARCH 31,	
	2002	2003
	-----	-----
<b>REVENUES</b>		
Prevention . . . . .	\$1,729,000	\$ 8,659,000
Response . . . . .	2,281,000	2,272,000
	-----	-----
	\$4,010,000	\$10,931,000
	-----	-----
<b>COST OF SALES</b>		
Prevention . . . . .	\$ 416,000	\$ 3,308,000
Response . . . . .	953,000	655,000
	-----	-----
	\$1,369,000	\$ 3,963,000
	-----	-----
<b>OPERATING EXPENSES (1)</b>		
Prevention . . . . .	\$ 806,000	\$ 1,516,000
Response . . . . .	820,000	343,000
	-----	-----
	\$1,626,000	\$ 1,859,000
	-----	-----
<b>SELLING, GENERAL AND ADMINISTRATIVE EXPENSES (2)</b>		
Prevention . . . . .	\$ 293,000	\$ 663,000
Response . . . . .	386,000	174,000
	-----	-----

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	\$ 679,000	\$ 837,000
	-----	-----
DEPRECIATION AND AMORTIZATION (3)		
Prevention . . . . .	\$ 109,000	\$ 194,000
Response . . . . .	177,000	51,000
	-----	-----
	\$ 286,000	\$ 245,000
	-----	-----
OPERATING INCOME (LOSS)		
Prevention . . . . .	\$ 105,000	\$ 2,978,000
Response . . . . .	(55,000)	1,049,000
	-----	-----
	\$ 50,000	\$ 4,027,000
	-----	-----