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UNIFAB INTERNATIONAL INC  
Form 10-Q  
January 28, 2005

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 Period Ended September 30, 2004

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 0-29416

UNIFAB International, Inc.

-----  
(Exact name of registrant as specified in its charter)

Louisiana

72-1382998

-----  
(State or other jurisdiction or  
incorporation or organization)

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

5007 Port Road  
New Iberia, LA

70560

-----  
(Address of principal executive offices)

-----  
(Zip Code)

(337) 367-8291

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

Not applicable

-----  
(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 periods 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 Securities and Exchange Act of 1934)  
Yes  No

Common Stock, \$0.01 Par Value--8,997,899 shares outstanding as of January 24, 2005.

UNIFAB INTERNATIONAL, INC.

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UNIFAB INTERNATIONAL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS  
(Unaudited)

	SEPTEMBER 2004 ----- (IN THOU
Assets	
Current assets:	
Cash and cash equivalents	\$ 1
Accounts receivable, net	3,7
Costs and estimated earnings in excess of billings on uncompleted contracts	2
Income tax receivable	
Prepaid expenses and other assets	2
Assets of discontinued operations	5,3
	-----
Total current assets	9,8

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Property, plant and equipment, net	16,1
Other assets	1,5
	-----
Total assets	\$ 27,5
	=====
Liabilities and shareholders' equity (deficit)	
Current liabilities:	
Accounts payable	\$ 1,9
Billings in excess of costs and estimated earnings on uncompleted contracts	9
Accrued liabilities	2,1
Contract loss reserves	
Notes payable to Midland	2,6
Current maturities of long-term debt	7,9
Liabilities of discontinued operations	2
	-----
Total current liabilities	15,9
Long-term debt, less current maturities	
Secured, subordinated notes payable	6,8
Secured, subordinated, convertible debenture, net of unamortized discount of \$1,896 and \$2,931, respectively	6,0
	-----
Total liabilities	28,8
Commitments and contingencies (Note 8)	
Shareholders' equity (deficit):	
Preferred stock, no par value, 5,000 shares authorized, no shares outstanding	
Common stock, \$0.01 par value, 150,000,000 shares authorized, 8,997,899 and 8,201,899 shares outstanding, respectively	
Additional paid-in capital	64,8
Accumulated deficit	(66,2)
	-----
Total shareholders' equity (deficit)	(1,2)
	-----
Total liabilities and shareholders' equity (deficit)	\$ 27,5
	=====

See accompanying notes.

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UNIFAB INTERNATIONAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

	THREE MONTHS ENDED SEPTEMBER 30		NINE M
	2004	2003	2004
	-----	-----	-----
	(In thousands except per sha		
Revenue.....	\$ 7,744	\$ 10,312	\$ 23,0
Cost of revenue.....	8,080	11,356	23,1
	-----	-----	-----
Gross loss.....	(336)	(1,044)	(

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Selling, general and administrative expense.....	458	587	1,8
	-----	-----	-----
Loss from operations.....	(794)	(1,631)	(1,8
Other income (expense):			
Interest expense.....	(1,216)	(489)	(2,2
Interest income.....	890	4	8
	-----	-----	-----
Loss from continuing operations before income taxes..	(1,120)	(2,116)	(3,2
Income tax benefit.....	2,212	-	2,2
	-----	-----	-----
Income (loss) from continuing operations.....	1,092	(2,116)	(1,0
Discontinued operations			
Loss from operation of discontinued process systems segment.....	(149)	(458)	(1,5
Loss from operation of discontinued drilling rig fabrication segment.....	(221)	(1,068)	(3,6
Income tax benefit.....	-	-	
	-----	-----	-----
Loss on discontinued operations.....	(370)	(1,526)	(5,1
	-----	-----	-----
Net income (loss).....	\$ 722	\$ (3,642)	\$ (6,2
	=====	=====	=====
Basic and diluted income (loss) per share from continuing operations.....	\$ 0.13	\$ (0.26)	\$ (0.
	=====	=====	=====
Basic and diluted loss per share from discontinued operations.....	\$ (0.04)	\$ (0.18)	\$ (0.
	=====	=====	=====
Basic and diluted income (loss) per share.....	\$ 0.09	\$ (0.44)	\$ (0.
	=====	=====	=====
Basic and diluted weighted average shares outstanding.....	8,235	8,193	8,2
	=====	=====	=====

(a) All earnings (loss) per share amounts and weighted average number of shares outstanding have been restated to give effect to a one-for-ten reverse stock split effected on August 3, 2003

See accompanying notes.

UNIFAB INTERNATIONAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

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### CASH FLOWS FROM OPERATING ACTIVITIES

Net loss

Adjustments to reconcile net loss to net cash provided by (used in) operating activities:

Depreciation

Amortization of discount on secured, subordinated convertible debenture

Write off of unamortized discount on debentures converted

Provision for doubtful accounts

Loss from discontinued operations

Changes in operating assets and liabilities, net of discontinued operations:

Accounts receivable

Net costs and estimated earnings in excess of billings and billings in excess of costs and estimated earnings on uncompleted contracts

Prepaid expenses and other assets

Reduction in valuation allowance related to income tax carryback refund received

Accounts payable and accrued liabilities

Net cash provided by (used in) operating activities

Investing activities:

Purchases of equipment

Proceeds from sale of equipment

Collections on notes receivable

Net cash provided by (used in) investing activities

Financing activities:

Proceeds from notes payable to Midland

Payments of notes payable to Midland

Net change in other borrowings

Proceeds from exercise of options

Net cash provided by (used in) financing activities

Net change in cash and cash equivalents

Cash and cash equivalents at beginning of period

Cash and cash equivalents at end of period

Supplemental disclosure of cash flow information:

Cash paid (received) during the period for:

Income taxes (refunded), net

Interest paid, net of capitalized interest

Interest received

Non cash activities:

Midland conversion of debenture into shares of common stock (Note 2)

See accompanying notes.

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UNIFAB INTERNATIONAL, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

SEPTEMBER 30, 2004

### 1. DESCRIPTION OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

UNIFAB International, Inc. (the Company) fabricates and assembles jackets, decks, topside facilities, quarters buildings, drilling rigs and equipment for installation and use offshore in the production, processing and storage of oil and gas. Through a wholly-owned subsidiary, Allen Process Systems, LLC, the Company designs and manufactures specialized process systems such as oil and gas separation systems, gas dehydration and treatment systems, and oil dehydration and desalting systems, and other production equipment related to the development and production of oil and gas reserves. Compression Engineering Services, Inc. (CESI), a division of Allen Process Systems, LLC, rents compressors. The Company's main fabrication facilities are located at the Port of Iberia in New Iberia, Louisiana. Through a wholly-owned subsidiary, Rig Port Services, LLC, the Company has provided repair, refurbishment and conversion services for oil and gas drilling rigs at its deep-water facility in Lake Charles, Louisiana. As more fully described below, during the quarter ended September 30, 2004, the Company has entered into a plan to dispose of assets and facilities related to its process systems design and manufacture and its drilling rig fabrication segments. As a result of entering into these plans, the operations of the process systems and rig fabrication segments have been accounted for as discontinued operations.

The operating cycle of the Company's contracts is typically less than one year, although some large contracts may exceed one year's duration. Assets and liabilities have been classified as current and noncurrent under the operating cycle concept whereby all contract-related items are regarded as current regardless of whether cash will be received within a 12-month period. At September 30, 2004, it was anticipated that substantially all contracts in progress, and receivables associated therewith, would be completed and collected within a 12-month period.

The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. Significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation have been included. Operating results for the three- and nine-month periods ended September 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004.

These financial statements should be read in conjunction with the financial statements and footnotes thereto for the year ended December 31, 2003 included in the Company's Annual Report on Form 10-K.

Certain amounts previously reported have been reclassified to conform to the presentation at September 30, 2004.

## 2. CURRENT MATTERS

## GOING PRIVATE TRANSACTION

On October 6, 2004, the Company announced that Midland Fabricators and Process Systems, LLC, the owner of 90.1% of the outstanding common shares of the Company, intends to take the Company private pursuant to the Louisiana short form merger law. Since the statute permits the holder of 90% interest in a Louisiana corporation to use this type of merger to cash out other shareholders, the transaction requires no action on the part of the Company's board of directors or shareholders. Midland will pay \$0.20 per share to all other shareholders of the Company. As part of the merger transaction, shareholders who are not willing to accept the merger price will have the right to exercise their dissenter's rights under Louisiana law. On September 30, 2004, Midland converted \$2.7 million of its convertible debenture into 771,000 shares of the Company's common stock at a conversion price of \$3.50 per share, which resulted in Midland increasing its ownership to 90.1% of the outstanding common stock of the Company. This conversion resulted in additional interest expense of \$643,000 during the quarter related to the write off of the unamortized discount on the debentures that were converted.

## OPERATING LOSSES AND DISCONTINUED OPERATIONS

Prior to and since the initiation of the Midland Recapitalization and Investment Transaction in April 2002, described more fully below, the Company has been incurring losses from operations. In response to this situation, the Company has eliminated noncore businesses and excess facilities, reduced overhead and restructured its management team and operations in an effort to return to profitability. In the three- and nine-month periods ended September 30, 2004, the Company incurred a net loss from continuing operations before income taxes of \$1.1 million and \$3.3 million, respectively. Management has initiated a plan to sell the rig fabrication facility and the process systems fabrication facility. Losses from operations of the discontinued process systems segment were \$149,000 and \$1.5 million, respectively, for the same periods. Losses from operation of the discontinued rig fabrication segment were \$221,000 and \$3.6 million, respectively for the same periods. The nine-month period ended September 30, 2004 includes a charge of \$260,000 related to goodwill associated with the Company's Compression Engineering business unit, which is included in the process systems segment, and which was recorded in the quarter ended March 31, 2004. During the first quarter of 2004 and as part of the Company's ongoing evaluation and reorganization of operations, the Company decided to suspend engineering and maintenance operations related to compressors, including compressors being rented from the Company. Included in the net loss from continuing operations before income taxes for the three- and nine-month periods ended September 30, 2004 are selling, general and administrative expenses of \$458,000 and \$1.8 million, respectively, and interest expense of \$1.2 million and \$2.3 million, respectively. Current pricing for the Company's services and the level of utilization of the Company's main fabrication facilities have not resulted in operating profits sufficient to cover these costs.

Operations at the Company's fabrication facility in Lake Charles, Louisiana throughout the first three quarters of 2004 related to one significant project at the facility, which was completed in April 2004. In the three-month period ended September 30, 2004, this facility produced an operating loss of \$220,000. During the nine-month period ended September 30, 2004, the facility produced revenue of \$3.8 million and an operating loss of \$303,000. Upon completion of the project referred to above, there was no backlog for the facility, and as a result management decided to temporarily idle this facility.

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The Company had received an offer to acquire the facility for \$2.5 million in cash and notes. Based on the current state of the drilling rig market, the low business level related to projects that could be placed at the facility, and the offer received to acquire the facility, the Company reduced the carrying value of the facility to \$2.5 million and recorded an impairment loss on these assets of \$3.3 million in the second quarter of 2004. During the September 2004 quarter, these negotiations ceased and the Company engaged a real estate broker and placed the facility for sale by closed bid auction held on November 18, 2004. The Company is currently negotiating the final documents to sell the facility, which will allow the recovery of the recorded value of the facility.

The Company recovered an income tax carryback refund of \$2.2 million plus interest of \$890,000 during the September quarter upon completion of an IRS review. This refund was not previously anticipated fully, pending the completion of this IRS review. The funds were used to pay down amounts owed to Midland. The refund resulted in the Company recognizing income tax benefit of \$2.2 million. Previously, the Company had recorded a valuation reserve against all tax net operating losses

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available for carryback refund treatment.

### FINANCIAL RELIANCE ON MIDLAND

The Company renewed the Credit Agreement in November 2003, with Midland's continuing guarantee, and extended the maturity to January 31, 2005. As a result, the amounts outstanding under the Credit Agreement were classified as noncurrent in the December 31, 2003 balance sheet and are classified as current in the September 30, 2004 balance sheet. Under an informal arrangement with the Company, Midland has agreed from time to time to provide financial support and funding for working capital or other needs at Midland's discretion. During the nine months ended September 30, 2004, Midland advanced \$12.1 million to the Company for working capital, of which \$2.6 million remains unpaid at September 30, 2004 and is classified as a current liability. At December 31, 2003, Midland was owed \$5.9 million related to advances under this informal arrangement, which was classified as a current liability. As a result of classifying the amounts outstanding related to the Credit Agreement and the informal arrangement with Midland, the Company has working capital deficits of \$6.1 million at September 30, 2004 and \$1.3 million at December 31, 2003. The liquidity afforded by these advances from Midland was necessary for the Company to meet its obligations and fund operations. At December 31, 2002, Midland provided a standby letter of credit to a customer in support of a contract, which was completed during the March 2004 quarter. The letter of credit expired in March 2004. Since that time, the Company has been awarded contracts totaling \$13.1 million, which have required a financial guarantee or letter of credit from Midland. Management believes that additional funds available from Midland under the informal arrangement described above are necessary to fund its working capital needs and planned capital expenditures for the next 12 months and that guarantees from Midland are necessary to win contract awards. However, the Company has no control over whether Midland will provide additional funding or financial guarantees in the future and does not know whether such additional funding or financial guarantees will be available from Midland as the Company requires them. If Midland does not provide such additional funding or financial guarantees to the Company when needed in the future, the Company will not be able to satisfy its working capital requirements and meet its obligations, including obligations under the Credit Agreement, in the ordinary course of business, or could be unable to qualify for contract awards. The Company requires the continued support from Midland until such time as it has sustained profitable operations and its financial condition is stable and no longer



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requires this support.

If the Company is unsuccessful in its efforts to return to profitability or obtain necessary capital from Midland as needed, it will not be able to meet its obligations in the ordinary course of business and remain a going concern. The financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

### 3. MIDLAND RECAPITALIZATION AND INVESTMENT TRANSACTION

In April 2002, the Company entered into an agreement with Midland Fabricators and Process Systems, LLC ("Midland") as a result of which, among other things, Midland acquired the rights of the Company's lenders under the Company's Senior Secured Credit Agreement. On August 13, 2002, pursuant to the agreement with Midland, Midland exchanged \$24.1 million outstanding under the Company's Senior Secured Credit Agreement and \$5.6 million in acquired claims of unsecured creditors for 738 shares of preferred stock, a secured subordinated convertible debenture in the amount of \$10.7 million and two secured subordinated notes which total in the aggregate \$6.8 million. The debenture is convertible into the Company's common stock at a price of \$3.50 per share on a post reverse split basis. Midland's 738 shares of preferred stock converted automatically into a total of 7,380,000 shares of the Company's common stock on August 1, 2003, the date the shareholders authorized additional shares of common stock. The Company also recorded additional paid in capital on the transaction of \$3.7 million resulting from the discount recorded on the secured subordinated convertible debenture, and capital contributions of \$680,000 resulting from forgiveness by Midland of penalties accrued under the Senior Secured Credit Agreement and \$914,000 resulting from partial forgiveness of the unsecured creditor claims acquired by Midland. Further, \$675,000 of the amount the Company owed Midland under the Company's Senior Secured Credit Agreement was cancelled in exchange for the assignment to Midland of certain accounts.

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### 4. CONTRACTS IN PROGRESS

Information pertaining to contracts in progress at September 30, 2004 and December 31, 2003 consisted of the following:

	SEPTEMBER 30, 2004	DECEMBER 2003
----- (In thousands)		
Costs incurred on uncompleted contracts	\$ 19,027	\$ 48
Estimated loss	(146)	(2)
	-----	-----
	18,881	46
Less billings to date	(19,546)	(45)
	-----	-----
	\$ (665)	\$
	=====	=====
Included in the accompanying balance sheets under the following captions:		
Costs and estimated earnings in excess of billings on		
uncompleted contracts	\$ 299	\$ 1

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Billings in excess of costs and estimated earnings on uncompleted contracts	(964)	-----
	\$ (665)	=====
		-----
		=====

Accounts receivable includes unbilled receivables and retainages, respectively, of \$10,000 and \$11,000 at September 30, 2004, and of \$138,000 and \$10,000 at December 31, 2003.

The Company had contract loss reserves of \$8,000 at September 30, 2004 and \$697,000 at December 31, 2003. At September 30, 2004, this reserve relates to one platform fabrication contract that is substantially complete. The reserve for this contract at December 31, 2003 was \$9,000. Substantially all of the contract reserves recorded at December 31, 2003 were realized in the nine-month period ended September 30, 2004.

### 5. CREDIT FACILITY

On November 18, 2002, the Company entered into a Commercial Business Loan Agreement with Whitney National Bank (the "Credit Agreement"), which provides for up to \$8.0 million in borrowings for working capital purposes, including up to \$2.0 million in letters of credit under a revolving credit facility. The Credit Agreement is guaranteed by Nassau Holding Company (an affiliate of Midland), the subsidiaries of Unifab, and the principle members of Midland, and is secured by the assets of Universal Fabricators, LLC and Allen Process Systems, LLC, both wholly-owned subsidiaries of the Company. At September 30, 2004, the Company had \$7.9 million in borrowings and letters of credit totaling \$3,000 outstanding under the Credit Agreement. Borrowings under the Credit Agreement bear interest at Libor plus 1.75% or the Prime rate (3.420% at September 30, 2004), at the Company's discretion. The Credit Agreement matures January 31, 2005. The Company expects to renew its Credit Agreement under the same general terms and with the continuing guarantee of Nassau Holding Company.

### 6. INCOME TAXES

The Company provides for income taxes using the liability method in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. As of September 30, 2004, the Company recorded deferred tax assets of \$21.2 million, including \$20.7 million related to net operating loss carryforwards which, if not used, expire in years 2020 through 2024. The ability of the Company to utilize net operating loss carryforwards is limited on an annual basis because the Midland transaction resulted in a change in control under the current tax regulations. The Company has recorded a valuation allowance of \$18.4 million to offset the deferred tax asset related to the net operating loss carryforward and other deferred tax assets that exceed deferred tax liabilities because the Company believes that it is more likely than not that these deferred tax assets will not be utilized.

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### 7. SHAREHOLDERS' EQUITY (DEFICIT)

#### EARNINGS (LOSS) PER SHARE

In April 2002, the Company entered into an agreement with Midland Fabricators and Process Systems, LLC ("Midland") as a result of which, among other things, Midland acquired the rights of the Company's lenders under the Company's Senior Secured Credit Agreement. On August 13, 2002, pursuant to the

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agreement with Midland, Midland exchanged \$24.1 million outstanding under the Company's Senior Secured Credit Agreement and \$5.6 million in acquired claims of unsecured creditors for 738 shares of our preferred stock, a secured subordinated convertible debenture in the amount of \$10.7 million and two secured subordinated notes which total in the aggregate \$6.8 million. The debenture is convertible into the Company's common stock at a price of \$3.50 per share on a post reverse split basis. Midland's 738 shares of preferred stock converted automatically into a total of 73,800,000 shares of the Company's common stock on August 1, 2003, the date the shareholders authorized additional shares of common stock. The Company also recorded additional paid in capital on the transaction of \$3.7 million resulting from the discount recorded on the secured subordinated convertible debenture, and capital contributions of \$680,000 resulting from forgiveness by Midland of penalties accrued under the Senior Secured Credit Agreement and \$914,000 resulting from partial forgiveness of the unsecured creditor claims acquired by Midland. Further, \$675,000 of the amount the Company owed Midland under the Company's Senior Secured Credit Agreement was cancelled in exchange for the assignment to Midland of certain accounts.

On August 1, 2003, the Company's shareholders approved a one-for-ten reverse stock split of the outstanding shares of the Company's common stock, to be effective immediately after the conversion of Midland's Series A preferred shares. Accordingly, on August 1, 2003, each share of series A preferred stock was converted into 100,000 shares of Unifab common stock and the one-for-ten reverse stock split was effected resulting in Midland holding a total of 7,380,000 common shares after the reverse stock split.

The denominator in the table below includes the common shares related to these Series A Preferred Shares as if they had been converted into shares of common stock on August 13, 2002, the date of the Midland Investment and Recapitalization Transaction. All prior periods weighted average share and option amounts have been restated for the effect of the reverse stock split. Midland's \$10,652,000 convertible debenture is convertible into Unifab common stock at a conversion price of \$3.50 per share on a post reverse split basis, for a total of 3,043,400 shares of common stock. On September 30, 2004, Midland converted \$2,698,500 of the convertible debenture into 771,000 shares of Unifab common stock. Since the conversion price is "out-of-the-money," the remaining shares are anti-dilutive and are not included in the computation of diluted earnings per share during periods when the Company incurs a loss.

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The following table sets forth the computation of basic and diluted earnings (loss) per share giving retroactive effect to the assumed conversion of Midland's 738 shares as of August 13, 2002 and giving effect to the one-for-ten reverse stock split:

	THREE MONTHS ENDED SEPTEMBER 30		NINE MONTHS ENDED
	2004	2003	2004
	(In thousands, except per share data)		
Numerator:			
Net income (loss)	\$ 722	\$ (3,642)	\$ (6,206)
Denominator:			
Weighted average shares of			

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common stock outstanding	8,235	8,193	8,219
Effect of issuance of convertible preferred stock on weighted average shares of common stock	-	-	-
-----			
Denominator for basic and diluted earnings per share - weighted average shares	8,235	8,193	8,219
=====			
Basic and diluted income (loss) per share	\$ 0.09	\$ (0.44)	\$ (0.76)
=====			

Options with an exercise price greater than the average market price of the Company's common stock for the year and options outstanding during years where the Company incurs a net loss are anti-dilutive and, therefore, not included in the computation of diluted earnings per share. During the nine month period ended September 30, 2004, 50,000 options and 6,000 warrants outstanding were anti-dilutive due to the net loss incurred by the Company. During the three month period ended September 30, 2004, these securities were anti-dilutive because the exercise prices of the securities exceeded the price per share of the common stock. During the period ended September 30, 2003, 133,500 options and 6,000 warrants outstanding were anti-dilutive due to the net loss incurred by the Company.

STOCK BASED COMPENSATION

The Company uses the intrinsic value method of accounting for employee-based compensation prescribed by Accounting Principles Board ("APB") Opinion No. 25 and, accordingly, follows the disclosure-only provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation." SFAS No. 123 encourages the use of fair value based method of accounting for compensation expense associated with stock option and similar plans. However, SFAS No. 123 permits the continued use of the intrinsic value based method prescribed by Opinion No. 25 but requires additional disclosures, including pro forma calculations of net earnings and earnings per share as if the fair value method of accounting prescribed by SFAS No. 123 had been applied.

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Had compensation cost for the Company's stock plans been determined based on the fair value at the grant dates consistent with the method of SFAS No. 123, the Company's net income and net income per share amounts would have approximated the following pro forma amounts (in thousands, except per share data):

	THREE MONTHS ENDED SEPTEMBER 30		NINE MONTHS ENDED SEPTEMBER 30	
	2004	2003	2004	2003
-----				
(IN THOUSANDS, EXCEPT PER SHARE DATA)				
Net income (loss), as reported	\$ 722	\$ (3,642)	\$ (6,206)	\$ (6,206)
Add: Total stock-based employee compensation expense included in				

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reported net loss, net of related tax effects	-	-	-	
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	-	(4)	-	
Pro forma net income (loss)	\$ 722	\$ (3,646)	\$ (6,206)	\$ (6,206)
Income (loss) per share				
Basic and diluted, as reported	\$ 0.09	\$ (0.44)	\$ (0.76)	\$ (0.76)
Basic and diluted, pro forma	\$ 0.09	\$ (0.45)	\$ (0.76)	\$ (0.76)
Weighted average fair value of grants	\$ -	\$ -	\$ -	\$ -

Black-Scholes option pricing model assumptions:

	NINE MONTHS ENDED SEPTEMBER 30, 2004	2003
Risk-free interest rate	N/A	1.82%
Volatility factor of the expected market price of UNIFAB stock	N/A	1.072
Weighted average expected life of the option	N/A	2 years
Expected dividend yield	-	-

There were no option grants in the three-month periods ended September 30, 2004 and 2003.

### 8. COMMITMENTS AND CONTINGENCIES

#### LEGAL MATTERS

In addition to the matter described below, the Company is a party to various routine legal proceedings primarily involving commercial claims, workers' compensation claims, and claims for personal injury under the General Maritime Laws of the United States. While the outcome of these legal proceedings and claims cannot be predicted with certainty, management believes that the outcome of such proceedings is not likely to have a material adverse effect on the Company's consolidated financial statements.

In a lawsuit filed against the Company in the 14th Judicial Court in the Parish of Calcasieu, State of Louisiana, Professional Industrial Maintenance, L.L.C., Don E. Spano and Kimberly Spano alleged multiple claims for breach of contract, breach of specific performance, a request for injunction, request for damages, and a request for treble damages and attorney fees for violations of the Louisiana Unfair Trade Practices Act. Mr. Spano was the managing member of Professional Industrial Maintenance, LLC, the company whose assets we acquired in January 1998. The Company filed a counterclaim for recovery of certain amounts paid on behalf of Professional Industrial Maintenance, LLC and Mr. Spano as a result of the transaction. In January 2004, the parties agreed to settle the disputes subject of the lawsuit with full and

final releases for all claims in exchange for a cash payment to the plaintiffs in the amount of \$300,000 and, accordingly, the Company recorded the related liability at December 31, 2003. However, as of the filing of this report, the details of the settlement agreement and release have not been finalized, and the Company has not yet made the cash payment.

#### LETTERS OF CREDIT

In the normal course of its business activities, the Company is required to provide letters of credit to secure performance. At September 30, 2004, letters of credit totaling \$3,000 were outstanding under the Credit Agreement.

#### EMPLOYMENT AGREEMENTS

The Company has an employment agreement with one of its former officers. This agreement terminates on August 18, 2006. The minimum annual compensation commitment by the Company under this agreement is \$60,000.

#### LEASES

The Company leases land, upon which portions of its structural fabrication and process equipment fabrication facilities in New Iberia are located, under noncancelable operating leases. The leases expire in 2013 for the structural fabrication facility with one 10-year renewal option, and in 2006 for the process equipment facilities with one 10-year renewal option. The Company also leases its facility in Lake Charles under a noncancelable operating lease. The lease expires in 2005 and has two five-year renewal options. At September 30, 2004, the Company had approximately \$9.5 million in aggregate lease commitments under operating leases, of which \$0.7 million is payable during the next twelve months.

#### 9. RELATED PARTY TRANSACTIONS

Under an informal arrangement with the Company, Midland has agreed to provide financial support and funding for working capital or other needs at Midland's discretion, from time to time. During the nine month period ended September 30, 2004, Midland advanced amounts to the Company for working capital, which were repaid and readvanced from time to time as needed. At September 30, 2004, \$2,600,000 was outstanding and owed to Midland. The liquidity afforded by these advances from Midland was necessary for the Company to meet its obligations and fund operations. However, the Company has no control over whether Midland will provide additional funding in the future and does not know whether such additional funding will be available from Midland as the Company requires it. If Midland does not make available such additional funding to the Company when needed in the future, the Company would not be able to meet its obligations, including obligations under the Credit Agreement, in the ordinary course of business. The Company requires the continued support from Midland until such time as it has sustained profitable operations and its financial condition is stable and no longer requires this support.

The Company provides health care benefits to its employees under a plan that covers the employees of companies owned by Nassau Holding Company, an affiliate of Midland ("Nassau"), including the employees of Nassau. In the nine-month periods ended September 30, 2004 and 2003, the Company incurred costs of approximately \$1,477,000 and \$1,319,000, respectively, for coverage under this plan.

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Midland provides accounting information system and reporting services to the Company, including maintaining computer hardware and software to process financial information and produce management reports, processing data associated with those reports, assisting in report design and preparation, processing operating and payroll checks, consulting assistance with the design and implementation of financial reporting systems, and other related services. Included in general and administrative expenses for the three- and nine-month periods ended September 30, 2004 and 2003 are \$45,000 and \$135,000, respectively, related to these services. At September 30, 2004, all amounts relative to these services had been paid.

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In the three-month period ended September 30, 2004, the Company had no contracts with any affiliates of Midland and had no uncollected receivables related to prior contract activity with any affiliates of Midland. In the nine-month period ended September 30, 2003, the Company executed several contracts with Ridgelake Energy, Inc. to fabricate a platform and design and manufacture process equipment. The total value of these contracts was \$6.9 million. In the three- and nine-month periods ended September 30, 2003, \$1.7 million and \$6.9 million, respectively, in revenue, and \$278,000 and \$920,000, respectively, in gross profit was recognized related to these contracts. At September 30, 2003, the Company had \$579,000 receivable from Ridgelake Energy, Inc. related to these contracts. Ridgelake Energy, Inc. is owned and controlled by Mr. William A. Hines, Chairman of our Board of Directors, and his family.

### 10. INDUSTRY SEGMENT INFORMATION

Effective January 1, 2003, as a result of the Midland Recapitalization and Investment transaction, management has evaluated the changed organizational and reporting structure and has concluded that the Company operates three reportable segments: the platform fabrication segment, the process systems segment and the drilling rig fabrication segment. The platform fabrication segment fabricates and assembles platforms and platform components for installation and use offshore in the production, processing and storage of oil and gas. The process systems segment designs and manufactures specialized process systems and equipment related to the development and production of oil and gas reserves. The drilling rig fabrication segment provides fabrication services for new construction and repair of drilling rigs. The accounting policies of the segments are the same as those described in the summary of significant accounting policies, except that income taxes are accounted for on a consolidated basis and deferred tax assets are managed as corporate assets and are not recorded in the operating segments. The Company evaluates performance based on segment income, which is defined as revenue less cost of revenue and selling, general and administrative expense allocated to the operating segment. The Company does not allocate interest expense to the operating segments. Unallocated overhead consists primarily of corporate general and administrative costs that the Company does not allocate to the operating segments. The Company accounts for intersegment sales at fixed labor rates and at cost for materials and other costs. Intersegment sales are not intended to represent current market prices for the services provided.

The following tables show information about the revenue, profit or loss, depreciation and amortization, assets and expenditures for long-lived assets of each of the Company's reportable segments for the three- and nine-month periods ended September 30, 2004 and 2003. Segment assets do not include intersegment receivable balances as the Company believes inclusion of such assets would not be meaningful. Segment assets are determined by their location at period end. Some assets that pertain to the segment operations are recorded on corporate books, such as prepaid insurance. These assets have been allocated to the

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segment in a manner that is consistent with the methodology used in recording the segment's expense.

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	THREE MONTHS ENDED SEPTEMBER 30		NINE MONTHS EN SEPTEMBER 30
	2004	2003	2004
	-----		
	(IN THOUSANDS)		
Segment revenue:			
Platform fabrication	\$ 7,744	\$ 10,312	\$ 23,095
Process systems (b)	1,727	3,068	5,890
Drilling rig fabrication (b)	107	2,475	3,803
Intersegment eliminations	-	-	-
	-----	-----	-----
	\$ 9,578	\$ 15,855	\$ 32,788
	=====	=====	=====
Segment income (loss):			
Platform fabrication	\$ (390)	\$ (1,207)	\$ (553)
Process systems (b)	(124)	(351)	(1,275)
Drilling rig fabrication (a) (b)	(220)	(1,004)	(3,522)
	-----	-----	-----
	(734)	(2,562)	(5,350)
Interest expense	(1,216)	(489)	(2,293)
Interest income	890	-	898
Unallocated corporate overhead	(430)	(591)	(1,673)
	-----	-----	-----
Loss before income tax	\$ (1,490)	(3,642)	\$ (8,418)
	=====	=====	=====

(a) Included in the Drilling rig fabrication segment loss for the nine month period ended September 30, 2004 is an impairment loss of \$3.3 million on the Lake Charles facility

(b) The Company has initiated a plan to sell the facilities related to the process systems segment and the drilling rig fabrication segment and discontinue these segments

Total assets of the Company by segment are as follows as of September 30, 2004 and December 31, 2003:

	SEPTEMBER 30, 2004	DECEMBER 31, 2003
	-----	
	(IN THOUSANDS)	
Segment assets at end of period:		
Platform fabrication	\$ 20,227	\$ 22,500
Process systems	3,978	6,827
Drilling rig fabrication	2,702	9,746
	-----	-----
	26,907	39,073
Corporate	620	1,146



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\$ 27,527	\$ 40,219
=====	=====

11. COMPREHENSIVE INCOME

The following is a summary of the Company's comprehensive income (loss) for the three- and nine- month periods ended September 30, 2004 and 2003.

	THREE MONTHS ENDED SEPTEMBER 30		NINE MONTHS ENDED SEPTEMBER 30	
	2004	2003	2004	2003
	-----			
	(IN THOUSANDS)			
Net income (loss)	\$ 722	\$ (3,642)	\$ (6,206)	\$ (6,263)
Currency translation adjustment	-	(5)	-	36
	-----	-----	-----	-----
	\$ 722	\$ (3,647)	\$ (6,206)	\$ (6,227)
	=====	=====	=====	=====

12. DISCONTINUED OPERATIONS

During the September 2004 quarter, the Company initiated a plan to sell the fabrication facilities related to the process systems segment and rig fabrication segment and discontinue operations in those segments.

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Revenues and loss from discontinued operations were:

	THREE MONTHS ENDED SEPTEMBER 30		NINE MONTHS ENDED SEPTEMBER 30	
	2004	2003	2004	2003
	-----			
	(IN THOUSANDS)			
Revenue from process systems segment	\$ 1,727	\$ 3,068	\$ 5,890	\$ 10,018
Revenue from drilling rig fabrication segment	107	2,475	3,803	2,742
Loss from process systems segment	\$ (124)	\$ (351)	\$ (1,275)	\$ (763)
Loss from drilling rig fabrication segment	(220)	(1,004)	(3,522)	(1,326)

Assets and liabilities from discontinued operations were:

SEPTEMBER 30, 2004	DECEMBER 31, 2003
-----	
(IN THOUSANDS)	

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Process systems segment assets (a)	\$ 2,695	\$ 4,486
Drilling rig fabrication segment assets (b)	2,691	9,488
Process systems segment liabilities	\$ 218	\$ 630
Drilling rig fabrication segment liabilities	11	1,609

- (a) Assets from discontinued operations exclude process systems segment assets related to rental compressor operations of \$1,271,000 and \$2,193,000 at September 30, 2004 and December 31, 2003, respectively. The Company continues to rent these compressors.
- (b) The Company recognized an impairment charge of \$3,307,000 on drilling rig fabrication segment assets in the three-month period ended June 30, 2004.

Significant components of assets of discontinued operations at September 30, 2004 were as follows:

	PROCESS SYSTEMS ASSETS	DRILLING RIG FABRICATION ASSETS
----- (IN THOUSANDS) -----		
Accounts receivable	\$ 647	\$ 189
Costs and earnings in excess of billings	801	-
Property, plant and equipment	1,075	2,500
Other assets	172	2
	-----	-----
Total assets	\$2,695 =====	\$2,691 =====

### 13. SHUT DOWN OF ALLEN PROCESS SYSTEMS LIMITED

On June 12, 2003, at a meeting of the creditors of Allen Process Systems Limited, Mr. Tony Freeman of Tony Freeman & Company, New Maxdov House, Manchester, England was appointed as Liquidator of Allen Process Systems Limited ("APS Limited"), located in London, England, for the purposes of ceasing and voluntarily winding up operations of that company. The Company, as the sole shareholder of APS Limited, ratified Mr. Freeman's appointment. APS Limited was acquired by the Company in June 1998 and has provided engineering and project management services for process systems mainly to Europe and the Middle East. Allen Process Systems, LLC, a wholly owned subsidiary of the Company has provided these services since that time. The Company does not expect that ceasing and winding up operations of APS Limited will have a material impact on the consolidated financial statements of the Company.

### 14. NEW ACCOUNTING PRONOUNCEMENTS

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In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46"). FIN 46 requires that companies that control another entity through interests other than voting interests should consolidate the controlled entity. FIN 46 applies to variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. In December 2003 the FASB issued modifications to FIN 46 ("FIN 46R")

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resulting in multiple effective dates based on the nature as well as the creation date of a variable interest entity. The adoption of FIN 46 did not have a material impact on the Company's consolidated financial position or results of operations because the Company does not believe that the Company has interests that would be considered variable interest entities under FIN 46.

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

The following discussion presents management's discussion and analysis of the Company's financial condition and results of operations and should be read in conjunction with the Consolidated Financial Statements.

#### SUMMARY

During the three- and nine- month periods ended September 30, 2004:

- On October 6, 2004, the Company announced that Midland Fabricators and Process Systems, LLC, the owner of 90.1% of the outstanding common shares of the Company, intends to take the Company private pursuant to the Louisiana short form merger law. Since the statute permits the holder of 90% interest in a Louisiana corporation to use this type of merger to cash out other shareholders, the transaction requires no action on the part of the Company's board of directors or shareholders. Midland will pay \$0.20 per share to all other shareholders of the Company. As part of the merger transaction, shareholders who are not willing to accept the merger price will have the right to exercise their dissenter's rights under Louisiana law.
- The Company has been awarded new work, which has required financial guarantees from Midland, including letters of credit provided by Midland. The Company currently has bids for new work outstanding that has required guarantees from Midland, including letters of credit to be provided by Midland. These guarantees are necessary for the Company to be successful in qualifying for and being awarded new work. The Company has no control over whether Midland will continue to provide these guarantees in the future, as the Company requires them. If Midland does not provide such guarantees in the future, the Company may be unable to qualify for or be successful in winning new work.
- Since the Midland Transaction, Midland has provided financial, operational, and management support to the Company. During the nine-month period ended September 30, 2004, the Company funded operations and capital expenditures through advances from Midland. At September 30, 2004, the Company had \$2.6 million in advances from Midland and \$7.9 million outstanding under its line of credit, which is guaranteed by Midland. The liquidity afforded by these advances from Midland was necessary for the Company to meet its obligations and fund operations. However, the Company has no control over whether Midland will provide additional funding in the future and does not know whether such additional funding will be available from Midland as the Company requires it. If Midland does not provide such additional funding in the future as the Company requires it, the Company will be unable to meet its obligations, including obligations under its line of credit, in the ordinary course of business.
- Revenue for the three-month period ended September 30, 2004 decreased from the same period last year by 25% to \$7.7 million. In the nine-month period ended September 30, 2004, revenue

decreased 16% to \$23.1 million. The platform fabrication segment and the process systems segment decreased relative to the same period last year, which was offset in part by an increase in revenue in the drilling rig fabrication segment. During the quarter ended September 30, 2004, the Company entered into a plan to dispose of the assets and facilities related to its process systems design and manufacture and drilling rig fabrication operations. As a result of entering into these plans, the operations of the process systems segment and the drilling rig fabrication segment have been accounted for as discontinued operations.

- Cost of sales for the three- and nine-month periods ended September 30, 2004 decreased compared to the same periods last year. Cost of sales exceeded revenue in the three- and nine- month periods ended September 30, 2004.
- Selling, general and administrative expenses were reduced by approximately 22% in the three-month period ended September 30, 2004, compared to the same period in 2003, and by approximately 7% in the nine-month period ended September 30, 2004, compared to the same period last year. This was achieved mainly by reducing administrative personnel and other administrative costs over the respective periods.
- The Company received a carryback refund of income taxes in the amount of \$2.2 million in the September 2004 quarter plus interest of \$890,000.
- The Company recorded an impairment charge of \$3.3 million in the June 2004 quarter related to the facility in Lake Charles, Louisiana, which is idle at this time. The charge increased the drilling rig fabrication segment operating loss and reduced the recorded value of the facility to \$2.5 million.
- The Company recorded a charge of \$260,000 related to goodwill associated with the Company's Compression Engineering business unit during the first quarter of 2004, which increased the process systems segment operating loss. As part of the Company's ongoing evaluation and reorganization of operations, the Company suspended engineering and maintenance operations related to compressors, including compressors rented from the Company.
- On August 1, 2003, the shareholders of the Company approved the increase in the number of shares of authorized common stock to 150,000,000 shares. This increase allowed Midland to convert the 738 shares of preferred stock issued in relation to the Midland Investment and Recapitalization transaction into 73,800,000 shares of common stock. The shareholders also approved a one-for-ten reverse stock split, which was effected on August 3, 2003. After giving effect to the one-for-ten reverse stock split, the number of shares of common stock held by Midland was 7,380,000. All earnings (loss) per share amounts and weighted average number of shares outstanding have been restated to give effect to the one-for-ten reverse stock split effected on August 3, 2003.
- On September 30, 2004, Midland converted \$2.7 million of its convertible debenture into 771,000 shares of the Company's common stock at a conversion price of \$3.50 per share, which resulted in

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Midland increasing its ownership to 90.1% of the outstanding common stock of the Company. This conversion resulted in additional interest expense of \$643,000 during the quarter related to the write off of the unamortized discount on the debentures that were converted.

### MIDLAND SUPPORT

Since the Midland Transaction, Midland has provided financial, operational and management support to the Company. Nassau Holding Company (an affiliate of Midland) has guaranteed the Company's Senior Secured Credit Agreement with Whitney National Bank. Under an informal arrangement with the Company, Midland has agreed to provide financial support and funding for working capital or other needs at

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Midland's discretion, from time to time. During the nine months ended September 30, 2004, Midland advanced \$12.1 million to the Company for working capital, of which \$2.6 million remains unpaid at September 30, 2004. From time to time as needed, Midland provides financial guarantees, including letters of credit, in support of contract awards to the Company. Midland provides accounting information system and reporting services to the Company, including maintaining computer hardware and software to process financial information and produce management reports, processing data associated with those reports, assisting in report design and preparation, processing operating and payroll checks, consulting assistance with the design and implementation of financial reporting systems, and other related services. Included in general and administrative expenses for the three- and nine- month periods ended September 30, 2004 and 2003 are \$45,000 and \$135,000, respectively, related to these services. This support was necessary to stabilize the financial position and operations of the Company. The Company will require the continued support from Midland, or another source of working capital until such time as it has sustained profitable operations and its financial condition is stable and no longer requires this support.

### IDENTIFICATION OF OPERATING SEGMENTS

Effective January 1, 2003, as a result of the Midland Recapitalization and Investment transaction, management has evaluated the changed organizational and reporting structure and has concluded that the Company operates three reportable segments: the platform fabrication segment, the process systems segment and the drilling rig fabrication segment. The platform fabrication segment fabricates and assembles platforms and platform components for installation and use offshore in the production, processing and storage of oil and gas. The process systems segment designs and manufactures specialized process systems and equipment related to the development and production of oil and gas reserves. The drilling rig fabrication segment provides fabrication services for new construction and repair of drilling rigs.

### THE MIDLAND TRANSACTION

On August 13, 2002, the Company and Midland Fabricators and Process Systems, LLC closed a transaction under which Midland exchanged \$24.1 million outstanding under the Company's Senior Secured Credit Agreement and \$5.6 million in claims of unsecured creditors for 738 shares of preferred stock, a secured subordinated debenture and two secured subordinated notes in the aggregate amount of \$17.5 million. The debenture, valued at \$10.7 million, is convertible into the Company's common stock at a price of \$3.50 per share on a post-reverse split basis. Midland's preferred stock was converted into a total of 7,380,000 shares of the Company's common stock on August 1, 2003. The Company also

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recorded additional capital contributions on the transaction of \$3.7 million resulting from the discount recorded on the convertible debenture, \$680,000 resulting from forgiveness by Midland of penalties accrued under the Senior Secured Credit Agreement, and \$914,000 resulting from partial forgiveness of unsecured creditor claims acquired by Midland. On November 18, 2002, the Company entered into a Senior Secured Credit Agreement with the Whitney National Bank, which is guaranteed by Nassau Holding Company (an affiliate of Midland), the subsidiaries of Unifab, and the principle members of Midland, in accordance with the terms of the Midland transaction.

### RESULTS OF OPERATIONS

Revenue for the three months ended September 30, 2004 decreased 25% to \$7.7 million from \$10.3 million for the three months ended September 30, 2003. In the nine-month period ended September 30, 2004, revenue decreased 16% to \$23.1 million. Backlog was approximately \$7.0 million and \$7.6 million at September 30, 2004 and December 31, 2003, respectively.

Total direct labor hours worked during the three-month period ended September 30, 2004 at the Company's platform fabrication facility decreased 50% from the levels experienced in the same period last year. For the nine-month period ended September 30, 2004, manhours at the platform fabrication facility were approximately 24% lower than for the same period last year.

Cost of revenue was \$8.1 million and \$23.1 million for the three- and nine-month periods ended September 30, 2004, compared to \$11.3 million and \$27.8 million for the same periods last year. Cost of revenue consists of costs associated with the fabrication process, including direct costs (such as direct labor

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costs and raw materials) and indirect costs that can be specifically allocated to projects (such as supervisory labor, utilities, welding supplies and equipment costs).

Gross profit (loss) for the three months ended September 30, 2004 was (\$336,000) compared to (\$1,044,000) for the same period last year.

Selling, general and administrative expense decreased to \$0.5 million in the three months ended September 30, 2004 and \$1.8 million in the nine months ended September 30, 2004, compared to \$0.6 million and \$2.0 million in the same periods in 2003, respectively. This decrease is mainly due to reduced general and administrative expenses associated with closing underutilized facilities, overall reductions in administrative overhead and employees and the receipt of \$150,000 related to an insurance claim.

Interest expense for the three- and nine-month periods ended September 30, 2004 was higher than the same periods in 2003 due to the higher levels of indebtedness maintained during 2004. Amortization of the discount on the secured, subordinated debenture is being recorded as interest expense. In each of the three-month periods ended September 30, 2004 and 2003, the Company recorded \$130,000 of interest expense related to amortization of the discount on the secured subordinated debenture. In each of the nine-month periods ended September 30, 2004 and 2003, the Company recorded \$390,000 interest expense related to amortization of the discount on the secured subordinated debenture. On September 30, 2004, Midland converted \$2.7 million of its convertible debenture into 771,000 shares of the Company's common stock at a conversion price of \$3.50 per share, which resulted in Midland increasing its ownership to 90.1% of the outstanding common stock of the Company. This conversion resulted in additional interest expense of \$643,000 during the quarter related to the

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write off of the unamortized discount on the debentures that were converted.

The Company recovered an income tax carryback refund of \$2.2 million plus interest of \$890,000 during the September quarter upon completion of an IRS review. This refund was not previously anticipated fully, pending the completion of this IRS review. The refund resulted in the Company recognizing income tax benefit of \$2.2 million. Previously, the Company had recorded a valuation reserve against all tax net operating losses available for carryback refund treatment. No net income tax benefit was recognized on the net loss recorded in the three-month periods ended September 30, 2004 and 2003. In accordance with FAS 109, the Company considered that it had a cumulative pre-tax loss for recent years, which must be carried forward and used to offset future taxable income. The ability of the Company to utilize net operating loss carryforwards is also limited on an annual basis because the transaction with Midland resulted in a change in control under tax regulations. The Company has recorded a valuation allowance to offset the deferred tax asset related to the net operating loss carryforward and other deferred tax assets that exceed net deferred tax liabilities of the Company at September 30, 2004. The valuation allowance reflects the Company's judgment that it is more likely than not that these deferred tax assets will not be realized. Management will continue to assess the adequacy of the valuation allowance on a quarterly basis.

Loss from operation of discontinued process systems segment was \$149,000 and \$1.5 million in the three- and nine- month periods ended September 30, 2004, respectively. Loss from operation of discontinued process systems segment was \$458,000 and \$1.3 million, respectively, in the same periods in 2003. In the three-month period ended March 31, 2004 the Company recorded an impairment charge of \$260,000 related to goodwill associated with the Company's Compression Engineering business unit. Also included in other operating expenses in the nine-month period ended September 30, 2004 is a \$389,000 loss on the disposal of a compressor, which was previously being rented from the Company. During the first quarter of 2004 and as part of the Company's ongoing evaluation and reorganization of operations, the Company decided to suspend engineering and maintenance operations related to compressors, including compressors being rented from the Company. Operating results for these operations are included in the process systems segment and are not significant to the historical operations of the Company.

Loss from operation of discontinued drilling rig fabrication segment was \$221,000 and \$3.6 million in the three- and nine- month periods ended September 30, 2004, respectively. Loss from operation of discontinued drilling rig segment was \$1.1 million and \$1.1 million, respectively, in the same periods in 2003. The loss recognized in the nine-month period ended September 30, 2004 includes an impairment loss of \$3.3 million on the Lake Charles facility. Operating losses incurred at the facility, the lack of backlog for the facility and the business outlook resulted in the Company closing the facility early in the June 2004

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quarter. In evaluating the recoverability of its investment in the Lake Charles facility, the Company concluded the carrying value of the facility was impaired. The Company then estimated the fair value of the facility based on the related discounted estimated cash flows and based on this analysis recorded an impairment loss of \$3.3 million. The impairment loss reduced the recorded net value of the facility to its estimated fair value of \$2.5 million. During the September 2004 quarter, the Company engaged a real estate broker and has placed the facility for sale by closed bid auction held on November 18, 2004. The Company is currently negotiating the completion of the offer on that facility, which does not indicate further impairment.

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### SEGMENT INFORMATION

The Company has identified three reportable segments as required by SFAS No. 131. The following discusses the results of operations for each of those reportable segments during the three- and nine-month periods ended September 30, 2004 and 2003. During the September 2004 quarter, the Company entered into a plan to dispose of the fabrication facilities related to the process systems segment and the drilling rig fabrication segment and discontinue operations related to those segments.

#### PLATFORM FABRICATION SEGMENT

Revenue for the platform fabrication segment decreased 25%, or \$2.6 million, to \$7.7 million in the quarter ended September 30, 2004 from \$10.3 million in the same quarter of 2003. Direct manhours in the September 2004 quarter decreased 50% from the September 2003 quarter. In the nine-month period ended September 30, 2004, revenue decreased 15% from the same period last year to \$23.1 million. Segment loss decreased to \$390,000 in the September 30, 2004 quarter from \$1.2 million in the September 30, 2003 quarter, and to \$553,000 in the nine-month period ended September 30, 2004 from \$820,000 in the same period last year. Fabrication activity has decreased from last year, and bidding for projects in this segment has remained competitive, causing lower profit margins. In the nine months ended September 30, 2003, segment income was reduced by \$292,000 related to the repair of the roof on the Company's main fabrication building. Savings from the reduction of administrative staff and the shifting of general and administrative functions to corporate reduced segment loss in the three- and nine-month periods ended September 30, 2004.

#### PROCESS SYSTEMS SEGMENT

Revenue for the process systems segment was \$1.7 million in the three-month period ended September 30, 2004 compared to \$3.1 million in the same quarter last year. In the quarter ended September 30, 2004, direct manhours decreased 46% from the September 2003 quarter. During the September 2004 quarter, the Company has moved all operations related to this segment to its main fabrication yard in New Iberia. As a result of this relocation, the segment loss for the three-month period ended September 30, 2004 was reduced to \$124,000 from \$351,000 in the same period last year. Savings from the reduction of administrative staff and the shifting of general and administrative functions to corporate decreased the segment loss in the September 30, 2004 quarter. Revenue for the nine-month period ended September 30, 2004 was \$5.9 million compared to \$10.0 million in the same period last year. Over this period, direct manhours at the facility decreased 39% from the same period last year. Due to this low level of activity and the increase in cost per manhour that resulted from it, segment loss increased in the nine-month period ended September 30, 2004 to \$1.3 million from \$763,000 in the same period in 2003. Included in segment loss in the nine-month period ended September 30, 2004 was a charge of \$260,000 related to goodwill associated with the Company's Compression Engineering business unit. Included in segment loss for the nine-month period ended September 30, 2003 were contract loss reserves of \$220,000, including \$117,000 recorded because of delays encountered on contracts to provide process equipment that was being manufactured overseas.

#### DRILLING RIG FABRICATION SEGMENT

The drilling rig fabrication segment, revenue was \$107,000 in the September 2004 quarter and \$2.5 million in the same quarter last year. In the nine-month period ended September 30, 2004, revenue was \$3.8 million compared to \$2.7 million in the same period last year. Nearly all of the operating results in this segment relate to one significant project performed at the Company's fabrication facility in Lake Charles,



Louisiana. Upon the completion of this project in April 2004, management decided to temporarily idle this facility. In evaluating the recoverability of the investment in the Lake Charles facility, the Company concluded the carrying value of the facility was impaired. The Company then estimated the fair value of the facility based on the related discounted estimated cash flows and based on this analysis recorded an impairment loss of \$3.3 million during the June 2004 quarter. The impairment loss reduced the recorded net value of the facility to its estimated fair value of \$2.5 million. During the September 2004 quarter, the Company engaged a real estate broker and placed the facility for sale by closed bid auction held on November 18, 2004. The Company is currently negotiating the final documents to sell the facility, which will allow the recovery of the recorded value of the facility.

#### LIQUIDITY AND CAPITAL RESOURCES

Historically, the Company has funded its business activities through borrowings from time to time as needed from Midland, as more fully described below, funds generated from operations, short - term borrowings on its revolving credit facilities for working capital needs and individual financing arrangements for equipment, facilities improvements, insurance premiums and long-term needs. During the nine-month period ended September 30, 2004, the Company's available funds, \$4.2 million generated from operating activities and \$23,000 provided by investing activities together funded cash used in financing activities of \$4.1 million.

Under an informal arrangement with the Company, Midland has agreed from time to time to provide financial support and funding for working capital or other needs at Midland's discretion. During the nine months ended September 30, 2004, Midland advanced \$12.1 million to the Company for working capital, of which \$2.6 million remains unpaid at September 30, 2004 and is classified as a current liability. During the three month period ended September 30, 2004, the Company recovered an income tax carryback refund of \$2.2 million plus interest of \$890,000, which was used to repay amounts advanced by Midland. At December 31, 2003, Midland was owed \$5.9 million related to advances under this informal arrangement, which was classified as a current liability. As a result of classifying the amounts outstanding related to the informal arrangement with Midland and the Credit Agreement as current liabilities, the Company has a working capital deficit of \$6.1 million at September 30, 2004. The liquidity afforded by the advances from Midland was necessary for the Company to meet its obligations and fund operations throughout the nine months ended September 30, 2004. Since the Midland investment, the Company has received contracts, which have required a financial guarantee or letter of credit from Midland. Management believes that additional funds available from Midland under the informal arrangement described above are necessary to fund its working capital needs and planned capital expenditures for the next 12 months and that guarantees from Midland are necessary to win contract awards. However, the Company has no control over whether Midland will provide additional funding or financial guarantees in the future and does not know whether such additional funding or financial guarantees will be available from Midland as the Company requires them. If Midland does not provide such additional funding or financial guarantees when needed in the future, the Company will not be able to satisfy its working capital requirements and meet its obligations, including obligations under the Credit Agreement, in the ordinary course of business. The Company requires the continued support from Midland until such time as it has sustained profitable operations and its financial condition is stable and no longer requires this support.

On November 18, 2002, the Company entered into a Commercial Business Loan with Whitney National Bank (the "Credit Agreement"), guaranteed by Nassau

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Holding Company, an affiliate of Midland, the subsidiaries of Unifab, and the principal members of Midland and secured by all of the assets of the Company, which provides for up to \$8.0 million in borrowings for working capital purposes, including up to \$2.0 million in letters of credit under a revolving credit facility. At September 30, 2004 and December 31, 2003, respectively, the Company had \$7.9 million in borrowings and letters of credit totaling \$3,000 outstanding under the revolving credit facility. Borrowings under the Credit Agreement bear interest at Libor plus 1.75% or the Prime rate (3.420% at September 30, 2004), at the Company's discretion. The Credit Agreement matures January 31, 2005. The Company expects to renew its Credit Agreement under the same general terms and with the continuing guarantee of Nassau Holding Company.

The table below sets out the cash contractual obligations of the Company. The operating leases are not recorded as liabilities on the balance sheet, but payments are treated as an expense as incurred. Each contractual obligation included in the table contains various terms, conditions, and covenants which, if violated, accelerate the payment of that obligation. The operating lease obligations primarily relate to the

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Company's operating facilities:

	Payment due by year					
	Total	Remainder 2004	2005	2006	2007	2008
Operating lease obligations	\$ 9,528	\$ 167	\$ 669	\$ 669	\$ 669	\$ 669
Settlement of lawsuit	300	300	-	-	-	-
Long-term debt	10,564	2,662	7,902	-	-	-
Secured, subordinated notes payable	6,848	-	2,139	4,709	-	-
Secured, subordinated, convertible debenture	7,953	-	-	-	2,130	2,130
	\$35,193	\$ 3,129	\$10,710	\$ 5,378	\$ 2,799	\$ 2,799

Management believes that additional funds available from Midland under the informal arrangement described above are necessary to fund its working capital needs and planned capital expenditures for the next 12 months. However, Management has no control over whether Midland will provide additional funding in the future and does not know whether such additional funding will be available from Midland as the Company requires it. If Midland does not provide such additional funding in the future as the Company requires it, the Company will not be able to meet its obligations, including obligations under the Credit Agreement, in the ordinary course of business.

### NEW ACCOUNTING PRONOUNCEMENTS

In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46"). FIN 46 requires that companies that control another entity through interests other than voting interests should consolidate the controlled entity. FIN 46 applies to variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that

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date. In December 2003 the FASB issued modifications to FIN 46 ("FIN 46R") resulting in multiple effective dates based on the nature as well as the creation date of a variable interest entity. The adoption of FIN 46 did not have a material impact on the Company's consolidated financial position or results of operations because the Company does not believe that the Company has interests that would be considered variable interest entities under FIN 46.

### CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to revenue recognition and long-lived assets. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The Company believes the following critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue from construction contracts, which are typically of short duration, are recognized on the percentage-of-completion method, measured by relating actual labor hours for work performed to date to the estimated total labor hours of the respective contract. Contract costs include all direct material and labor costs and those indirect costs related to contract performance, such as indirect labor, supplies, and repairs. Provisions for estimated losses, if any, on uncompleted contracts are made in the period in which such losses are determined. Significant changes in cost estimates due to adverse market conditions or poor

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contract performance could affect estimated gross profit, possibly resulting in a contract loss.

The Company's customers are principally major and large independent oil and gas companies and drilling companies. These concentrations of customers may impact our overall exposure to credit risk, either positively or negatively, in that our customers may be similarly affected by changes in economic or other conditions. Reserves for uncollectible accounts receivable are evaluated periodically against specific accounts that are known to be uncollectible. Increases in the reserves for uncollectible accounts are charged to operating results in the period they are identified. Receivables are generally not collateralized. Significant adverse changes in the economic environment of the oil and gas industry could result in materially lower collectibility of recorded receivables and could require a charge for uncollectible accounts in the future.

Long-lived assets held and used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company assesses the recoverability of long-lived assets by determining whether the carrying values can be recovered through projected net cash flows undiscounted, based on expected operating results over their remaining lives. If impairment is indicated, the asset is written down to its fair market value, or if fair market value is not readily determinable, to its estimated discounted net cash flows. Future adverse market

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conditions or poor operating results could result in the inability to recover the current carrying value of the long-lived asset, thereby possibly requiring an impairment charge in the future.

Income taxes have been provided using the liability method. Deferred income taxes reflect the net effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The amount of future income tax assets recognized is limited to the amount of benefit that is more likely than not to be realized. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or the entire deferred tax asset will not be realized. The ultimate realization of the deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversals of deferred tax liabilities, the likelihood of future taxable income and tax planning strategies when making this assessment. Based on this assessment, the Company records a valuation allowance against deferred tax assets that are more likely than not unrealizable. The amount of the deferred tax asset considered realizable, however, could be reduced in the future if taxable income is not available to allow for the deduction of the deferred tax assets.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to the risk of changing interest rates and foreign currency exchange rate risks. The Company does not use derivative financial instruments to hedge the interest or currency risks. Interest on approximately \$25.5 million, substantially all of the Company's debt, was variable, based on short-term interest rates. A general increase of 1.0% short-term market interest rates would result in additional interest cost of \$255,000 per year if the Company were to maintain the same debt level and structure.

The Company has a subsidiary located in the United Kingdom for which the functional currency is the British Pound. The subsidiary is being liquidated, and therefore there are no operations at September 30, 2004. However, the liquidation proceeds are held in British Pounds pending the resolution of the liquidation and final distribution of the proceeds, if any. The Company typically does not hedge its foreign currency exposure. Historically, fluctuations in British Pound/US Dollar exchange rates have not had a material effect on the Company. Future changes in the exchange rate of the US Dollar to the British Pound may positively or negatively impact the final amount distributed; however, the Company does not anticipate its exposure to foreign currency rate fluctuations to be material in 2004.

While the Company does not currently use derivative financial instruments, it may use them in the future if deemed appropriate.

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### CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING INFORMATION

Certain statements included in this report and in oral statements made from time to time by management of the Company that are not statements of historical fact are forward-looking statements. In this report, forward-looking statements are included primarily in the sections entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations." The words "expect," "believe," "anticipate," "project," "plan," "estimate," "predict," and similar expressions often identify forward-looking statements. Such statements may involve risks and uncertainties and include, among other things, information as to possible future increases in oil and gas prices and drilling activity and the effect of current and future levels of prices and

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drilling activity on demand for products and services of the Company, on the prices the Company can obtain for its products and services and on the profitability of the Company. All such statements are subject to factors that could cause actual results and outcomes to differ materially from the results and outcomes predicted in the statements, and investors are cautioned not to place undue reliance upon them. Those factors include, but are not limited to, the risks, contingencies and uncertainties described immediately below:

- advances and financial guarantees from Midland have been necessary for the Company to meet its obligations and fund operations and for contract awards. However, the Company has no control over whether Midland will provide additional funding or financial guarantees in the future and does not know whether such additional funding or financial guarantees will be available from Midland as the Company requires them. If Midland or some other source of financial support does not provide such additional funding or financial guarantees in the future as the Company requires them, the Company probably will not be able to meet its obligations, including obligations under the Credit Agreement, in the ordinary course of business. The Company requires the continued support from Midland or another source of financial support until such time as it has sustained profitable operations and its financial condition is stable and no longer requires this support;
- general economic and business conditions and industry trends;
- the economic strength of our customers and potential customers;
- decisions about offshore developments to be made by oil and gas companies;
- the highly competitive nature of our businesses;
- our future financial performance, including availability, terms and deployment of capital;
- the continued availability of qualified personnel;
- changes in, or our failure or inability to comply with, government regulations and adverse outcomes from legal and regulatory proceedings;
- changes in existing environmental regulatory matters;
- rapid technological changes;
- realization of deferred tax assets;
- consequences of significant changes in interest rates and currency exchange rates;
- difficulties we may encounter in obtaining regulatory or other necessary approvals of any strategic transactions;
- social, political and economic situations in foreign countries where we do business, including among others, countries in the Middle East;
- effects of asserted and unasserted claims;
- our ability to obtain surety bonds and letters of credit; and

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- our ability to maintain builder's risk, liability and property insurance in amounts we consider adequate at rates that we consider economical.

### ITEM 4. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, the Company carried out an evaluation under the supervision of and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and implementation of its disclosure controls and procedures. Based on and as of the date of that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company, including its consolidated

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subsidiaries, required to be included in reports the Company files with or submits to the Securities and Exchange Commission under the Securities Act of 1934.

There have been no significant changes in the Company's internal control over financial reporting or in other factors during the first three quarters of fiscal year 2004 that have materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

### PART II

#### ITEM 1. LEGAL PROCEEDINGS.

In addition to the matter described below, the Company is a party to various routine legal proceedings primarily involving commercial claims, workers' compensation claims, and claims for personal injury under the General Maritime Laws of the United States. While the outcome of these legal proceedings and claims cannot be predicted with certainty, management believes that the outcome of such proceedings is not likely to have a material adverse effect on the Company's consolidated financial statements.

In a lawsuit filed against the Company in the 14th Judicial Court in the Parish of Calcasieu, State of Louisiana, Professional Industrial Maintenance, L.L.C., Don E. Spano and Kimberly Spano alleged multiple claims for breach of contract, breach of specific performance, a request for injunction, request for damages, and a request for treble damages and attorney fees for violations of the Louisiana Unfair Trade Practices Act. Mr. Spano was the managing member of Professional Industrial Maintenance, LLC, the company whose assets we acquired in January 1998. The Company filed a counterclaim for recovery of certain amounts paid on behalf of Professional Industrial Maintenance, LLC and Mr. Spano as a result of the transaction. In January 2004, the parties agreed to settle the disputes subject of the lawsuit with full and final releases for all claims in exchange for a cash payment to the plaintiffs in the amount of \$300,000 and, accordingly, the Company recorded the related liability at December 31, 2003. However, as of the filing of this report, the details of the settlement agreement and release have not been finalized, and the Company has not yet made the cash payment.

#### ITEM 5. OTHER INFORMATION

This report on Form 10-Q is accompanied by a statement of the Principal Executive Officer and the Chief Financial Officer of the registrant making certain certifications as to the contents hereof, as required by Section 906 of

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the Sarbanes-Oxley Act of 2002.

The Company's common stock was delisted from the NASDAQ SmallCap Market effective June 28, 2004, as the Company ceased to meet the NASDAQ's listing requirements. Since that time, shares of the Company's common stock have traded, from time to time, in the over-the-counter market and on the Pink Sheets.

On March 29, 2004, the Company's independent auditor issued its audit report on the Company's December 31, 2003 financial statements. The audit report included a "going concern qualification" which is an explanatory paragraph relating to the Company's ability to continue as a going concern due to its recurring losses from operations, negative working capital position and difficulties in meeting its financial obligations and funding its operations.

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

#### (a) Exhibits

Exhibit Number -----	Description -----
31.1	Certification pursuant to Exchange Act 13a-15 and 15d-15(e) accompanying and furnished with this quarterly report on Form 10-Q for the nine-month period ended September 30, 2004
31.2	Certification pursuant to Exchange Act 13a-15 and 15d-15(e) accompanying and furnished with this quarterly report on Form 10-Q for the nine-month period ended September 30, 2004
32.1	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350, as adopted) accompanying and furnished with this quarterly report on Form 10-Q for the nine-month period ended September 30, 2004
32.2	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350, as adopted) accompanying and furnished with this quarterly report on Form 10-Q for the nine-month period ended September 30, 2004
99.1	Press release issued by the Company on October 6, 2004 announcing Midland Fabricators and Process Systems, LLC, intentions to take the Company private.

#### (b) Reports on form 8-K

On October 7, 2004, the Company filed a current report on Form 8-K dated October 6, 2004 related to the press release issued on October 6, 2004 announcing that Midland Fabricators and Process Systems, LLC, the owner of 90.1% of the outstanding shares of the Company's common stock, intends to take the Company private pursuant to the Louisiana short form merger law.

SIGNATURES

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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.

Date January 24, 2005

UNIFAB International, Inc.

/s/ Frank J. Cangelosi, Jr.  
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Frank J. Cangelosi, Jr.  
Chief Financial Officer  
(Principal Financial and Accounting  
Officer)