

TAL International Group, Inc.  
Form 10-Q  
November 13, 2006

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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FORM 10-Q

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

For The Quarterly Period Ended September 30, 2006  
or

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

For the Transition Period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number- 001-32638

TAL International Group, Inc.

(Exact name of registrant as specified in the charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

100 Manhattanville Road,  
Purchase, New York  
(Address of principal executive office)

20-1796526  
(I.R.S. Employer  
Identification Number)

10577-2135  
(Zip Code)

(914) 251-9000

(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 requirement for the past 90 days. Yes      No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

As of November 3, 2006, there were 33,166,781 shares of the Registrant's common stock, \$.001 par value outstanding.

TAL INTERNATIONAL GROUP, INC.  
INDEX

|                                                                                                                     | Page<br>No. |
|---------------------------------------------------------------------------------------------------------------------|-------------|
| Part I — Financial Information                                                                                      |             |
| Item 1. Financial Statements (unaudited)                                                                            | 1           |
| Consolidated Balance Sheets at September 30, 2006 and December 31, 2005                                             | 2           |
| Consolidated Statements of Operations for the three and nine months ended September 30, 2006 and September 30, 2005 | 3           |
| Consolidated Statements of Cash Flows for the nine months ended September 30, 2006 and September 30, 2005           | 4           |
| Notes to Consolidated Financial Statements                                                                          | 5-13        |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations                       | 14-27       |
| Item 3. Quantitative and Qualitative Disclosures About Market Risk                                                  | 27-28       |
| Item 4. Controls and Procedures                                                                                     | 29          |
| Part II — Other Information                                                                                         |             |
| Item 1. Legal Proceedings                                                                                           | 30          |
| Item 1A. Risk Factors                                                                                               | 30          |
| Item 2. Unregistered Sales of Equity Securities, Use of Proceeds and Issuer Repurchases of Equity Securities        | 30          |
| Item 6. Exhibits                                                                                                    | 30          |
| Signature                                                                                                           | 31          |

Table of Contents

CAUTIONARY STATEMENT FOR PURPOSES OF THE “SAFE HARBOR” PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Quarterly Report on Form 10-Q contains certain forward-looking statements, including, without limitation, statements concerning the conditions in our industry, our operations, our economic performance and financial condition, including, in particular, statements relating to our business and growth strategy and service development efforts. The Private Securities Litigation Reform Act of 1995 provides a “safe harbor” for certain forward-looking statements so long as such information is identified as forward-looking and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those projected in the information. When used in this Quarterly Report on Form 10-Q, the words “may”, “might”, “should”, “estimate”, “project”, “anticipate”, “expect”, “intend”, “outlook”, “believe” and other similar expressions are intended to identify forward-looking

statements and information. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their dates. These forward-looking statements are based on estimates and assumptions by our management that, although we believe to be reasonable, are inherently uncertain and subject to a number of risks and uncertainties. These risks and uncertainties include, without limitation, those identified under “Risk Factors” in our Annual Report on Form 10-K filed with the Securities and Exchange Commission (“SEC”), on March 20, 2006, and all of our other filings filed with the SEC from October 11, 2005 through the current date pursuant to the Securities Exchange Act of 1934.

We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events or otherwise, except as otherwise required by law. Reference is also made to such risks and uncertainties detailed from time to time in our filings with the SEC.

## PART I — FINANCIAL INFORMATION

### ITEM 1. FINANCIAL STATEMENTS

The consolidated financial statements of TAL International Group, Inc. (“TAL” or the “Company,”) as of September 30, 2006 (unaudited) and December 31, 2005 and for the three and nine months ended September 30, 2006 (unaudited) and September 30, 2005 (unaudited) included herein have been prepared by the Company, without audit, pursuant to U.S. generally accepted accounting principles and the rules and regulations of the SEC. However, certain information and note disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading. These financial statements reflect, in the opinion of management, all adjustments (consisting only of normal recurring adjustments) necessary to present fairly the results for the interim periods. The results of operations for such interim periods are not necessarily indicative of the results for the full year. These financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K filed with the SEC, on March 20, 2006, from which the accompanying December 31, 2005 Balance Sheet information was derived, and all of our other filings filed with the SEC from October 11, 2005 through the current date pursuant to the Securities Exchange Act of 1934.

1

## Table of Contents

### TAL INTERNATIONAL GROUP, INC.

#### Consolidated Balance Sheets

(Dollars in thousands, except share data)

|                                                                           | September<br>30,<br>2006<br>(Unaudited) | December<br>31,<br>2005 |
|---------------------------------------------------------------------------|-----------------------------------------|-------------------------|
| Assets:                                                                   |                                         |                         |
| Cash and cash equivalents (including restricted cash of \$13,274 and \$0) | \$ 45,712                               | \$ 27,259               |

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|                                                                                                                        |              |              |
|------------------------------------------------------------------------------------------------------------------------|--------------|--------------|
| Accounts receivable, net of allowances of \$295 and \$820                                                              | 35,724       | 36,470       |
| Net investment in finance leases                                                                                       | 129,163      | 73,819       |
| Leasing equipment, net of accumulated depreciation and allowances of \$188,479 and \$124,543                           | 1,099,755    | 1,036,363    |
| Leasehold improvements and other fixed assets, net of accumulated depreciation and amortization of \$1,878 and \$1,312 | 3,109        | 3,771        |
| Equipment held for sale                                                                                                | 17,559       | 24,844       |
| Goodwill                                                                                                               | 71,898       | 71,898       |
| Deferred financing costs                                                                                               | 7,150        | 3,540        |
| Other assets (including fair value of derivative instruments)                                                          | 22,484       | 26,304       |
| Total assets                                                                                                           | \$ 1,432,554 | \$ 1,304,268 |
| Liabilities and stockholders' equity:                                                                                  |              |              |
| Accounts payable                                                                                                       | \$ 24,442    | \$ 12,256    |
| Accrued expenses                                                                                                       | 40,207       | 30,063       |
| Income taxes payable                                                                                                   | 320          | 116          |
| Deferred income tax liability                                                                                          | 26,733       | 9,239        |
| Debt:                                                                                                                  |              |              |
| Asset securitization facility                                                                                          | —            | 710,000      |
| Asset backed securities (ABS):                                                                                         |              |              |
| Term notes                                                                                                             | 651,667      | —            |
| Warehouse facility                                                                                                     | 106,500      | —            |
| Revolving credit facilities                                                                                            | 131,500      | 148,000      |
| Finance lease facility                                                                                                 | 12,500       | —            |
| Other debt                                                                                                             | 11,798       | —            |
| Capital lease obligations                                                                                              | 24,369       | 14,627       |
| Total liabilities                                                                                                      | 1,030,036    | 924,301      |
| Stockholders' equity:                                                                                                  |              |              |
| Preferred stock, \$.001 par value, 500,000 shares authorized, none issued                                              | —            | —            |
| Common stock, \$.001 par value, 100,000,000 shares authorized, 33,303,031 and 32,882,208 shares issued, respectively   | 33           | 33           |
| Treasury stock, at cost, 136,250 shares and 0 shares, respectively                                                     | (2,862)      | —            |
| Additional paid-in capital                                                                                             | 394,434      | 394,389      |
| Accumulated earnings (deficit)                                                                                         | 6,901        | (13,737)     |
| Accumulated other comprehensive income (loss)                                                                          | 4,012        | (718)        |
| Total stockholders' equity                                                                                             | 402,518      | 379,967      |
| Total liabilities and stockholders' equity                                                                             | \$ 1,432,554 | \$ 1,304,268 |

The accompanying notes to the unaudited consolidated financial statements are an integral part of these statements.

2

Table of Contents

TAL INTERNATIONAL GROUP, INC.

Consolidated Statements of Operations  
(Dollars and shares in thousands, except earnings per share)

|                                                                                                                        | Three Months Ended<br>September 30,<br>2006      2005<br>(Unaudited) |             | Nine Months Ended<br>September 30,<br>2006      2005<br>(Unaudited) |             |
|------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------|-------------|---------------------------------------------------------------------|-------------|
| Revenues:                                                                                                              |                                                                      |             |                                                                     |             |
| Leasing revenues, including income recognized on finance leases of \$3,399, \$1,934, \$8,516 and \$3,356, respectively | \$ 67,827                                                            | \$ 71,001   | \$ 201,523                                                          | \$ 215,084  |
| Equipment trading revenue                                                                                              | 6,897                                                                | 7,774       | 17,673                                                              | 17,173      |
| Management fee income                                                                                                  | 1,538                                                                | 1,566       | 4,687                                                               | 4,978       |
| Other revenues                                                                                                         | 413                                                                  | 738         | 1,453                                                               | 1,909       |
| Total revenues                                                                                                         | 76,675                                                               | 81,079      | 225,336                                                             | 239,144     |
| Expenses:                                                                                                              |                                                                      |             |                                                                     |             |
| Equipment trading expenses                                                                                             | 5,606                                                                | 6,026       | 14,545                                                              | 13,257      |
| Direct operating expenses                                                                                              | 6,311                                                                | 6,410       | 19,734                                                              | 20,707      |
| Administrative expenses                                                                                                | 9,350                                                                | 9,411       | 28,009                                                              | 28,362      |
| Depreciation and amortization                                                                                          | 26,590                                                               | 29,418      | 77,782                                                              | 88,076      |
| (Reversal) provision for doubtful accounts                                                                             | (58)                                                                 | 528         | (500)                                                               | 567         |
| Net (gain) on sale of leasing equipment                                                                                | (1,883)                                                              | (1,178)     | (2,859)                                                             | (8,133)     |
| Write-off of deferred financing costs                                                                                  | —                                                                    | 24,313      | 2,367                                                               | 24,313      |
| Interest and debt expense                                                                                              | 11,686                                                               | 21,239      | 35,266                                                              | 63,849      |
| Unrealized loss (gain) on interest rate swaps                                                                          | 12,174                                                               | (7,589)     | 8,584                                                               | (8,975)     |
| Management fees                                                                                                        | —                                                                    | 1,346       | —                                                                   | 4,598       |
| Total expenses                                                                                                         | 69,776                                                               | 89,924      | 182,928                                                             | 226,621     |
| Income (loss) before income taxes                                                                                      | 6,899                                                                | (8,845)     | 42,408                                                              | 12,523      |
| Income tax expense (benefit)                                                                                           | 2,449                                                                | (3,090)     | 15,133                                                              | 4,577       |
| Net income (loss)                                                                                                      | 4,450                                                                | (5,755)     | 27,275                                                              | 7,946       |
| Preferred stock dividends                                                                                              | —                                                                    | (6,568)     | —                                                                   | (18,727)    |
| Net income (loss) applicable to common stockholders                                                                    | \$ 4,450                                                             | \$ (12,323) | \$ 27,275                                                           | \$ (10,781) |
| Net income (loss) per common share — Basic                                                                             | \$ 0.13                                                              | \$ (1.21)   | \$ 0.83                                                             | \$ (1.06)   |
| Net income (loss) per common share — Diluted                                                                           | \$ 0.13                                                              | \$ (1.21)   | \$ 0.82                                                             | \$ (1.06)   |
| Weighted average number of common shares outstanding — Basic                                                           | 33,001                                                               | 10,204      | 32,927                                                              | 10,186      |
| Weighted average number of common shares outstanding — Diluted                                                         | 33,421                                                               | 10,204      | 33,450                                                              | 10,186      |
| Cash dividends paid per common share                                                                                   | \$ 0.20                                                              | —           | \$ 0.20                                                             | —           |

The accompanying notes to the unaudited consolidated financial statements are an integral part of these statements.

## Table of Contents

### TAL INTERNATIONAL GROUP, INC.

#### Consolidated Statements of Cash Flows (Dollars in thousands)

|                                                                                   | Nine months ended<br>September 30,<br>2006                      2005<br>(Unaudited) |           |
|-----------------------------------------------------------------------------------|-------------------------------------------------------------------------------------|-----------|
| Cash flows from operating activities:                                             |                                                                                     |           |
| Net income                                                                        | \$ 27,275                                                                           | \$ 7,946  |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                                                                     |           |
| Depreciation and amortization                                                     | 77,782                                                                              | 88,076    |
| Write-off of deferred financing costs                                             | 2,367                                                                               | 24,313    |
| Amortization of deferred financing costs                                          | 556                                                                                 | 3,918     |
| Net (gain) on sale of leasing equipment                                           | (2,859)                                                                             | (8,133)   |
| Unrealized loss (gain) on interest rate swaps                                     | 8,584                                                                               | (8,975)   |
| Deferred income taxes                                                             | 17,494                                                                              | 4,469     |
| Stock compensation charge                                                         | 32                                                                                  | 490       |
| Changes in operating assets and liabilities                                       | 23,191                                                                              | 21,083    |
| Net cash provided by operating activities                                         | 154,422                                                                             | 133,187   |
| Cash flows from investing activities:                                             |                                                                                     |           |
| Purchases of leasing equipment                                                    | (189,794)                                                                           | (132,235) |
| Investment in finance leases                                                      | (39,895)                                                                            | (42,110)  |
| Proceeds from sale of equipment                                                   | 42,999                                                                              | 77,213    |
| Cash collections on financing leases, net of unearned income                      | 10,446                                                                              | 4,181     |
| Other                                                                             | 180                                                                                 | —         |
| Net cash used in investing activities                                             | (176,064)                                                                           | (92,951)  |
| Cash flows from financing activities:                                             |                                                                                     |           |
| Proceeds from issuance of common and preferred stock                              | —                                                                                   | 1,206     |
| Purchases of treasury stock                                                       | (2,862)                                                                             | —         |
| Stock options exercised                                                           | 13                                                                                  | —         |
| Dividends paid                                                                    | (6,637)                                                                             | —         |
| Initial borrowings under asset securitization facility                            | —                                                                                   | 705,000   |
| Net payments under asset securitization facility                                  | (710,000)                                                                           | (10,000)  |
| Net payments under senior secured credit facility                                 | —                                                                                   | (710,000) |
| Borrowings under long-term credit facilities                                      | 799,000                                                                             | —         |
| Payments of finance fees related to new debt agreements                           | (6,384)                                                                             | —         |
| Payments under long-term credit facilities                                        | (44,833)                                                                            | —         |
| Increase in other debt                                                            | 11,798                                                                              | —         |
| (Increase) in restricted cash                                                     | (13,274)                                                                            | —         |
| Net cash provided by (used in) financing activities                               | 26,821                                                                              | (13,794)  |
| Net increase in cash and cash equivalents                                         | 5,179                                                                               | 26,442    |
| Unrestricted cash and cash equivalents, beginning of period                       | 27,259                                                                              | 16,424    |
| Unrestricted cash and cash equivalents, end of period                             | \$ 32,438                                                                           | \$ 42,866 |
| Supplemental non-cash financing activities:                                       |                                                                                     |           |
| Purchases of leasing equipment financed through capital lease obligations         | \$ 9,742                                                                            | \$ —      |

The accompanying notes to the unaudited consolidated financial statements are an integral part of these statements.

Table of Contents

TAL INTERNATIONAL GROUP, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — Description of the Business, Basis of Presentation, Recently Issued Accounting Pronouncements

A. Description of the Business

TAL International Group, Inc. (“TAL,” or the “Company”) was formed on October 26, 2004 and commenced operations on November 4, 2004. TAL consists of the consolidated accounts of TAL International Container Corporation (“TALI”), formerly known as Transamerica Leasing Inc., Trans Ocean Ltd. (“TOL”) and their subsidiaries. Effective October 31, 2004, TAL acquired all of the outstanding capital stock of TALI and TOL for approximately \$1.2 billion in cash (“the Acquisition”).

The Company provides long-term leases, service leases and finance leases of maritime containers and related equipment, along with maritime container management services, through a worldwide network of offices, third party depots and other facilities. The Company operates in both international and domestic markets. The majority of the Company's business is derived from leasing its containers to shipping line customers through a variety of long-term and short-term contractual lease arrangements. The Company also provides container sales and positioning services, enters into management agreements with third party container owners under which the Company manages the leasing and selling of containers on behalf of the third party owners, and leases chassis used for the transportation of containers domestically.

B. Basis of Presentation

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the reported amounts of revenues and expenses during the reporting period and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

The consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany transactions and balances have been eliminated in consolidation. Certain reclassifications have been made to the accompanying prior period financial statements and notes to conform with the current year's presentation.

C. Recently Issued Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (“SFAS No. 157”) which addresses how companies should measure fair value when they are required to use a fair value measure for recognition or disclosure purposes under generally accepted accounting principles (GAAP). Under SFAS No. 157, there is now a common definition of fair value to be used throughout GAAP. The new standard will make the measurement of fair value more consistent and comparable and improve disclosures about those measures. The Company is required to adopt the provisions of SFAS No. 157 during the first fiscal year beginning after November 15, 2007. The Company is currently evaluating the impact of SFAS No. 157 on its consolidated results of operations and financial position.

In June 2006, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109,” (“FIN 48”). FIN 48 clarifies the accounting

for uncertainty in income taxes recognized in financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods,

5

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## Table of Contents

disclosure, and transition. The Company is required to adopt the provisions of FIN 48 during the first fiscal year beginning after December 15, 2006. The Company is currently evaluating the impact of FIN 48 on its consolidated results of operations and financial position.

### Note 2 — Initial Public Offering

On October 17, 2005, the Company sold 11.5 million shares of common stock at a price of \$18.00 per share in an initial public offering (“IPO”) which generated net proceeds of approximately \$189.2 million, after deducting underwriter discounts and other offering expenses. The Company used the net proceeds of this offering, together with additional borrowings under certain of its debt facilities and available cash, to repay the entire outstanding principal and accrued cash interest due on the senior unsecured credit agreement which was approximately \$288.0 million on October 17, 2005. On October 21, 2005, the underwriters of TAL’s IPO exercised their over-allotment option in part and purchased 1.0 million additional shares of common stock from certain of TAL’s stockholders. TAL did not receive any proceeds from the sale of the shares pursuant to the over-allotment option.

### Note 3 — Capital Stock and Stock-Based Compensation Plans

#### Preferred Stock Exchange

All 201,205 outstanding shares of the Company’s Series A 12.0% cumulative senior preferred stock were converted into 11,178,035 shares of common stock on October 17, 2005, based on the IPO price of \$18.00 per common share. The Company paid the aggregate outstanding accrued dividends on the Series A 12.0% cumulative senior preferred stock of \$23.6 million in November 2005.

#### Treasury Stock

On March 13, 2006, the Company’s Board of Directors authorized a stock buyback program for the repurchase of up to 1.5 million shares of its common stock. The Company repurchased 136,250 shares of its outstanding common stock in the open market during the quarter ended September 30, 2006 at a total cost of approximately \$2.9 million.

#### Dividends Paid

On September 26, 2006, the Company paid a quarterly dividend of \$0.20 per share or an aggregate of approximately \$6.6 million on its issued and outstanding common stock. The dividend was paid to shareholders of record at the close of business on September 12, 2006.

#### 2004 Management Stock Plan

During 2004, the Company adopted the 2004 Management Stock Plan (the “2004 Plan”), which provides for the issuance of awards in the form of stock options, stock appreciation rights, restricted stock and certain other instruments to employees, consultants and members of the Company's board of directors. A total of 534,425 shares were reserved for issuance under the 2004 Plan.

During 2004, options to purchase a total of 400,945 shares were granted at an exercise price of \$0.01 per share, which the board of directors believed equaled the fair value per share of the Company's common stock.

During 2005, options to purchase an additional 53,667 shares were granted at an exercise price of \$0.01 per share.

Upon completion of the IPO on October 17, 2005, all 454,612 options outstanding under the 2004 Plan became fully vested. All options granted during 2004 and 2005 have a contractual life of ten years.

#### 2005 Management Omnibus Incentive Plan

In October 2005, the Company adopted the TAL International Group, Inc. 2005 Management Omnibus Incentive Plan (the “2005 Plan”), which provided for the issuance of awards in the form of

6

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#### Table of Contents

stock options, stock appreciation rights and restricted stock. A total of 2,500,000 shares of common stock were reserved for issuance under the 2005 Plan.

In October 2005, the board of directors approved the grant of options under the 2005 Plan to purchase an aggregate of 612,195 shares of the Company's common stock upon consummation of the IPO with an exercise price equal to the IPO price of the common stock, a vesting period of four years, and a contractual life of ten years. All 612,195 options granted on the IPO date became fully vested as of December 30, 2005, the date their acceleration was approved by the Compensation Committee of the Company's board of directors. The purpose of the accelerated vesting was to avoid future compensation expense associated with these options that the Company would otherwise recognize in its consolidated statements of operations upon the adoption of SFAS No.123(R).

During the nine months ended September 30, 2006, options to purchase 21,000 shares were granted at exercise prices equal to fair market values of the stock as of the grant date, with exercise prices ranging from \$21.99 to \$24.69 per share. These options vest ratably over four years, and have a contractual life of ten years.

#### Adoption of New Accounting Standard — Share-Based Payment

Effective January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (SFAS No.123R) requiring that compensation cost relating to share-based payment transactions be recognized in the financial statements. The cost is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity award). Prior to January 1, 2006, the Company accounted for share-based compensation to employees in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB No. 25), and related interpretations. The Company also followed the disclosure requirements of Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation, as amended by Statement of Financial Accounting Standards No. 148, Accounting for Stock-Based

Compensation-Transition and Disclosure. The Company adopted SFAS No.123R using the modified prospective method and, accordingly, financial statement amounts for prior periods presented in this Form 10-Q have not been restated to reflect the fair value method of recognizing compensation cost relating to stock options. Given that the options outstanding upon adoption of SFAS No. 123R were fully vested, the adoption of SFAS No.123R did not have an impact on the financial position, results of operations or cash flows of the Company. However, grants made during the second and third quarters of 2006 and any future grants of share-based compensation did and will result in the recognition of compensation expense.

There was approximately thirteen thousand dollars of compensation cost reflected in administrative expense in the Company's statement of operations related to the Company's stock-based compensation plans as a result of 21,000 new options granted during the nine months ended September 30, 2006. Total unrecognized compensation cost of approximately ninety thousand dollars as of September 30, 2006 related to the new options granted during the nine months ended September 30, 2006 will be recognized over the remaining vesting period of approximately 3.75 years.

In addition, approximately twenty thousand dollars of compensation cost is reflected in administrative expense related to a stock option modification related to a previously vested option grant. The Board of Directors approved an amendment to the stock option plans to permit participants whose employment terminates to exercise any unexercised vested options within 90 days of the date their employment terminates.

The Company computed the estimated fair value of each option award on the date of grant using the Black-Scholes option-pricing model. Expected volatility was based on computed volatility from trading activity of TAL stock since its IPO date and volatilities of other similar companies. The Company derives an expected term for its options using an estimated option exercise date based on historical employee termination behavior. The expected term represents an estimate of the time options are expected to remain outstanding. The risk-free rate for periods within the contractual life of the option is based on the U.S. treasury yield curve in effect at the time of grant. For options granted during the

7

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## Table of Contents

nine months ended September 30, 2006, the following assumptions were utilized in computing the fair value of the options: expected volatility of 28%, expected term of 6.5 years, expected annual dividends of \$0.80, and risk-free rates of 4.73% – 4.82%.

The weighted-average fair value of options granted during the nine months ended September 30, 2006 was \$4.88. Cash received from employee exercises of stock options for the nine months ended September 30, 2006 was approximately thirteen thousand dollars. TAL did not recognize any tax benefits associated with these exercises.

All previously granted options in 2005 and 2004 were fully vested as of December 30, 2005.

The following table illustrates the effect on net income and earnings per share had the fair value method of accounting been applied consistent with the requirements of SFAS No. 123 to the Company's stock compensation plans for the three and nine months ended September 30, 2005 (in thousands, except earnings per share):

|                       |                      |
|-----------------------|----------------------|
| Three months<br>ended | Nine months<br>ended |
|-----------------------|----------------------|

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|                                                                                 | September 30,<br>2005 | September 30,<br>2005 |
|---------------------------------------------------------------------------------|-----------------------|-----------------------|
| Net (loss) income applicable to common stockholders:                            |                       |                       |
| As reported                                                                     | \$ (12,323)           | \$ (10,781)           |
| Add: Stock-based compensation expense included in reported net income           | 245                   | 490                   |
| Deduct: Stock-based compensation expense determined under the fair value method | (245)                 | (490)                 |
| Pro forma net (loss) applicable to common stockholders                          | \$ (12,323)           | \$ (10,781)           |
| (Loss) earnings per common share:                                               |                       |                       |
| As reported — Basic and Diluted                                                 | \$ (1.21)             | \$ (1.06)             |
| Pro forma — Basic and Diluted                                                   | \$ (1.21)             | \$ (1.06)             |
| Weighted average number of common shares outstanding                            |                       |                       |
| — Basic                                                                         | 10,204                | 10,186                |
| — Diluted                                                                       | 10,204                | 10,186                |

Stock option activity under the Plans from January 1, 2006 to September 30, 2006 was as follows:

|                                | Options   | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Life<br>(Yrs) | Aggregate<br>Intrinsic<br>Value<br>\$ in 000's |
|--------------------------------|-----------|------------------------------------------|---------------------------------------------------|------------------------------------------------|
| Outstanding January 1, 2006    | 1,066,807 | \$ 10.33                                 | 9.4                                               |                                                |
| Granted                        | 21,000    | \$ 23.28                                 |                                                   |                                                |
| Exercised                      | (420,823) | \$ 0.03                                  |                                                   | \$ 9,521                                       |
| Canceled                       | (1,500)   |                                          |                                                   |                                                |
| Outstanding September 30, 2006 | 665,484   | \$ 17.24                                 | 9.0                                               | \$ 2,642                                       |
| Exercisable:                   |           |                                          |                                                   |                                                |
| September 30, 2006             | 644,484   | \$ 17.04                                 | 9.0                                               | \$ 2,687                                       |

Note 4 — Debt

#### Asset Backed Securitization Program

Effective August 1, 2005, the Company entered into an asset securitization facility (the “Asset Securitization Facility”) pursuant to which it had contributed certain eligible containers, together with the related leases, to TAL Advantage I LLC, a special purpose entity (the “SPE”) which is a wholly-owned consolidated subsidiary of the Company, whose primary business activity is to issue asset backed notes.

On April 12, 2006, the SPE issued two series of floating rate secured notes under its Asset Backed Securitization (“ABS”) program designed to reduce borrowing costs and enhance financing resources

for the Company's equipment fleet. Included in the issuance was \$680.0 million of floating rate secured term notes (the "Series 2006-1 Notes" or "ABS Term Notes"). The proceeds from this issuance, along with available cash, were used to repay the outstanding borrowings under the Asset Securitization Facility. A write-off of \$2.4 million was recorded for certain deferred financing fees during the nine months ended September 30, 2006 associated with this re-financing. The Series 2006-1 Notes amortize in equal monthly installments and have a legal final maturity of April 2021. At September 30, 2006, the outstanding balance under the ABS Term Notes was \$651.7 million. At September 30, 2006, the applicable interest rate, including the insurance premium, was LIBOR plus 0.48%. The weighted average interest rate on the ABS Term Notes for the period from the refinancing date to September 30, 2006 was 5.7%.

On April 12, 2006, the SPE entered into a floating rate revolving facility (the "Series 2005-1 Notes" or the "ABS Warehouse Facility") under the ABS program. The ABS Warehouse Facility provides up to \$300.0 million of borrowing capacity to support future fleet expansion. The Series 2005-1 Notes have a two year revolving period that precedes a term period in which the outstanding balance amortizes in equal monthly installments. The ABS Warehouse Facility has a legal final maturity of April 2023. At September 30, 2006, the outstanding balance under the ABS Warehouse Facility was \$106.5 million. At September 30, 2006, the applicable commitment fee was 0.30%, including the insurance premium, and the applicable interest rate was LIBOR plus 0.74%, including the insurance premium. The weighted average interest rate on the ABS Warehouse Facility for the period from the refinancing date to September 30, 2006 was 6.0%.

All debt issued under the ABS program is collateralized by the assets of the SPE consisting of the revenue earning containers used in the Company's leasing business, restricted cash and certain receivables related to revenue earning equipment. The SPE's borrowing capacity under the ABS program is determined by reference to an advance rate percentage of the net book values, as calculated in the ABS program documents of the SPE's eligible containers, subject to certain adjustments and restricted cash. Under the ABS program, the SPE is required to maintain restricted cash balances on deposit in a designated bank account.

Based on the applicable advance rate of 82%, the SPE's borrowing capacity was \$761.2 million at September 30, 2006. At September 30, 2006, the Company was in compliance with all of the various ABS program covenant requirements.

#### Revolving Credit Facilities

In connection with the Acquisition, the Company entered into an \$875.0 million Senior Secured Credit Facility ("SSCF"). Upon the closing of the Asset Securitization Facility on August 1, 2005, the Company amended and restated the SSCF to, among other things, reduce the maximum aggregate commitments thereunder to \$175.0 million. Effective June 1, 2006, the Company further amended the SSCF to reduce the interest rate margin from LIBOR plus 2.125% to LIBOR plus 1.375% and to reduce the maximum aggregate commitments thereunder to \$165.0 million. The final maturity date of this facility is August 1, 2008. The outstanding balance under the facility was \$131.5 million at September 30, 2006 and \$148.0 million at December 31, 2005.

The Company's borrowing capacity under this facility is based upon a variable advance rate percentage of the net book values, as calculated in the credit agreement, of the Company's eligible containers and eligible chassis, subject to certain adjustments. At September 30, 2006, the variable advance rate percentage was 85%, and is subject to annual decreases of 1% for each full calendar year following the IPO until a minimum advance rate of 82% is reached. At September 30, 2006, the unused borrowing capacity was \$33.5 million based on aggregate availability of \$165.0 million. The Company's eligible containers for the purposes of determining borrowing capacity under this facility does not include any containers transferred to the SPE. The SSCF is secured by a first priority lien on the Company's eligible containers, eligible chassis, related leases and lease rights and a pledge of the equity interests of the SPE.

At September 30, 2006, the SSCF applicable commitment fee was 0.375%, and the applicable interest rate was LIBOR plus 1.375%. Interest and fees and a portion of the outstanding principal amount of

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## Table of Contents

the loans under this facility, together with certain other amounts, are payable on a quarterly basis. The portion of the outstanding principal amount of the loans, if any, payable on any such payment date will be equal to the amount by which the outstanding principal amount of the loans exceeds the Company's then effective borrowing capacity. The weighted average interest rate under this facility for the nine months ended September 30, 2006 was 6.8%. At September 30, 2006, the Company was compliant with all of the various covenant requirements under this facility.

Effective June 7, 2006, the Company entered into an additional revolving credit facility (the "Swing Line Facility") to support general working capital requirements. The Company's borrowing capacity under this facility is based upon a 90% advance rate on the net book values of the containers and chassis not included in the SPE. The commitment under the Swing Line Facility is \$10.0 million and there was no outstanding balance at September 30, 2006. At September 30, 2006, the applicable commitment fee was 0.375%, and the applicable interest rate was LIBOR plus 2.00%.

### Finance Lease Facility

On July 31, 2006, the Company entered into a credit facility to support the growth of its finance lease business (the "Finance Lease Facility"). The Company's borrowing capacity under this facility is based upon a 90% advance rate on the net present values of finance lease receivables on certain containers and chassis not included in the SPE. The Finance Lease Facility has a two year revolving period that precedes a 10 year term in which the outstanding balance, as of the term conversion date, amortizes in monthly installments. The commitment under the Finance Lease Facility is \$50.0 million. At September 30, 2006, the applicable commitment fee and interest rate is 0.30% and LIBOR plus 1.00%, respectively. The outstanding balance under the facility was \$12.5 million at September 30, 2006. The weighted average interest rate on the Finance Lease Facility for the three months ended September 30, 2006 was 6.3%.

### Capital Lease Obligations and Other Debt

The Company has entered into a series of capital leases with various financial institutions to finance the purchase of chassis. The lease agreements are structured as ten year Terminal Rental Adjustment Clause ("TRAC") leases with purchase options at the end of the lease terms equal to the TRAC amount as defined in each lease. For income tax purposes, these leases are treated as operating leases. The weighted average interest rate for these leases as of September 30, 2006 is 5.3%. The total lease obligation was \$24.4 million as of September 30, 2006, and was \$14.6 million as of December 31, 2005.

During June 2006, the Company entered into an interim agreement with a financial institution to provide funding for chassis equipment that will be included in a TRAC lease by the end of 2006. At September 30, 2006, the advances totaled \$11.8 million and are classified as "Other Debt" on the consolidated balance sheet. The interest rate at September 30, 2006 was LIBOR plus 1.375% and the weighted average interest rate for the three months ended September 30, 2006 was 6.8%.

### Interest Rate Swaps

To hedge the risk associated with fluctuations in interest rates on long-term borrowings, the Company has entered into interest rate swap contracts with various financial institutions. The counterparties to these agreements are highly rated

financial institutions. In the unlikely event that the counterparties fail to meet the terms of the interest rate swap contracts, the Company's exposure is limited to the interest rate differential on the notional amount at each monthly settlement period over the life of the agreements. The Company does not anticipate any non-performance by the counterparties.

10

## Table of Contents

As of September 30, 2006, the Company had in place interest rate swap contracts to fix the floating interest rates on a portion of the borrowings under its debt facilities as summarized below:

| Swap Date         | Notional Amount | Fixed Leg Interest Rate | Term                        |
|-------------------|-----------------|-------------------------|-----------------------------|
| December 14, 2004 | \$200.0 million | 3.82%                   | 7 years — amortizing        |
| December 14, 2004 | \$200.0 million | 3.82%                   | 7 years — amortizing        |
| December 14, 2004 | \$100.0 million | 3.82%                   | 7 years — amortizing        |
| October 28, 2005  | \$100.0 million | 4.82%                   | 6 years — non-amortizing    |
| October 28, 2005  | \$25.0 million  | 4.71%                   | 2.75 years — non-amortizing |
| July 13, 2006     | \$50.0 million  | 5.52%                   | 5 years — non-amortizing    |
| July 19, 2006     | \$33.0 million  | 5.56%                   | 11 years — amortizing       |

As of April 12, 2006, in conjunction with the ABS program described above, the Company de-designated all of its existing interest rate swap contracts. Previously, the Company had designated all existing interest rate swap contracts as cash flow hedges, in accordance with Statement of Financial Accounting Standards No.133, "Accounting for Derivative Instruments and Hedging Activities". Therefore, during the designation period beginning November 1, 2005 through April 12, 2006, substantially all changes in the fair value of the interest rate swap contracts were reflected in accumulated other comprehensive income (loss). Changes in the fair value of these interest rate swap contracts in periods before and after designation have been recognized in the consolidated statements of operations as unrealized losses or gains on interest rate swaps.

At the time of de-designation, the change in fair value reflected in accumulated other comprehensive income was \$7.5 million. This amount is being recognized in income as unrealized (gain) loss on interest rate swaps using the interest method over the remaining life of the contracts. As of September 30, 2006, the unamortized pre-tax balance of the change in fair value reflected in accumulated other comprehensive income was \$6.0 million. The amount of other comprehensive income which will be amortized to income over the next 12 months is approximately \$2.4 million. Amounts recorded in accumulated other comprehensive income (loss) would be reclassified into earnings upon termination of these interest rate swap contracts and related debt instruments prior to their contractual maturity.

The net fair value of the interest rate swap contracts was \$12.4 million at September 30, 2006, and \$13.9 million at December 31, 2005. Fair value of \$13.4 million as of September 30, 2006 and \$13.9 million at December 31, 2005 are

included in other assets in the consolidated balance sheets. Fair value of \$1.0 million at September 30, 2006 is a liability and is included in accrued expenses in the consolidated balance sheets. In its consolidated statements of operations, the Company recognized a net unrealized loss of \$12.2 million for the three months ended September 30, 2006, a net unrealized (gain) of \$(7.6) million for the three months ended September 30, 2005, a net unrealized loss of \$8.6 million for the nine months ended September 30, 2006, and a net unrealized (gain) of \$(9.0) million for the nine months ended September 30, 2005, which predominantly represents the change in fair value of the interest rate swap contracts.

11

## Table of Contents

### Note 5 — Earnings (Loss) Per Share

The following table sets forth the calculation of basic and diluted earnings (loss) per share for the three and nine months ended September 30, 2006 and 2005 (in thousands, except earnings per share):

|                                                                                              | Three Months Ended<br>September 30, |             | Nine Months Ended<br>September 30, |             |
|----------------------------------------------------------------------------------------------|-------------------------------------|-------------|------------------------------------|-------------|
|                                                                                              | 2006                                | 2005        | 2006                               | 2005        |
| Numerator:                                                                                   |                                     |             |                                    |             |
| Net income (loss) applicable to common stockholders for basic and diluted earnings per share | \$ 4,450                            | \$ (12,323) | \$ 27,275                          | \$ (10,781) |
| Denominator:                                                                                 |                                     |             |                                    |             |
| Weighted average shares outstanding for basic earnings (loss) per share                      | 33,001                              | 10,204      | 32,927                             | 10,186      |
| Dilutive stock options                                                                       | 420                                 | —           | 523                                | —           |
| Weighted average shares for diluted earnings (loss) per share                                | 33,421                              | 10,204      | 33,450                             | 10,186      |
| Earnings (loss) per share:                                                                   |                                     |             |                                    |             |
| Basic                                                                                        | \$ 0.13                             | \$ (1.21)   | \$ 0.83                            | \$ (1.06)   |
| Diluted                                                                                      | \$ 0.13                             | \$ (1.21)   | \$ 0.82                            | \$ (1.06)   |

Options for 16,500 shares were considered to be anti-dilutive for the three and nine months ended September 30, 2006 and were therefore not included in the calculation of diluted earnings per share.

### Note 6 — Related Party Transactions

The Company recognized \$1.3 million for the three months ended September 30, 2005, and \$4.6 million for the nine months ended September 30, 2005 of management fees and expenses relating to the management consulting agreements with certain of the Company's stockholders. The management consulting agreements were terminated as of the effective date of the IPO, October 17, 2005.

### Note 7 — Segment and Geographic Information

#### Industry Segment Information

The Company operates in one industry segment, intermodal equipment leasing.

### Geographic Segment Information

The Company's customers use the containers for their global trade utilizing many worldwide trade routes. The following table represents the allocation of domestic (U.S.) and international revenues for the periods indicated based on the customers' primary domicile (in thousands):

|                     | Three Months Ended<br>September 30, |           | Nine Months Ended<br>September 30, |            |
|---------------------|-------------------------------------|-----------|------------------------------------|------------|
|                     | 2006                                | 2005      | 2006                               | 2005       |
| Total revenues:     |                                     |           |                                    |            |
| Domestic            | \$ 7,754                            | \$ 7,866  | \$ 22,517                          | \$ 23,474  |
| Asia                | 36,028                              | 36,790    | 105,203                            | 106,918    |
| Europe              | 27,665                              | 31,682    | 82,774                             | 95,314     |
| Other International | 5,228                               | 4,741     | 14,842                             | 13,438     |
| Total               | \$ 76,675                           | \$ 81,079 | \$ 225,336                         | \$ 239,144 |

12

### Table of Contents

As substantially all of the Company's containers are used internationally, where no one container is domiciled in one particular place for a prolonged period of time, all of the Company's containers are considered to be international.

### Note 8 — Commitments and Contingencies

At September 30, 2006, commitments for capital expenditures totaled approximately \$15.2 million, principally through the remainder of 2006.

### Note 9 — Income Taxes

The consolidated income tax expense for the nine month periods ended September 30, 2006 and 2005 was determined based upon estimates of the Company's consolidated effective income tax rates for the years ending December 31, 2006 and 2005, respectively. The difference between the consolidated effective income tax rate and the U.S. federal statutory rate is primarily attributable to state income taxes, foreign income taxes and the effect of certain permanent differences.

### Note 10 — Comprehensive Income

The following table provides a reconciliation of the Company's net income to comprehensive income (in thousands):

| Three Months Ended<br>September 30, | Nine Months Ended<br>September 30, |
|-------------------------------------|------------------------------------|
|-------------------------------------|------------------------------------|

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|                                                                                                                                                | 2006     | 2005       | 2006      | 2005     |
|------------------------------------------------------------------------------------------------------------------------------------------------|----------|------------|-----------|----------|
| Net income (loss)                                                                                                                              | \$ 4,450 | \$ (5,755) | \$ 27,275 | \$ 7,946 |
| Other comprehensive income (loss):                                                                                                             |          |            |           |          |
| Foreign currency translation adjustments                                                                                                       | 45       | (2)        | 180       | (45)     |
| Unrealized (loss) gain on derivative instruments designated as cash flow hedges (net of taxes of \$(243), \$0, \$2,162 and \$0, respectively ) | (433)    | —          | 4,550     | —        |
| Total                                                                                                                                          | \$ 4,062 | \$ (5,757) | \$ 32,005 | \$ 7,901 |

The balance included in comprehensive income for cumulative translation adjustments as of September 30, 2006 and September 30, 2005 was \$130 and \$(28), respectively.

## Note 11 — Subsequent Events

### Fourth Quarter Dividend

The Company's Board of Directors approved and declared a \$0.25 per share quarterly cash dividend on its issued and outstanding common stock, payable on December 8, 2006 to shareholders of record at the close of business on November 21, 2006.

13

## Table of Contents

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

The following discussion and analysis of the consolidated financial condition and results of operations of TAL International Group, Inc. and its subsidiaries should be read in conjunction with related consolidated financial data and our annual audited consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 20, 2006. The statements in this discussion regarding industry outlook, our expectations regarding our future performance, liquidity and capital resources and other non-historical statements are subject to numerous risks and uncertainties, including, but not limited to, the risks and uncertainties described under "Risk Factors" and "Forward-Looking Statements" in our Form 10-K. Our actual results may differ materially from those contained in or implied by any forward-looking statements.

### Our Company

We are one of the world's largest and oldest lessors of intermodal freight containers and chassis. Intermodal freight containers are large, standardized steel boxes used to transport freight by ship, rail or truck. Chassis are used for the transportation of containers domestically via rail and roads. Because of the handling efficiencies they provide, intermodal freight containers are the primary means by which many goods and materials are shipped internationally.

Our operations include the acquisition, leasing, re-leasing and subsequent sale of multiple types of intermodal containers and chassis. As of September 30, 2006, our fleet consisted of 645,622 containers and chassis, including 72,257 containers under management for third parties, representing more than one million twenty-foot equivalent units (TEU). We have an extensive global presence, offering leasing services through 20 offices in 12 countries and approximately 190 third party container depot facilities in 41 countries as of September 30, 2006. Our customers are among the world's largest shipping lines.

Our lease products provide numerous operational and financial benefits to our shipping line customers. These benefits include:

- Operating Flexibility — The timing, location and daily volume of cargo movements for a shipping line are often unpredictable. Leasing containers helps the shipping lines manage this uncertainty and minimize the requirement for large inventory buffers by allowing them to pick-up leased containers on short notice.
- Fleet Size Flexibility — Container leases allow shipping lines to adjust the size and mix of their fleets as their trade volumes change due to seasonality, market changes or changes in company strategies.
- Alternative Source of Financing — Container leases provide an additional source of equipment financing to help shipping lines manage the high level of investment required to maintain pace with the rapid growth of the asset-intensive container shipping industry.

We lease three principal types of containers: (1) dry freight containers, which are used for general cargo such as manufactured component parts, consumer staples, electronics and apparel, (2) refrigerated containers, which are used for perishable items such as fresh and frozen foods, and (3) special containers, which are used for heavy and oversized cargo such as marble slabs, building products and machinery. We also manage our own container disposals, act as the disposal agent for a number of our shipping line customers, and buy and sell used containers through our Trader group. As of September 30, 2006, dry, refrigerated, special containers and Trader represented approximately 86%, 5%, 7% and 1% of our fleet on a unit basis, respectively. Our chassis leasing business, which commenced in the fourth quarter of 2005, represented approximately 1% of our fleet on a unit basis as of September 30, 2006.

14

## Table of Contents

The following tables provide the composition of our equipment fleet as of the dates indicated below (in both units and TEU's). Certain reclassifications have been made to the accompanying prior period equipment fleet data to conform with the current year's presentation.

|              | Equipment Fleet in Units |         |         |                   |         |         |                    |         |         |
|--------------|--------------------------|---------|---------|-------------------|---------|---------|--------------------|---------|---------|
|              | September 30, 2006       |         |         | December 31, 2005 |         |         | September 30, 2005 |         |         |
|              | Owned *                  | Managed | Total   | Owned *           | Managed | Total   | Owned *            | Managed | Total   |
| Dry          | 499,947                  | 55,864  | 555,811 | 464,353           | 59,180  | 523,533 | 470,187            | 60,055  | 530,242 |
| Refrigerated | 34,300                   | 1,251   | 35,551  | 34,006            | 1,625   | 35,631  | 34,322             | 1,648   | 35,970  |
| Special      | 27,577                   | 15,142  | 42,719  | 27,389            | 16,025  | 43,414  | 27,443             | 16,315  | 43,758  |
| Chassis      | 6,079                    | —       | 6,079   | 1,210             | —       | 1,210   | —                  | —       | —       |
| Subtotal     | 567,903                  | 72,257  | 640,160 | 526,958           | 76,830  | 603,788 | 531,952            | 78,018  | 609,970 |
| Trader       | 5,462                    | —       | 5,462   | 10,123            | —       | 10,123  | 14,386             | —       | 14,386  |
| Total        | 573,365                  | 72,257  | 645,622 | 537,081           | 76,830  | 613,911 | 546,338            | 78,018  | 624,356 |

|     | Equipment Fleet in TEU's |         |         |                   |         |         |                    |         |         |
|-----|--------------------------|---------|---------|-------------------|---------|---------|--------------------|---------|---------|
|     | September 30, 2006       |         |         | December 31, 2005 |         |         | September 30, 2005 |         |         |
|     | Owned *                  | Managed | Total   | Owned *           | Managed | Total   | Owned *            | Managed | Total   |
| Dry | 798,123                  | 95,473  | 893,596 | 737,802           | 100,759 | 838,561 | 745,106            | 102,167 | 847,273 |

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|              |         |         |           |         |         |         |         |         |           |
|--------------|---------|---------|-----------|---------|---------|---------|---------|---------|-----------|
| Refrigerated | 61,682  | 1,898   | 63,580    | 60,674  | 2,394   | 63,068  | 61,019  | 2,435   | 63,454    |
| Special      | 43,465  | 24,994  | 68,459    | 42,249  | 26,179  | 68,428  | 42,195  | 26,594  | 68,789    |
| Chassis      | 10,608  | —       | 10,608    | 2,270   | —       | 2,270   | —       | —       | —         |
| Subtotal     | 913,878 | 122,365 | 1,036,243 | 842,995 | 129,332 | 972,327 | 848,320 | 131,196 | 979,516   |
| Trader       | 7,698   | —       | 7,698     | 15,968  | —       | 15,968  | 22,985  | —       | 22,985    |
| Total        | 921,576 | 122,365 | 1,043,941 | 858,963 | 129,332 | 988,295 | 871,305 | 131,196 | 1,002,501 |

\*Includes units placed on finance lease contracts.

We lease our equipment on a per diem basis to our customers under three types of leases: long-term leases, service leases and finance leases. Long-term leases, typically with terms of three to eight years, provide us with stable cash flow and low transaction costs by requiring customers to maintain specific containers on-hire for the duration of the lease. Service leases command a premium per diem rate in exchange for providing customers with a greater level of operational flexibility by allowing the pick-up and drop-off of containers during the lease term. Finance leases, which are typically structured as full payout leases, provide for a predictable recurring revenue stream with the lowest daily cost to the customer because customers are generally required to retain the container for the duration of its useful life. As of September 30, 2006, approximately 93% of our containers were on-hire to customers, with approximately 58% of our containers on long-term leases, approximately 27% on service leases or long-term leases whose fixed terms have expired but for which the related units remain on-hire and for which we continue to receive rental payments, and approximately 8% on finance leases. In addition, approximately 5% of our containers were available for lease and approximately 2% were available for sale.

15

## Table of Contents

The following table provides a summary of our lease portfolio, based on units in the fleet as of the dates indicated below:

|                                    | September<br>30,<br>2006 | December<br>31,<br>2005 | September<br>30,<br>2005 |
|------------------------------------|--------------------------|-------------------------|--------------------------|
| Lease Portfolio                    |                          |                         |                          |
| Long-term lease                    | 58.0%                    | 59.0%                   | 59.2%                    |
| Service lease                      | 26.8                     | 25.6                    | 26.7                     |
| Finance lease                      | 7.7                      | 4.6                     | 4.3                      |
| Total leased                       | 92.5                     | 89.2                    | 90.2                     |
| Existing units available for lease | 3.3                      | 5.1                     | 4.5                      |
| New units available for lease      | 1.8                      | 2.6                     | 2.7                      |
| Available for sale                 | 2.4                      | 3.1                     | 2.6                      |
| Total portfolio                    | 100.0%                   | 100.0%                  | 100.0%                   |

## Operating Performance

Our profitability is primarily determined by the extent to which our leasing and other revenues exceed our ownership, operating and administrative expenses. Our profitability is also impacted by the gain or loss that we realize on the sale of our used containers. During the first quarter of 2006, seasonal factors and market conditions placed pressure on our

profitability. Our operating profitability improved in the second and third quarters as we were able to benefit from an increase in container prices and an improvement in market conditions.

Our leasing revenue is primarily driven by our owned fleet size, utilization and average rental rates. Our leasing revenue is also impacted by the mix of leases in our portfolio. As of September 30, 2006, our owned fleet included 921,576 TEU, an increase of 7.3% from December 31, 2005. The increase in fleet size relative to the fourth quarter of 2005 was mainly due to the delivery of a large number of containers purchased in the first and second quarters of 2006. These container deliveries proved to be timely since they allowed us to capitalize on the strong leasing demand for dry containers that we experienced early in the second quarter and late in the third quarter. We expect the pace of container deliveries to slow in the fourth quarter since we ordered fewer containers in the third quarter due to price uncertainty and our expectation for reduced dry container demand after the end of the summer peak season.

Our September 30, 2006 owned container fleet size was 5.8% greater than our owned container fleet size as of September 30, 2005. Our fleet size decreased during the fourth quarter of 2005 due to a reduction in our trading equipment resale inventories and a reduction in our investment in new containers due to a temporary surplus of new containers in China.

Our average utilization was 91.0% in the third quarter of 2006, an increase of 1.2% from the second quarter of 2006. Ending utilization increased 1.6% from 90.9% as of June 30, 2006 to 92.5% as of September 30, 2006. We experienced strong demand for dry and special containers in the latter half of the third quarter, and we managed to increase our average utilization while also absorbing a net increase of over 20,000 TEU of containers in our fleet. Demand for refrigerated containers remained weak in the 2006 third quarter and the average utilization of our refrigerated containers decreased during the quarter. While the utilization of our refrigerated containers does not heavily influence our overall utilization, it has a disproportionate impact on our leasing revenue due to the much higher unit cost and lease rates of refrigerated containers.

Our average utilization in the third quarter of 2006 was 1.2% higher than it was in the third quarter of 2005, while our average utilization for the nine months ending September 30, 2006 was 0.9 % lower than our average utilization for the nine months ending September 30, 2005. In 2006, our utilization has increased on a quarterly basis due to the strong leasing demand for dry containers we experienced early in the second quarter and late in the third quarter of this year. During 2005, utilization was very high at the beginning of the year after the exceptional leasing market of 2004, but then decreased throughout the year due to a build-up of an excess inventory of new containers in China during the middle of the year.

16

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## Table of Contents

The following table sets forth our average fleet utilization for the periods indicated below:

|                     | September<br>30,<br>2006<br>3 months | September<br>30,<br>2005<br>3 months | September<br>30,<br>2006<br>9 months | September<br>30,<br>2005<br>9 months |
|---------------------|--------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|
| Average Utilization | 91.0%                                | 89.8%                                | 90.0%                                | 90.9%                                |

Average lease rates for our dry container product line in the third quarter decreased by 1.6% from the average level of the second quarter despite the high new container prices that prevailed during the third quarter. The decrease in average dry container leasing rates was primarily caused by several large lease extension transactions completed during the second and third quarters. The profitability of our shipping line customers has come under pressure this year due to a large increase in vessel capacity and declining freight rates, and our customers are actively seeking ways to reduce operating expenses. In several cases, we have responded to our customers' requests for lease rate reductions by renewing or extending lease agreements in return for lease rate savings, and in 2006 we have completed lease extension transactions that cover more than 10% of the dry containers and nearly 10% of the refrigerated containers in our fleet. While these lease extension transactions have reduced our current revenue, we expect they will have a positive impact on the net present value of our lease portfolio, particularly for our older containers, since they extend the revenue-earning life of the containers. The higher price of new containers has also not been heavily reflected in our average lease rates since most of the containers we supplied to our customers in the third quarter were placed on leases negotiated during the first quarter when container prices and market leasing rates were lower. New container prices began to decrease at the end of the third quarter, although they remain 15% to 20% higher than they were at the beginning of the year.

Average lease rates for refrigerated containers in the third quarter decreased by 4.8% from the average level in the second quarter mainly due to a large lease extension transaction completed at the beginning of the third quarter. Average rental rates for special containers decreased by 1.1% during the third quarter.

During the third quarter of 2006, the percentage of our units on finance leases increased to 7.7% compared to 4.3% as of September 30, 2005. Finance lease revenue increased from \$1.9 million to \$3.4 million for the three months ended September 30, 2006 as compared to the prior year period. Additionally, finance lease revenue increased from \$3.4 million to \$8.5 million for the nine months ended September 30, 2006 as compared to the prior year period. However, the increase in the portion of our units on finance leases resulted in a reduction in our overall leasing revenue, since under a finance lease we recognize interest income as revenue, whereas under an operating lease we recognize the entire monthly billing as revenue.

During the third quarter of 2006, we recognized a \$(1.9) million (gain) on the sale of our used containers compared to a \$(1.1) million (gain) in the second quarter of 2006 and a \$(1.2) million (gain) in the third quarter of 2005. The improvement compared to the second quarter of 2006 mainly resulted from higher sales volumes which reduced the number of containers in the assets held for sale category and allowed us to realize unrecognized gains on the units previously held for sale. The portion of our container fleet identified as for sale decreased from 3.3% as of June 30, 2006 to 2.4% as of September 30, 2006. The increase in gain relative to the third quarter of 2005 mainly resulted from higher volume of units sold, and placement of certain existing equipment on finance leases.

Our direct operating expenses decreased by \$1.1 million in the third quarter of 2006 from the second quarter of 2006 mainly due to lower positioning and storage costs. Our direct operating expenses for the third quarter of 2006 were also slightly less than our direct operating expenses in the third quarter of 2005.

Our ownership expenses, principally depreciation and interest expense increased by \$1.4 million in the third quarter of 2006 from the second quarter, mainly due to the increase in the size of our owned container fleet. However, our ownership expenses were much lower in the third quarter of 2006 than they were for the third quarter of 2005. The decrease in depreciation expense in 2006 resulted from the termination of depreciation charges for containers that reached the end of their accounting useful life at the end of 2005 but remain in our fleet. The significant reduction in interest expense in the third quarter of 2006 compared to the level we experienced in 2005 was due to the benefits of our

Table of Contents

securitization as well as the large reduction in the amount of outstanding debt and interest rates that we achieved as a result of our initial public offering in the fourth quarter of last year.

On July 31, 2006, we entered into a credit facility to support the growth of our finance lease business (the ‘‘Finance Lease Facility’’). Our borrowing capacity under this facility is based upon a 90% advance rate on the net present values of finance lease receivables on certain containers and chassis not included in the SPE. The Finance Lease Facility has a two year revolving period that precedes a 10 year term in which the outstanding balance, as of the term conversion date, amortizes in monthly installments.

On September 26, 2006, we paid a quarterly dividend of \$0.20 per share or an aggregate of approximately \$6.6 million on our issued and outstanding common stock. The dividend was paid to shareholders of record at the close of business on September 12, 2006. In addition, the Company repurchased 136,250 shares of its outstanding common stock in the open market during the quarter ended September 30, 2006 at a total cost of approximately \$2.9 million.

## Results of Operations

The following table summarizes our results of operations for the three months and nine months ended September 30, 2006 and 2005 in dollars and as a percentage of total revenues:

|                                               | Three Months Ended September 30, |         |          |         | Nine Months Ended September 30, |         |           |         |
|-----------------------------------------------|----------------------------------|---------|----------|---------|---------------------------------|---------|-----------|---------|
|                                               | 2006                             |         | 2005     |         | 2006                            |         | 2005      |         |
|                                               | Dollars                          | Percent | Dollars  | Percent | Dollars                         | Percent | Dollars   | Percent |
| Leasing revenues                              | \$67,827                         | 88.5%   | \$71,001 | 87.6%   | \$201,523                       | 89.4%   | \$215,084 | 89.9%   |
| Equipment trading revenue                     | 6,897                            | 9.0     | 7,774    | 9.6     | 17,673                          | 7.8     | 17,173    | 7.2     |
| Management fee income                         | 1,538                            | 2.0     | 1,566    | 1.9     | 4,687                           | 2.1     | 4,978     | 2.1     |
| Other revenues                                | 413                              | 0.5     | 738      | 0.9     | 1,453                           | 0.7     | 1,909     | 0.8     |
| Total revenues                                | 76,675                           | 100.0   | 81,079   | 100.0   | 225,336                         | 100.0   | 239,144   | 100.0   |
| Equipment trading expenses                    | 5,606                            | 7.3     | 6,026    | 7.4     | 14,545                          | 6.5     | 13,257    | 5.6     |
| Direct operating expenses                     | 6,311                            | 8.2     | 6,410    | 7.9     | 19,734                          | 8.8     | 20,707    | 8.7     |
| Administrative expenses                       | 9,350                            | 12.2    | 9,411    | 11.6    | 28,009                          | 12.4    | 28,362    | 11.9    |
| Depreciation and amortization                 | 26,590                           | 34.7    | 29,418   | 36.3    | 77,782                          | 34.5    | 88,076    | 36.8    |
| (Reversal) provision for doubtful accounts.   | (58)                             | (0.1)   | 528      | 0.7     | (500)                           | (0.2)   | 567       | 0.2     |
| Net (gain) on sale of leasing equipment       | (1,883)                          | (2.5)   | (1,178)  | (1.5)   | (2,859)                         | (1.3)   | (8,133)   | (3.4)   |
| Write-off of deferred financing costs         | —                                | —       | 24,313   | 30.0    | 2,367                           | 1.0     | 24,313    | 10.2    |
| Interest and debt expense                     | 11,686                           | 15.3    | 21,239   | 26.2    | 35,266                          | 15.7    | 63,849    | 26.7    |
| Unrealized loss (gain) on interest rate swaps | 12,174                           | 15.9    | (7,589)  | (9.4)   | 8,584                           | 3.8     | (8,975)   | (3.8)   |
| Management fees                               | —                                | —       | 1,346    | 1.7     | —                               | —       | 4,598     | 1.9     |
| Total expenses                                | 69,776                           | 91.0    | 89,924   | 110.9   | 182,928                         | 81.2    | 226,621   | 94.8    |
| Income (loss) before income taxes             | 6,899                            | 9.0     | (8,845)  | (10.9)  | 42,408                          | 18.8    | 12,523    | 5.2     |
| Income tax expense (benefit)                  | 2,449                            | 3.2     | (3,090)  | (3.8)   | 15,133                          | 6.7     | 4,577     | 1.9     |

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|                   |          |      |            |        |           |       |          |      |
|-------------------|----------|------|------------|--------|-----------|-------|----------|------|
| Net income (loss) | \$ 4,450 | 5.8% | \$ (5,755) | (7.1)% | \$ 27,275 | 12.1% | \$ 7,946 | 3.3% |
|-------------------|----------|------|------------|--------|-----------|-------|----------|------|

Comparison of Three Months Ended September 30, 2006 to Three Months Ended September 30, 2005.

Leasing revenues. The principal components of our leasing revenues are presented in the following table. Per diem revenue represents revenue earned under operating lease contracts; finance lease revenue represents interest income earned under finance lease contracts; and fee and ancillary lease revenue represent fees billed for the pick-up and drop-off of containers in certain geographic locations and billings of certain reimbursable operating costs such as repair and handling expenses.

18

Table of Contents

|                                 | Three Months Ended September<br>30, |           |
|---------------------------------|-------------------------------------|-----------|
|                                 | 2006                                | 2005      |
| Leasing revenues:               |                                     |           |
| Per diem revenue                | \$ 57,857                           | \$ 61,848 |
| Finance lease revenue           | 3,399                               | 1,934     |
| Fee and ancillary lease revenue | 6,571                               | 7,219     |
| Total leasing revenues          | \$ 67,827                           | \$ 71,001 |

Total leasing revenues were \$67.8 million for the three months ended September 30, 2006, compared to \$71.0 million for the three months ended September 30, 2005, a decrease of \$3.2 million, or 4.5%. The decrease primarily resulted from lower per diem rates for dry and refrigerated containers, and decreased utilization of refrigerated containers, partially offset by an increase in finance lease revenue and an increase in dry container utilization.

Equipment Trading Activities. Equipment trading revenue represents the proceeds on the sale of equipment purchased for resale. Equipment trading expenses represents the cost of equipment sold as well as related selling costs.

|                              | Three Months Ended September<br>30, |          |
|------------------------------|-------------------------------------|----------|
|                              | 2006                                | 2005     |
| Equipment trading revenues   | \$ 6,897                            | \$ 7,774 |
| Equipment trading expenses   | (5,606)                             | (6,026)  |
| Net equipment trading margin | \$ 1,291                            | \$ 1,748 |

The net equipment trading margin decreased \$0.5 million for the three months ended September 30, 2006 compared to the three months ended September 30, 2005. In 2005, third-party selling margins were supported by increasing used container sale prices for most of the year, which generally increased the value of our trading inventory during the period the containers were held.

Direct operating expenses. Direct operating expenses primarily consist of our costs to repair containers and chassis returned off lease, to store the equipment when it is not on lease, and to reposition equipment that has been returned to locations with weak leasing demand.

During the three months ended September 30, 2006, direct operating costs decreased by \$0.1 million compared to the same period of 2005, mainly due to a decrease in repair costs of \$0.5 million and positioning costs of \$0.5 million. These decreases were partially offset by higher surveying and inspection costs incurred on the acceptance of new units.

**Depreciation and amortization.** Depreciation and amortization was \$26.6 million for the three months ended September 30, 2006, compared to \$29.4 million for the three months ended September 30, 2005, a decrease of \$2.8 million or 9.5%. The decrease was primarily due to certain equipment becoming fully depreciated in the fourth quarter of 2005. In addition, a larger portion of our fleet was placed on finance leases in 2006, which are not subject to depreciation.

**(Reversal) provision for doubtful accounts.** There was a (reversal) for doubtful accounts for \$(0.1) million for the three months ended September 30, 2006, compared to a provision of \$0.5 million for the three months ended September 30, 2005.

**Net (gain) on sale of leasing equipment.** (Gain) on sale of equipment was \$(1.9) million for the three months ended September 30, 2006, compared to a (gain) of \$(1.2) million for the three months ended September 30, 2005, an increase of \$0.7 million. Results in 2006 were impacted by higher volume of units sold and gains related to the placement of certain existing equipment on finance leases.

**Write-off of deferred financing costs.** Write-off of deferred financing costs was zero for the three months ended September 30, 2006, compared to \$24.3 million for the three months ended September 30, 2005. The prior year write-off was the result of the refinancing of the Company's senior secured credit facility in August 2005.

19

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## Table of Contents

**Interest and debt expense.** Interest and debt expense was \$11.7 million for the three months ended September 30, 2006, compared to \$21.2 million for the three months ended September 30, 2005, a decrease of \$9.5 million. The decrease was primarily due to changes in our capital structure resulting from the IPO, which decreased our debt level and effective interest rate.

**Unrealized loss (gain) on interest rate swaps.** Unrealized loss on interest rate swaps was \$12.2 million for the three months ended September 30, 2006, compared to an unrealized (gain) of \$(7.6) million for the three months ended September 30, 2005. The fair market value of the swap contracts decreased to approximately \$12.4 million in the third quarter of 2006 due to a decrease in interest rates. The \$(7.6) million unrealized (gain) incurred in the three months ended September 30, 2005 represented an increase in the fair value of the interest rate swap contracts due to an increase in interest rates from the second quarter of 2005.

**Management fees.** Management fees were zero for the three months ended September 30, 2006, compared to \$1.3 million for the three months ended September 30, 2005. Management fees of \$1.3 million for the period ended September 30, 2005 were payable pursuant to certain management agreements which terminated upon the completion of the IPO in October 2005.

**Income tax expense (benefit).** Income tax expense was \$2.4 million for the three months ended September 30, 2006, compared to an income tax (benefit) of \$(3.1) million for the three months ended September 30, 2005, and the effective tax rates were 35.5% for the three months ended September 30, 2006 and 34.9% for the three months ended

September 30, 2005.

We do not expect to pay any significant U.S. federal or state or local income taxes for a number of years due to the availability of accelerated U.S. tax depreciation for our existing container fleet and our planned future equipment purchases. Any material changes in market conditions or company strategy could either accelerate or further defer the timing of our tax payments.

Comparison of Nine Months Ended September 30, 2006 to Nine Months Ended September 30, 2005.

**Leasing revenues.** The principal components of our leasing revenues are presented in the following table. Per diem revenue represents revenue earned under operating lease contracts; finance lease revenue represents interest income earned under finance lease contracts; and fee and ancillary lease revenue represent fees billed for the pick-up and drop-off of containers in certain geographic locations and billings of certain reimbursable operating costs such as repair and handling expenses.

|                                 | Nine Months Ended September 30, |            |
|---------------------------------|---------------------------------|------------|
|                                 | 2006                            | 2005       |
| Leasing revenues:               |                                 |            |
| Per diem revenue                | \$ 170,952                      | \$ 189,076 |
| Finance lease revenue           | 8,516                           | 3,356      |
| Fee and ancillary lease revenue | 22,055                          | 22,652     |
| Total leasing revenues          | \$ 201,523                      | \$ 215,084 |

Total leasing revenues were \$201.5 million for the nine months ended September 30, 2006, compared to \$215.1 million for the nine months ended September 30, 2005, a decrease of \$13.6 million, or 6.3%. The decrease primarily resulted from lower utilization and lower per diem rates for dry and refrigerated containers, partially offset by an increase in finance lease revenue due to an increase in the finance lease portfolio.

**Equipment Trading Activities.** Equipment trading revenue represents the proceeds on the sale of equipment purchased for resale. Equipment trading expenses represents the cost of equipment sold as well as related selling costs.

20

#### Table of Contents

|                              | Nine Months Ended September 30, |           |
|------------------------------|---------------------------------|-----------|
|                              | 2006                            | 2005      |
| Equipment trading revenues   | \$ 17,673                       | \$ 17,173 |
| Equipment trading expenses   | (14,545)                        | (13,257)  |
| Net equipment trading margin | \$ 3,128                        | \$ 3,916  |

The net equipment trading margin decreased \$0.8 million for the nine months ended September 30, 2006 compared to the nine months ended September 30, 2005. In 2005, third-party selling margins were supported by increasing used container sale prices for most of the year, which generally increased the value of our trading inventory during the period the containers were held.

**Direct operating expenses.** Direct operating expenses primarily consist of our costs to repair containers and chassis returned off lease, to store the equipment when it is not on lease, and to reposition equipment that has been returned to locations with weak leasing demand.

During the nine months ended September 30, 2006, direct operating expenses were \$19.7 million, compared to \$20.7 million for the nine months ended September 30, 2005, a decrease of 4.8%. Positioning costs decreased by \$1.0 million and repair costs decreased by \$2.7 million in the nine months ended September 30, 2006 compared to the same period of 2005. These decreases were partially offset by an increase in handling and storage costs of \$2.3 million.

**Depreciation and amortization.** Depreciation and amortization was \$77.8 million for the nine months ended September 30, 2006, compared to \$88.1 million for the nine months ended September 30, 2005, a decrease of \$10.3 million or 11.7%. The decrease was primarily due to certain equipment becoming fully depreciated in the fourth quarter of 2005. In addition, a larger portion of our fleet was placed on finance leases in 2006, which are not subject to depreciation.

**(Reversal) provision for doubtful accounts.** There was a (reversal) for doubtful accounts for \$(0.5) million for the nine months ended September 30, 2006, compared to a provision of \$0.6 million for the nine months ended September 30, 2005. In the nine months ended September 30, 2006, we recorded a benefit for the reversal of an allowance upon collecting a past due repair receivable from one of our large customers.

**Net (gain) on sale of leasing equipment.** (Gain) on sale of equipment was \$(2.9) million for the nine months ended September 30, 2006, compared to a (gain) of \$(8.1) million for the nine months ended September 30, 2005, a decrease of \$5.2 million. The (gain) recorded in 2005 included a \$(2.9) million benefit from the sale of on-hire containers to one of our customers and a sale of equipment to an investor as part of our managed equipment program. In addition, results in 2005 were supported by very strong selling prices for used containers.

**Write-off of deferred financing costs.** Write-off of deferred financing costs was \$2.4 million for the nine months ended September 30, 2006, compared to \$24.3 million for the nine months ended September 30, 2005. The current year write-off is the result of the refinancing of the Company's asset securitization facility in April 2006. The prior year write-off was the result of the refinancing of the Company's senior secured credit facility in August 2005.

**Interest and debt expense.** Interest and debt expense was \$35.3 million for the nine months ended September 30, 2006, compared to \$63.8 million for the nine months ended September 30, 2005, a decrease of \$28.5 million. The decrease was primarily due to changes in our capital structure resulting from the IPO, which decreased our debt level and effective interest rate.

**Unrealized loss (gain) on interest rate swaps.** Unrealized loss on interest rate swaps was \$8.6 million for the nine months ended September 30, 2006, compared to an unrealized (gain) of \$(9.0) million for the nine months ended September 30, 2005. The fair market value of the swap contracts decreased to approximately \$12.4 million as of September 30, 2006 due to a decrease in interest rates over the last nine months of 2006. The \$(9.0) million unrealized (gain) incurred in the nine months ended September 30, 2005 represented an increase in the fair value of the interest rate swap contracts due to an increase in expected interest rates from the beginning of 2005.

**Management fees.** Management fees were zero for the nine months ended September 30, 2006, compared to \$4.6 million for the nine months ended September 30, 2005. Management fees of

Table of Contents

\$4.6 million for the period ended September 30, 2005 were payable pursuant to certain management agreements which terminated upon the completion of the IPO in October 2005.

**Income tax expense.** Income tax expense was \$15.1 million for the nine months ended September 30, 2006, compared to income tax expense of \$4.6 million for the nine months ended September 30, 2005, and the effective tax rates were 35.7% for the nine months ended September 30, 2006 and 36.5% for the nine months ended September 30, 2005.

We do not expect to pay any significant U.S. federal or state or local income taxes for a number of years due to the availability of accelerated U.S. tax depreciation for our existing container fleet and our planned future equipment purchases. Any material changes in market conditions or company strategy could either accelerate or further defer the timing of our tax payments.

### Liquidity and Capital Resources

Our principal sources of liquidity are cash flows generated from operations, borrowings under our Asset Backed Securitization (“ABS”) program and our revolving credit facilities. Our cash flows will be used to finance capital expenditures, provide working capital, meet debt service requirements, and pay dividends. We believe that cash from operations and existing cash, together with available borrowings under our ABS program and our revolving credit facilities will be sufficient to meet our liquidity requirements for at least the next twelve months. However, our future operating performance and ability to extend or refinance our indebtedness will be dependent on future economic conditions and financial, business and other factors that are beyond our control.

At September 30, 2006, our outstanding indebtedness was comprised of the following (amounts in millions):

|                           | Current<br>Amount<br>Outstanding | Current<br>Maximum<br>Commitment<br>Level |
|---------------------------|----------------------------------|-------------------------------------------|
| ABS Term Notes            | \$ 651.7                         | \$ 651.7                                  |
| ABS Warehouse Facility    | 106.5                            | 300.0                                     |
| Revolving Credit Facility | 131.5                            | 165.0                                     |
| Finance Lease Facility    | 12.5                             | 50.0                                      |
| Swing Line Facility       | —                                | 10.0                                      |
| Other Debt                | 11.8                             | 11.8                                      |
| Capital Lease Obligations | 24.4                             | 24.4                                      |
| <b>Total Debt</b>         | <b>\$ 938.4</b>                  | <b>\$ 1,212.9</b>                         |

The maximum commitment levels depicted in the chart above may not reflect the actual availability under all of the credit facilities. Certain of these facilities are governed by borrowing bases that limit borrowing capacity to an established percentage of relevant assets.

### ABS Term Notes

On April 12, 2006, we issued our \$680.0 million floating rate secured notes (“ABS Term Notes”). The proceeds from the issuance were used to repay outstanding borrowings under our asset securitization facility. The ABS Term Notes

amortize in equal monthly installments and have a legal final maturity of April 2021.

#### ABS Warehouse Facility

On April 12, 2006, we entered into a floating rate revolving facility (the “ABS Warehouse Facility”). The ABS Warehouse Facility has a two year revolving period that precedes a term period in which the outstanding balance amortizes in equal monthly installments. The ABS Warehouse Facility has a legal final maturity of April 2023.

All debt to be issued under the ABS program is collateralized by the assets of TAL Advantage I LLC, a special purpose entity (the “SPE”) consisting of revenue earning containers that we use in our

22

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#### Table of Contents

leasing business, restricted cash and certain receivables related to revenue earning equipment. The Series 2005-1 Notes and the Series 2006-1 Notes were both issued by the SPE.

#### Revolving Credit Facilities

In connection with the Acquisition, the Company entered into an \$875.0 million Senior Secured Credit Facility (“SSCF”). Upon the closing of the Asset Securitization Facility on August 1, 2005, the Company amended and restated the SSCF to, among other things, reduce the maximum aggregate commitments thereunder to \$175.0 million. Effective June 1, 2006, the Company further amended the SSCF to reduce the interest rate margin from LIBOR plus 2.125% to LIBOR plus 1.375% and to reduce the maximum aggregate commitments thereunder to \$165.0 million. The final maturity date of this facility is August 1, 2008.

#### Finance Lease Facility

On July 31, 2006, the Company entered into a credit facility to support the growth of our finance lease business (the “Finance Lease Facility”). The Finance Lease Facility has a two year revolving period that precedes a 10 year term in which the outstanding balance, as of the term conversion date, amortizes in monthly installments. The Finance Lease Facility is secured by the finance lease receivables associated with certain containers and chassis not included in the SPE.

#### Capital Lease Obligations and Other Debt

The Company has entered into a series of capital leases with various financial institutions to finance the purchase of chassis. The lease agreements are structured as ten year Terminal Rental Adjustment Clause (“TRAC”) leases with purchase options at the end of the lease terms equal to the TRAC amount as defined in each lease. For income tax purposes, these leases are treated as operating leases.

During June 2006, the Company entered into an interim agreement with a financial institution to provide funding for chassis equipment that is intended to be included in a TRAC lease.

The Company is subject to various covenant requirements under its debt facilities. At September 30, 2006, the Company was in compliance with all covenants.

## Treasury Stock

On March 13, 2006, the Company's Board of Directors authorized a stock buyback program for the repurchase of up to 1.5 million shares of its common stock. The Company repurchased 136,250 shares of its outstanding common stock in the open market during the quarter ended September 30, 2006 at a total cost of approximately \$2.9 million.

## Dividends Paid

On September 26, 2006, the Company paid a quarterly dividend of \$0.20 per share or an aggregate of approximately \$6.6 million on its issued and outstanding common stock. The dividend was paid to shareholders of record at the close of business on September 12, 2006.

23

## Table of Contents

### Cash Flow

The following table sets forth certain cash flow information for the nine months ended September 30, 2006 and 2005 (in thousands):

|                                                              | Nine Months Ended September 30, |              |
|--------------------------------------------------------------|---------------------------------|--------------|
|                                                              | 2006                            | 2005         |
| Net cash provided by operating activities                    | \$ 154,422                      | \$ 133,187   |
| Net cash provided by (used in) investing activities:         |                                 |              |
| Purchases of leasing equipment                               | \$ (189,794)                    | \$ (132,235) |
| Investment in finance leases                                 | (39,895)                        | (42,110)     |
| Proceeds from sale of equipment                              | 42,999                          | 77,213       |
| Cash collections on financing leases, net of unearned income | 10,446                          | 4,181        |
| Other                                                        | 180                             | —            |
| Net cash (used in) investing activities                      | \$ (176,064)                    | \$ (92,951)  |
| Net cash provided by (used in) financing activities          | \$ 26,821                       | \$ (13,794)  |

### Operating Activities

Net cash provided by operating activities increased by \$21.2 million to \$154.4 million in the nine months ended September 30, 2006, compared to \$133.2 million in the nine months ended September 30, 2005 primarily due to an increase in net income.

### Investing Activities

Net cash used in investing activities was \$176.1 million in the nine months ended September 30, 2006, as compared to \$93.0 million in the nine months ended September 30, 2005. Capital expenditures were \$229.7 million, including investments in finance leases of \$39.9 million, in the nine months ended September 30, 2006, compared to \$174.3 million, including investments in finance leases of \$42.1 million, in the nine months ended September 30, 2005.

Capital expenditures increased by \$55.4 million primarily due to an increase in the number of units purchased, as well as higher per unit costs. Sales proceeds from the disposal of equipment decreased \$34.2 million to \$43.0 million in the nine months ended September 30, 2006, compared to \$77.2 million in the nine months ended September 30, 2005. Included in sales proceeds in the first nine months of 2005 were \$26.4 million of sale proceeds related to the sale of on-hire containers to one of our customers and the sale of containers to an investor as part of our managed equipment program. The remaining decrease in sales proceeds is primarily due to a decrease in equipment selling prices. Cash collections on financing leases, net of unearned income increased by \$6.2 million to \$10.4 million for the nine months ended September 30, 2006, compared to \$4.2 million for the nine months ended September 30, 2005 as a result of an increase in our finance lease portfolio.

## Financing Activities

Net cash provided by financing activities was \$26.8 million for the nine months ended September 30, 2006, compared to net cash used in financing activities of \$13.8 million for the nine months ended September 30, 2005. On April 12, 2006, we issued secured term notes under our ABS program and used the proceeds to pay off the outstanding balance on our Asset Securitization Facility. In addition, during the nine months ended September 30, 2006, we increased borrowings under our ABS Warehouse Facility and finance lease facility, the proceeds of which were primarily used to finance the purchase of new equipment. This was offset by net cash used to pay down borrowings on our ABS term notes and revolving credit facilities. In addition, cash was used during the third quarter 2006 to purchase treasury shares and pay dividends on our common stock outstanding. In the nine months ended September 30, 2005, net cash used in financing activities was primarily used to pay down borrowings under our senior secured credit facility.

24

## Table of Contents

### Contractual Obligations

We are party to various operating and capital leases and are obligated to make payments related to our long term borrowings. We are also obligated under various commercial commitments, including obligations to our equipment manufacturers. Our equipment manufacturer obligations are in the form of conventional accounts payable, and are satisfied from cash flows from operating and long term financing activities.

The following table summarizes our contractual obligations and commercial commitments as of September 30, 2006:

| Contractual Obligations by Twelve Month Period Ending September 30,<br>(dollars in millions) |            |          |          |          |          |                     |
|----------------------------------------------------------------------------------------------|------------|----------|----------|----------|----------|---------------------|
| Contractual Obligations:                                                                     | Total      | 2007     | 2008     | 2009     | 2010     | 2011 and thereafter |
| Total debt obligations <sup>(1)</sup> :                                                      | \$ 1,139.1 | \$ 126.4 | \$ 248.1 | \$ 112.2 | \$ 108.8 | \$ 543.6            |
| Capital lease obligations                                                                    | 33.2       | 2.9      | 4.1      | 2.2      | 2.5      | 21.5                |
| Operating leases (mainly facilities)                                                         | 5.3        | 1.6      | 1.2      | 1.2      | 1.3      | —                   |
| Equipment purchase obligations                                                               | 15.2       | 15.2     | —        | —        | —        | —                   |
| Total contractual obligations                                                                | \$ 1,192.8 | \$ 146.1 | \$ 253.4 | \$ 115.6 | \$ 112.6 | \$ 565.1            |

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<sup>(1)</sup>Amounts include actual and estimated interest for floating-rate debt based on September 30, 2006 rates and the net effect of the interest rate swaps.

#### Off-Balance Sheet Arrangements

At September 30, 2006, we did not have any relationships with unconsolidated entities or financial partnerships, such entities which are often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements. We are, therefore, not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

#### Critical Accounting Policies

Our consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States, which require us to make estimates and assumptions that affect the amounts and disclosures reported in the consolidated financial statements and accompanying notes. Our estimates are based on historical experience and currently available information. Actual results could differ from such estimates. The following paragraphs summarize our critical accounting policies. Additional accounting policies are discussed in the notes to our 2005 Form 10-K and elsewhere in this Form 10-Q.

#### Revenue Recognition

##### Operating Leases with Customers

We enter into long-term leases and service leases with ocean carriers and other parties, principally as lessor in operating leases, for marine cargo containers. Long-term leases provide the ocean carriers with specified container equipment for a specified term. Our leasing revenues are based upon the number of containers leased, the applicable per diem rate and the length of the lease. Long-term leases typically range for a period of three to eight years. Revenues are recognized on a straight-line basis over the life of the respective lease. Advanced billings are deferred and recognized in the period earned. Service leases do not specify the exact number of containers to be leased or the term that each container will remain on-hire but allow the lessee to pick up and drop off containers at various locations specified in the lease agreement. Under a service lease, rental revenue is based on the number of containers utilized at contracted per diem rates. Revenue for customers where collection is

25

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#### Table of Contents

not assured is deferred and recognized when the amounts are received. Also, in accordance with FASB EITF No. 99-19, Reporting Revenue Gross as a Principal versus Net as an Agent, we recognize billings to customers for damages incurred and certain other pass through costs as leasing revenue based on the terms of the contractual agreements with the customer.

#### Finance Leases with Customers

We enter into finance leases as lessor for container equipment that we own. The net investment in finance leases represents the receivables due from lessees, net of unearned income. Unearned income is recognized on a level yield basis over the lease term and is recognized as leasing revenue. Finance leases are usually long-term in nature, typically ranging for a period of five to ten years and may include a bargain purchase option to purchase the equipment at the

end of the lease term.

#### Leasing Equipment

Leasing equipment is recorded at cost and depreciated to an estimated residual value on a straight-line basis over the estimated useful life. We will continue to review our depreciation policies on a regular basis to determine whether changes have taken place that would suggest that a change in our depreciation policies, useful lives of our equipment or the assigned residual values is warranted. In addition, periodically a determination is made, if indicators of impairment are present, as to whether the carrying value of our fleet exceeds its estimated future undiscounted cash flows. The estimated useful lives for our leasing equipment ranges from 10 to 20 years from the date of manufacture. Estimated useful lives have been based on independent appraisals and will be adjusted if necessary based on actual experience. Costs incurred to place new equipment into service, including costs to transport the equipment to its initial on-hire location, are capitalized. We charge repair and maintenance costs as incurred and include these costs in direct operating expenses.

An allowance is provided through direct operating expenses based on the net book value of a percentage of the units on lease to certain customers that are considered to be non-performing which we believe we will not ultimately recover. The percentage is developed based on historical experience.

#### Equipment Held for Sale

In accordance with the Financial Accounting Standards Board ("FASB") Statement No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets ("SFAS No. 144"), container equipment held for sale is carried at the lower of its fair value, less costs to sell, based on current transactions, or carrying value; depreciation on such assets is halted and disposals generally occur within ninety days. Subsequent changes to the asset's fair value, either increases or decreases, are recorded as adjustments to the carrying value of the equipment held for sale; however, any such adjustments would not exceed the equipment's carrying value at the time it was initially classified as held for sale. Initial write-downs of assets held for sale are recorded as an impairment charge and are included in net (gain) loss on sale of leasing equipment. Realized gains and losses resulting from the sale of equipment held for sale are recorded as a net (gain) loss on sale of leasing equipment.

#### Allowance for Doubtful Accounts

Our allowance for doubtful accounts is updated on a regular basis and is based upon a review of the collectibility of our receivables. This review considers the risk profile of the customer, credit quality indicators such as the level of past-due amounts and economic conditions. An account is considered past due when a payment has not been received in accordance with the contractual terms. Accounts are generally charged off after an analysis is completed which indicates that collection of the full principal balance is deemed uncollectible. Changes in economic conditions or other events may necessitate additions or deductions to the allowance for doubtful accounts. The allowance for doubtful accounts is intended to provide for losses inherent in the accounts receivable, and requires the application of estimates and judgments as to the outcome of collection efforts and the realization of collateral, among other things. We believe our allowance for doubtful accounts is adequate to provide for credit losses inherent in our accounts receivable. However, actual losses could exceed the amounts provided for in certain periods.

## Recently Issued Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (“SFAS No. 157”) which addresses how companies should measure fair value when they are required to use a fair value measure for recognition or disclosure purposes under generally accepted accounting principles (GAAP). Under SFAS No. 157, there is now a common definition of fair value to be used throughout GAAP. The new standard will make the measurement of fair value more consistent and comparable and improve disclosures about those measures. The Company is required to adopt the provisions of SFAS No. 157 during the first fiscal year beginning after November 15, 2007. The Company is currently evaluating the impact of SFAS No. 157 on its consolidated results of operations and financial position.

In June 2006, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109,” (“FIN 48”). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The Company is required to adopt the provisions of FIN 48 during the first fiscal year beginning after December 15, 2006. The Company is currently evaluating the impact of FIN 48 on its consolidated results of operations and financial position.

### ITEM 3: Quantitative and Qualitative Disclosures About Market Risk

Market risk represents the risk of changes in value of a financial instrument, derivative or non-derivative, caused by fluctuations in interest rates, foreign exchange rates and equity prices. Changes in these factors could cause fluctuations in results of our operations and cash flows. In the ordinary course of business, we are exposed to foreign currency, interest rate, and credit risks.

#### Foreign Currency Exchange Rate Risk

Although we have significant foreign-based operations, the U.S. dollar is the operating currency for the large majority of our leases (both customers obligations and company obligations), and most of our revenues and expenses in 2006 and 2005 were denominated in U.S. dollars. As a result, foreign currency fluctuations did not materially impact our financial results in those periods.

#### Interest Rate Risk

We enter into interest rate swap contracts to fix the interest rates on a portion of our debt. We assess and manage the external and internal risk associated with these derivative instruments in accordance with the overall operating goals. External risk is defined as those risks outside of our direct control, including counterparty credit risk, liquidity risk, systemic risk and legal risk. Internal risk relates to those operational risks within the management oversight structure and includes actions taken in contravention of our policy.

The primary external risk of our interest rate swap contracts is counterparty credit exposure, which is defined as the ability of a counterparty to perform its financial obligations under a derivative contract. All derivative agreements are with major money center financial institutions rated investment grade by nationally recognized rating agencies, with our counterparties rated “AA” or better. Credit exposures are measured based on the market value of outstanding derivative instruments. Both current exposures and potential exposures are calculated for each derivative contract to monitor counterparty credit exposure.

Table of Contents

As of September 30, 2006, the Company had in place interest rate swap contracts to fix the floating interest rates on a portion of the borrowings under its debt facilities as summarized below:

| Swap Date         | Notional Amount | Fixed Leg<br>Interest Rate | Term                        |
|-------------------|-----------------|----------------------------|-----------------------------|
| December 14, 2004 | \$200.0 million | 3.82%                      | 7 years — amortizing        |
| December 14, 2004 | \$200.0 million | 3.82%                      | 7 years — amortizing        |
| December 14, 2004 | \$100.0 million | 3.82%                      | 7 years — amortizing        |
| October 28, 2005  | \$100.0 million | 4.82%                      | 6 years — non-amortizing    |
| October 28, 2005  | \$25.0 million  | 4.71%                      | 2.75 years — non-amortizing |
| July 13, 2006     | \$50.0 million  | 5.52%                      | 5 years — non-amortizing    |
| July 19, 2006     | \$33.0 million  | 5.56%                      | 11 years — amortizing       |

Changes in the fair value on these interest rate swap contracts will be recognized in the consolidated statements of operations as unrealized gains or losses on interest rate swaps.

While we utilize interest rate swap contracts to manage the market risk associated with fluctuations in interest rates on a large portion of our variable rate indebtedness, our earnings are affected by changes in interest rates. If market interest rates for our variable rate indebtedness averaged 50 basis points more than the weighted average interest rate actually paid during the three months ended September 30, 2006, our interest expense, after considering the effects of our interest rate swap agreements, would have increased, and income before incomes taxes would have decreased, by \$0.8 million for the three months ended September 30, 2006. These amounts are determined by considering the impact of the hypothetical interest rates on our borrowings and interest rate swap agreements. This analysis does not consider the effects of the reduced level of overall economic activity that could exist in such an environment.

Credit Risk

We maintain detailed credit records regarding our customers and set maximum exposure limits for our significant customers based on our review of these records. Credit criteria include, but are not limited to, customer payment history, customer financial position and performance (e.g., net worth leverage, profitability, trade routes, country of domicile, social and political climate, and the type of, and location of, containers that are to be supplied.) We diligently monitor our customers' performance and our lease exposures on an ongoing basis, and our credit management processes are aided by the long payment experience we have with most of our customers and our broad network of long-standing relationships in the shipping industry that provide current information about our customers.

Industry factors that provide incremental credit protection include the strong growth in the container industry, effective collection tools, our high recovery rate for containers in default situations and the re-marketability of our container fleet. The strong growth in the container industry helps minimize the risk of customer defaults since the core assets of a poorly performing shipping line, its ships and containers, are generally needed to meet world containerized trade demand. As a result, poorly performing shipping lines are often acquired by others. In addition, the law in certain major port locations is highly favorable to creditors and many of our large customers call on ports that will allow us to arrest, or seize, the customer's ships or bunkers, or repossess our containers if the customer is in default under our container leases. We have historically recovered approximately 90% of our containers that were the subject of defaulted contracts and we are able to successfully re-market these repossessed containers through our worldwide

sales infrastructure. However, we typically incur operating expenses such as repairs and positioning when containers are recovered after a customer default.

For the nine months ended September 30, 2006, our five largest customers accounted for approximately 46% of our leasing revenues, with our largest customer accounting for approximately 18% of our leasing revenues. As of September 30, 2006, approximately 78% of our containers were on-hire to our 20 largest customers.

The allowance for doubtful accounts is an estimate of allowances necessary for receivables on our operating lease receivables.

28

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## Table of Contents

### ITEM 4. CONTROLS AND PROCEDURES.

Based upon the required evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended (the “Exchange Act”)), our President and Chief Executive Officer and our Vice President and Chief Financial Officer concluded that as of September 30, 2006 our disclosure controls and procedures were adequate and effective to ensure that information was gathered, analyzed and disclosed on a timely basis.

There has been no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during our fiscal quarter ended September 30, 2006, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

29

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## Table of Contents

## PART II — OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS.

From time to time, we are a party to litigation matters arising in connection with the normal course of our business. While we cannot predict the outcome of these matters, in the opinion of our management, based on information presently available to us, we believe that we have adequate legal defenses, reserves or insurance coverage and any liability arising from these matters will not have a material adverse effect on our business. Nevertheless, unexpected adverse future events, such as an unforeseen development in our existing proceedings, a significant increase in the number of new cases or changes in our current insurance arrangements could result in liabilities that have a material adverse impact on our business.

### ITEM 1A. RISK FACTORS.

For a complete listing of our risk factors, refer to our 2005 Form 10-K filed with the Securities and Exchange Commission on March 20, 2006.

### ITEM 2.

**UNREGISTERED SALES OF EQUITY SECURITIES, USE OF PROCEEDS AND  
ISSUER REPURCHASES OF EQUITY SECURITIES.**

The following table provides information relating to the Company's repurchase of common stock for the quarter ended September 30, 2006:

| Period                           | Total<br>Number<br>Of<br>Shares<br>Purchased | Average<br>Price<br>Paid<br>Per Share | Total Number<br>Of<br>Shares<br>Purchased<br>As Part Of<br>Publicly<br>Announced Plan | Maximum<br>Number<br>Of Shares That<br>May Yet Be<br>Purchased<br>Under<br>The Plan <sup>(1)</sup> |
|----------------------------------|----------------------------------------------|---------------------------------------|---------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------|
| July 1 – July 31, 2006           | —                                            | —                                     | —                                                                                     | 1,500,000                                                                                          |
| August 1 – August 31, 2006       | 118,550                                      | \$ 20.95                              | 118,550                                                                               | 1,381,450                                                                                          |
| September 1 – September 30, 2006 | 17,700                                       | \$ 21.36                              | 17,700                                                                                | 1,363,750                                                                                          |
| Total                            | 136,250                                      |                                       | 136,250                                                                               |                                                                                                    |

<sup>(1)</sup>In March 2006, the Board of Directors of the Company authorized a stock buyback program for the repurchase of up to 1,500,000 shares of our common stock. As of September 30, 2006, 1,363,750 shares may yet be purchased under the stock buyback program.

**ITEM 6. EXHIBITS.**

| Exhibit<br>Number | Exhibit Description                                                                                                                       |
|-------------------|-------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1*             | Certification of the Chief Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as amended |
| 31.2*             | Certification of the Chief Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as amended |
| 32.1*             | Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350                                                               |
| 32.2*             | Certification by Chief Financial Officer pursuant to 18 U.S.C. Section 1350                                                               |

\*Filed herewith.

30

Table of Contents

**SIGNATURE**

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.

TAL International Group, Inc.

November 9, 2006

/s/ Chand Khan  
Chand Khan  
Vice President and  
Chief Financial Officer  
(Principal Accounting Officer)

31

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