

BARRETT BUSINESS SERVICES INC
Form 10-Q
August 08, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2012

Commission File No. 0-21886

BARRETT BUSINESS SERVICES, INC.

(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of

52-0812977
(IRS Employer

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incorporation or organization)

Identification No.)

8100 NE Parkway Drive, Suite 200

Vancouver, Washington
(Address of principal executive offices)

(360) 828-0700

98662
(Zip Code)

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Number of shares of common stock, \$.01 par value, outstanding at July 31, 2012 was 7,003,931 shares.

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Part I Financial Information

Item 1. Financial Statements

BARRETT BUSINESS SERVICES, INC.

Consolidated Balance Sheets

(Unaudited)

(In thousands, except per share amounts)

	June 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 36,358	\$ 49,571
Marketable securities	14,240	16,878
Trade accounts receivable, net	63,433	46,520
Income taxes receivable	3,432	4,133
Prepaid expenses and other	2,914	5,897
Deferred income taxes	5,931	5,958
Total current assets	126,308	128,957
Marketable securities	17,439	15,395
Property, equipment and software, net	15,832	15,007
Restricted marketable securities and workers' compensation deposits	9,932	9,923
Other assets	3,035	3,027
Workers' compensation receivables for insured losses and recoveries	1,601	2,968
Goodwill	47,820	47,820
	\$ 221,967	\$ 223,097

LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 1,913	\$ 1,639
Accrued payroll, payroll taxes and related benefits	68,385	52,340
Income taxes payable	193	0
Other accrued liabilities	350	300
Workers' compensation claims liabilities	19,670	18,718
Safety incentives liability	7,541	6,321
Total current liabilities	98,052	79,318
Long-term workers' compensation claims liabilities	35,231	30,596
Long-term workers' compensation claims liabilities for insured claims	864	1,879
Deferred income taxes	8,152	8,152
Mandatorily redeemable preferred stock, \$.01 par value; 50 shares authorized; 35 and 0 shares issued and outstanding	34,800	0
Customer deposits and other long-term liabilities	1,502	1,497
Commitments and contingencies		
Stockholders' equity:		

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Preferred stock, \$.01 par value; 450 shares authorized; no shares issued and outstanding	0	0
Common stock, \$.01 par value; 20,500 shares authorized, 7,003 and 9,871 shares issued and outstanding	70	99
Additional paid-in capital	316	20,943
Accumulated other comprehensive income (loss)	9	(34)
Retained earnings	42,971	80,647
	43,366	101,655
	\$ 221,967	\$ 223,097

The accompanying notes are an integral part of these financial statements

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BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Operations

(Unaudited)

(In thousands, except per share amounts)

	Three Months Ended June 30,	
	2012	2011
Revenues:		
Staffing services	\$ 30,387	\$ 30,518
Professional employer service fees	65,113	45,495
Total revenues	95,500	76,013
Cost of revenues:		
Direct payroll costs	22,843	23,093
Payroll taxes and benefits	39,332	28,886
Workers compensation	16,984	10,753
Total cost of revenues	79,159	62,732
Gross margin	16,341	13,281
Selling, general and administrative expenses	10,549	8,871
Depreciation and amortization	357	331
Income from operations	5,435	4,079
Other income:		
Investment income, net	205	273
Other	(9)	(7)
Other income	196	266
Income before income taxes	5,631	4,345
Provision for income taxes	1,888	896
Net income	\$ 3,743	\$ 3,449
Basic earnings per common share	\$.54	\$.34
Weighted average number of basic common shares outstanding	6,995	10,196
Diluted earnings per common share	\$.53	\$.34
Weighted average number of diluted common shares outstanding	7,078	10,245
Dividends declared per common share	\$.11	\$.09

The accompanying notes are an integral part of these financial statements

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BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Operations

(Unaudited)

(In thousands, except per share amounts)

	Six Months Ended June 30,	
	2012	2011
Revenues:		
Staffing services	\$ 56,598	\$ 58,850
Professional employer service fees	121,324	85,932
Total revenues	177,922	144,782
Cost of revenues:		
Direct payroll costs	42,495	44,541
Payroll taxes and benefits	82,324	60,649
Workers compensation	30,205	20,713
Total cost of revenues	155,024	125,903
Gross margin	22,898	18,879
Selling, general and administrative expenses	20,313	17,698
Depreciation and amortization	704	666
Income from operations	1,881	515
Other income:		
Life insurance proceeds	0	10,000
Investment income, net	428	628
Other	(16)	92
Other income	412	10,720
Income before income taxes	2,293	11,235
Provision for income taxes	763	2,240
Net income	\$ 1,530	\$ 8,995
Basic earnings per common share	\$.18	\$.88
Weighted average number of basic common shares outstanding	8,435	10,198
Diluted earnings per common share	\$.18	\$.88
Weighted average number of diluted common shares outstanding	8,511	10,246
Dividends declared per common share	\$.22	\$.18

The accompanying notes are an integral part of these financial statements

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BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Comprehensive Income

(Unaudited)

(In thousands)

	Three Months Ended June 30,	
	2012	2011
Net income	\$ 3,743	\$ 3,449
Unrealized gains on marketable securities, net of tax of \$1 and \$6 in 2012 and 2011, respectively	2	10
Comprehensive income	\$ 3,745	\$ 3,459

	Six Months Ended June 30,	
	2012	2011
Net income	\$ 1,530	\$ 8,995
Unrealized gains on marketable securities, net of tax of \$27 and \$22 in 2012 and 2011, respectively	43	35
Comprehensive income	\$ 1,573	\$ 9,030

The accompanying notes are an integral part of these financial statements

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BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Stockholders' Equity

Six Months Ended June 30, 2012 and 2011

(In thousands)

	Common Stock		Additional	Accumulated	Retained	Total
	Shares	Amount	Paid-in	Comprehensive	Earnings	
			Capital	(Loss)		
				Income		
Balance, December 31, 2010	10,202	\$ 102	\$ 25,164	\$ (65)	\$ 70,164	\$ 95,365
Common stock issued on exercise of options	3	0	5	0	0	5
Stock option compensation expense, net of tax	0	0	192	0	0	192
Tax benefit of stock option exercises	0	0	13	0	0	13
Repurchase of common stock	(65)	(1)	(922)	0	0	(923)
Cash dividend on common stock	0	0	0	0	(1,837)	(1,837)
Unrealized holding gains on marketable securities, net of tax	0	0	0	35	0	35
Net income	0	0	0	0	8,995	8,995
Balance, June 30, 2011	10,140	101	24,452	(30)	77,322	101,845
Balance, December 31, 2011	9,871	99	20,943	(34)	80,647	101,655
Common stock issued on exercise of options	118	1	1,688	0	0	1,689
Stock option compensation expense, net of tax	0	0	285	0	0	285
Tax benefit of stock option exercises	0	0	264	0	0	264
Repurchase of common stock	(2,986)	(30)	(22,864)	0	(37,338)	(60,232)
Cash dividend on common stock	0	0	0	0	(1,868)	(1,868)
Unrealized holding gains on marketable securities, net of tax	0	0	0	43	0	43
Net income	0	0	0	0	1,530	1,530
Balance, June 30, 2012	7,003	70	\$ 316	\$ 9	\$ 42,971	\$ 43,366

The accompanying notes are an integral part of these financial statements

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BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Six Months Ended June 30,	
	2012	2011
Cash flows from operating activities:		
Net income	\$ 1,530	\$ 8,995
Reconciliations of net income to net cash provided by operating activities:		
Depreciation and amortization	704	666
Gains recognized on marketable securities	0	(100)
Gain recognized on sale and leaseback	(61)	(61)
Deferred income taxes	53	292
Share based compensation	285	192
Changes in certain assets and liabilities:		
Trade accounts receivable, net	(16,913)	(22,142)
Income taxes receivable	701	0
Prepaid expenses and other	2,983	(628)
Accounts payable	274	(270)
Accrued payroll, payroll taxes and related benefits	16,045	22,830
Other accrued liabilities	50	364
Income taxes payable	193	498
Workers compensation claims liabilities	5,939	1,810
Safety incentives liability	1,220	33
Customer deposits, long-term liabilities and other assets, net	56	23
Net cash provided by operating activities	13,059	12,502
Cash flows from investing activities:		
Purchase of property and equipment	(1,527)	(445)
Proceeds from sales and maturities of marketable securities	22,924	18,562
Purchase of marketable securities	(22,313)	(32,710)
Proceeds from maturities of restricted marketable securities	4,671	3,360
Purchase of restricted marketable securities	(4,680)	(3,979)
Net cash used in investing activities	(925)	(15,212)
Cash flows from financing activities:		
Proceeds from exercise of stock options	1,689	5
Dividends paid	(1,868)	(1,837)
Repurchase of common stock	(25,432)	(923)
Tax benefit of stock option exercises	264	13
Net cash used in financing activities	(25,347)	(2,742)
Net decrease in cash and cash equivalents	(13,213)	(5,452)
Cash and cash equivalents, beginning of period	49,571	30,924

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Cash and cash equivalents, end of period	\$ 36,358	\$ 25,472
Supplemental schedule of noncash financing activities:		
Issuance of mandatorily redeemable preferred stock	\$ 34,800	\$ 0
	\$ 34,800	\$ 0

The accompanying notes are an integral part of these financial statements

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BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited)

Note 1 Basis of Presentation of Interim Period Statements

The accompanying consolidated financial statements are unaudited and have been prepared by Barrett Business Services, Inc. (Barrett , BBSI , the Company , our or we), pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures typically included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the results for the interim periods presented. The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from such estimates and assumptions. The consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s 2011 Annual Report on Form 10-K at pages F1 F28. The results of operations for an interim period are not necessarily indicative of the results of operations for a full year.

Revenue recognition

We recognize revenue as services are rendered by our workforce. Staffing services are engaged by customers to meet short-term and long-term personnel needs. Professional employer organization (PEO) services are normally used by organizations to satisfy ongoing human resource management needs and typically involve contracts with a minimum term of one year, which cover all employees at a particular work site. Our PEO contracts are renewable on an annual basis and typically require 30 days written notice to cancel or terminate the contract by either party. Our PEO contracts provide for immediate termination upon any default of the client regardless of when notice is given. We report PEO revenues on a net basis because we are not the primary obligor for the services provided by our PEO clients to their customers pursuant to our PEO contracts. Consequently, our PEO service fee revenues represent the gross margin generated from our PEO services after deducting the amounts invoiced to PEO customers for direct payroll expenses such as salaries, wages, health insurance and employee out-of-pocket expenses incurred incidental to employment and safety incentives. These amounts are also excluded from cost of revenues. PEO service fees also include amounts invoiced to our clients for employer payroll-related taxes and workers compensation coverage.

Marketable securities

As of June 30, 2012, the Company s marketable securities consisted of tax-exempt municipal securities, corporate bonds and U.S. treasuries. The Company classifies municipal securities, U.S. treasuries, and certain of its corporate bonds as available for sale; they are reported at fair value with unrealized gains and losses, net of taxes, shown as a component of accumulated other comprehensive income (loss) in stockholders equity. In the event a loss is determined to be other-than-temporary, the loss will be recognized in the statement of operations. Certain of the Company s corporate bonds are classified as held-to-maturity and are reported at amortized cost.

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BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) *(Continued)*

Note 1 Basis of Presentation of Interim Period Statements (Continued)

Allowance for doubtful accounts

The Company had an allowance for doubtful accounts of \$366,000 and \$452,000 at June 30, 2012 and December 31, 2011, respectively. The Company must make estimates of the collectibility of accounts receivable. Management analyzes historical bad debts, customer concentrations, customer creditworthiness, current economic conditions and changes in customers' payment trends when evaluating the adequacy of the allowance for doubtful accounts. The Company deems an account balance uncollectible only after it has pursued all available assets of the customer and, where applicable, the assets of the personal guarantor.

Workers' compensation claims

The Company is a self-insured employer with respect to workers' compensation coverage for all of its employees (including employees subject to PEO contracts) working in California, Oregon, Maryland, Delaware and Colorado. In the state of Washington, state law allows only the Company's staffing services and internal management employees to be covered under the Company's self-insured workers' compensation program. Additionally, the Company operates a wholly-owned fully licensed insurance company, Ecole Insurance Company (Ecole), in Arizona to provide workers' compensation coverage to our employees in Arizona.

To manage our financial exposure, in the event of catastrophic injuries or fatalities, the Company maintains excess workers' compensation insurance through our wholly owned captive insurance company, Associated Insurance Company for Excess (AICE), with a per occurrence retention of \$5.0 million, except in Maryland and Colorado, where our per occurrence retention is \$1.0 million and \$500,000, respectively. AICE maintains excess workers' compensation insurance coverage with Chartis, formerly known as American Insurance Group, Inc., between \$5.0 million and \$15.0 million per occurrence, except in Maryland, where coverage with Chartis is between \$1.0 million and \$25.0 million per occurrence, and in Colorado, where the coverage with Chartis is between \$500,000 and statutory limits per occurrence. The Company continues to evaluate the financial capacity of our insurers to assess the recoverability of the related insurer receivables.

The Company has provided a total of \$55.8 million and \$51.2 million at June 30, 2012 and December 31, 2011, respectively, as an estimated future liability for unsettled workers' compensation claims liabilities. Included in the foregoing liabilities are insured claims that will be paid by the Company's former excess workers' compensation insurer and for which the Company has reported a receivable from the insurer for the insured claims liability. These insured claims totaled \$864,000 at June 30, 2012 and \$1.9 million at December 31, 2011. The estimated liability for unsettled workers' compensation claims represents management's best estimate based upon an actuarial valuation provided by a third party actuary. Included in the claims liabilities are case reserve estimates for reported losses, plus additional amounts based on projections for incurred but not reported claims and anticipated increases in case reserve estimates. Also included in these estimates are amounts for unallocated loss adjustment expenses, including legal costs. These estimates are continually reviewed and adjustments to liabilities are reflected in current operating results as they become known.

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BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) *(Continued)*

Note 1 Basis of Presentation of Interim Period Statements (Continued)

Safety incentives liability

Safety incentives represent cash incentives paid to certain PEO client companies for maintaining safe-work practices in order to minimize workplace injuries, thereby meeting agreed-upon loss objectives. The Company has provided \$7.5 million at June 30, 2012 and \$6.3 million at December 31, 2011 as an estimate of the liability for unpaid safety incentives. The incentive is based on a percentage of annual payroll and is paid annually to customers who meet predetermined workers' compensation claims cost objectives. Safety incentive payments are made only after closure of all workers' compensation claims incurred during the customer's contract period. The liability is estimated and accrued each month based upon the incentive earned less the then-current amount of the customer's estimated workers' compensation claims reserves as established by the Company's internal and third-party claims administrators, and the expected payout as determined by historical incentive payment trends. Safety incentive expense is netted against PEO services revenue in our consolidated statements of operations.

Note 2 Stock Repurchase

Effective March 28, 2012, the Company repurchased 2,485,929 shares of the Company's common stock held by the Estate of William W. Sherertz and 500,000 common shares held by Nancy Sherertz. Mr. Sherertz, a founder and former president and CEO of the Company, died January 20, 2011. Nancy Sherertz is also a founder of the Company. The common shares were repurchased at a price of \$20 per share, representing total consideration of \$59.7 million. The Company used a combination of \$24.9 million in cash and issued 34,800 shares of Series A Nonconvertible, Non-Voting Redeemable Preferred Stock with a liquidation preference of \$1,000 per share. Additionally, the Company incurred professional and legal fees totaling \$514,000 related to the transaction. The preferred stock is entitled to receive cumulative preferential dividends at the rate of 5% per annum based upon the \$1,000 liquidation preference with such rate increasing by 2% on each April 1 beginning April 1, 2013, until all of the outstanding preferred stock has been redeemed. The Company may pay the dividends in cash or in additional shares of preferred stock at its option. The Company may redeem all or a portion of the preferred stock at its option at any time at a price of \$1,000 per share. The preferred stock is subject to mandatory redemption five years from the original issue date. Due to the mandatory redemption provision the preferred stock is classified as a liability on the Company's consolidated balance sheet.

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BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 3 Basic and Diluted Earnings Per Share

Basic earnings per share are computed based on the weighted average number of common shares outstanding during the period. Diluted earnings per common share reflect the potential effects of the exercise of outstanding stock options. Basic and diluted common shares outstanding are summarized as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Weighted average number of basic common shares outstanding	6,995,066	10,195,989	8,434,962	10,198,440
Assumed exercise of stock options, net of shares assumed repurchased at average market price during the period using proceeds received upon exercise of options	83,010	48,725	76,313	47,805
Weighted average number of diluted common shares outstanding	7,078,076	10,244,714	8,511,275	10,246,245

Note 4 Stock Incentive Plans and Stock-Based Compensation

The following table summarizes stock option activity in 2012 under the Company's 2009 Stock Incentive Plan:

	Number of Options	Weighted Average Exercise Price
Outstanding at December 31, 2011	671,294	\$ 14.48
Options granted	7,500	\$ 17.55
Options exercised	(118,472)	\$ 14.26
Options cancelled or expired	0	
Outstanding at June 30, 2012	560,322	\$ 14.57
Exercisable at June 30, 2012	252,797	\$ 13.49
Available for grant at June 30, 2012	626,300	

During 2012, the Company granted 7,500 options at a fair value of \$9.08 per share as determined under the Black-Scholes option-pricing model.

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BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) *(Continued)*

Note 4 Stock Incentive Plans and Stock-Based Compensation (Continued)

The following table presents information on stock options outstanding for the periods shown: