BARRETT BUSINESS SERVICES INC
Form 10-Q
May 10, 2007
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 March 31, 2007

Commission File No. 0-21886

BARRETT BUSINESS SERVICES, INC.

(Exact name of registrant as specified in its charter)

Maryland	52-0812977
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
8100 NE Parkway Drive, Suite 200 Vancouver, Washington (Address of principal executive offices)	98662 (Zip Code)

(360) 828-0700

(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 x No o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

Number of shares of common stock, $.01 par value, outstanding at April 27, 2007 was 11,260,796 shares.

BARRETT BUSINESS SERVICES, INC.

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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)

	March 31, 2007	December 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 69,707	$ 69,874
Marketable securities	3,845	3,159
Trade accounts receivable, net	35,420	31,328
Prepaid expenses and other	2,551	1,940
Deferred income taxes	4,719	4,699
Workers compensation receivables for insured claims	225	225
Total current assets	116,467	111,225
Marketable securities	409	406
Goodwill, net	28,036	27,536
Intangibles, net	69	75
Property, equipment and software, net	13,383	13,502
Restricted marketable securities and workers compensation deposits	2,703	2,616
Other assets	1,718	2,143
Workers compensation receivables for insured claims	4,629	4,678
	$ 167,414	$ 162,181
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,842	$ 1,545
Accrued payroll, payroll taxes and related benefits	38,133	33,372
Income taxes payable	216	
Other accrued liabilities	752	516
Workers compensation claims liabilities	2,904	3,843
Workers compensation claims liabilities for insured claims	225	225
Safety incentives liability	7,447	7,519
Total current liabilities	51,519	47,020
Customer deposits	685	817
Long-term workers compensation claims liabilities	5,288	5,295
Long-term workers compensation claims liabilities for insured claims	2,962	3,011
Deferred income taxes	1,545	1,545
Deferred gain on sale and leaseback	762	793
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $.01 par value; 500,000 shares authorized; no shares issued and outstanding		
Common stock, $.01 par value; 20,500 shares authorized, 11,257 and 11,253 shares issued and outstanding	113	112
Additional paid-in capital	40,691	40,647
Other comprehensive loss	(275)	(244)
Retained earnings	64,124	63,185

	104,653	103,700
	$ 167,414	$ 162,181

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

BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Operations

(Unaudited)

(In thousands, except per share amounts)

	Three Months Ended March 31, 2007	2006
Revenues:		
Staffing services	$ 28,015	$ 26,661
Professional employer service fees	32,573	31,624
Total revenues	60,588	58,285
Cost of revenues:		
Direct payroll costs	21,142	19,851
Payroll taxes and benefits	23,911	22,837
Workers compensation	5,844	6,554
Total cost of revenues	50,897	49,242
Gross margin	9,691	9,043
Selling, general and administrative expenses	7,388	7,220
Depreciation and amortization	349	301
Income from operations	1,954	1,522
Other income (expense):		
Interest expense	(2)	(22)
Investment income, net	779	645
Other	8	9
Other income (expense)	785	632
Income before provision for income taxes	2,739	2,154
Provision for income taxes	1,011	797
Net income	$ 1,728	$ 1,357
Basic earnings per share	$ .15	$ .12
Weighted average number of basic shares outstanding	11,255	11,076
Diluted earnings per share	$ .15	$ .12
Weighted average number of diluted shares outstanding	11,681	11,661

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

BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Three Months Ended March 31, 2007	2006
Cash flows from operating activities:		
Net income	$ 1,728	$ 1,357
Reconciliations of net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	349	301
(Gains) losses recognized on marketable securities	11	(52)
Purchase of marketable securities	(2)	
Gain recognized on sale and leaseback	(31)	(30)
Deferred income taxes	(20)	(111)
Changes in certain assets and liabilities, net of amounts purchased in acquisitions:		
Trade accounts receivable, net	(4,092)	(3,025)
Prepaid expenses and other	(611)	(2,241)
Accounts payable	297	443
Accrued payroll, payroll taxes and related benefits	4,761	5,083
Income taxes payable	216	
Other accrued liabilities	236	3,199
Workers compensation claims liabilities	(946)	(748)
Safety incentives liability	(72)	(171)
Customer deposits and other assets, net	293	(1,387)
Net cash provided by operating activities	2,117	2,618
Cash flows from investing activities:		
Cash paid for acquisition, including other direct costs	(500)	(3,963)
Purchase of property and equipment, net of amounts purchased in acquisition	(224)	(749)
Purchase of marketable securities	(729)	
Proceeds from maturities of restricted marketable securities	1,017	920
Purchase of restricted marketable securities	(1,104)	(1,012)
Net cash used in investing activities	(1,540)	(4,804)
Cash flows from financing activities:		
Proceeds from credit-line borrowings	4,879	
Payments on credit-line borrowings	(4,879)	
Payments on long-term debt		(237)
Proceeds from the exercise of stock options	13	211
Dividends paid	(789)	
Tax benefit of stock option exercises	32	208
Net cash (used in) provided by financing activities	(744)	182
Net decrease in cash and cash equivalents	(167)	(2,004)
Cash and cash equivalents, beginning of period	69,874	61,361
Cash and cash equivalents, end of period	$ 69,707	$ 59,357
Supplemental schedule of noncash investing activities:		
Acquisition of other businesses:		
Cost of acquisition in excess of fair market value of net assets acquired	$ 500	$ 4,120
Intangible assets acquired		

Tangible assets acquired		10
Less stock issued in connection with acquisition		(167)
Net cash paid for acquisition	$ 500	$ 3,963

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

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" or the "Company"), 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 2006 Annual Report on Form 10-K at pages F1 - F25. The results of operations for an interim period are not necessarily indicative of the results of operations for a full year. Certain prior year amounts have been reclassified to conform with the current year presentation. Such reclassifications had no impact on net income or stockholders' equity.

Effective January 1, 2007, the Company formed a wholly-owned captive insurance company, Associated Insurance Company for Excess ("AICE"). AICE is a fully licensed captive insurance company holding a certificate of authority from the Arizona Department of Insurance. The purpose of AICE is twofold: (1) to provide access to more competitive and cost effective insurance markets and (2) to provide additional flexibility in cost effective risk management. The captive will handle only workers' compensation claims occurring on or after January 1, 2007.

Allowance for doubtful accounts

The Company had an allowance for doubtful accounts of $344,000 and $319,000 at March 31, 2007 and December 31, 2006, respectively. The Company must make estimates of the collectibility of accounts receivables. 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 Professional Employer Organization ("PEO") contracts) working in California, Oregon, Maryland and Delaware. In the state of Washington, state law allows only the Company's staffing services and management employees to be covered under the Company's self-insured workers' compensation program. To manage our financial exposure in the event of catastrophic injuries or fatalities, we maintain excess workers' compensation insurance with a per occurrence retention of $5.0 million (through our captive insurance company) effective January 1, 2007. Prior to January 1, 2007, our self-insured retention was $1.0 million.

BARRETT BUSINESS SERVICES, INC.

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

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

Workers' compensation claims (continued)

The Company has provided a total of $11.4 million and $12.4 million at March 31, 2007 and December 31, 2006, respectively, as an estimated liability for unsettled workers' compensation claims liabilities. Included in the foregoing liabilities are insured claims that will be paid by the Company's excess workers' compensation insurer and for which the Company has reported a receivable for the insured claims liability. Insured claims totaled $3.2 million at March 31, 2007 and at December 31, 2006. The estimated liability for unsettled workers' compensation claims represents management s best estimate, which includes an evaluation of information provided by the Company's third-party administrators for workers' compensation claims and, in part, an annual actuarial analysis from an independent 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, anticipated increases in case reserve estimates and additional claims administration expenses. These estimates are continually reviewed and adjustments to liabilities are reflected in current operating results as they become known.

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. The Company has provided $7.4 million and $7.5 million at March 31, 2007 and December 31, 2006, respectively, as an estimated liability for 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 third party administrator.

Comprehensive income (loss)

Comprehensive income (loss) includes all changes in equity during a period except those that resulted from investments by or distributions to a company's stockholders. Other comprehensive income (loss) refers to revenues, expenses, gains and losses that under GAAP are included in comprehensive income (loss), but are excluded from net income as these amounts are recorded directly as an adjustment to stockholders' equity. The Company s other comprehensive income (loss) is comprised of unrealized holding gains and losses on its publicly-traded marketable securities designated as "available-for-sale", net of realized gains included in net income.

Note 2 - Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation ("FIN") No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 is an interpretation of Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for

Income Taxes." FIN 48 provides interpretive guidance for the financial statement recognition

BARRETT BUSINESS SERVICES, INC.

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

Note 2 - Recent Accounting Pronouncements (Continued)

and measurement of a tax position taken, or expected to be taken, in a tax return. FIN 48 requires the affirmative evaluation that it is more-likely-than-not, based on the technical merits of a tax position, that an enterprise is entitled to economic benefits resulting from positions taken in income tax returns. If a tax position does not meet the "more-likely-than-not" recognition threshold, the benefit of that position is not recognized in the financial statements. FIN 48 also requires companies to disclose additional quantitative and qualitative information in their financial statements about uncertain tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006, and the cumulative effect of applying FIN 48 shall be reported as an adjustment to the opening balance of retained earnings for that fiscal year. Effective January 1, 2007, we formed AICE, a wholly owned captive insurance subsidiary. We recognize AICE as an insurance company for federal income tax purposes, with respect to our consolidated federal income tax return. In the event the Internal Revenue Service ("IRS") were to determine that AICE does not qualify as an insurance company, we could be required to make accelerated income tax payments to the IRS that we otherwise would have deferred until future periods. The adoption of FIN 48 has not had a material effect on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We will be required to adopt SFAS 157 in the first quarter of 2008. Our management is currently evaluating the requirements of SFAS 157 and has not yet determined the impact on our consolidated financial statements.

In September 2006, the Securities and Exchange Commission Staff issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in the Current Year Financial Statements" ("SAB No. 108"). SAB No. 108 requires the use of two alternative approaches in quantitatively evaluating materiality of misstatements. If the misstatement as quantified under either approach is material to the current year financial statements, the misstatement must be corrected. If the effect of correcting the prior year misstatements, if any, in the current year income statement is material, the prior year financial statements should be corrected. In the year of adoption (fiscal years ending after November 15, 2006, or calendar year 2006 for us), the misstatements may be corrected as an accounting change by adjusting opening retained earnings rather than including the adjustment in the current year income statement. Upon completing our evaluation of the requirements of SAB No. 108, we determined it did not affect our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities," ("SFAS 159"). This statement provides the Company the option to elect to carry certain financial assets and liabilities at fair value with change in fair value recorded in earnings. SFAS 159 is effective for the Company beginning January 1, 2008. The Company is currently evaluating the potential impact of this statement.

Note 3 - Acquisitions

Effective January 1, 2006, we acquired certain assets of Pro HR, LLC, a privately-held PEO company with offices in Boise and Rexburg, Idaho and Grand Junction, Colorado. We

BARRETT BUSINESS SERVICES, INC.

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

Note 3 Acquisitions (Continued)

paid $4.0 million in cash for the assets of Pro HR and the selling shareholders' noncompete agreements and agreed to pay up to $1.5 million additional cash based upon the level of financial performance achieved by the Pro HR offices during calendar 2006. The transaction resulted in $5.4 million of goodwill, $100,000 of intangible assets and $10,000 of fixed assets. In October 2006, we paid $1.0 million in cash in partial satisfaction of the contingent consideration of this acquisition based upon the financial performance of Pro HR for the first six months of 2006. Effective February 28, 2007, we paid $500,000 in cash in final satisfaction of the contingent consideration based upon the financial performance of Pro HR for the full 2006 year. The Company's consolidated income statements for the three months ended March 31, 2007 and 2006 include Pro HR's results of operations since January 1, 2006.

Note 4 - 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 share reflect the potential effects of the exercise of outstanding stock options. Basic and diluted shares outstanding are summarized as follows:

	Three Months Ended March 31,	
	2007	2006
Weighted average number of basic shares outstanding	11,255,075	11,076,150
Stock option plan shares to be issued at prices ranging from $0.97 to $17.50 per share	737,302	906,020
Less: Assumed purchase at average market price during the period using proceeds received upon exercise of options and purchase of stock, and using tax benefits of compensation due to premature dispositions	(311,766)	(321,445)
Weighted average number of diluted shares	&nb	