PRGX GLOBAL, INC.
Form 10-Q
May 12, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)

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

For the quarterly period ended March 31, 2014

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 0-28000

PRGX Global, Inc.
(Exact name of registrant as specified in its charter)

Georgia	58-2213805
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
600 Galleria Parkway Suite 100 Atlanta, Georgia (Address of principal executive offices)	30339-5986 (Zip Code)

Registrant's telephone number, including area code: (770) 779-3900

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 ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý 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. See definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check One):

¨ Large accelerated filer	ý Accelerated filer
¨ Non-accelerated filer (Do not check if a smaller reporting company)	¨ Smaller reporting company

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

Common shares of the registrant outstanding at April 25, 2014 were 30,071,462.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
PRGX GLOBAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per share data)

	Three Months Ended March 31, 2014	2013
Revenue	$37,901	$45,101
Operating expenses:		
Cost of revenue	27,467	30,184
Selling, general and administrative expenses	11,341	11,934
Depreciation of property and equipment	1,682	2,008
Amortization of intangible assets	903	1,276
Total operating expenses	41,393	45,402
Operating loss	(3,492)	(301)
Foreign currency transaction (gains) losses on short-term intercompany balances	15	357
Interest expense (income), net	54	(217)
Loss before income taxes	(3,561)	(441)
Income tax expense	113	56
Net loss	$(3,674)	$(497)
Basic earnings (loss) per common share (Note B)	$(0.12)	$(0.02)
Diluted earnings (loss) per common share (Note B)	$(0.12)	$(0.02)
Weighted-average common shares outstanding (Note B):		
Basic	30,159	28,770
Diluted	30,159	28,770

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Unaudited)
(In thousands)

	Three Months Ended March 31, 2014	2013
Net loss	$(3,674)	$(497)
Foreign currency translation adjustments	(70)	(484)
Comprehensive loss	$(3,744)	$(981)

See accompanying Notes to Condensed Consolidated Financial Statements.

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PRGX GLOBAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands, except share data)

	March 31, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents (Note E)	$45,697	$43,700
Restricted cash	126	57
Receivables:		
Contract receivables, less allowances of $1,924 in 2014 and $1,996 in 2013:		
Billed	25,121	28,175
Unbilled	6,290	9,904
	31,411	38,079
Employee advances and miscellaneous receivables, less allowances of $294 in 2014 and $402 in 2013	1,703	2,242
Total receivables	33,114	40,321
Prepaid expenses and other current assets	3,814	3,917
Total current assets	82,751	87,995
Property and equipment	55,146	58,796
Less accumulated depreciation and amortization	(41,956)	(44,802)
Property and equipment, net	13,190	13,994
Goodwill	13,691	13,686
Intangible assets, less accumulated amortization of $33,669 in 2014 and $32,717 in 2013	12,693	13,582
Noncurrent portion of unbilled receivables	816	1,379
Other assets	2,253	2,193
Total assets	$125,394	$132,829
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$7,640	$10,809
Accrued payroll and related expenses	13,991	15,415
Refund liabilities	6,053	6,597
Deferred revenue	1,822	1,512
Business acquisition obligations	—	3,156
Total current liabilities	29,506	37,489
Noncurrent refund liabilities	847	950
Other long-term liabilities	574	562
Total liabilities	30,927	39,001
Commitments and contingencies (Note H)		
Shareholders' equity (Note B):		
Common stock, no par value; $.01 stated value per share. Authorized 50,000,000 shares; 30,093,546 shares issued and outstanding as of March 31, 2014 and 29,367,439 shares issued and outstanding as of December 31, 2013	301	294
Additional paid-in capital	609,182	604,806

Accumulated deficit	(517,060)	(513,386)
Accumulated other comprehensive income	2,044	2,114
Total shareholders' equity	94,467	93,828
Total liabilities and shareholders' equity	$125,394	$132,829

See accompanying Notes to Condensed Consolidated Financial Statements.

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PRGX GLOBAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Three Months Ended March 31, 2014	2013
Cash flows from operating activities:		
Net loss	$(3,674)	$(497)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	2,585	3,284
Amortization of deferred loan costs	16	46
Stock-based compensation expense	1,021	1,318
Deferred income taxes	(209)	(45)
Foreign currency transaction (gains) losses on short-term intercompany balances	15	357
Changes in operating assets and liabilities:		
Restricted cash	(69)	(64)
Billed receivables	3,055	5,163
Unbilled receivables	4,177	1,507
Prepaid expenses and other current assets	706	(313)
Other assets	1	20
Accounts payable and accrued expenses	(3,192)	(2,359)
Accrued payroll and related expenses	(1,453)	(6,985)
Refund liabilities	(647)	(273)
Deferred revenue	309	279
Noncurrent compensation obligations	184	197
Other long-term liabilities	87	(786)
Net cash provided by operating activities	2,912	849
Cash flows from investing activities:		
Purchases of property and equipment, net of disposal proceeds	(844)	(2,207)
Net cash used in investing activities	(844)	(2,207)
Cash flows from financing activities:		
Repayments of long-term debt	—	(750)
Payment of deferred loan costs	(80)	—
Restricted stock repurchased from employees for withholding taxes	(5)	(430)
Proceeds from option exercises	2,183	336
Payments of deferred acquisition consideration	(1,978)	(1,656)
Net proceeds from issuance of common stock	—	4,118
Repurchase of common stock	(40)	—
Net cash provided by financing activities	80	1,618
Effect of exchange rates on cash and cash equivalents	(151)	(279)
Net increase (decrease) in cash and cash equivalents	1,997	(19)
Cash and cash equivalents at beginning of period	43,700	37,806
Cash and cash equivalents at end of period	$45,697	$37,787
Supplemental disclosure of cash flow information:		
Cash paid during the period for interest	$19	$71

Cash paid during the period for income taxes, net of refunds received	$948	$294

See accompanying Notes to Condensed Consolidated Financial Statements.

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PRGX GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note A – Basis of Presentation

The accompanying Condensed Consolidated Financial Statements (Unaudited) of PRGX Global, Inc. and its wholly owned subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month period ended March 31, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014.

Except as otherwise indicated or unless the context otherwise requires, “PRGX,” “we,” “us,” “our” and the “Company” refer to PRGX Global, Inc. and its subsidiaries. For further information, refer to the Consolidated Financial Statements and Footnotes thereto included in the Company’s Form 10-K for the year ended December 31, 2013.

Beginning with the first quarter of 2014, we present the former New Services segment as two separate segments: Adjacent Services, which were formerly referred to as Profit Optimization services, and Healthcare Claims Recovery Audit Services. We have revised the presentation of our operating segments and related information in Note D - Operating Segments and Related Information.

Beginning with the third quarter of 2013, we present fair value adjustments to acquisition-related contingent consideration as an adjustment to our segment measure—earnings before interest, taxes, depreciation and amortization ("Adjusted EBITDA") as presented in Note D - Operating Segments and Related Information. We now include these fair value adjustments in the Adjusted EBITDA calculation in the "Acquisition-related charges (benefits)" line, which we renamed from "Acquisition transaction costs and acquisition obligations classified as compensation." Accordingly, we have revised the presentation of our Adjusted EBITDA calculation for all relevant prior periods.

Unbilled Receivables

A significant portion of the unbilled receivables presented in the Condensed Consolidated Balance Sheets (Unaudited) relate to our Healthcare Claims Recovery Audit Services as we generally cannot invoice the prime contractors for whom we operate as a subcontractor under the Medicare RAC program until cash is collected by the prime contractors. These unbilled receivables, net of the related reserves, were $3.5 million and $5.6 million as of March 31, 2014 and December 31, 2013, respectively. As of May 2, 2014, we billed $2.5 million of the unbilled receivables relating to the Medicare RAC program that were outstanding as of March 31, 2014.

New Accounting Standards

A summary of the new accounting standard issued by the Financial Accounting Standards Board (“FASB”) and included in the Accounting Standards Codification (“ASC”) that applies to PRGX is set forth below:

FASB ASC Update No. 2014-08. In April 2014, the FASB issued Accounting Standards Update No. 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360)—Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity (“ASU 2014-08”). ASU 2014-08 raises the threshold for a disposal to qualify as a discontinued operation and requires new disclosures of both discontinued operations and certain other disposals that do not meet the definition of a discontinued operation. ASU 2014-08 is effective for annual periods beginning on or after December 15, 2014. We do not expect the adoption of ASU No. 2014-08 to have a material impact on our consolidated results of operations, financial position or cash flows.

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PRGX GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Note B – Earnings (Loss) Per Common Share
The following tables set forth the computations of basic and diluted earnings (loss) per common share for the three months ended March 31, 2014 and 2013 (in thousands, except per share data):

	Three Months Ended March 31,	
Basic earnings (loss) per common share:	2014	2013
Numerator:		
Net loss	$(3,674)	$(497)
Denominator:		
Weighted-average common shares outstanding	30,159	28,770
Basic earnings (loss) per common share	$(0.12)	$(0.02)

	Three Months Ended March 31,	
Diluted earnings (loss) per common share:	2014	2013
Numerator:		
Net loss	$(3,674)	$(497)
Denominator:		
Weighted-average common shares outstanding	30,159	28,770
Incremental shares from stock-based compensation plans	—	—
Denominator for diluted earnings (loss) per common share	30,159	28,770
Diluted earnings (loss) per common share	$(0.12)	$(0.02)

Weighted-average shares outstanding excludes antidilutive shares underlying options that totaled 2.4 million shares and antidilutive Performance Units issuable under the Company's 2006 Management Incentive Plan that totaled less than 0.1 million shares from the computation of diluted earnings (loss) per common share for the three months ended March 31, 2014. Weighted-average shares outstanding excludes antidilutive shares underlying options that totaled 2.9 million shares and anti-dilutive Performance Units related to the Company's 2006 Management Incentive Plan that totaled 0.1 million from the computation of diluted earnings (loss) per common share for the three months ended March 31, 2013. As a result of the net loss for the three months ended March 31, 2014 and March 31, 2013, all shares underlying stock options and Performance Units were considered antidilutive. The number of common shares we used in the basic and diluted earnings (loss) per common share computations include nonvested restricted shares of 0.7 million and 0.8 million for the three months ended March 31, 2014 and 2013, respectively, and nonvested restricted share units that we consider to be participating securities of 0.2 million for both the three months ended March 31, 2014 and 2013.

On December 11, 2012, we closed a public offering of 6,249,234 shares of our common stock, which consisted of 2,500,000 shares sold by us and 3,749,234 shares sold by certain selling shareholders, at a price to the public of $6.39 per share. The net proceeds to us from the public offering, after deducting underwriting discounts and commissions and offering expenses, were $14.7 million. We did not receive any proceeds from the sale of shares by the selling shareholders. In addition, the underwriters elected to exercise an overallotment option for an additional 687,385 shares, and completed the additional sale on January 8, 2013. The net proceeds to us from the overallotment, after deducting underwriting discounts and commission and offering expenses, were $4.1 million.

In partial satisfaction of a business acquisition obligation, we issued 187,620 shares of our common stock having a value of $1.3 million in the three months ended March 31, 2014 and 217,155 shares of our common stock having a value of $1.4 million in the three months ended March 31, 2013.

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PRGX GLOBAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Note C – Stock-Based Compensation
The Company currently has three stock-based compensation plans under which awards have been granted: (1) the Stock Incentive Plan; (2) the 2006 Management Incentive Plan ("2006 MIP"); and (3) the 2008 Equity Incentive Plan ("2008 EIP") (collectively, the "Plans"). We describe the Plans in the Company's Annual Report on Form 10–K for the fiscal year ended December 31, 2013.
2008 EIP Awards
Stock options granted under the 2008 EIP generally have a term of seven years and vest in equal annual increments over the vesting period, which typically is three years for employees and one year for directors. There were no stock option grants during the three months ended March 31, 2014. The following table summarizes stock option grants during the three months ended March 31, 2013:

Grantee Type	# of Options Granted	Vesting Period	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value
2013				
Director group	7,122	1 year or less	$6.83	$2.35
Director group	17,092	3 years	$6.83	$3.76
Employee group	5,000	3 years	$6.83	$3.65
Employee inducement [(1)]	20,000	3 years	$7.14	$3.81

(1) The Company granted non-qualified performance-based stock options outside its existing stock-based compensation plans in the first quarter of 2013 to one employee in connection with the employee joining the Company.

Nonvested stock awards, including both restricted stock and restricted stock units, generally are nontransferable until vesting and the holders are entitled to receive dividends with respect to the nonvested shares. Prior to vesting, the grantees of restricted stock are entitled to vote the shares, but the grantees of restricted stock units are not entitled to vote the shares. Generally, nonvested stock awards vest in equal annual increments over the vesting period, which typically is three years for employees and one year for directors. There were no nonvested stock awards (restricted stock and restricted stock units) granted during the three months ended March 31, 2014. The following table summarizes nonvested stock awards granted during the three months ended March 31, 2013:

Grantee Type	# of Shares Granted	Vesting Period	Weighted Average Grant Date Fair Value
2013			
Director group	7,122	1 year or less	$6.83
Director group	17,092	3 years	$6.83
Employee group	5,000	3 years	$6.83
Employee inducement [(1)]	20,000	3 years	$7.14

(1) The Company granted nonvested performance-based stock awards (restricted stock) outside its existing stock-based compensation plans in the first quarter of 2013 to one employee in connection with the employee joining the Company.

2006 MIP Performance Units
On June 19, 2012, seven senior officers of the Company were granted 154,264 Performance Units under the 2006 MIP, comprising all remaining available awards under the 2006 MIP. The awards had an aggregate grant date fair value of $1.2 million and vest ratably over three years. Upon vesting, the Performance Units will be settled by the issuance of Company common stock equal to 60% of the number of Performance Units being settled and the payment

of cash in an amount equal to 40% of the fair market value of that number of shares of common stock equal to the number of Performance Units being settled. During 2013, an aggregate of 93,664 Performance Units were settled by four current executive officers and two former executive officers, and 16,524 Performance Units were forfeited by one former executive officer. Such settlements resulted in the issuance of 56,197 shares of common stock and cash payments totaling $0.2 million. As of March 31, 2014, a total of 44,076 Performance Units were outstanding, none of which were vested. There was no settlement of Performance Units during the three months ended March 31, 2014.

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Selling, general and administrative expenses for the three months ended March 31, 2014 and 2013 include $1.0 million and $1.3 million, respectively, related to stock-based compensation charges. At March 31, 2014, there was $5.5 million of unrecognized stock-based compensation expense related to stock options, restricted stock awards, restricted stock unit awards, and Performance Unit awards which we expect to recognize over a weighted-average period of 1.7 years.

Note D – Operating Segments and Related Information

Beginning with the first quarter of 2014, we present the former New Services segment as two separate segments: Adjacent Services, which were formerly referred to as Profit Optimization services, and Healthcare Claims Recovery Audit Services. We now conduct our operations through the following four reportable segments:

Recovery Audit Services – Americas represents recovery audit services (other than Healthcare Claims Recovery Audit services) provided in the United States of America (“U.S.”), Canada and Latin America.

Recovery Audit Services – Europe/Asia-Pacific represents recovery audit services (other than Healthcare Claims Recovery Audit services) provided in Europe, Asia and the Pacific region.

Adjacent Services (formerly known as Profit Optimization services) represents data transformation and financial advisory services.

Healthcare Claims Recovery Audit Services represents recovery audit services for healthcare claims, which consist primarily of services provided under subcontracts related to the Medicare Recovery Audit Contractor program.

Additionally, Corporate Support includes the unallocated portion of corporate selling, general and administrative expenses not specifically attributable to the four reportable segments.

We evaluate the performance of our reportable segments based upon revenue and measures of profit or loss we refer to as EBITDA and Adjusted EBITDA. We define Adjusted EBITDA as earnings from continuing operations before interest and taxes (“EBIT”), adjusted for depreciation and amortization (“EBITDA”), and then further adjusted for unusual and other significant items that management views as distorting the operating results of the various segments from period to period. Such adjustments include restructuring charges, stock-based compensation, bargain purchase gains, acquisition-related charges and benefits (acquisition transaction costs, acquisition obligations classified as compensation, and fair value adjustments to acquisition-related contingent consideration), tangible and intangible asset impairment charges, certain litigation costs and litigation settlements, certain severance charges and foreign currency transaction gains and losses on short-term intercompany balances viewed by management as individually or collectively significant. We do not have any inter-segment revenue.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Segment information for the three months ended March 31, 2013 has been revised to reflect the change in reportable segments. Segment information for the three months ended March 31, 2014 and 2013 (in thousands) is as follows:

	Recovery Audit Services – Americas	Recovery Audit Services – Europe/Asia-Pacific	Adjacent Services	Healthcare Claims Recovery Audit Services	Corporate Support	Total
Three Months Ended March 31, 2014						
Revenue	$24,798	$ 9,702	$2,283	$1,118	$—	$37,901
Net loss						$(3,674)
Income tax expense						113
Interest expense, net						54
EBIT	$4,084	$ 101	$(1,574)	$(2,006)	$(4,112)	(3,507)
Depreciation of property and equipment	1,256	146	160	120	—	1,682
Amortization of intangible assets	500	307	96	—	—	903
EBITDA	5,840	554	(1,318)	(1,886)	(4,112)	(922)
Foreign currency transaction (gains) losses on short-term intercompany balances	110	(73)	—	—	(22)	15
Acquisition-related charges	—	—	19	—	—	19
Transformation severance and related expenses	8	79	143	155	—	385
Stock-based compensation	—	—	—	—	1,021	1,021
Adjusted EBITDA	$5,958	$ 560	$(1,156)	$(1,731)	$(3,113)	$518