NAVIGANT CONSULTING INC
Form 10-Q
July 29, 2011

Table of Contents

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2011

OR

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

Commission File No. 1-12173

Navigant Consulting, Inc.
(Exact name of Registrant as specified in its charter)

Delaware	**36-4094854**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

30 South Wacker Drive, Suite 3550, Chicago, Illinois 60606
(Address of principal executive offices, including zip code)
(312) 573-5600
(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 þ NO o

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES þ NO o

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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES o NO þ

As of July 26, 2011, 52,248,259 shares of the Registrant s common stock, par value $.001 per share, were outstanding.

NAVIGANT CONSULTING, INC.
AS OF AND FOR THE SIX MONTHS ENDED JUNE 30, 2011
INDEX

Forward-Looking Statements

Statements included in this report which are not historical in nature are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements may generally be identified by words such as anticipate, believe, intend, estimate, expect, plan, outlook and similar expressions. We cauti that there may be events in the future that we are not able to accurately predict or control and the information contained in the forward-looking statements is inherently uncertain and subject to a number of risks that could cause actual results to differ materially from those contained in or implied by the forward-looking statements, including the factors described in the section entitled Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2010 and in Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations in this report. We cannot guarantee any future results, levels of activity, performance or achievement, and we undertake no obligation to update any of the forward-looking statements contained in this report.

Table of Contents

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

NAVIGANT CONSULTING, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands)

	June 30, 2011 (unaudited)	December 31, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	$ 384	$ 1,981
Accounts receivable, net	190,730	179,058
Prepaid expenses and other current assets	26,293	19,697
Deferred income tax assets	13,425	18,749
Total current assets	230,832	219,485
Property and equipment, net	35,800	38,903
Intangible assets, net	19,533	23,194
Goodwill	566,213	561,002
Other assets	27,552	26,451
Total assets	$ 879,930	$ 869,035
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 11,821	$ 10,900
Accrued liabilities	7,781	7,936
Accrued compensation-related costs	60,991	72,639
Income tax payable		2,306
Term loan current		18,397
Other current liabilities	29,017	43,401
Total current liabilities	109,610	155,579
Non-current liabilities:		
Deferred income tax liabilities	49,241	42,274
Other non-current liabilities	22,278	25,907
Bank debt non-current	205,221	33,695
Term loan non-current		150,859
Total non-current liabilities	276,740	252,735
Total liabilities	386,350	408,314
Stockholders equity:		
Common stock	61	61

Additional paid-in capital	562,089	564,214
Treasury stock	(194,519)	(206,162)
Retained earnings	134,781	115,243
Accumulated other comprehensive loss	(8,832)	(12,635)
Total stockholders equity	493,580	460,721
Total liabilities and stockholders equity	$ 879,930	$ 869,035

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

NAVIGANT CONSULTING, INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except per share data)

	For the three months ended June 30,		For the six months ended June 30,	
	2011	**2010**	**2011**	**2010**
Revenues before reimbursements	$ 173,293	$ 154,617	$ 342,897	$ 308,487
Reimbursements	21,115	17,706	40,310	37,386
Total revenues	194,408	172,323	383,207	345,873
Cost of services before reimbursable expenses	116,822	102,128	231,637	204,358
Reimbursable expenses	21,115	17,706	40,310	37,386
Total costs of services	137,937	119,834	271,947	241,744
General and administrative expenses	31,143	29,089	63,552	59,549
Depreciation expense	3,206	3,553	6,583	7,354
Amortization expense	2,163	2,962	4,464	5,758
Operating income	19,959	16,885	36,661	31,468
Interest expense	1,911	3,508	3,751	6,986
Interest income	(429)	(311)	(796)	(624)
Other expense (income), net	72	(44)	36	61
Income before income tax expense	18,405	13,732	33,670	25,045
Income tax expense	7,645	5,904	14,132	10,770
Net income	$ 10,760	$ 7,828	$ 19,538	$ 14,275
Basic net income per share	$ 0.21	$ 0.16	$ 0.39	$ 0.29
Shares used in computing income per basic share	50,820	49,205	50,498	48,948
Diluted net income per share	$ 0.21	$ 0.16	$ 0.38	$ 0.28
Shares used in computing income per diluted share	51,270	50,264	51,153	50,180

See accompanying notes to the unaudited consolidated financial statements.

Table of Contents

NAVIGANT CONSULTING, INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	For the six months ended June 30,	
	2011	**2010**
Cash flows from operating activities:		
Net income	$ 19,538	$ 14,275
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	6,583	7,354
Amortization expense	4,464	5,758
Share-based compensation expense	4,133	2,938
Accretion of interest expense	529	401
Deferred income taxes	11,313	7,814
Allowance for doubtful accounts receivable	3,028	3,938
Changes in assets and liabilities, net of acquisitions:		
Accounts receivable	(13,962)	(3,541)
Prepaid expenses and other assets	(4,745)	(9,780)
Accounts payable	889	1,561
Accrued liabilities	(217)	1,203
Accrued compensation-related costs	(11,751)	(19,120)
Income taxes payable	(2,266)	(1,782)
Other liabilities	(3,577)	(3,370)
Net cash provided by operating activities	13,959	7,649
Cash flows from investing activities:		
Purchases of property and equipment	(3,401)	(5,479)
Acquisitions of businesses, net of cash acquired	(1,046)	(33,870)
Payments of acquisition liabilities	(10,217)	
Other, net	(225)	
Net cash used in investing activities	(14,889)	(39,349)
Cash flows from financing activities:		
Issuances of common stock	1,050	1,533
Payment upon termination of credit agreement	(250,613)	
Proceeds from new credit agreement	250,613	
Borrowings from banks, net of repayments	6,432	25,049
Payments of term loan	(4,599)	(40,920)
Payments of debt issuance costs	(2,814)	
Other, net	(839)	(119)
Net cash used in financing activities	(770)	(14,457)
Effect of exchange rate changes on cash and cash equivalents	103	13
Net decrease in cash and cash equivalents	(1,597)	(46,144)

Cash and cash equivalents at beginning of the period		1,981		49,144
Cash and cash equivalents at end of the period	$	384	$	3,000

See accompanying notes to the unaudited consolidated financial statements.

5

Table of Contents

NAVIGANT CONSULTING, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Basis of Presentation

Navigant Consulting, Inc. (we , us or our) is an independent specialty consulting firm that combines deep industry knowledge with technical expertise to enable companies to create and protect value in the face of complex and critical business risks and opportunities. Professional services include dispute, investigative, economic, operational, risk management and financial and regulatory advisory solutions. We provide our services to governmental agencies, legal counsel and large companies facing the challenges of uncertainty, risk, distress and significant change. We focus on industries undergoing substantial regulatory or structural change and on the issues driving these transformations.

The accompanying unaudited interim consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) for interim reporting and do not include all of the information and footnote disclosures required by accounting principles generally accepted in the United States of America (GAAP). The information furnished herein includes all adjustments, consisting of normal and recurring adjustments except where indicated, which are, in the opinion of management, necessary for a fair presentation of the results of operations for the interim periods presented.

The results of operations for the six months ended June 30, 2011 are not necessarily indicative of the results to be expected for the entire year ending December 31, 2011.

These financial statements should be read in conjunction with the audited consolidated financial statements and related notes as of and for the year ended December 31, 2010 included in our Annual Report on Form 10-K filed with the SEC on February 18, 2011.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and the related notes. Actual results could differ from those estimates and may affect future results of operations and cash flows. We have evaluated subsequent events through the date of this filing.

Note 2. Acquisitions

On October 1, 2010, we acquired the assets of EthosPartners Healthcare Management Group, Inc. for approximately $37.0 million, which consisted of $28.0 million in cash paid at closing, $2.0 million in restricted common stock issued at closing and $7.0 million in deferred payments. The restricted stock and deferred payments were recorded at fair value, and the deferred payments were recorded in other current and non-current liabilities. The deferred payments are payable in cash in two equal installments on the first and second anniversaries of the closing date. In addition, EthosPartners can earn up to a total of $8.0 million of additional payments based on the business achieving certain performance targets during each of the three years after closing. Fair value of the contingent consideration, recorded in other current and non-current liabilities, was estimated to be $5.6 million and was determined based on level two observable inputs and will be recalculated each reporting period with any resulting gains or losses being recorded in the income statement. No such gains or losses were recorded during the six months ended June 30, 2011. The additional purchase price payments, if earned, would be payable approximately 90 days after the end of the annual period in which the performance targets were attained. As part of the purchase price allocation, we recorded $6.4 million in identifiable intangible assets and $35.8 million in goodwill. The purchase price paid in cash at closing was funded under our credit facility.

We acquired EthosPartners to enhance our Healthcare practice. EthosPartners is a national healthcare consulting group specializing in physician and hospital alignment, physician practice operations management, and physician revenue cycle management. This acquisition included 180 consulting professionals and has been integrated into our Business Consulting Services segment.

On May 14, 2010, we acquired the assets of Daylight Forensic & Advisory LLC, located in New York, New York for approximately $40.0 million, which consisted of $29.9 million in cash paid at closing and $10.0 million in cash paid on the first anniversary of the closing date during the three months ended June 30, 2011. As part of the purchase price allocation, we recorded $4.5 million in identifiable intangible assets and $35.2 million in goodwill. The purchase price paid in cash at closing was funded under our credit facility.

We acquired Daylight to enhance our investigative service offerings and to add significant presence in the New York market. Daylight is a consulting and investigative firm specializing in regulatory compliance and fraud risk management, with extensive

Table of Contents

capabilities in anti-money laundering and Foreign Corrupt Practices Act related matters. This acquisition included 65 consulting professionals and has been integrated into our Dispute and Investigative Services segment.

On January 20, 2010, we acquired the assets of Empiris, LLC, located in Washington, D.C. for $5.5 million, which consisted of $4.0 million in cash paid at closing and $1.5 million, recorded in other current and non-current liabilities, to be paid in cash in two equal installments on December 31, 2010 and January 3, 2012. On December 31, 2010, we paid the first cash installment of $0.8 million. In addition, the purchase agreement contains a provision for contingent consideration of up to $2.0 million in cash. The contingent consideration is based on the business achieving certain performance targets during the periods from closing to December 31, 2010 and in calendar years 2011 and 2012 and will be payable in March of the year following the year in which such performance targets are attained. During the quarter ended March 31, 2011, we paid approximately $0.2 million of this consideration. Fair value of the contingent consideration, recorded in other current and non-current liabilities, was estimated to be $1.9 million and was determined based on level two observable inputs and will be recalculated each reporting period with any resulting gains or losses being recorded in the income statement. No such gains or losses were recorded during the six months ended June 30, 2011 or 2010. As part of the purchase price allocation, we recorded $1.6 million in identifiable intangible assets and $5.8 million in goodwill. The purchase price paid in cash at closing was funded with cash from operations.

We acquired Empiris to enhance our Economic Consulting segment. Empiris provides significant expertise and growth opportunities in our Washington, D.C. market by servicing relevant governmental agencies, corporations and law firms. This acquisition consisted of nine professionals and has been integrated into our Economic Consulting segment.

We acquired two other small businesses, one in December 2010 and the other in May 2011, for an aggregate purchase price of $3.2 million. The acquired businesses have been integrated in our International Consulting segment.

Pro Forma Information

The following table summarizes certain supplemental unaudited pro forma financial information which was prepared as if the acquisitions described above had occurred as of the beginning of the periods presented. The unaudited pro forma financial information was prepared for comparative purposes only and does not purport to be indicative of what would have occurred had the acquisitions been made at that time or of results which may occur in the future.

	For the three months ended June 30,		For the six months ended June 30,	
	2011	**2010**	**2011**	**2010**
Total revenues (in thousands)	$ 194,682	$ 184,749	$ 384,303	$ 376,872
Net income (in thousands)	$ 10,805	$ 7,736	$ 19,718	$ 14,989
Basic net income per share	$ 0.21	$ 0.16	$ 0.39	$ 0.31
Diluted net income per share	$ 0.21	$ 0.15	$ 0.39	$ 0.30

Note 3. Segment Information

Our business is organized into four reporting segments Business Consulting Services, Dispute and Investigative Services, Economic Consulting and International Consulting. These reporting segments are generally defined by the nature of their services and geography and may be the aggregation of multiple operating segments as indicated in the description below. We have two additional operating segments within the Business Consulting Services segment. Our business is managed and resources are allocated on the basis of the six operating segments.

The Business Consulting Services reporting segment provides strategic, operational, financial, regulatory and technical management consulting services to clients, principally C suite and corporate management, government entities and law firms. The reporting segment is comprised of three operating segments, Energy, Healthcare and Other Business Consulting practices. The Energy and Healthcare business units are defined as operating segments due to their size, importance and organizational reporting relationships. The Energy and Healthcare operating segments provide services to clients in those respective markets, and the Other Business Consulting practice provides operations advisory, valuation and restructuring services to financial services and other markets.

The Dispute and Investigative Services reporting segment provides a wide range of services to clients facing the challenges of disputes, litigation, forensic investigation, discovery and regulatory compliance. The clients of this segment are principally law firms, corporate general counsel and corporate boards.

Table of Contents

The Economic Consulting reporting segment provides economic and financial analyses of complex legal and business issues principally for law firms, corporations and governmental agencies. Expertise includes areas such as antitrust, corporate finance and governance, bankruptcy, intellectual property, investment banking, labor market discrimination and compensation, corporate valuation and securities litigation.

The International Consulting reporting segment provides a mix of dispute and business consulting services to clients predominately outside North America. The clients are principally C suite and corporate management, governmental entities and law firms.

The following information includes segment revenues before reimbursements, segment total revenues and segment operating profit. Certain unallocated expense amounts related to specific reporting segments have been excluded from the calculation of segment operating profit to be consistent with the information used by management to evaluate segment performance. Segment operating profit represents total revenues less costs of services excluding long-term compensation expense related to consulting personnel. The information presented does not necessarily reflect the results of segment operations that would have occurred had the segments been stand-alone businesses. Long-term compensation expense related to consulting personnel includes share-based compensation expense and compensation expense attributed to forgivable loans (see Note 8 Supplemental Consolidated Balance Sheet Information).

	For the three months ended June 30,		For the six months ended June 30,	
(Amounts in Thousands)	**2011**	**2010**	**2011**	**2010**
Revenues before reimbursements:				
Business Consulting Services	$ 71,710	$ 63,430	$ 142,179	$ 120,829
Dispute and Investigative Services	66,789	59,737	132,542	123,075
Economic Consulting	18,475	16,966	36,349	33,954
International Consulting	16,319	14,484	31,827	30,629
Total revenues before reimbursements	$ 173,293	$ 154,617	$ 342,897	$ 308,487
Total revenues:				
Business Consulting Services	$ 81,193	$ 71,756	$ 160,820	$ 138,006
Dispute and Investigative Services	73,117	63,867	145,123	131,761
Economic Consulting	19,889	18,622	38,428	37,231
International Consulting	20,209	18,078	38,836	38,875
Total revenues	$ 194,408	$ 172,323	$ 383,207	$ 345,873
Segment operating profit:				
Business Consulting Services	$ 23,453	$ 23,148	$ 46,635	$ 42,165
Dispute and Investigative Services	27,279	21,585	53,056	46,993
Economic Consulting	6,029	6,273	11,786	12,569
International Consulting	3,549	3,663	6,831	7,403
Total combined segment operating profit	60,310	54,669	118,308	109,130
Segment operating profit reconciliation to income before income tax expense:				
Unallocated:				
General and administrative expenses	31,143	29,089	63,552	59,549
Depreciation expense	3,206	3,553	6,583	7,354
Amortization expense	2,163	2,962	4,464	5,758

Long-term compensation expense related to consulting personnel (including share-based compensation)	3,839	2,180	7,048	5,001
Operating income	19,959	16,885	36,661	31,468
Interest and other expense, net	1,554	3,153	2,991	6,423
Income before income tax expense	$ 18,405	$ 13,732	$ 33,670	$ 25,045

Table of Contents

Total assets by segment were as follows (shown in thousands):

	June 30, 2011	December 31, 2010
Business Consulting Services	$ 264,120	$ 263,465
Dispute and Investigative Services	347,419	343,531
Economic Consulting	88,784	86,719
International Consulting	76,153	69,539
Unallocated assets	103,454	105,781
Total assets	$ 879,930	$ 869,035

Note 4. Goodwill and Intangible Assets, net

Goodwill and other intangible assets consisted of (shown in thousands):

	June 30, 2011	December 31, 2010
Goodwill	$ 571,638	$ 566,427
Less accumulated amortization	(5,425)	(5,425)
Goodwill, net	566,213	561,002
Intangible assets:		
Customer lists and relationships	72,455	71,153
Non-compete agreements	21,260	20,994
Other	24,031	23,521
Intangible assets, at cost	117,746	115,668
Less accumulated amortization	(98,213)	(92,474)
Intangible assets, net	19,533	23,194
Goodwill and intangible assets, net	$ 585,746	$ 584,196

Our annual goodwill impairment test is completed in the second quarter of each year. During the second quarter of 2011, we performed our annual goodwill impairment test based on balances as of May 31, 2011. We completed the first step of the goodwill impairment test and determined that the estimated fair value of each reporting unit exceeded its net asset carrying value. Accordingly, there was no indication of impairment and the second step was not performed.

As of our annual goodwill impairment test, the excess of estimated fair value over net asset carrying value of our reporting units was consistent or higher for all reporting units when compared to our November 30, 2010 interim goodwill impairment test and approximated 29% for Energy; 19% for Healthcare, 15% for Dispute and Investigative Services, 15% for Economic Consulting, 64% for Other Business Consulting Services, and 9% for International Consulting. In determining estimated fair value of our reporting units, we used internal projections completed during our quarterly forecasting process. The key assumptions reflected profit margin improvement that was generally consistent with our longer term historical performance, revenue growth rates that were higher than our peer group in the near term, discount rates that were determined based on comparables for our peer group and cost of capital that was based on company averages. In general, growth rates used in our annual impairment test were the same as in our interim goodwill impairment test with the exception of the International Consulting reporting unit, which was favorably impacted by two small acquisitions since the date of the last fair value estimation. The profit margin expectations used in our May 31, 2011 analysis for all reporting units were materially the same as those used in our prior goodwill analysis. Our fair value estimates were made as of the date of our analysis and are subject to change.

As we complete our tests of goodwill impairment, if the excess of estimated fair value over the net asset carrying value of our reporting units decreases, there is increased risk that the second step of the goodwill impairment test will be required, and that goodwill impairment could result. International Consulting had the smallest excess at approximately 9% and the Dispute and Investigative Services, Healthcare, and Economic Consulting reporting units had excess between 15% and 20%. Our International Consulting segment fair value is more volatile due to its smaller size, assumed higher growth rates, involvement in emerging markets and exposure to multiple markets outside the United States. The higher growth rates are based on our ability to leverage current and future investments and other factors which may be beyond our control. Further, the Economic Consulting reporting unit is substantially comprised of recent acquisitions and its estimated fair value depends on various factors including the success of those acquisitions and the ability to leverage our recent investments. The Economic Consulting reporting unit fair value also assumes higher growth rates and is subject to volatility due to its smaller size. The Dispute and Investigative Services and Healthcare reporting units are our largest and their fair values will depend on the ability to achieve profitable growth.

In addition to our annual goodwill impairment test, on a periodic basis, we are required to consider whether it is more likely than not that the fair value of each of the reporting units has fallen below its carrying value. We consider elements and other factors including, but not limited to, adverse changes in the business climate in which we operate, attrition of key personnel, unanticipated competition, our market capitalization in excess of our book value, our recent operating performance and our financial projections. As a result of this review we are required to determine whether such an event or condition existed that would require us to perform an interim goodwill impairment test prior to our annual test date.

During the fourth quarter of 2010, our average stock price traded near or below our book value for a prolonged period of time and we recorded an intangible assets impairment charge. As a result of these factors, we completed an interim impairment test of our goodwill balances as of November 30, 2010. At that time, we completed the first step of the goodwill impairment test and determined that the estimated fair value of each reporting unit exceeded its net asset carrying value. Accordingly, there was no indication of impairment and the second step was not performed.

As of June 30, 2011, there was no indication of impairment related to our goodwill or other intangible assets; however, there can be no assurance that goodwill or these assets will not be impaired in the future and we will continue to monitor the factors noted above.

As we review our portfolio of services in the future, we may exit certain markets or reposition certain service offerings within our business. Consistent with past evaluations, further evaluations may result in our redefining our operating segments and may impact a significant portion of one or more of our reporting units. As noted above, if such actions occur, they may be considered triggering events that would result in our performing an interim impairment test of our goodwill and an impairment test of our intangible assets.

We use various methods to determine fair value, including market, income and cost approaches. With these approaches, we adopt certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk or the risks inherent in the inputs to the valuation. Inputs to the valuation can be readily observable, market-corroborated, or unobservable. We use valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs.

The fair value measurements used for our goodwill impairment testing use significant unobservable inputs which reflect our own assumptions about the inputs that market participants would use in measuring fair value including risk considerations. The fair value of our reporting units is also impacted by our overall market capitalization and may be impacted by volatility in our stock price and assumed control premium, among other things.

Our intangible assets have estimated useful lives which range up to nine years. We will amortize the remaining net book values of intangible assets over their remaining useful lives, which approximate the estimated period of consumption. As of June 30, 2011, our intangible assets consisted of the following (amounts shown in thousands):

Category	**Weighted Average Remaining Years**	**Amount**
Customer lists and relationships, net	4.0	$ 14,491