

SPAR GROUP INC  
Form 10-Q  
May 14, 2015

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

**Form 10-Q**

**(Mark One)**

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for the first quarterly period ended **March 31, 2015**.

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: 0-27824

**SPAR Group, Inc.**

(Exact name of registrant as specified in its charter)

Delaware 33-0684451

State of Incorporation

IRS Employer Identification No.

333 Westchester Avenue, South Building, Suite 204,  
White Plains, New York 10604  
(Address of principal executive offices, including zip  
code)

Registrant's telephone number, including area code: (914) 332-4100

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Indicate by check 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 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    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 the definitions of "large accelerated filer", "accelerated filer", "non-accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act).

Large Accelerated Filer	Accelerated Filer
Non-Accelerated Filer	Smaller Reporting Company

(Do not check if a 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

On May 14, 2015, there were 20,580,303 shares of Common Stock outstanding.

**SPAR Group, Inc.**

Index

**PART I: FINANCIAL INFORMATION**

Item 1	Consolidated Financial Statements	
	Consolidated Balance Sheets as of March 31, 2015 and December 31, 2014	2
	Consolidated Statements of Income (Loss) and Comprehensive Loss for the three months ended March 31, 2015 and 2014	3
	Consolidated Statement of Equity for the three months ended March 31, 2015	4
	Consolidated Statements of Cash Flows for the three months ended March 31, 2015 and 2014	5
	Notes to Consolidated Financial Statements	6
Item 2	Management's Discussion and Analysis of Financial Condition, Results of Operations, Liquidity and Capital Resources	17
Item 3	Quantitative and Qualitative Disclosures about Market Risk	23
Item 4	Controls and Procedures	23

**PART II: OTHER INFORMATION**

Item 1	Legal Proceedings	25
Item 1A	Risk Factors	25
Item 2	Unregistered Sales of Equity Securities and Use of Proceeds	25
Item 3	Defaults upon Senior Securities	25
Item 4	Mine Safety Disclosures	25
Item 5	Other Information	25
Item 6	Exhibits	25

<b>SIGNATURES</b>		26
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**PART I: FINANCIAL INFORMATION****Item 1. Consolidated Financial Statements****SPAR Group, Inc. and Subsidiaries****Consolidated Balance Sheets***(In thousands, except share and per share data)*

	<b>March 31, 2015 (Unaudited)</b>	<b>December 31, 2014 (Note)</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 4,292	\$ 4,382
Accounts receivable, net	24,895	26,245
Deferred income taxes	411	464
Prepaid expenses and other current assets	597	868
Total current assets	30,195	31,959
Property and equipment, net	2,456	2,175
Goodwill	1,800	1,800
Intangible assets, net	2,981	3,149
Deferred income taxes	5,134	5,134
Other assets	31	353
Total assets	\$ 42,597	\$ 44,570
<b>Liabilities and equity</b>		
Current liabilities:		
Accounts payable	\$ 3,753	\$ 4,011
Accrued expenses and other current liabilities	6,864	8,149
Accrued expenses due to affiliates	984	487
Deferred income taxes	1,540	1,540
Customer deposits	557	659
Lines of credit	679	658
Total current liabilities	14,377	15,504
Long-term debt and other liabilities	5,400	5,855
Total liabilities	19,777	21,359
Commitments and Contingencies – See Note 9		
Equity:		
SPAR Group, Inc. equity		
Preferred stock, \$.01 par value: Authorized and available shares– 2,445,598 Issued and outstanding shares– None – March 31, 2015 and None – December 31, 2014	-	-
Common stock, \$.01 par value: Authorized shares – 47,000,000 Issued shares – 20,680,717 – March 31, 2015 and December 31, 2014	207	207

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Treasury stock, at cost 116,164 shares – March 31, 2015 and 121,663 shares – December 31, 2014	(173 )	(183 )
Additional paid-in capital	15,613	15,519
Accumulated other comprehensive loss	(2,220 )	(1,556 )
Retained earnings	4,696	4,770
Total SPAR Group, Inc. equity	18,123	18,757
Non-controlling interest	4,697	4,454
Total equity	22,820	23,211
Total liabilities and equity	\$ 42,597	\$ 44,570

The Balance Sheet at December 31, 2014, is excerpted from the consolidated audited financial statements as of Note: that date but does not include certain information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.  
*See accompanying notes.*

**SPAR Group, Inc. and Subsidiaries****Consolidated Statements of Income (Loss) and Comprehensive Loss****(unaudited)***(In thousands, except per share data)*

	<b>Three Months Ended March 31,</b>	
	<b>2015</b>	<b>2014</b>
Net revenues	<b>\$29,266</b>	\$28,036
Cost of revenues	<b>22,353</b>	21,806
Gross profit	<b>6,913</b>	6,230
Selling, general and administrative expense	<b>6,096</b>	5,921
Depreciation and amortization	<b>468</b>	412
Operating income (loss)	<b>349</b>	(103 )
Interest expense	<b>58</b>	43
Other income, net	<b>(29 )</b>	(45 )
Income (loss) before income tax expense	<b>320</b>	(101 )
Income tax expense	<b>151</b>	119
Net income (loss)	<b>169</b>	(220 )
Net income attributable to non-controlling interest	<b>243</b>	149
Net income (loss) attributable to SPAR Group, Inc.	<b>\$(74 )</b>	\$(369 )
Basic and diluted loss per common share:	<b>\$-</b>	\$(0.02 )
Weighted average common shares – basic and diluted	<b>20,562</b>	20,557
Net income (loss)	<b>\$169</b>	\$(220 )
Other comprehensive loss:		
Foreign currency translation adjustments	<b>(664 )</b>	(47 )
Comprehensive loss	<b>(495 )</b>	(267 )
Comprehensive loss attributable to non-controlling interest	<b>(243 )</b>	(149 )
Comprehensive income (loss) attributable to SPAR Group, Inc.	<b>\$(738 )</b>	\$(416 )

*See accompanying notes.*





**SPAR Group, Inc. and Subsidiaries****Consolidated Statement of Equity****(unaudited)***(In thousands)*

	Common Stock		Treasury Stock		Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Non- Controlling Interest	Total Equity
	Shares	Amount	Shares	Amount					
Balance at January 1, 2015	20,681	\$ 207	122	\$ (183 )	\$ 15,519	\$ (1,556 )	\$ 4,770	\$ 4,454	\$ 23,211
Share-based compensation	-	-	-	-	102	-	-	-	102
Exercise of stock options	-	-	(6 )	10	(8 )	-	-	-	2
Other comprehensive loss	-	-	-	-	-	(664 )	-	-	(664 )
Net (loss) income	-	-	-	-	-	-	(74 )	243	169
<b>Balance at March 31, 2015</b>	<b>20,681</b>	<b>\$ 207</b>	<b>116</b>	<b>\$ (173 )</b>	<b>\$ 15,613</b>	<b>\$ (2,220 )</b>	<b>\$ 4,696</b>	<b>\$ 4,697</b>	<b>\$ 22,820</b>

*See accompanying notes.*

**SPAR Group, Inc. and Subsidiaries****Consolidated Statements of Cash Flows****(unaudited)***(In thousands)*

	<b>Three Months Ended March 31,</b>	
	<b>2015</b>	<b>2014</b>
<b>Operating activities</b>		
Net income (loss)	<b>\$169</b>	\$(220 )
Adjustments to reconcile net income (loss) to net cash provided by operating activities		
Depreciation and amortization	<b>468</b>	412
Bad debt expense, net of recoveries	<b>19</b>	24
Share based compensation	<b>102</b>	252
Changes in operating assets and liabilities, net of business acquisitions and disposition:		
Accounts receivable	<b>1,186</b>	1,043
Prepaid expenses and other assets	<b>646</b>	326
Accounts payable	<b>(258 )</b>	(376 )
Accrued expenses, other current liabilities and customer deposits	<b>(890 )</b>	1,011
Net cash provided by operating activities	<b>1,442</b>	2,472
<b>Investing activities</b>		
Purchases of property and equipment and capitalized software	<b>(584 )</b>	(358 )
Net cash used in investing activities	<b>(584 )</b>	(358 )
<b>Financing activities</b>		
Net payments on lines of credit	<b>(428 )</b>	(671 )
Proceeds from stock options exercised	<b>2</b>	18
Payments on term debt	<b>(6 )</b>	(7 )
Payments on capital lease obligations	<b>-</b>	(34 )
Net cash used in financing activities	<b>(432 )</b>	(694 )
Effect of foreign exchange rate changes on cash	<b>(516 )</b>	2
Net change in cash and cash equivalents	<b>(90 )</b>	1,422
Cash and cash equivalents at beginning of year	<b>4,382</b>	2,814
Cash and cash equivalents at end of period	<b>\$4,292</b>	\$4,236
<b>Supplemental disclosure of cash flows information</b>		
Interest paid	<b>\$72</b>	\$31
Income taxes paid	<b>\$55</b>	\$113

*See accompanying notes.*



SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited)

## 1. Basis of Presentation

The unaudited, consolidated financial statements of SPAR Group, Inc., a Delaware corporation ("SGRP"), and its subsidiaries (together with SGRP, collectively, the "Company" or the "SPAR Group"), accompanying this Quarterly Report on Form 10-Q for the quarter ended March 31, 2015 (this "Quarterly Report"), have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to 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 for complete financial statements. In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation have been included in these interim financial statements. However, these interim financial statements should be read in conjunction with the annual consolidated financial statements and notes thereto for the Company as contained in the SGRP's Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the Securities and Exchange Commission (the "SEC") on April 15, 2015 (the "2014 Annual Report"), and SGRP's Proxy Statement for its 2015 Annual Meeting of Stockholders as filed with the SEC on April 20, 2015 (the "2015 Proxy Statement"). Particular attention should be given to Items 1 and 1A of the 2014 Annual Report respecting the Company's Business and Risk Factors, respectively, and the following parts of SGRP's 2015 Proxy Statement: (i) *SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT*, (ii) *CORPORATE GOVERNANCE*, (iii) *EXECUTIVE OFFICERS, COMPENSATION, DIRECTORS AND OTHER INFORMATION* and (iv) *EXECUTIVE COMPENSATION, EQUITY AWARDS AND OPTIONS*. The Company's results of operations for the interim period are not necessarily indicative of its operating results for the entire year.

## 2. Business and Organization

SPAR Group is a supplier of merchandising and other marketing services throughout the United States and internationally. The Company also provides in-store event staffing, product sampling, audit services, furniture and other product assembly services, technology services and marketing research services. Assembly services are performed in stores, homes and offices while those other services are primarily performed in mass merchandisers, office supply, grocery, drug store, home improvement, independent, convenience and electronics stores.

Merchandising services primarily consist of regularly scheduled, special project and other product services provided at the store level, and the Company may be engaged by either the retailer or the manufacturer. Those services may include restocking and adding new products, removing spoiled or outdated products, resetting categories "on the

shelf" in accordance with client or store schematics, confirming and replacing shelf tags, setting new sale or promotional product displays and advertising, replenishing kiosks, providing in-store event staffing and providing assembly services in stores, homes and offices. Other merchandising services include whole store or departmental product sets or resets, including new store openings, new product launches and in-store demonstrations, audit services, special seasonal or promotional merchandising, focused product support and product recalls. The Company also provides technology services and marketing research services.

As of March 31, 2015, the Company operates in 9 countries and divides its operations into two reportable segments: its Domestic Division, which provides those services in the United States of America since certain of its predecessors were formed in 1979, and its International Division, which began operations in May 2001 and provides similar merchandising, marketing, audit and in-store event staffing services in Japan, Canada, South Africa, India, China, Australia, Mexico and Turkey.

The Company continues to focus on expanding its merchandising and marketing services business throughout the world.

SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited) (continued)

**3. Earnings Per Share**

The following table sets forth the computations of basic and diluted net income per share (in thousands, except per share data):

	<b>Three Months Ended March 31,</b>	
	<b>2015</b>	<b>2014</b>
Numerator:		
Net loss attributable to SPAR Group, Inc.	\$(74 )	\$(369 )
Denominator:		
Shares used in basic and diluted net income per share calculation	<b>20,562</b>	20,557
Basic and diluted net loss per common share:	\$-	\$(0.02 )

For the three months ended March 31, 2015, and March 31, 2014, 1,029,000 and 1,255,000 vested and non-vested stock options were not included in the calculation because they would have had an anti-dilutive effect.

**4. Credit Facilities*****Sterling Credit Facility:***

SGRP and certain of its US and Canadian subsidiaries, (namely SPAR Marketing Force, Inc., SPAR National Assembly Services, Inc., SPAR Group International, Inc., SPAR Trademarks, Inc., SPAR Acquisition, Inc., SPAR Canada, Inc. and SPAR Canada Company) (together with SGRP each a "Borrower"), are parties to a Revolving Loan and Security Agreement dated as of July 6, 2010, as amended in (as amended, the "Sterling Loan Agreement"), with Sterling National Bank (the "Lender"), and their Secured Revolving Loan Note in the amended maximum principal

amounts of \$7.5 million (see below) to Sterling National Bank (as amended, the "Sterling Note"), to document and govern their credit facility with the Lender (including such agreement and note, the "Sterling Credit Facility"). The Sterling Credit Facility currently is scheduled to expire and the Borrowers' loans thereunder will become due on July 6, 2016 (with no early termination fee).

The Sterling Loan Agreement currently requires the Borrowers to pay interest on the loans thereunder equal to the Agent's floating Prime Rate (as defined in such agreement) minus one half of one percent (1/2%) per annum, and a fee on the maximum unused line thereunder equal to one-eighth of one percent (0.125%) per annum.

Revolving Loans of up to \$7.5 million are available to the Borrowers under the Sterling Credit Facility based upon the borrowing base formula defined in the Sterling Loan Agreement (principally 85% of "eligible" US and Canadian accounts receivable less certain reserves). The Sterling Credit Facility is secured by substantially all of the assets of the Borrowers (other than the Company's non-Canadian foreign subsidiaries, certain designated domestic subsidiaries, and those subsidiaries' respective equity and assets). The Sterling Credit Facility amendment dated July 1, 2013 eliminated the requirement for a "closed lock box" account with Sterling so that collections are no longer used to automatically pay down the loans under the Sterling Credit Facility and that account is no longer used. Therefore, the Sterling Credit Facility is now classified as long term debt.

The amendment to the Sterling Credit Facility effective as of July 1, 2014, among other things, extended the scheduled term of the Sterling Credit Facility to July 6, 2016 (with no early termination fee), increased the maximum principal amounts of Sterling's Commitment under the Sterling Loan Agreement to \$7.5 million, and provided for the amendment and restatement of the Sterling Note with a new \$7.5 million note from the Borrowers in replacement of the old notes.

The Sterling Loan Agreement contains certain financial and other restrictive covenants and also limits certain expenditures by the Borrowers, including, but not limited to, capital expenditures and other investments. At March 31, 2015, the Company was in compliance with such covenants.

## SPAR Group, Inc. and Subsidiaries

## Notes to Consolidated Financial Statements

(unaudited) (continued)

**International Credit Facilities:**

SPARFACTS Australia Pty. Ltd., has a secured line of credit facility with Oxford Funding Pty Ltd. for \$1.2 million (Australian) or approximately \$900,000 (based upon the exchange rate at March 31, 2015). The facility provides for borrowing based upon a formula, as defined in the agreement (principally 80% of eligible accounts receivable less certain deductions). The agreement is on a month to month basis at the Company's request. The outstanding balance at March 31, 2015, was approximately \$553,000 (Australian) or \$426,000 (based on the exchange rate at March 31, 2015).

On March 7, 2011, the Japanese subsidiary, SPAR FM Japan, Inc., a wholly owned subsidiary, secured a term loan with Mizuho Bank in the amount of approximately 20.0 million Yen (Japanese) or \$168,000. The loan is payable in monthly installments of 238,000 Yen or \$2,000 at an interest rate of 0.1% per annum with a maturity date of February 28, 2018. The outstanding balance at March 31, 2015, was approximately 8.3 million Yen or \$70,000 (based upon the exchange rate at March 31, 2015).

The China Unilink subsidiary secured a loan with China Construction Bank in the amount of 1.4 million Chinese Yuan Renminbi or approximately \$229,000 (based on the exchange rate at March 31, 2015). The loan is collateralized with the personal property of one of the minority shareholders of Unilink. The loan has an interest rate of 7.2% per annum and a maturity date of February 11, 2016, at which time the full amount outstanding is to be paid in full. The full amount was outstanding as of March 31, 2015.

***Summary of Company Credit and Other Debt Facilities (dollars in thousands) :***

	March 31, 2015	Interest Rate <sup>1</sup>	December 31, 2014	Interest Rate <sup>2</sup>
<b><u>Credit Facilities Loan Balance:</u></b>				
United States	\$ 5,354	2.8%	\$ 5,804	2.8%
Australia	426	6.7%	406	7.1%
China	229	7.2%	228	7.2%
	\$ 6,009		\$ 6,438	



Other Debt Facility:

Japan Term Loan	\$ 70	0.1%	\$ 75	0.1%
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	March 31, 2015	December 31, 2014
<u>Unused Availability:</u>		
United States	\$ 1,574	\$ 1,696
Australia	497	573
	\$ 2,071	\$ 2,269

(1) Based on interest rate at March 31, 2015

(2) Based on interest rate at December 31, 2014

SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited) (continued)

Management believes that based upon the continuation of the Company's existing credit facilities, projected results of operations, vendor payment requirements and other financing available to the Company (including amounts due to affiliates), sources of cash availability should be manageable and sufficient to support ongoing operations over the next year. However, delays in collection of receivables due from any of the Company's major clients, or a significant reduction in business from such clients could have a material adverse effect on the Company's cash resources and its ongoing ability to fund operations.

## **5. Related-Party Transactions**

SGRP's policy respecting approval of transactions with related persons, promoters and control persons is contained in the SPAR Group Code of Ethical Conduct for its Directors, Senior Executives and Employees Amended and Restated (as of) August 1, 2012 (the "Ethics Code"). Article V of the Ethics Code generally prohibits each "Covered Person" (including SGRP's officers and directors) from engaging in any business activity that conflicts with his or her duties to the Company, and directs each "Covered Person" to avoid any activity or interest that is inconsistent with the best interests of the SPAR Group, in each case except for any "Approved Activity" (as such terms are defined in the Ethics Code). Examples of violations include (among other things) having any ownership interest in, acting as a director or officer of or otherwise personally benefiting from business with any competitor, customer or vendor of the Company other than pursuant to any Approved Activity. Approved Activities include (among other things) any contract with an affiliated person (each an "Approved Affiliate Contract") or anything else disclosed to and approved by SGRP's Board of Directors (the "Board"), its Governance Committee or its Audit Committee, as the case may be, as well as the ownership, board, executive and other positions held in and services and other contributions to affiliates of SGRP and its subsidiaries by certain directors, officers or employees of SGRP, any of its subsidiaries or any of their respective family members. The Company's senior management is generally responsible for monitoring compliance with the Ethics Code and establishing and maintaining compliance systems, including conflicting relationships and transactions, subject to the review and oversight of SGRP's Governance Committee as provided in clause IV.11 of the Governance Committee's Charter, and SGRP's Audit Committee as provided in clause I.2(1) of the Audit Committee's Charter. The Governance Committee and Audit Committee each consist solely of independent outside directors.

SGRP's Audit Committee has the specific duty and responsibility to review and approve the overall fairness of all material related-party transactions. The Audit Committee receives affiliate contracts and amendments thereto for its review and approval (to the extent approval is given), and these contracts are periodically (often annually) again reviewed, in accordance with the Audit Committee Charter, the Ethics Code, the rules of the Nasdaq Stock Market, Inc. ("Nasdaq"), and other applicable law to ensure that the overall economic and other terms will be (or continue to be) no less favorable to the Company than would be the case in an arms-length contract with an unrelated provider of

similar services (i.e., its overall fairness to the Company including pricing and the ability to provide services at comparable performance levels). The Audit Committee periodically reviews all of the related party relationships, agreements and transactions described below.

SPAR Business Services, Inc. ("SBS"), SPAR Administrative Services, Inc. ("SAS") and SPAR InfoTech, Inc. ("SIT") are affiliates of SGRP but are not part of the consolidated Company. Mr. Robert G. Brown, a Director, the Chairman and a major stockholder of SGRP, and Mr. William H. Bartels, a Director and the Vice Chairman of the Company and a major stockholder of SGRP, are the sole stockholders of SBS. Mr. Brown is the sole stockholder of SIT. Mr. Brown is a director and officer of SBS and SIT. Mr. Bartels is a director and officer of SAS. During 2014 the stockholders of SAS were Mr. Bartels and Mr. Brown, and as of January 1, 2015, Mr. Brown had transferred approximately 84% of his ownership to related parties.

## SPAR Group, Inc. and Subsidiaries

## Notes to Consolidated Financial Statements

(unaudited) (continued)

SBS provided approximately 86% and 82% of the domestic merchandising specialist field force used by the Company (as a percentage of the total cost for such field force, including field force provided by NRS, as defined below) for the three months ended March 31, 2015 and 2014, respectively, and SAS provided approximately 91% and 93% of the direct domestic field administration used by the Company (as a percentage of the total cost for such field administrators) at a total cost for the services of SBS and SAS of approximately \$6.6 million for both the three months ended March 31, 2015 and 2014. Pursuant to the terms of the Amended and Restated Field Service Agreement dated as of January 1, 2004, as amended in 2011, the Company received services from SBS through the use of approximately 4,800 field merchandising specialists during the quarter ended March 31, 2015. Pursuant to the terms of the Amended and Restated Field Management Agreement dated as of January 1, 2004, the Company received administrative services from SAS through the use of 54 full-time national, regional and district administrators during the three months ended March 31, 2015. For those services, the Company contracted in the Existing Agreements to pay SBS and SAS on a "Cost Plus Fee" arrangement, which provides that the Company is to pay SBS and SAS for their costs of providing those services plus 4% for 2014 of such costs (the "Cost Plus Fee") while those agreements were in effect (see below). Those costs include all field expenses of SBS (effectively including net workers compensation insurance expense), all payroll and employment tax expenses of SAS and all legal and other administrative expenses paid by either of them. The net total Cost Plus Fee earned by SAS and SBS for services rendered was approximately \$133,000 and \$255,000 for the three months ended March 31, 2015 and 2014, respectively. In order to obtain and continue its favorable fee arrangement with SBS and SAS, the Company also arranged to provide certain administrative services directly to SBS and SAS without charge, including certain human resource and legal services. The Company believes this arrangement also is more efficient and cost effective. The unaudited value of these services was approximately \$163,000 and \$106,000 for the three months ended March 31, 2015 and 2014, respectively.

The service agreements with SBS and SAS were scheduled to automatically renew on December 31, 2013, but in order to prevent such automatic renewal and permit renegotiation after the end of 2013, the Company gave SBS and SAS the required notice of non-renewal under those agreements and from time to time has entered into temporary extension agreements with them to temporarily extend the Existing Agreements to November 30, 2014. The parties have had extensive negotiations for over a year, principally over pricing. The Company has most recently offered to pay reduced Cost Plus Fees of 2%, while SBS has most recently proposed a Cost Plus Fee of 2.97% while making certain other adjustments to reimbursable expenses and previous credits (the net of which would effectively be approximately equal to the annual rates previously paid to SBS by the Company), and SAS has most recently proposed a Cost Plus Fee of 4%. Neither party has accepted the other party's proposals. SAS and SBS have stated their intent to continue to provide their services while negotiations continue. As the extension of the existing agreements expired on November 30, 2014, the potential differences between the Company's proposal and the SBS and SAS proposals became potentially relevant from and after December 1, 2014. The difference in the net expense for SBS and SAS proposals when compared to the Company proposals was approximately \$52,000 and \$22,000 for the three month period ended March 31, 2015.

No salary reimbursements for Mr. Brown or Mr. Bartels are included in such reimbursable costs or Cost Plus Fee during 2014 and 2015 for SBS. However, since SBS is a "Subchapter S" corporation and owned by Messrs. Brown and Bartels, all income from SBS is allocated to them. A similar approach has been taken for SAS, which is partially owned by Mr. Bartels.

National Merchandising Services, LLC ("NMS"), is a consolidated domestic subsidiary of the Company and is owned jointly by SGRP through its indirect ownership of 51% of the NMS membership interests and by National Merchandising of America, Inc. ("NMA"), through its ownership of the other 49% of the NMS membership interests. Mr. Edward Burdekin is the Chief Executive Officer and President and a director of NMS and also is an executive officer and director of NMA and the sole member and manager of National Retail Source, LLC ("NRS"). Ms. Andrea Burdekin, Mr. Burdekin's wife, is the sole stockholder and a director of NMA and a director of NMS. NRS and NMA are affiliates of the Company but are not consolidated with the Company. NMS commenced operations as of September 1, 2012.

NRS is expected to provide substantially all of the domestic merchandising specialist field force used by NMS. Pursuant to the terms of the Master Field Services Agreement dated as of August 1, 2013 (the "NRS Services Agreement"), NMS will receive merchandising services from NRS through the use of approximately 294 field merchandising specialists. Prior to that date, NMS received such merchandising services from NMA pursuant to the terms of the substantially similar Field Services Agreement dated as of July 31, 2012, as amended (the "NMA Services Agreement"). For those services, the Company has agreed to reimburse NRS (and NMA before it) for its total costs of providing those services and to pay NRS (and NMA before it) a fee equal to 2% of its total costs (the "Plus 2% Fee"). Those costs include all field and administrative costs and expenses (effectively including net workers compensation insurance expenses) of NRS (and NMA before it) but exclude certain legal and other administrative expenses. Accordingly, no salary reimbursement for Mr. Burdekin or Ms. Burdekin are included in such reimbursable costs or Plus 2% Fee.

SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited) (continued)

NRS (and before that, NMA) provided all of the domestic merchandising specialist field force used by NMS and 4% of all of the domestic merchandising specialist field force used by the Company (as a percentage of the total cost for such field force, including the field force provided by SBS) for both three months ended March 31, 2015 and 2014. The total Plus 2% Fee earned by NRS for services rendered was approximately \$5,000 and \$10,000 for the three months ended March 31, 2015 and 2014, respectively.

SGRP Meridian (Pty), Ltd. ("Meridian") is a consolidated international subsidiary of the Company and is owned 51% by SGRP and 49% by the following individuals: Mr. Brian Mason, Mr. Garry Bristow, and Mr. Adrian Wingfield. Mr. Mason is President and a director and Mr. Bristow is an officer and director of Meridian. Mr. Mason is also an officer and director and 50% shareholder of Merhold Property Trust ("MPT"). Mr. Mason and Mr. Bristow are both officers and directors and both own 50% of Merhold Cape Property Trust ("MCPT"). MPT owns the building where Meridian is headquartered and also owns two vehicles both of which are subleased to Meridian. MCPT provides a fleet of 126 vehicles to Meridian under a 4 year lease program. These leases are provided to Meridian at local market rates.

SGRP NDS Tanitim Ve Danismanlik A.S. ("NDS") is a consolidated international subsidiary of the Company and is owned 51% by SGRP and 49% by Mr. and Ms. Yilmaz. Mr. Yilmaz is President and a director and Ms. Yilmaz is an officer and director of NDS. They are both officers and directors of NDS Tanitim Danismanlik Hizmetleri Gida Tekstil Turizm Pazarlama Ticaret Limited Sirketi ("NDS Tanitim") and NDS Reklam Tanitim Ve Danismanlik Hizmetleri Pazarlama Ticaret Limited Sirketi ("NDS Reklam"). Mr. and Ms. Yilmaz, in total, own 40% of NDS Tanitim and NDS Reklam. NDS Tanitim provides NDS field management services while NDS Reklam provides NDS field merchandising services both at local market rates.

The Company continues to purchase services from SBS, SAS, NRS, MPT, MCPT, NDS Tanitim, and NDS Reklam because it believes the value of services it receives from them are at least as favorable to the Company as it could obtain from non-affiliated providers of similar services. The Company believes it is the largest and most important customer of SBS, SAS, NRS, MPT, MCPT, NDS Tanitim, and NDS Reklam (and from time to time may be their only customer), and accordingly the Company generally has been able to negotiate better terms, receives more personal and responsive service and is more likely to receive credits and other financial accommodations from SBS, SAS, NRS, MPT, MCPT, NDS Tanitim, and NDS Reklam than the Company could reasonably expect to receive from an unrelated service provider who has significant other customers and business. SBS, SAS and NRS affiliate contracts and arrangements are annually reviewed and considered for approval by SGRP's Audit Committee, subject to the ongoing negotiations as described above. MPT, MCPT, NDS Tanitim, and NDS Reklam affiliate contracts are currently scheduled to be reviewed and considered for approval by SGRP's Audit Committee at their August 2015 meeting.

The following costs of affiliates were charged to the Company (in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2015</b>	<b>2014</b>
Services provided by affiliates:		
Field merchandiser services (SBS)	<b>\$ 5,499</b>	\$5,459
Field management services (SAS)	<b>\$ 1,113</b>	\$1,178
Field merchandiser services (NMA and NRS)	<b>\$ 244</b>	\$502
Office and vehicle rental (MPT)	<b>\$ 12</b>	\$16
Vehicle rental (MCPT)	<b>\$ 197</b>	\$145
Field management services (NDS Tanitim)	<b>\$ 9</b>	\$9
Field merchandiser services (NDS Reklam)	<b>\$ 70</b>	\$373
 Total services provided by affiliates	 <b>\$ 7,144</b>	 \$7,682

Accrued expenses due to affiliates (in thousands):	<b>March 31, 2015</b>	<b>December 31, 2014</b>
Total accrued expenses due to affiliates	<b>\$ 984</b>	\$ 487

SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited) (continued)

In July 1999, SPAR Marketing Force, Inc. ("SMF"), SBS and SIT entered into a perpetual software ownership agreement providing that each party independently owned an undivided share of and had the right to unilaterally license and exploit their "Business Manager" Internet job scheduling software (which had been jointly developed by such parties), and all related improvements, revisions, developments and documentation from time to time voluntarily made or procured by any of them at its own expense. In addition, SPAR Trademarks, Inc. ("STM"), SBS and SIT entered into separate perpetual trademark licensing agreements whereby STM has granted non-exclusive royalty-free licenses to SIT and SBS (and through them to their commonly controlled subsidiaries and affiliates by sublicenses, including SAS) for their continued use of the name "SPAR" and certain other trademarks and related rights of STM, a wholly owned subsidiary of SGRP. SBS and SAS provide services to the Company, as described above, and SIT no longer provides services to and does not compete with the Company.

Through arrangements with the Company, SBS, SAS and other companies owned by Mr. Brown or Mr. Bartels participate in various benefit plans, insurance policies and similar group purchases by the Company, for which the Company charges them their allocable shares of the costs of those group items and the actual costs of all items paid specifically for them. All such transactions between the Company and the above affiliates are paid and/or collected by the Company in the normal course of business.

In addition to the above, SAS purchases insurance coverage for worker compensation, casualty and property insurance risk for itself, SBS and (through SBS under contracts with them) its field merchandising specialists and the Company from Affinity Insurance, Ltd. ("Affinity"). SAS owns a minority (less than 1%) of the common stock in Affinity. The Affinity insurance premiums for such coverage are ultimately charged to SAS, SBS (and through SBS to its covered field merchandising specialists) and the Company based on the contractual arrangements of the parties.

## **6. Preferred Stock**

SGRP's certificate of incorporation authorizes it to issue 3,000,000 shares of preferred stock with a par value of \$0.01 per share (the "SGRP Preferred Stock"), which may have such preferences and priorities over the SGRP Common Stock and other rights, powers and privileges as the Company's Board of Directors may establish in its discretion from time to time. The Company has created and authorized the issuance of a maximum of 3,000,000 shares of Series A Preferred Stock pursuant to SGRP's Certificate of Designation of Series "A" Preferred Stock (the "SGRP Series A Preferred Stock"), which have dividend and liquidation preferences, have a cumulative dividend of 10% per year, are redeemable at the Company's option and are convertible at the holder's option (and without further consideration) on a



one-to-one basis into SGRP Common Stock. The Company issued 554,402 of SGRP shares to affiliated retirement plans which were all converted into common shares in 2011 (including dividends earned thereon), leaving 2,445,598 shares of remaining authorized preferred stock. At March 31, 2015, no shares of SGRP Series A Preferred Stock were issued and outstanding.

## **7. Stock-Based Compensation and Other Plans**

SGRP has granted restricted stock and stock option awards to its eligible directors, officers and employees and certain employees of its affiliates respecting shares of Common Stock issued by SGRP ("SGRP Shares") pursuant to SGRP's 2008 Stock Compensation Plan (as amended, the "2008 Plan"), which was approved by SGRP's stockholders in May of 2008 and 2009. The 2008 Plan provides for the granting of restricted SGRP shares, stock options to purchase SGRP shares (either incentive or nonqualified), and restricted stock units, stock appreciation rights and other awards based on SGRP shares ("Awards") to SGRP Directors and the Company's specified executives, employees and consultants (which are employees of certain of its affiliates), although to date SGRP has not issued any permissible form of Award other than stock option and restricted share awards. As of March 31, 2015, approximately 1.3 million SGRP shares were available for Award grants under the amended 2008 Plan.

SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited) (continued)

The Company recognized \$93,000 and \$132,500 in stock-based compensation expense relating to stock option Awards during the three month periods ended March 31, 2015 and 2014, respectively. The tax benefit, available to the Company, from stock based compensation expense related to stock options during the three months ended March 31, 2015 and 2014 was approximately \$35,500 and \$50,400, respectively. However, since the Company has NOL's available for the next several years, these tax benefits have not been realized as of this report. As of March 31, 2015, total unrecognized stock-based compensation expense related to stock options was \$825,900.

During the three months ended March 31, 2015 and 2014, the Company recognized approximately \$9,000 and \$128,000, respectively, of stock-based compensation expense related to restricted stock. The tax benefit available to the Company, from stock based compensation expense related to restricted stock during the three months ended March 31, 2015 and 2014 was approximately \$3,400 and \$48,500, respectively. However, since the Company has NOL's available for the next several years, these tx benefits have not been realized as of this report. As of March 31, 2015, total unrecognized stock-based compensation expense related to unvested restricted stock Awards was \$134,900.

## **8. Recent Accounting Pronouncements & Developments**

### **April 2015**

The FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs". ASU 2015-03 modifies the requirements for reporting debt issuance costs. Under the amendments in ASU 2015-03, debt issuance costs related to a recognized debt liability will be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by ASU 2015-03. ASU 2015-03 shall be applied retrospectively for periods beginning on or after December 15, 2015, and interim periods within those fiscal years, with early adoption permitted. The Company is currently evaluating the impact of its pending adoption of ASU 2015-03 on its consolidated financial statements.

### **May 2014**

The FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers," which supersedes nearly all existing revenue recognition guidance under GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing GAAP. The standard is effective for annual periods beginning after December 15, 2016, and interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures). The Company is currently evaluating the impact of its pending adoption of ASU 2014-09 on its consolidated financial statements and has not yet determined the method by which the standard will be adopted in 2017.

#### **April 2014**

The FASB issued ASU No. 2014-08, "Presentation of Financial Statements and Property, Plant and Equipment; Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity." ASU 2014-08 modifies the requirements for reporting discontinued operations. Under the amendments in ASU 2014-08, the definition of discontinued operation has been modified to only include those disposals of an entity that represent a strategic shift that has (or will have) a major effect on an entity's operations and financial results. ASU 2014-08 shall be applied prospectively for periods beginning on or after December 15, 2014, with early adoption permitted. The Company adopted ASU 2014-08 for the quarter ended March 31, 2014. The Company has adopted this standard on a prospective basis for transactions that have occurred after the adoption date. The adoption of ASU 2014-08 did not have a material effect on the Company's financial position or results of operations.

SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited) (continued)

## **9. Commitments and Contingencies**

### **Legal Matters**

The Company is a party to various legal actions and administrative proceedings arising in the normal course of business. In the opinion of Company's management, disposition of these other matters are not anticipated to have a material adverse effect on the Company or its estimated or desired assets, business, capital, cash flow, credit, expenses, financial condition, income, liabilities, liquidity, locations, marketing, operations, prospects, sales, strategies, taxation or other achievement, results or condition.

## **10. Segment Information**

The Company reports net revenues from continuing operations and operating income from continuing operations by reportable segment. Reportable segments are components of the Company for which separate financial information is available that is evaluated on a regular basis by the chief operating decision maker in deciding how to allocate resources and in assessing performance.

The Company provides similar merchandising and marketing services throughout the world, operating within two reportable segments, its Domestic Division and its International Division. The Company uses those divisions to improve its administration and operational and strategic focuses, and it tracks and reports certain financial information separately for each of those divisions. The Company measures the performance of its Domestic and International Divisions and subsidiaries using the same metrics. The primary measurement utilized by management is operating profits, historically the key indicator of long-term growth and profitability, as the Company is focused on reinvesting the operating profits of each of its international subsidiaries back into its local markets in an effort to improve market share and continued expansion efforts.



## SPAR Group, Inc. and Subsidiaries

## Notes to Consolidated Financial Statements

(unaudited) (continued)

Management evaluates performance as follows (in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2015</b>	<b>2014</b>
Revenue, net:		
United States	\$ 10,972	\$ 10,958
International	18,294	17,078
Total revenue	\$ 29,266	\$ 28,036
Operating income (loss):		
United States	\$(74 )	\$(264 )
International	423	161
Total operating income (loss)	\$ 349	\$(103 )
Interest expense:		
United States	\$ 21	\$ 20
International	37	23
Total interest expense	\$ 58	\$ 43
Other income, net:		
United States	\$(2 )	\$-
International	(27 )	(45 )
Total other income, net	\$(29 )	\$(45 )
Income (loss) before income tax expense:		
United States	\$(93 )	\$(284 )
International	413	183
Total income (loss) before income tax expense	\$ 320	\$(101 )
Income tax expense:		
United States	\$-	\$-
International	151	119
Total income tax expense	\$ 151	\$ 119
Net income (loss) from continuing operations:		
United States	\$(93 )	\$(284 )
International	262	64
Total net income (loss) from continuing operations	\$ 169	\$(220 )

Depreciation and amortization:		
United States	\$320	\$320
International	148	92
Total depreciation and amortization	\$468	\$412

Capital expenditures:		
United States	\$494	\$297
International	90	61
Total capital expenditures	\$584	\$358

Note: There were no inter-company sales for 2015 or 2014.

	<b>March 31, 2015</b>	<b>December 31, 2014</b>
Assets:		
United States	\$21,688	\$ 21,748
International	20,909	22,822
Total assets	\$42,597	\$ 44,570

SPAR Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(unaudited) (continued)

**Geographic Data** (in thousands)

	<b>Three Months Ended March 31,</b>					
	<b>2015</b>	<b>2014</b>	<b>% of</b>	<b>% of</b>		
<u>Net international revenues:</u>			consolidated	consolidated		
			<u>net revenue</u>	<u>net revenue</u>		
South Africa	\$4,891	16.7	%	\$3,871	13.8	%
Mexico	4,181	14.3		4,339	15.5	
China	3,028	10.3		1,916	6.8	
India	1,911	6.5		1,618	5.8	
Canada	1,556	5.3		1,238	4.4	
Australia	1,345	4.6		1,454	5.2	
Japan	1,201	4.1		2,095	7.5	
Turkey	181	0.6		547	2.0	
Total international revenue	\$18,294	62.4	%	\$17,078	61.0	%

	<b>March</b>	<b>December</b>
	<b>31,</b>	<b>31,</b>
	<b>2015</b>	<b>2014</b>
<u>Long lived assets:</u>		
United States	\$9,530	\$ 9,368
International	2,872	3,243
Total long lived assets	\$12,402	\$ 12,611



**SPAR Group, Inc. and Subsidiaries**

**Item Management's Discussion and Analysis of Financial Condition, Results of Operations, Liquidity and  
2. Capital Resources**

**Forward-Looking Statements**

*There are "forward-looking statements" contained in this Quarterly Report on Form 10-Q for the three months ended March 31, 2015 (this "Quarterly Report"), of SPAR Group, Inc. ("SGRP", and together with its subsidiaries, the "SPAR Group" or the "Company"), in SGRP's Annual Report on Form 10-K for the fiscal year ended December 31, 2014 (as filed, the "Annual Report"), as filed with the Securities and Exchange Commission (the "SEC") on April 15, 2015, in SGRP's definitive Proxy Statement respecting its Annual Meeting of Stockholders held on May 12, 2015 (as filed, the "Proxy Statement"), which SGRP filed with the SEC on April 20, 2015, and the Company's other filings under applicable law with the SEC (including this Quarterly Report, the Annual Report and the Proxy Statement, each a "SEC Report"). "Forward-looking statements" are defined in Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and other applicable federal and state securities laws, rules and regulations, as amended (together with the Securities Act and Exchange Act, collectively, "Securities Laws"). The Company's forward-looking statements include, in particular and without limitation, this "Management's Discussion and Analysis of Financial Condition, Results of Operations, Liquidity and Capital Resources" in this Quarterly Report, and "Business", "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report. You can identify forward-looking statements in such information by the Company's use of terms such as "may", "will", "expect", "intend", "believe", "estimate", "anticipate", "continue" or similar words or variations or negatives of those words.*

*You should carefully consider all forward-looking statements, risk factors and the other risks, cautions and information noted in this Quarterly Report, the Annual Report, the Proxy Statement and the Company's SEC Reports that could cause the Company's actual assets, business, capital, cash flow, credit, expenses, financial condition, income, liabilities, liquidity, locations, marketing, operations, prospects, sales, strategies, taxation or other achievement, results, risks or condition to differ materially from those anticipated by the Company and described in the information in the Company's forward-looking and other statements, whether express or implied, as the Company's anticipations are based upon the Company's plans, intentions, expectations and estimates and (although the Company believe them to be reasonable) involve known and unknown risks, uncertainties and other unpredictable factors (many of which are beyond the Company's control) that could cause them to fail to occur or be realized or to be materially and adversely different from those the Company anticipated.*

*Although the Company believes that its plans, intentions, expectations and estimates reflected or implied in such forward-looking statements are reasonable, the Company cannot assure you that such plans, intentions,*

*expectations or estimates will be achieved in whole or in part, that the Company has identified all potential risks, or that the Company can successfully avoid or mitigate such risks in whole or in part. You should carefully review the risk factors described below (See Item 1A – Risk Factors - in the Annual Report) and any other risks, cautions or information contained or incorporated by reference into this Annual Report or other applicable SEC Report. All forward-looking and other statements or information attributable to the Company or persons acting on its behalf are expressly subject to and qualified by all such risk factors and other risks, cautions and information.*

*You should not place undue reliance on the Company's forward-looking statements and similar information because the matters they describe are subject to known and unknown risks, uncertainties and other unpredictable factors, many of which are beyond its control. The Company's forward-looking statements, risk factors and other risks, cautions and information (whether contained in this Quarterly Report, the Annual Report, the Proxy Statement or any other applicable SEC Report) are based on the information currently available to the Company and speak only as of the date specifically referenced, or if no date is referenced, then as of December 31, 2014, in the case of this Quarterly Report, the Annual Report or the Proxy Statement or the last day of the period covered by any other applicable SEC Report. New risks and uncertainties arise from time to time, and it is impossible for the Company to predict these matters or how they may arise or affect the Company. Over time, the Company's actual assets, business, capital, cash flow, credit, expenses, financial condition, income, liabilities, liquidity, locations, marketing, operations, prospects, sales, strategies, taxation or other achievements, results, risks or condition will likely differ from those expressed or implied by the Company's forward-looking statements, and such difference could be significant and materially adverse to the Company and the value of your investment in the Company's Common Stock.*

## **SPAR Group, Inc. and Subsidiaries**

*The Company does not intend or promise, and the Company expressly disclaims any obligation, to publicly update or revise any forward-looking statements, risk factors or other risks, cautions or information (in whole or in part), whether as a result of new information, risks or uncertainties, future events or recognition or otherwise, except as and to the extent required by applicable law.*

### **GENERAL**

SPAR Group, Inc. ("SGRP"), and its subsidiaries (together with SGRP, the "SPAR Group" or the "Company"), is a diversified international merchandising and marketing services company and provides a broad array of services worldwide to help companies improve their sales, operating efficiency and profits at retail locations. The Company provides its merchandising and other marketing services to manufacturers, distributors and retailers worldwide, primarily in mass merchandisers, office supply, grocery, drug store, independent, convenience, toy, home improvement and electronics stores. The Company also provides furniture and other product assembly services in stores, homes and offices. The Company has supplied these services in the United States since certain of its predecessors were formed in 1979 and internationally since the Company acquired its first international subsidiary in Japan in May of 2001. The Company currently does business in 9 countries that encompass approximately 50% of the total world population through its operations in the United States, Canada, Japan, South Africa, India, China, Australia, Mexico and Turkey.

Merchandising services primarily consist of regularly scheduled, special project and other product services provided at store level, and the Company may be engaged by either the retailer or the manufacturer. Those services may include restocking and adding new products, removing spoiled or outdated products, resetting categories "on the shelf" in accordance with client or store schematics, confirming and replacing shelf tags, setting new sale or promotional product displays and advertising, replenishing kiosks, demonstrating or promoting a product, providing on-site audit and in-store event staffing services and providing product assembly services in stores, homes and offices. Other merchandising services include whole store or departmental product sets or resets, including new store openings, new product launches and in-store demonstrations, special seasonal or promotional merchandising, focused product support and product recalls. The Company continues to seek to expand its merchandising, assembly and marketing services business throughout the world.

### **An Overview of the Merchandising and Marketing Services Industry**

According to industry estimates over two billion dollars are spent annually in the United States alone on retail merchandising and marketing services. The merchandising and marketing services industry includes manufacturers,

retailers, brokers, distributors and professional service merchandising companies. The Company believes that merchandising and marketing services add value to retailers, manufacturers and other businesses and enhance sales by making a product more visible and more available to consumers. These services primarily involve placing orders, shelf maintenance, display placement, reconfiguring products on store shelves and replenishing product inventory.

Historically, retailers staffed their stores as needed to provide these services to ensure, that manufacturers' inventory levels, the advantageous display of new items on shelves, and the maintenance of shelf schematics and product placement were properly merchandised. However retailers, in an effort to improve their margins, have decreased their own store personnel and increased their reliance on manufacturers to perform such services. Initially, manufacturers attempted to satisfy the need for merchandising and marketing services in retail stores by utilizing their own sales representatives. Additionally, retailers also used their own employees to merchandise their stores to satisfy their own merchandising needs. However, both the manufacturers and the retailers discovered that using their own sales representatives and employees for this purpose was expensive and inefficient.

Most manufacturers and retailers have been, and SPAR Group believes they will continue outsourcing their merchandising and marketing service needs to third parties capable of operating at a lower cost by (among other things) serving multiple manufacturers simultaneously. The Company also believes that it is well positioned, as a domestic and international merchandising and marketing services company, to more effectively provide these services to retailers, manufacturers and other businesses around the world.

## **SPAR Group, Inc. and Subsidiaries**

Another significant trend impacting the merchandising and marketing services business is the tendency of consumers to make product purchase decisions once inside the store. Accordingly, merchandising and marketing services and in-store product promotions have proliferated and diversified. Retailers are continually re-merchandising and re-modeling entire stores in an effort to respond to new product developments and changes in consumer preferences. We estimate that these activities have increased in frequency over the last five years. Both retailers and manufacturers are seeking third parties to help them meet the increased demand for these labor-intensive services.

In addition, the consolidation of many retailers has created opportunities for third party merchandisers when an acquired retailer's stores are converted to the look and format of the acquiring retailer. In many cases, stores are completely remodeled and re-merchandised after a consolidation.

SPAR Group believes the current trend in business toward globalization fits well with its expansion model. As companies expand into foreign markets they will need assistance in merchandising or marketing their products. As evidenced in the United States, retailer and manufacturer sponsored merchandising and marketing programs are both expensive and inefficient. The Company also believes that the difficulties encountered by these programs are only exacerbated by the logistics of operating in foreign markets. This environment has created an opportunity for the Company to exploit its Internet, hand-held computers, tablets and smart phone based technology and business model worldwide.

### ***The Company's Domestic and International Geographic Segments:***

The Company provides similar merchandising and marketing services throughout the world, operating within two reportable segments, its Domestic and International Divisions. The Company tracks and reports certain financial information separately for these two segments using the same metrics. The primary measurement utilized by management is operating profit level, historically the key indicator of long-term growth and profitability, as the Company is focused on reinvesting the operating profits of each of its international subsidiaries back into local markets in an effort to improve its market share and continued expansion efforts. Certain financial information regarding each of the Company's two segments, which includes their respective net revenues and operating income for each of the three months ended March 31, 2015 and 2014, and their respective assets as of March 31, 2015 and 2014, is provided above in Note 10 to the Company's Consolidated Financial Statements – *Segment Information*.

The Company's international business in each territory outside the United States is conducted through a foreign subsidiary incorporated in its primary territory. The primary territory establishment date (which may include predecessors), the percentage of the Company's equity ownership, and the principal office location for its US

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(domestic) subsidiaries and each of its foreign (international) subsidiaries is as follows:

	Date	SGRP Percentage	
<u>Primary Territory</u>	<u>Established</u>	<u>Ownership</u>	<u>Principal Office Location</u>
United States of America	1979	100%	White Plains, New York, United States of America <sup>6</sup>
Japan	May 2001	100%	Tokyo, Japan
Canada	June 2003	100%	Toronto, Canada
South Africa	April 2004	51% <sup>1</sup>	Durban, South Africa
India	April 2004	51% <sup>2</sup>	New Delhi, India
Australia	April 2006	51%	Melbourne, Australia
Romania	July 2009	100% <sup>3</sup>	Bucharest, Romania
China	March 2010	51% <sup>4</sup>	Shanghai, China
Mexico	August 2011	51%	Mexico City, Mexico
Turkey	November 2011	51% <sup>5</sup>	Istanbul, Turkey

1 In September 2012, the Company, through its subsidiary in South Africa (SGRP Meridian), entered into a joint venture agreement to expand its operations in South Africa. SGRP Meridian owns a 51% ownership interest in the new company; CMR Meridian (Pty) Ltd. ("CMR-Meridian"). (See Note 5 to the Consolidated Financial Statements – *Related-Party Transactions*).

2 In June 2011, the Company sold 49% of its interest in its Indian subsidiary to KROGNOS Integrated Marketing Services Private Limited. In March 2013, the Company purchased a 51% interest in a new subsidiary in India, Preceptor Marketing Services Private Limited, which began operations in March 2013.

3 In August 2013, the Company sold its 51% ownership in its active Romania subsidiary to SPAR InfoTech, Inc. (See Note 5 to the Consolidated Financial Statements – *Related-Party Transactions*). The Company continues to have one Romanian subsidiary that is 100% owned and is inactive.

4 Currently the Company owns two subsidiaries in China. One subsidiary is 100% owned and is inactive, and the second subsidiary, acquired in March 2010 and operational in August 2010, is 51% owned. In July 2011, the Company, through its active subsidiary in China (SPAR Shanghai), entered into a joint venture agreement to expand its operations in China. SPAR Shanghai has a 75.5% ownership interest in the new company; SPAR DSI Human Resource Company. In August 2014, the Company, through its subsidiary in Hong Kong, SPAR China Ltd., purchased certain business assets, fixed assets and merchandising teams of three companies in China (collectively Unilink). As consideration for the purchase, Unilink is paid in cash and 20% ownership in SPAR Shanghai, leaving SPAR with a 51% ownership interest in SPAR Shanghai.

5 In November 2011, the Company started a new 51% owned subsidiary to compete in this important market. (See Note 5 to the Consolidated Financial Statements – *Related-Party Transactions*).

6 In September 2012, the Company established a new subsidiary, National Merchandising Services, LLC, ("NMS") 61% owned by the Company, with its principal office in Georgia. In March 2013, the Company purchased general merchandising service and certain in-store audit service businesses from Market Force Information, Inc. ("MFI").

## Critical Accounting Policies

There were no material changes during the three months ended March 31, 2015, to the Company's critical accounting policies as reported in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2014, as filed with the SEC on April 15, 2015.

## Results of Operations

### **Three months ended March 31, 2015, compared to three months ended March 31, 2014**

The following table sets forth selected financial data and data as a percentage of net revenues for the periods indicated (in thousands, except percent data).

	Three Months Ended March 31,			
	2015		2014	
	\$	%	\$	%
Net revenues	\$29,266	100.0%	\$28,036	100.0%
Cost of revenues	22,353	76.4	21,806	77.8
Gross profit	6,913	23.6	6,230	22.2
Selling, general & administrative expense	6,096	20.8	5,921	21.1
Depreciation & amortization	468	1.6	412	1.5
Operating income (loss)	349	1.2	(103 )	(0.4 )
Interest expense, net	58	0.2	43	0.2
Other income, net	(29 )	(0.1 )	(45 )	(0.2 )
Income (loss) before income taxes	320	1.1	(101 )	(0.4 )
Income tax expense	151	0.5	119	0.4
Net income (loss)	169	0.6	(220 )	(0.8 )
Net income attributable to non-controlling interest	243	0.8	149	0.5
Net income (loss) attributable to Spar Group, Inc.	\$(74 )	(0.2 )%	\$(369 )	(1.3 )%



## **SPAR Group, Inc. and Subsidiaries**

### **Net Revenues**

Net revenues for the three months ended March 31, 2015, were \$29.3 million, compared to \$28.0 million for the three months ended March 31, 2014, an increase of \$1.3 million or 4.4%.

Domestic net revenues totaled \$11.0 million in the three months ended March 31, 2015, compared to \$10.9 million for the same period in 2014.

International net revenues totaled \$18.3 million for the three months ended March 31, 2015, compared to \$17.1 million for the same period in 2014, an increase of \$1.2 million or 7.1%. The increase in net revenues was primarily due to incremental revenue from the integration of the acquisition in China and increased revenue in South Africa, Canada, and India, partially offset by lower revenue in Japan, Mexico, Australia and Turkey. Foreign currency had a \$4.8 million or 26.2% negative impact.

### **Cost of Revenues**

The Company's cost of revenues consists of its on-site labor and field administration fees, travel and other direct labor-related expenses and was 76.4% of its net revenues for the three months ended March 31, 2015, and 77.8% of its net revenues for the three months ended March 31, 2014.

Domestic cost of revenues was 69.2% of net revenues for the three months ended March 31, 2015, and 72.2% of net revenues for the three months ended March 31, 2014. The decrease in cost of revenues as a percentage of net revenues of 3 percentage points was due primarily to a favorable mix of project work compared to last year. For the three months ended March 31, 2015 and 2014, approximately 87% and 84%, respectively, of the Company's domestic cost of revenues resulted from in-store merchandiser specialist, on-site assembly technician and field administration services purchased from certain of the Company's affiliates, SPAR Business Services, Inc. ("SBS"), and SPAR Administrative Services, Inc. ("SAS"), respectively, and approximately 4% and 8% of the Company's domestic cost of revenues for the three months ended March 31, 2015 and 2014, respectively, resulted from in-store merchandiser specialist services purchased from certain of the Company's other affiliates, National Retail Source, LLC ("NRS"), and prior to August 1, 2013, National Merchandising of America, Inc. ("NMA") (See Note 5 to the Consolidated Financial Statements - *Related-Party Transactions*).

Internationally, the cost of revenues decreased to 80.7% of net revenues for the three months ended March 31, 2015, compared to 81.3% of net revenues for the three months ended March 31, 2014. The cost of revenue percentage decrease of 0.6% was primarily due to lower cost margin business in South Africa, Japan, and Turkey partially offset by higher cost margin business in Mexico and India.

### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses of the Company include its corporate overhead, project management, information technology, executive compensation, human resources, legal and accounting expenses. Selling, general and administrative expenses were approximately \$6.1 million and \$5.9 million for the three months ended March 31, 2015 and 2014, respectively.

Domestic selling, general and administrative expenses totaled \$3.1 million for three months ended March 31, 2015, compared to \$3.0 million for the three months ended March 31, 2014. The increase of \$100,000 was primarily due to salaries and related costs.

International selling, general and administrative expenses totaled \$3.0 million for the three months ended March 31, 2015, compared to \$2.9 million for the same period in 2014. The increase of approximately \$100,000 was primarily attributable to an increase in South Africa and the acquisition in China, partially offset by decreases in Japan, Mexico, Canada, and Australia.

## **SPAR Group, Inc. and Subsidiaries**

### **Depreciation and Amortization**

Depreciation and amortization charges totaled \$468,000 for the three months ended March 31, 2015, and \$412,000 for the same period in 2014.

### **Interest Expense**

The Company's net interest expense was \$58,000 and \$43,000 for the three months ended March 31, 2015 and 2014, respectively.

### **Other Income**

Other income totaled \$29,000 and \$45,000 for the three months ended March 31, 2015 and 2014, respectively.

### **Income Taxes**

The income tax provision totaled \$151,000 for the three months ended March 31, 2015 and \$119,000 for the three months ended March 31, 2014.

### **Non-controlling Interest**

Net operating profits from the non-controlling interest, from the Company's 51% owned subsidiaries, resulted in a reduction of net income of \$243,000 and \$149,000 for the three months ended March 31, 2015 and 2014, respectively.

## Net Loss

The Company reported net loss of \$74,000 for the three months ended March 31, 2015, or \$0.00 per diluted share, compared to a net loss of \$369,000, or \$0.02 per diluted share, for the corresponding period last year.

## Liquidity and Capital Resources

In the three months ended March 31, 2015, the Company had a net income before non-controlling interest of \$169,000.

Net cash provided by operating activities was \$1.4 million and \$2.5 million for the three months ended March 31, 2015 and 2014, respectively. The net cash provided by operating activities was primarily due to a decrease in accounts receivable and prepaid expenses, partially offset by a decrease in accounts payable and accrued expenses.

Net cash used in investing activities for the three months ended March 31, 2015, and March 31, 2014, was approximately \$600,000 and \$400,000, respectively. The net cash used in investing activities in 2015 was due to fixed asset additions.

Net cash used in financing activities for the three months ended March 31, 2015, and March 31, 2014, was approximately \$400,000 and \$700,000, respectively. Net cash used in financing activities was primarily a result of payments on lines of credit.

The above activity resulted in a decrease in cash and cash equivalents for the three months ended March 31, 2015 of \$90,000.

At March 31, 2015, the Company had net working capital of \$15.8 million, as compared to net working capital of \$16.5 million at December 31, 2014. The Company's current ratio was 2.1 at both March 31, 2015 and December 31, 2014.

**SPAR Group, Inc. and Subsidiaries****Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The Company's accounting policies for financial instruments and disclosures relating to financial instruments require that the Company's consolidated balance sheets include the following financial instruments: cash and cash equivalents, accounts receivable, accounts payable and lines of credit. The Company carries current assets and liabilities at their stated or face amounts in its consolidated financial statements, as the Company believes those amounts approximate the fair value for these items because of the relatively short period of time between origination of the asset or liability and their expected realization or payment. The Company monitors the risks associated with asset and liability positions, as well as interest rates. The Company's investment policy objectives require the preservation and safety of the principal, and the maximization of the return on investment based upon its safety and liquidity objectives.

The Company is exposed to market risk related to the variable interest rate on its lines of credit, both in its United States subsidiaries (*i.e.*, the Domestic Division) and in its International (non-U.S.) subsidiaries (*i.e.*, the International Division). At March 31, 2015, the Company's outstanding lines of credit and other debt totaled approximately \$6.1 million, as noted in the table below (in thousands):

Location	Variable Interest Rate <sup>(1)</sup>	US Dollars <sup>(2)</sup>
United States	2.8%	\$ 5,354
International	0.1%-7.2%	725
		\$ 6,079

(1)Based on interest rate at March 31, 2015.

(2)Based on exchange rate at March 31, 2015.

The Company has foreign currency exposure associated with its international subsidiaries. In both 2015 and 2014, these exposures are primarily concentrated in the South African Rand, the Canadian Dollar, the Mexican Peso, the Australian Dollar and the Japanese Yen.

**Item 4. Controls and Procedures****Management's Report on Internal Control Over Financial Reporting**

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting for the registrant, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Management has designed such internal control over financial reporting by the Company to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles in the United States of America.

The Company's management has evaluated the effectiveness of the Company's internal control over financial reporting using the "Internal Control – Integrated Framework (1992)" created by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") framework. Based on this evaluation, management has concluded that internal controls over financial reporting were effective as of March 31, 2015.

### **Management's Evaluation of Disclosure Controls and Procedures**

The Company's chief executive officer and chief financial officer have each reviewed and evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this report, as required by Exchange Act Rules 13a-15(b) and Rule 15d-15(b). Based on that evaluation, the chief executive officer and chief financial officer have each concluded that the Company's current disclosure controls and procedures are effective to insure that the information required to be disclosed by the Company in reports it files, or submits under the Exchange Act were recorded, processed, summarized and reported within the time period specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

**SPAR Group, Inc. and Subsidiaries**

**Changes in Internal Controls Over Financial Reporting**

There have been no changes in the Company's internal controls over financial reporting that occurred during the Company's first quarter of its 2015 fiscal year that materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

**SPAR Group, Inc. and Subsidiaries**

**PART II: OTHER INFORMATION**

**Item 1. Legal Proceedings**

The Company is a party to various legal actions and administrative proceedings arising in the normal course of business. See Note 9 to Consolidated Financial Statements – *Commitments and Contingencies*.

**Item 1A. Risk Factors**

*Existing Risk Factors*

Various risk factors applicable to the Company and its businesses are described in Item 1A under the caption "Risk Factors" in SGRP's Annual Report on Form 10-K for the fiscal year ended December 31, 2014, as filed with the Securities and Exchange Commission (the "SEC") on April 15, 2015 (the "2014 Annual Report"), which risk factors are incorporated by reference into this Quarterly Report. There have been no material changes in the Company's risk factors since those reports.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

Item 2(a): Not applicable

Item 2(b): Not applicable

Item 2(c): Not applicable

**Item 3. Defaults upon Senior Securities**



Item 3(a): Defaults under Indebtedness: None.

Item 3(b): Defaults under Preferred Stock: None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

Not applicable.

**Item 6. Exhibits**

10.1 Sixth Agreement of Amendment to Revolving Loan and Security Agreement And Other Documents, dated and effective as of July 1, 2014, by and among Sterling National Bank, as "Lender" and "Agent", and SPAR Group, Inc., National Assembly Services, Inc., SPAR Group International, Inc., SPAR Acquisition, Inc., SPAR Trademarks, Inc., SPAR Marketing Force, Inc., SPAR Canada, Inc., and SPAR Canada Company, each as a "Borrower" under such loan agreement as of such amendment date (as filed herewith).

10.2 Amended and Restated Secured Revolving Loan Note dated as of July 1, 2014, in the original maximum principal amount of \$7,500,000 issued to Sterling National Bank by SPAR Group, Inc., National Assembly Services, Inc., SPAR Group International, Inc., SPAR Acquisition, Inc., SPAR Trademarks, Inc., SPAR Marketing Force, Inc., SPAR Canada, Inc., and SPAR Canada Company, each as a "Borrower" under such note, pursuant to (and governed by) the Sterling Loan Agreement as amended (as filed herewith).

31.1 Certification of the CEO pursuant to 18 U.S.C. Section 1350 adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, as filed herewith.

31.2 Certification of the CFO pursuant to 18 U.S.C. Section 1350 adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, as filed herewith.

32.1 Certification of the CEO pursuant to 18 U.S.C. Section 1350 adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, as filed herewith.

32.2 Certification of the CFO pursuant to 18 U.S.C. Section 1350 adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, as filed herewith.

101.INS\* XBRL Instance

101.SCH\* XBRL Taxonomy Extension Schema

101.CAL\* XBRL Taxonomy Extension Calculation

101.DEF\* XBRL Taxonomy Extension Definition

101.LAB\* XBRL Taxonomy Extension Labels

101.PRE\* XBRL Taxonomy Extension Presentation

\* XBRL information is furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

**SPAR Group, Inc. and Subsidiaries**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: May 14, 2015 SPAR Group, Inc., Registrant

By: /s/ James R. Segreto  
James R. Segreto  
Chief Financial Officer, Treasurer, Secretary  
and duly authorized signatory