ERESEARCHTECHNOLOGY INC /DE/
Form 10-Q
August 04, 2005

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 quarterly period ended June 30, 2005.

or

Transitional report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the transitional period from_________________ to_________________

Commission file number 0-29100

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

Delaware	22-3264604
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
30 South 17th Street Philadelphia, PA	19103
(Address of principal executive offices)	(Zip Code)

215-972-0420
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports, and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).
Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

The number of shares of Common Stock, $.01 par value, outstanding as of July 29, 2005, was 50,363,767.

Back to Contents

eResearchTechnology, Inc. and Subsidiaries

INDEX

Back to Contents

Part 1. Financial Information
Item 1. Consolidated Financial Statements

eResearchTechnology, Inc. and Subsidiaries
Consolidated Balance Sheets
(In thousands of dollars, except per share amounts)

	December 31, 2004	June 30, 2005
		(unaudited)
Assets		
Current Assets:		
Cash and cash equivalents	$ 45,806	$ 40,661
Short-term investments	22,942	33,217
Accounts receivable, net	14,798	11,055
Prepaid expenses and other	3,522	6,872
Deferred income taxes	323	323
Total current assets	87,391	92,128
Property and equipment, net	25,204	25,882
Goodwill	1,212	1,212
Other assets	782	485
Deferred income taxes	1,936	962
Total assets	$ 116,525	$ 120,669
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable	$ 2,455	$ 3,000
Accrued expenses	4,318	4,162
Income taxes payable	2,147	687
Current portion of capital lease obligations	233	141
Deferred revenues	20,325	20,742
Total current liabilities	29,478	28,732
Capital lease obligations, excluding current portion	193	124
Commitments and contingencies		
Stockholders' Equity:		
Preferred stock $10.00 par value, 500,000 shares authorized, none issued and outstanding		
Common stock $.01 par value, 175,000,000 shares authorized, 56,396,696 and 56,619,865 shares issued, respectively	564	566

Additional paid-in capital	69,694	71,402
Accumulated other comprehensive income	1,601	1,055
Retained earnings	46,550	52,588
Treasury stock, 6,067,519 and 6,267,519 shares at cost, respectively	(31,555)	(33,798)
Total stockholders' equity	86,854	91,813
Total liabilities and stockholders' equity	$ 116,525	$ 120,669

The accompanying notes are an integral part of these statements.

Back to Contents

eResearchTechnology, Inc. and Subsidiaries
Consolidated Statements of Operations
(In thousands, except per share amounts)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2005	2004	2005
Net revenues:				
Licenses	$ 2,670	$ 1,746	$ 5,123	$ 3,409
Services	20,308	11,245	38,318	27,147
Site support	5,186	4,586	10,815	9,935
Total net revenues	28,164	17,577	54,256	40,491
Costs of revenues:				
Cost of licenses	231	104	353	237
Cost of services	6,081	5,576	12,066	12,066
Cost of site support	2,582	3,148	4,945	6,331
Total costs of revenues	8,894	8,828	17,364	18,634
Gross margin	19,270	8,749	36,892	21,857
Operating expenses:				
Selling and marketing	2,364	2,107	4,817	4,445
General and administrative	2,350	2,639	4,500	5,535
Research and development	1,042	903	2,015	1,894
Total operating expenses	5,756	5,649	11,332	11,874
Operating income	13,514	3,100	25,560	9,983
Other income, net	84	170	192	165
Income before income taxes	13,598	3,270	25,752	10,148
Income tax provision	5,466	1,304	10,352	4,110
Net income	$ 8,132	$ 1,966	$ 15,400	$ 6,038
Basic net income per share	$ 0.16	$ 0.04	$ 0.30	$ 0.12
Diluted net income per share	$ 0.15	$ 0.04	$ 0.28	$ 0.11
Shares used to calculate basic net income per share	51,579	50,388	51,256	50,379
Shares used to calculate diluted net income per share	55,571	53,133	55,488	53,229

The accompanying notes are an integral part of these statements.

Back to Contents

eResearchTechnology, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
(In thousands of dollars)
(unaudited)

	Six Months Ended June 30,	
	2004	**2005**
Operating activities:		
Net income	$ 15,400	$ 6,038
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,143	5,209
Cost of sale of equipment	—	281
Provision for uncollectible accounts	84	89
Stock option income tax benefits	9,954	993
Investment impairment charge	—	284
Changes in operating assets and liabilities:		
Accounts receivable	(3,716)	3,552
Prepaid expenses and other	(1,577)	(3,026)
Accounts payable	290	569
Accrued expenses	(348)	(211)
Income taxes	(1,089)	(486)
Deferred revenues	7,010	524
Net cash provided by operating activities	30,151	13,816
Investing activities:		
Purchases of property and equipment	(7,313)	(6,726)
Purchases of short-term investments	(17,552)	(23,025)
Proceeds from sales of short-term investments	9,723	12,750
Net cash used in investing activities	(15,142)	(17,001)
Financing activities:		
Repayment of capital lease obligations	(324)	(161)
Proceeds from exercise of stock options	2,681	722
Repurchase of common stock for treasury	—	(2,243)
Net cash provided by (used in) financing activities	2,357	(1,682)
Effect of exchange rate changes on cash	42	(278)
Net increase (decrease) in cash and cash equivalents	17,408	(5,145)
Cash and cash equivalents, beginning of period	38,364	45,806

Cash and cash equivalents, end of period	$ 55,772	$ 40,661

The accompanying notes are an integral part of these statements.

Back to Contents

eResearchTechnology, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements, which include the accounts of eResearchTechnology, Inc. (the “Company” or “we”) and its wholly owned subsidiaries, have been prepared in accordance with generally accepted accounting principles 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 the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the six month period ended June 30, 2005 are not necessarily indicative of the results that may be expected for the year ending December 31, 2005. Further information on potential factors that could affect our financial results can be found in our Report on Form 10-K for the year ended December 31, 2004 filed with the Securities and Exchange Commission and in this Form 10-Q.

Note 2. Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenses during the reporting period. Actual results could differ from those estimates.

Property and Equipment

Pursuant to Statement of Position 98-1, “Accounting for the Costs of Computer Software Developed or Obtained for Internal Use,” we capitalize costs associated with internally developed and/or purchased software systems for new products and enhancements to existing products that have reached the application development stage and meet recoverability tests. These costs are included in property and equipment. Capitalized costs include external direct costs of materials and services utilized in developing or obtaining internal-use software, and payroll and payroll-related expenses for employees who are directly associated with and devote time to the internal-use software project.

Amortization of capitalized software development costs is charged to cost of revenues. Amortization of capitalized software development costs was $597,000 and $304,000 for the three months ended June 30, 2004 and 2005, respectively, and $1,178,000 and $674,000 for the six months ended June 30, 2004 and 2005, respectively. For the six months ended June 30, 2004 and 2005, we capitalized $1,039,000 and $1,650,000, respectively, of software development costs related to labor and consulting, and $1,139,000 and $0, respectively, of software development costs related to direct costs of materials. As of June 30, 2005, $4,708,000 of capitalized costs have not yet been placed in service and are therefore not being amortized.

Long-lived Assets

In accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets,” when events or circumstances so indicate, we assess the potential impairment of our long-lived assets based on anticipated undiscounted cash flows from the assets. Such events and circumstances include a sale of all or a significant part of the operations associated with the long-lived asset, or a significant decline in the operating performance of the asset. If an impairment is indicated, the amount of the impairment charge would be calculated by comparing the anticipated discounted future cash flows to the carrying value of the long-lived asset. At June 30, 2005, no impairment was indicated.

Back to Contents

Software Development Costs

Research and development expenditures are charged to operations as incurred. SFAS No. 86, “Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed,” requires the capitalization of certain software development costs subsequent to the establishment of technological feasibility. Since software development costs have not been significant after the establishment of technological feasibility, all such costs have been charged to expense as incurred.

Stock-Based Compensation

In December 2002, SFAS No. 148, “Accounting for Stock-Based Compensation — Transition and Disclosure,” was issued. SFAS No. 148 amended SFAS No. 123, “Accounting for Stock-Based Compensation,” to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amended the disclosure requirements of SFAS No. 123.

SFAS No. 123, as amended by SFAS No. 148, permits companies to (i) recognize as expense the fair value of stock-based awards, or (ii) continue to apply the provisions of Accounting Principles Board (APB) Opinion No. 25, “Accounting for Stock Issued to Employees” and related interpretations, and provide pro forma net income and earnings per share disclosures for employee stock option grants as if the fair value based method defined in SFAS No. 123 had been applied. We continue to apply the provisions of APB Opinion No. 25 and provide the pro forma disclosures in accordance with the provisions of SFAS Nos. 123 and 148. Under APB Opinion No. 25, we have not recorded any stock-based employee compensation cost associated with our stock option plans, as all options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS No. 123 to our stock option plans (in thousands, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2005	2004	2005
Net income, as reported	$ 8,132	$ 1,966	$ 15,400	$ 6,038
Deduct: Net stock-based employee compensation expense determined under fair value based method, net of related tax effects	(1,210)	(846)	(1,915)	(1,528)
Pro forma net income	$ 6,922	$ 1,120	$ 13,485	$ 4,510
Earnings per share:				
Basic — as reported	$ 0.16	$ 0.04	$ 0.30	$ 0.12
Basic — pro forma	$ 0.13	$ 0.02	$ 0.26	$ 0.09
Diluted — as reported	$ 0.15	$ 0.04	$ 0.28	$ 0.11
Diluted — pro forma	$ 0.12	$ 0.02	$ 0.24	$ 0.08

Pro forma net income reflects only options granted through June 30, 2005 and, therefore, may not be representative of the effect for future periods.

Back to Contents

Stock Splits

On May 27, 2004, we effected a 3-for-2 split of our common stock. All share and per share data have been restated to reflect this split of our common stock as if the stock split had occurred as of December 31, 2003.

Note 3. Net Income per Common Share

Basic net income per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted net income per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the period, adjusted for the dilutive effect of common stock equivalents, which consist of stock options. The dilutive effect of stock options is calculated using the treasury stock method.

The tables below set forth the reconciliation of the numerators and denominators of the basic and diluted net income per share computations (in thousands, except per share amounts):

Three Months Ended June 30,

2004	Net Income	Shares	Per Share Amount
Basic net income	$ 8,132	51,579	$ 0.16
Effect of dilutive shares	—	3,992	(0.01)