

BARRETT BUSINESS SERVICES INC
Form 10-Q
August 09, 2011

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

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2011

Commission File No. 0-21886

BARRETT BUSINESS SERVICES, INC.

(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of
incorporation or organization)

52-0812977
(IRS Employer
Identification No.)

98662

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8100 NE Parkway Drive, Suite 200
Vancouver, Washington
(Address of principal executive offices)

(Zip Code)

(360) 828-0700

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 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 (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer Accelerated filer Non-accelerated filer 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

Number of shares of common stock, \$.01 par value, outstanding at July 29, 2011 was 10,129,399 shares.

BARRETT BUSINESS SERVICES, INC.

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Part I Financial Information

Item 1. Financial Statements

BARRETT BUSINESS SERVICES, INC.

Consolidated Balance Sheets

(Unaudited)

(In thousands, except per share amounts)

| | June 30, 2011 | December 31, 2010 |
|--|-------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 25,472 | \$ 30,924 |
| Marketable securities | 34,707 | 24,511 |
| Trade accounts receivable, net | 59,738 | 37,596 |
| Income taxes receivable | 2,356 | 2,356 |
| Prepaid expenses and other | 2,426 | 1,798 |
| Deferred income taxes | 5,810 | 6,101 |
| Total current assets | 130,509 | 103,286 |
| Marketable securities | 10,007 | 5,921 |
| Property, equipment and software, net | 14,819 | 15,037 |
| Restricted marketable securities and workers' compensation deposits | 9,430 | 8,811 |
| Other assets | 3,100 | 3,094 |
| Workers' compensation receivables for insured losses and recoveries | 3,800 | 3,915 |
| Goodwill, net | 47,820 | 47,820 |
| | \$ 219,485 | \$ 187,884 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 694 | \$ 964 |
| Accrued payroll, payroll taxes and related benefits | 60,355 | 37,525 |
| Income taxes payable | 498 | 0 |
| Other accrued liabilities | 806 | 442 |
| Workers' compensation claims liabilities | 14,850 | 14,768 |
| Safety incentives liability | 5,057 | 5,024 |
| Total current liabilities | 82,260 | 58,723 |
| Long-term workers' compensation claims liabilities | 23,504 | 21,847 |
| Long-term workers' compensation claims liabilities for insured claims | 2,642 | 2,686 |
| Deferred income taxes | 7,841 | 7,841 |
| Customer deposits and other long-term liabilities | 1,393 | 1,422 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Preferred stock, \$.01 par value; 500 shares authorized; no shares issued and outstanding | 0 | 0 |
| Common stock, \$.01 par value; 20,500 shares authorized, 10,140 and 10,202 shares issued and outstanding | 101 | 102 |
| Additional paid-in capital | 24,452 | 25,164 |
| Accumulated other comprehensive loss | (30) | (65) |
| Retained earnings | 77,322 | 70,164 |

| | | |
|--|---------|--------|
| | 101,845 | 95,365 |
|--|---------|--------|

| | | |
|--|------------|------------|
| | \$ 219,485 | \$ 187,884 |
|--|------------|------------|

The accompanying notes are an integral part of these financial statements

BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Operations

(Unaudited)

(In thousands, except per share amounts)

| | Three Months Ended June 30, | |
|---|--------------------------------|--|
| | 2011 | 2010 |
| | | As Restated, See Note 1 to Consolidated Financial Statements |
| Revenues: | | |
| Staffing services | \$ 30,518 | \$ 31,975 |
| Professional employer service fees | 45,495 | 35,457 |
| Total revenues | 76,013 | 67,432 |
| Cost of revenues: | | |
| Direct payroll costs | 23,093 | 24,237 |
| Payroll taxes and benefits | 28,886 | 22,861 |
| Workers compensation | 10,753 | 8,602 |
| Total cost of revenues | 62,732 | 55,700 |
| Gross margin | 13,281 | 11,732 |
| Selling, general and administrative expenses | 8,871 | 8,407 |
| Depreciation and amortization | 331 | 333 |
| Income from operations | 4,079 | 2,992 |
| Other income: | | |
| Investment income, net | 273 | 217 |
| Other | (7) | 163 |
| Other income | 266 | 380 |
| Income before income taxes | 4,345 | 3,372 |
| Provision for income taxes | 896 | 1,113 |
| Net income | \$ 3,449 | \$ 2,259 |
| Basic earnings per share | \$.34 | \$.22 |
| Weighted average number of basic shares outstanding | 10,196 | 10,446 |
| Diluted earnings per share | \$.34 | \$.22 |
| Weighted average number of diluted shares outstanding | 10,245 | 10,485 |

BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Operations

(Unaudited)

(In thousands, except per share amounts)

| | Six Months Ended June 30, | |
|--|------------------------------|--|
| | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements |
| Revenues: | | |
| Staffing services | \$ 58,850 | \$ 59,037 |
| Professional employer service fees | 85,932 | 66,655 |
| Total revenues | 144,782 | 125,692 |
| Cost of revenues: | | |
| Direct payroll costs | 44,541 | 44,673 |
| Payroll taxes and benefits | 60,649 | 47,489 |
| Workers compensation | 20,713 | 16,433 |
| Total cost of revenues | 125,903 | 108,595 |
| Gross margin | 18,879 | 17,097 |
| Selling, general and administrative expenses | 17,698 | 16,631 |
| Depreciation and amortization | 666 | 710 |
| Income (loss) from operations | 515 | (244) |
| Other income: | | |
| Life insurance proceeds | 10,000 | 0 |
| Investment income, net | 628 | 401 |
| Other | 92 | 264 |
| Other income | 10,720 | 665 |
| Income before income taxes | 11,235 | 421 |
| Provision for (benefit from) income taxes | 2,240 | (135) |
| Net income | \$ 8,995 | \$ 556 |
| Basic earnings per share | \$.88 | \$.05 |
| Weighted average number of basic shares outstanding | 10,198 | 10,456 |
| Diluted earnings per share | \$.88 | \$.05 |
| Weighted average number of diluted shares outstanding | 10,246 | 10,490 |

BARRETT BUSINESS SERVICES, INC.

Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

| | Six Months Ended June 30, | |
|---|------------------------------|--|
| | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements |
| Cash flows from operating activities: | | |
| Net income | \$ 8,995 | \$ 556 |
| Reconciliations of net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 666 | 710 |
| Gains recognized on marketable securities | (100) | (207) |
| Gain recognized on sale and leaseback | (61) | (61) |
| Deferred income taxes | 292 | (25) |
| Share based compensation | 192 | 84 |
| Changes in certain assets and liabilities, net of amounts purchased in acquisitions: | | |
| Trade accounts receivable, net | (22,142) | (17,231) |
| Income taxes receivable | 0 | 275 |
| Prepaid expenses and other | (628) | (1,286) |
| Accounts payable | (270) | (415) |
| Accrued payroll, payroll taxes and related benefits | 22,830 | 17,609 |
| Other accrued liabilities | 364 | 25 |
| Income taxes payable | 498 | 0 |
| Workers compensation claims liabilities | 1,810 | 1,727 |
| Safety incentives liability | 33 | (196) |
| Customer deposits, long-term liabilities and other assets, net | 23 | 19 |
| Net cash provided by operating activities | 12,502 | 1,584 |
| Cash flows from investing activities: | | |
| Cash paid for acquisitions | 0 | (375) |
| Purchase of property and equipment, net of amounts purchased in acquisitions | (445) | (754) |
| Proceeds from sales and maturities of marketable securities | 18,562 | 6,741 |
| Purchase of marketable securities | (32,710) | (19,694) |
| Proceeds from maturities of restricted marketable securities | 3,360 | 1,421 |
| Purchase of restricted marketable securities | (3,979) | (4,376) |
| Net cash used in investing activities | (15,212) | (17,037) |
| Cash flows from financing activities: | | |
| Proceeds from exercise of stock options | 5 | 0 |
| Dividends paid | (1,837) | (1,674) |
| Repurchase of common stock | (923) | (2,100) |
| Tax benefit of stock option exercises | 13 | 0 |
| Net cash used in financing activities | (2,742) | (3,774) |

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| | | |
|---|-----------|-----------|
| Net decrease in cash and cash equivalents | (5,452) | (19,227) |
| Cash and cash equivalents, beginning of period | 30,924 | 36,671 |
| Cash and cash equivalents, end of period | \$ 25,472 | \$ 17,444 |
| Supplemental schedule of noncash investing activities: | | |
| Acquisitions of other businesses: | | |
| Cost of acquisitions in excess of fair value of net assets acquired | \$ 0 | \$ 357 |
| Intangible assets acquired | 0 | 15 |
| Tangible assets acquired | 0 | 3 |
| Net cash paid for acquisitions | \$ 0 | \$ 375 |

BARRETT BUSINESS SERVICES, INC.

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

Note 1 - Basis of Presentation of Interim Period Statements

The accompanying consolidated financial statements are unaudited and have been prepared by Barrett Business Services, Inc. (Barrett , BBSI or the Company), pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures typically included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the results for the interim periods presented. The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from such estimates and assumptions. The consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s 2010 Annual Report on Form 10-K at pages F1 F32. The results of operations for an interim period are not necessarily indicative of the results of operations for a full year.

Effective January 5, 2010, the Company formed a wholly owned insurance company, Ecole Insurance Company (Ecole). Ecole is a fully licensed insurance company holding a certificate of authority from the Arizona Department of Insurance. Ecole provides workers compensation coverage to the Company s employees working in Arizona for claims occurring on or after March 1, 2010. The cost to capitalize the insurance company was approximately \$6.1 million and is included in restricted marketable securities and workers compensation deposits in the consolidated balance sheet.

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 1 - Basis of Presentation of Interim Period Statements (Continued)**Restatement of prior period**

As described in Note 2 of the Consolidated Financial Statements in Item 15 in the Company's 2010 Annual Report on Form 10-K, the Company restated its consolidated financial statements to correct an error related to legal expenses incurred for the administration of workers compensation claims by Associated Insurance Company for Excess (AICE), the Company's captive insurance subsidiary formed January 1, 2007. The Company's historical accounting method for legal expenses incurred for claims administration had been to recognize the expenses in the period incurred. The Company's captive insurance subsidiary is subject to industry specific authoritative accounting guidance that requires the insurance subsidiary to include an estimate for such legal fees in its workers' compensation claims liabilities. Therefore, the Company's method of recording legal fees in the period incurred for claims administration was determined to be an error. As a result, the Company has presented its consolidated financial statements for the three and six months ended June 30, 2010, as restated to reflect the correction of this error. The Company also determined to make a conforming change to its accounting method for legal expenses incurred for the administration of workers compensation claims that arose prior to the formation of AICE. The impact of the correction of the error and change in accounting method for the three and six months ended June 30, 2010, which has been reflected throughout the consolidated financial statements and accompanying notes, is as follows:

| (in thousands, except per share amounts) | Consolidated Statement of Operations for the Three Months Ended June 30, 2010 | | | | |
|--|--|---------------------------|-----------------------------------|-------------------|-----------|
| | As Previously Reported | Correction of an Error | Change in Accounting Policy | Net Adjustment | Restated |
| Cost of revenues | \$ 55,687 | \$ 198 | \$ (185) | \$ 13 | \$ 55,700 |
| Provision from income taxes | 1,107 | 91 | (85) | 6 | 1,113 |
| Net income | 2,278 | (289) | 270 | (19) | 2,259 |
| Basic income per share | 0.22 | (0.03) | 0.03 | 0 | 0.22 |
| Diluted income per share | 0.22 | (0.03) | 0.03 | 0 | 0.22 |

| (in thousands, except per share amounts) | Consolidated Statement of Operations for the Six Months Ended June 30, 2010 | | | | |
|--|--|---------------------------|-----------------------------------|-------------------|------------|
| | As Previously Reported | Correction of an Error | Change in Accounting Policy | Net Adjustment | Restated |
| Cost of revenues | \$ 108,570 | \$ 396 | \$ (371) | \$ 25 | \$ 108,595 |
| Benefit from income taxes | (146) | 182 | (171) | 11 | (135) |
| Net income | 592 | (578) | 542 | (36) | 556 |
| Basic income per share | 0.06 | (0.06) | 0.06 | 0 | 0.06 |
| Diluted income per share | 0.06 | (0.06) | 0.06 | 0 | 0.06 |

| (in thousands) | Consolidated Statement of Cash Flows for the Six Months Ended June 30, 2010 | | | | |
|---|--|---------------------------|-----------------------------------|-------------------|----------|
| | As Previously Reported | Correction of an Error | Change in Accounting Policy | Net Adjustment | Restated |
| Net income | \$ 592 | \$ (578) | \$ 542 | \$ (36) | \$ 556 |
| Reconciliations of net income to cash provided by operating activities: | | | | | |
| Deferred income taxes | (148) | 60 | 63 | 123 | (25) |
| Income taxes receivable | 387 | (186) | 74 | (112) | 275 |

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| | | | | | |
|---|-------|-----|-------|----|-------|
| Workers compensation claims liabilities | 1,702 | 396 | (371) | 25 | 1,727 |
| Net cash provided by operating activities | 1,584 | 0 | 0 | 0 | 1,584 |

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BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

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

Revenue recognition

We recognize revenue as services are rendered by our workforce. Staffing services are engaged by customers to meet short-term and long-term personnel needs. Professional employer organization (PEO) services are normally used by organizations to satisfy ongoing human resource management needs and typically involve contracts with a minimum term of one year, which cover all employees at a particular work site. Our PEO contracts are renewable on an annual basis and typically require 30 days' written notice to cancel or terminate the contract by either party. Our PEO contracts provide for immediate termination upon any default of the client regardless of when notice is given. We report PEO revenues in accordance with the current accounting guidance for revenue recognition, which requires us to report such revenues on a net basis because we are not the primary obligor for the services provided by our PEO clients to their customers pursuant to our PEO contracts. Consequently, our PEO service fee revenues represent the gross margin generated from our PEO services after deducting the amounts invoiced to PEO customers for direct payroll expenses such as salaries, wages, health insurance and employee out-of-pocket expenses incurred incidental to employment and safety incentives. These amounts are also excluded from cost of revenues. PEO service fees also include amounts invoiced to our clients for employer payroll-related taxes and workers' compensation coverage.

Marketable securities

As of June 30, 2011, the Company's marketable securities consisted of tax-exempt municipal securities, corporate bonds and U.S. treasuries. The Company classifies municipal securities, U.S. treasuries, and certain of its corporate bonds as available for sale; they are reported at fair value with unrealized gains and losses, net of taxes, shown as a component of accumulated other comprehensive income (loss) in stockholders' equity. In the event a loss is determined to be other-than-temporary, the loss will be recognized in the statement of operations. Certain of the Company's corporate bonds are classified as held-to-maturity and are reported at amortized cost.

Allowance for doubtful accounts

The Company had an allowance for doubtful accounts of \$463,000 and \$374,000 at June 30, 2011 and December 31, 2010, respectively. The Company must make estimates of the collectibility of accounts receivable. Management analyzes historical bad debts, customer concentrations, customer creditworthiness, current economic conditions and changes in customers' payment trends when evaluating the adequacy of the allowance for doubtful accounts. The Company deems an account balance uncollectible only after it has pursued all available assets of the customer and, where applicable, the assets of the personal guarantor.

Workers' compensation claims

The Company is a self-insured employer with respect to workers' compensation coverage for all of its employees (including employees subject to Professional Employer Organization (PEO) contracts) working in California, Oregon, Maryland, Delaware and Colorado. In the state of Washington, state law allows only the Company's staffing services and internal management employees to be covered under the Company's self-insured workers' compensation program. Additionally, effective January 5, 2010, we formed a wholly-owned fully licensed insurance company in Arizona to provide workers' compensation coverage to our employees in Arizona.

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

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

Workers' compensation claims (Continued)

To manage our financial exposure, in the event of catastrophic injuries or fatalities, we maintain excess workers' compensation insurance through our wholly owned captive insurance company, Associated Insurance Company for Excess (AICE), with a per occurrence retention of \$5.0 million, except in Maryland and Colorado, where our per occurrence retention is \$1.0 million and \$500,000, respectively. AICE maintains excess workers' compensation insurance coverage with American Insurance Group, Inc. (AIG) between \$5.0 million and \$15.0 million per occurrence, except in Maryland, where coverage with AIG is between \$1.0 million and \$25.0 million per occurrence, and in Colorado, where the coverage with AIG is between \$500,000 and statutory limits per occurrence. We continue to evaluate the financial capacity of our insurers to assess the recoverability of the related insurer receivables.

The Company has provided a total of \$41.0 million and \$39.3 million at June 30, 2011 and December 31, 2010, respectively, as an estimated future liability for unsettled workers' compensation claims liabilities. Included in the foregoing liabilities are insured claims that will be paid by the Company's former excess workers' compensation insurer and for which the Company has reported a receivable from the insurer for the insured claims liability. Insured claims totaled \$2.6 million at June 30, 2011 and \$2.7 million at December 31, 2010, respectively. The estimated liability for unsettled workers' compensation claims represents management's best estimate based upon an actuarial valuation provided by a third party actuary. Included in the claims liabilities are case reserve estimates for reported losses, plus additional amounts based on projections for incurred but not reported claims and anticipated increases in case reserve estimates. Also included in these estimates are amounts for unallocated loss adjustment expenses, including legal costs. These estimates are continually reviewed and adjustments to liabilities are reflected in current operating results as they become known.

Safety incentives liability

Safety incentives represent cash incentives paid to certain PEO client companies for maintaining safe-work practices in order to minimize workplace injuries, thereby meeting agreed-upon loss objectives. The Company has provided \$5.1 million at June 30, 2011 and \$5.0 million at December 31, 2010 as an estimate of the liability for unpaid safety incentives. The incentive is based on a percentage of annual payroll and is paid annually to customers who meet predetermined workers' compensation claims cost objectives. Safety incentive payments are made only after closure of all workers' compensation claims incurred during the customer's contract period. The liability is estimated and accrued each month based upon the incentive earned less the then-current amount of the customer's estimated workers' compensation claims reserves as established by the Company's internal and third-party claims administrators, and the expected payout as determined by historical incentive payment trends. Safety incentive expense is netted against PEO services revenue in our consolidated statements of operations.

BARRETT BUSINESS SERVICES, INC.

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

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

Comprehensive income

Comprehensive income includes all changes in equity during a period except those that resulted from investments by or distributions to a company's stockholders. Comprehensive income totaled \$3.5 million and \$2.1 million for the three months ended June 30, 2011 and 2010 and \$9.0 million and \$459,000 for the six months ended June 30, 2011 and 2010, respectively. Other comprehensive income (loss) refers to revenues, expenses, gains and losses that under GAAP are included in comprehensive income, but are excluded from net income as these amounts are recorded directly as an adjustment to stockholders' equity. The Company's other comprehensive income (loss) is comprised of unrealized holding gains and losses on its publicly traded marketable securities designated as available-for-sale, net of realized gains or losses included in net income.

Note 2 - Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (FASB) issued ASU No. 2011-05, *Comprehensive Income: Presentation of Comprehensive Income*. This new guidance requires the components of net income and other comprehensive income to be either presented in one continuous statement, referred to as the statement of comprehensive income, or in two separate, but consecutive statements. It also eliminates the current option to report other comprehensive income and its components in the statement of stockholders' equity. While the new guidance changes the presentation of comprehensive income, there are no changes to the components that are recognized in net income or other comprehensive income under current accounting guidance. This new guidance is effective for the Company beginning January 1, 2012. As this guidance only alters the presentation of the components of comprehensive income, the adoption will not have an impact on the Company's consolidated financial position or results of operations.

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 3 - Basic and Diluted Earnings Per Share

Basic earnings per share are computed based on the weighted average number of common shares outstanding during the period. Diluted earnings per share reflect the potential effects of the exercise of outstanding stock options. Basic and diluted shares outstanding are summarized as follows:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|------------|------------------------------|------------|
| | 2011 | 2010 | 2011 | 2010 |
| Weighted average number of basic shares outstanding | 10,195,989 | 10,446,350 | 10,198,440 | 10,456,006 |
| Assumed exercise of stock options, net of shares assumed repurchased at average market price during the period using proceeds received upon exercise of options | 48,725 | 38,880 | 47,805 | 33,581 |
| Weighted average number of diluted shares outstanding | 10,244,714 | 10,485,230 | 10,246,245 | 10,489,587 |

Note 4 - Stock Incentive Plans and Stock-Based Compensation

The Company's 2009 Stock Incentive Plan (the 2009 Plan), which provides for stock-based awards to Company employees, non-employee directors and outside consultants or advisors, was approved by shareholders on May 13, 2009. No options have been issued to outside consultants or advisors. The number of shares of common stock reserved for issuance under the 2009 Plan is 1,000,000, of which the aggregate number of shares for which incentive stock options may be granted under the Plan is 900,000. No new grants of stock options may be made under the Company's 2003 Stock Incentive Plan (the 2003 Plan). At June 30, 2011, there were option awards covering 686,169 shares outstanding under the 2009 Plan, together with the 2003 Plan and its predecessor, the 1993 Stock Incentive Plan. Outstanding options under all three plans typically expire ten years after the date of grant and are generally exercisable in four equal annual installments beginning one year after the date of grant. During April 2011, 200,000 options were granted to officers and directors which become exercisable in eight equal annual installments beginning one year after the date of grant.

In accordance with accounting guidance for share-based payments, the Company recognizes compensation expense for options awarded under its stock incentive plans. Current accounting guidance requires the grant-date fair value of all share-based payment awards, including employee stock options, to be recognized as employee compensation expense over the requisite service period.

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 4 - Stock Incentive Plans and Stock-Based Compensation (Continued)

The following table summarizes options activity in 2011:

| | Number of Options | Grant Prices |
|--|----------------------|------------------------|
| Outstanding at December 31, 2010 | 399,569 | \$ 2.00 to \$17.50 |
| Options granted | 289,200 | \$ 14.87 to \$16.53 |
| Options exercised | (2,600) | \$2.00 |
| Options cancelled or expired | 0 | |
| Outstanding at June 30, 2011 | 686,169 | \$ 2.00 to \$17.50 |
| Exercisable at June 30, 2011 | 286,969 | |
| Available for grant at June 30, 2011 | 623,800 | |

The following table presents information on stock options outstanding for the periods shown:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|------------|------------------------------|------|
| | 2011 | 2010 | 2011 | 2010 |
| (\$ in thousands, except per share data) | | | | |
| Intrinsic value of options exercised in the period | \$ 0 | \$ 0 | \$ 34 | \$ 0 |
| | As of June 30, | | | |
| | 2011 | 2010 | | |
| Stock options: | | | | |
| Number of options | 686,169 | 392,319 | | |
| Options fully vested and currently exercisable | 286,969 | 250,694 | | |
| Weighted average exercise price | \$ 13.56 | \$ 13.59 | | |
| Aggregate intrinsic value | \$ 415 | \$ 258 | | |
| Weighted average contractual term of options | 7.41 years | 6.55 years | | |

The aggregate intrinsic value of stock options represents the difference between the Company's closing stock price at the end of the period and the relevant exercise price multiplied by the number of options outstanding at the end of the period at each such price.

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 4 - Stock Incentive Plans and Stock-Based Compensation (Continued)

The fair value of the stock-based awards, as determined under the Black-Scholes model, granted in the six months ended June 30, 2011 and 2010 were \$2.1 million and \$344,000, or \$7.20 and \$5.54 per share, respectively, estimated with the following weighted-average assumptions:

| | Six Months Ended June 30, 2011 | Six Months Ended June 30, 2010 |
|-------------------------|-----------------------------------|-----------------------------------|
| Stock options: | | |
| Risk-free interest rate | 2.88% | 3.00% |
| Expected dividend yield | 2.28% | 2.39% |
| Expected term | 7.3 years | 7.0 years |
| Expected volatility | 65.94% | 58.83% |

The following table summarizes stock-based compensation expense related to stock option awards for the three months and six months ended June 30, 2011 and 2010 (in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|-------|------------------------------|-------|
| | 2011 | 2010 | 2011 | 2010 |
| Stock-based compensation expense included inselling, general and administrative expenses | \$ 136 | \$ 52 | \$ 192 | \$ 84 |
| Deferred income taxes | 54 | 21 | 76 | 34 |
| Stock-based compensation expense related to stock options, net of tax | \$ 82 | \$ 31 | \$ 116 | \$ 50 |

As of June 30, 2011 unrecognized compensation expense related to stock options was \$2.5 million.

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 5 - Workers Compensation

The following table summarizes the aggregate workers compensation reserve activity (in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|--|------------------------------|--|
| | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements |
| Beginning balance | | | | |
| Workers compensation claims liabilities | \$ 39,783 | \$ 36,766 | \$ 39,301 | \$ 35,957 |
| Add: claims expense accrual: | | | | |
| Current period | 5,279 | 3,971 | 9,985 | 7,671 |
| Prior periods | 286 | 44 | 522 | 191 |
| Total expense accrual | 5,565 | 4,015 | 10,507 | 7,862 |
| Less: claim payments related to: | | | | |
| Current period | 962 | 668 | 1,219 | 855 |
| Prior periods | 3,390 | 2,655 | 7,593 | 5,506 |
| Total paid | 4,352 | 3,323 | 8,812 | 6,361 |
| Ending balance | | | | |
| Workers compensation claims liabilities | \$ 40,996 | \$ 37,458 | \$ 40,996 | \$ 37,458 |
| Incurring but not reported (IBNR) | \$ 29,738 | \$ 25,937 | \$ 29,738 | \$ 25,937 |

Note 6 - Fair Value Measurement

The Company has determined that its marketable securities should be presented at their fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Factors used in determining the fair value of our financial assets and liabilities are summarized into three broad categories:

Level 1 quoted prices in active markets for identical securities;

Level 2 other significant observable inputs, including quoted prices for similar securities, interest rates, prepayment speeds, credit risk, etc.; and

Level 3 significant unobservable inputs, including our own assumptions in determining fair value.

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 6 - Fair Value Measurement (Continued)

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

The Company has determined that its U.S. treasuries component of its marketable securities falls into the Level 1 category. The Company has also determined that its municipal bonds and corporate bonds components fall into the Level 2 category. We classify our municipal bonds as level 2 due to our use of fair value pricing provided by an independent third-party based on observable market prices in less active markets or quoted market prices for securities with similar credit characteristics and rates traded in an active market. There were no assets or liabilities where Level 3 valuation techniques were used and there were no assets and liabilities measured at fair value on a non-recurring basis.

Marketable securities consist of the following investments (in thousands):

| | June 30, 2011 | | | December 31, 2010 | | | Fair Value Category |
|----------------------------|---------------|---------------------------------|----------------|-------------------|---------------------------------|----------------|---------------------|
| | Cost | Gross Unrealized Gains (Losses) | Recorded Basis | Cost | Gross Unrealized Gains (Losses) | Recorded Basis | |
| Current: | | | | | | | |
| Trading: | | | | | | | |
| Equity securities | \$ 0 | \$ 0 | \$ 0 | \$ 349 | \$ 21 | \$ 370 | 1 |
| Available-for-sale: | | | | | | | |
| Municipal bonds | 15,868 | 13 | 15,881 | 22,997 | (32) | 22,965 | 2 |
| Corporate bonds | 18,823 | 3 | 18,826 | 861 | 15 | 876 | 2 |
| Variable rate demand notes | 0 | 0 | 0 | 300 | 0 | 300 | 2 |
| | \$ 34,691 | \$ 16 | \$ 34,707 | \$ 24,507 | \$ 4 | \$ 24,511 | |
| Long term: | | | | | | | |
| Available-for-sale: | | | | | | | |
| Corporate bonds | \$ 9,601 | \$ (46) | \$ 9,555 | \$ 5,513 | \$ (39) | \$ 5,474 | 2 |
| Held-to-maturity: | | | | | | | |
| Corporate bonds | 452 | 0 | 452 | 447 | 0 | 447 | 2 |
| | \$ 10,053 | \$ (46) | \$ 10,007 | \$ 5,960 | \$ (39) | \$ 5,921 | |

BARRETT BUSINESS SERVICES, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

Note 6 - Fair Value Measurement (Continued)

The Company's restricted marketable securities component of restricted marketable securities and workers' compensation deposits consists of the following (in thousands):

| | June 30, 2011 | | | December 31, 2010 | | | Fair Value Category |
|---------------------|---------------|---------------------------------|----------------|-------------------|---------------------------------|----------------|---------------------|
| | Cost | Gross Unrealized Gains (Losses) | Recorded Basis | Cost | Gross Unrealized Gains (Losses) | Recorded Basis | |
| Available-for-sale: | | | | | | | |
| Municipal bonds | \$ 5,376 | \$ 28 | \$ 5,404 | \$ 5,147 | \$ 0 | \$ 5,147 | 2 |
| Corporate bonds | 45 | 0 | 45 | 323 | 0 | 323 | 2 |
| U.S. treasuries | 1,567 | 0 | 1,567 | 1,567 | 0 | 1,567 | 1 |
| | \$ 6,988 | \$ 28 | \$ 7,016 | \$ 7,037 | \$ 0 | \$ 7,037 | |

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

Barrett Business Services, Inc. (Barrett , the Company or we), a Maryland corporation, offers a comprehensive range of human resource management services to help small and medium-sized businesses manage the increasing costs and complexities of a broad array of employment-related issues. The Company's principal services, professional employer organization (PEO) services and staffing services, assist its clients in leveraging their investment in human capital. The Company believes that the combination of these two principal services enables it to provide clients with a unique blend of services not offered by the Company's competition. Barrett's platform of outsourced human resource management services is built upon expertise in payroll processing, employee benefits and administration, workers' compensation coverage, effective risk management and workplace safety programs, and human resource administration.

To provide PEO services to a client, the Company enters into a contract to become a co-employer of the client's existing workforce and Barrett assumes responsibility for some or all of the client's human resource management responsibilities. PEO services are normally used by organizations to satisfy ongoing human resource management needs and typically involve contracts with a minimum term of one year, renewable annually, which cover all employees at a particular work site. Staffing services include on-demand or short-term staffing assignments, long-term or indefinite-term contract staffing and comprehensive on-site management. The Company's staffing services also include direct placement services, which involve fee-based search efforts for specific employee candidates at the request of PEO clients, staffing customers or other businesses.

The Company's ability to offer clients a broad mix of services allows Barrett to effectively become the human resource department and a strategic business partner for its clients. The Company believes its approach to human resource management services is designed to positively affect its clients' business results by:

allowing clients to focus on core business activities instead of human resource matters;

increasing clients' productivity by improving employee satisfaction and generating greater employee retention;

reducing overall payroll expenses due to lower workers' compensation and health insurance costs; and

assisting clients in complying with complex and evolving human resource-related regulatory and tax issues.

The Company serves a growing and diverse client base of small and medium-sized businesses in a wide variety of industries through a network of branch offices in California, Oregon, Washington, Idaho, Arizona, Utah, Colorado, Maryland, Delaware and North Carolina. Barrett also has several smaller recruiting offices in its general market areas, which are under the direction of a branch office.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)**Results of Operations**

The following table sets forth percentages of total revenues represented by selected items in the Company's Consolidated Statements of Operations for the three and six months ended June 30, 2011 and 2010.

| | Percentage of Total Revenues Three Months Ended June 30, | | Percentage of Total Revenues Six Months Ended June 30, | |
|--|--|---|--|---|
| | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements |
| Revenues: | | | | |
| Staffing services | 40.1 % | 47.4 % | 40.6 % | 47.0 % |
| Professional employer service fees | 59.9 | 52.6 | 59.4 | 53.0 |
| Total revenues | 100.0 | 100.0 | 100.0 | 100.0 |
| Cost of revenues: | | | | |
| Direct payroll costs | 30.4 | 35.9 | 30.8 | 35.5 |
| Payroll taxes and benefits | 38.0 | 33.9 | 41.9 | 37.8 |
| Workers' compensation | 14.1 | 12.8 | 14.3 | 13.1 |
| Total cost of revenues | 82.5 | 82.6 | 87.0 | 86.4 |
| Gross margin | 17.5 | 17.4 | 13.0 | 13.6 |
| Selling, general and administrative expenses | 11.7 | 12.5 | 12.2 | 13.2 |
| Depreciation and amortization | 0.4 | 0.5 | 0.4 | 0.6 |
| Income (loss) from operations | 5.4 | 4.4 | 0.4 | (0.2) |
| Other income | 0.3 | 0.6 | 7.4 | 0.5 |
| Income before income taxes | 5.7 | 5.0 | 7.8 | 0.3 |
| Provision for income taxes | 1.2 | 1.6 | 1.6 | (0.1) |
| Net income | 4.5 % | 3.4 % | 6.2 % | 0.4 % |

We report PEO revenues on a net basis because we are not the primary obligor for the services provided by our PEO clients to their customers pursuant to our PEO contracts. The presentation of revenues on a net basis and the relative contributions of staffing and PEO revenues can create volatility in our gross margin percentage. The general impact of fluctuations in our revenue mix is described below.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Results of Operations (Continued)

A relative increase in staffing revenues will typically result in a lower gross margin percentage. Staffing revenues are presented at gross with the related direct costs reported in cost of sales. While staffing relationships typically have higher margins than PEO relationships, an increase in staffing revenues and related costs presented at gross dilutes the impact of the net PEO revenue on gross margin percentage.

A relative increase in PEO revenue will result in a higher gross margin percentage. Improvement in gross margin percentage occurs because incremental PEO revenue dollars are reported as revenue net of all related direct costs.

We present for comparison purposes the gross revenues and cost of revenues information set forth in the table below. Although not in accordance with GAAP, management believes this information is more informative as to the level of our business activity and more illustrative of how we manage our operations, including the preparation of our internal operating forecasts, because it presents our PEO services on a basis comparable to our staffing services.

| (in thousands) | Unaudited Three Months Ended June 30, | | Unaudited Six Months Ended June 30, | |
|--------------------------------|---|--|---|--|
| | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements |
| Revenues: | | | | |
| Staffing services | \$ 30,518 | \$ 31,975 | \$ 58,850 | \$ 59,037 |
| Professional employer services | 336,380 | 265,121 | 639,114 | 500,616 |
| Total revenues | 366,898 | 297,096 | 697,964 | 559,653 |
| Cost of revenues: | | | | |
| Direct payroll costs | 312,385 | 252,722 | 595,027 | 476,269 |
| Payroll taxes and benefits | 28,886 | 22,861 | 60,649 | 47,489 |
| Workers' compensation | 12,346 | 9,781 | 23,409 | 18,798 |
| Total cost of revenues | 353,617 | 285,364 | 679,085 | 542,556 |
| Gross margin | \$ 13,281 | \$ 11,732 | \$ 18,879 | \$ 17,097 |

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Results of Operations (Continued)

A reconciliation of non-GAAP gross PEO revenues to net PEO revenues is as follows:

| (in thousands) | Gross Revenue Reporting Method | | Unaudited Three Months Ended June 30, Reclassification | | Net Revenue Reporting Method | |
|--------------------------------|--------------------------------|------------|--|--------------|------------------------------|--|
| | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements |
| Revenues: | | | | | | |
| Staffing services | \$ 30,518 | \$ 31,975 | \$ 0 | \$ 0 | \$ 30,518 | \$ 31,975 |
| Professional employer services | 336,380 | 265,121 | (290,885) | (229,664) | 45,495 | 35,457 |
| Total revenues | \$ 366,898 | \$ 297,096 | \$ (290,885) | \$ (229,664) | \$ 76,013 | \$ 67,432 |
| Cost of revenues | \$ 353,617 | \$ 285,364 | \$ (290,885) | \$ (229,664) | \$ 62,732 | \$ 55,700 |

| (in thousands) | Gross Revenue Reporting Method | | Unaudited Six Months Ended June 30, Reclassification | | Net Revenue Reporting Method | |
|--------------------------------|--------------------------------|------------|--|--------------|------------------------------|--|
| | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 As Restated, See Note 1 to Consolidated Financial Statements |
| Revenues: | | | | | | |
| Staffing services | \$ 58,850 | \$ 59,037 | \$ 0 | \$ 0 | \$ 58,850 | \$ 59,037 |
| Professional employer services | 639,114 | 500,616 | (553,182) | (433,961) | 85,932 | 66,655 |
| Total revenues | \$ 697,964 | \$ 559,653 | \$ (553,182) | \$ (433,961) | \$ 144,782 | \$ 125,692 |
| Cost of revenues | \$ 679,085 | \$ 542,556 | \$ (553,182) | \$ (433,961) | \$ 125,903 | \$ 108,595 |

The amount of the reclassification is comprised of direct payroll costs and safety incentives attributable to our PEO client companies.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Results of Operations (Continued)

Three months ended June 30, 2011 and 2010

Net income for the second quarter of 2011 amounted to \$3.4 million, an improvement of \$1.1 million over the net income of \$2.3 million for the second quarter of 2010. The improvement for the second quarter of 2011 was primarily due to a 12.7% increase in revenues coupled with a lower income tax expense rate. Diluted earnings per share for the second quarter of 2011 were \$.34 compared to diluted income per share of \$.22 for the comparable 2010 period.

Revenues for the second quarter of 2011 totaled \$76.0 million, an increase of approximately \$8.6 million or 12.7%, which reflects an increase in the Company's PEO service fee revenue of \$10.0 million or 28.3%, partially offset by a decline in staffing services revenue of \$1.5 million or 4.6%. Our growth in PEO revenues continues to be primarily attributable to new customers as PEO business from new customers during the second quarter of 2011 more than tripled our lost PEO business from former customers compared to the second quarter of 2010. PEO revenues from continuing customers reflected a 3.6% increase on a quarter over quarter basis. Staffing revenues decreased as a result of the loss of business from certain former customers. The decline in economic activity and associated reductions in employment levels in the Company's market areas in late 2008 and 2009 continue to impact our existing client base, resulting in ongoing pressure on demand for the Company's staffing services.

Gross margin for the second quarter of 2011 totaled approximately \$13.3 million or an increase of \$1.5 million over the second quarter of 2010, primarily due to the 12.7% increase in revenues and a decline in direct payroll costs, partially offset by higher payroll taxes and benefits and workers' compensation expense, as a percentage of revenues.

The decrease in direct payroll costs, as a percentage of revenues, from 35.9% for the second quarter of 2010 to 30.4% for the second quarter of 2011 was primarily due to the increase in our mix of PEO services in the Company's customer base over the second quarter of 2010 and the effect of each customer's unique mark-up percent.

Payroll taxes and benefits, as a percentage of revenues, for the second quarter of 2011 was 38.0% compared to 33.9% for the second quarter of 2010. The percentage rate increase was largely due to the effect of significant growth in PEO services, where payroll taxes and benefits are presented at gross cost whereas the related direct payroll costs are netted against PEO services revenue, and to higher effective state unemployment tax rates in various states in which the Company operates as compared to the second quarter of 2010. Management expects the trend in payroll taxes and benefits, as a percentage of revenues, to continue to increase as a result of continued growth in PEO services on a quarter over quarter basis.

Workers' compensation expense, as a percentage of revenues, increased from 12.8% in the second quarter of 2010 to 14.1% in the second quarter of 2011. Workers' compensation expense for the second quarter of 2011 totaled \$10.8 million, compared to \$8.6 million for the second quarter of 2010. The increase was primarily due to an increase in the number of injury claims incurred during the 2011 second quarter.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Results of Operations (Continued)

Three months ended June 30, 2011 and 2010 (Continued)

Selling, general and administrative (SG&A) expenses for the second quarter of 2011 totaled approximately \$8.9 million, an increase of \$464,000 or 5.5% over the second quarter of 2010. The increase was primarily attributable to increases in management payroll, legal expenses and stock-based compensation expense.

Other income for the second quarter of 2011 was \$266,000 compared to other income of \$380,000 for the second quarter of 2010. Other income for the 2011 second quarter was primarily attributable to investment income earned on the Company's cash and marketable securities. The second quarter of 2010 included gains of approximately \$200,000 on the sale of certain marketable securities.

The income tax rate for the 2011 second quarter was 20.6% which included a favorable benefit from the effect of a much lower annual effective tax rate attributable to the non-taxable \$10.0 million life insurance proceeds from a key man life insurance policy the Company carried on William W. Sherertz, the Company's President and Chief Executive Officer, who passed away January 20, 2011. We expect the effective income tax rate for the balance of 2011 to remain at a rate similar to the 2011 second quarter income tax rate.

Six months ended June 30, 2011 and 2010

Net income for the six months ended June 30, 2011 amounted to \$9.0 million, an improvement of \$8.4 million over the net income of \$556,000 for the second quarter of 2010. The improvement for the first six months ended June 30, 2011 was primarily due to the \$10.0 million life insurance proceeds as well as a 15.2% increase in revenues. Diluted earnings per share for the first six months ended June 30, 2011 was \$.88 compared to diluted earnings per share of \$.05 for the comparable 2010 period.

Revenues for the six months ended June 30, 2011 totaled \$144.8 million, an increase of approximately \$19.1 million or 15.2%, which reflects an increase in the Company's PEO service fee revenue of \$19.3 million or 28.9% offset in part by a small decline in staffing services revenue of \$187,000 or 0.3%. Our growth in PEO revenues was primarily attributable to new customers as PEO business from new customers during the first six months of 2011 tripled our lost PEO business from former customers compared to the first six months of 2010. PEO revenues from continuing customers reflected a 4.9% increase on a comparable six month basis. Staffing revenues decreased slightly as a result of lost business from former customers, offset in part by new staffing business during the first six months of 2011.

Gross margin for the six months ended June 30, 2011 totaled approximately \$18.9 million or an increase of \$1.8 million over the comparable period of 2010, primarily due to the 15.2% increase in revenues and a decline in direct payroll costs, partially offset by higher payroll taxes and benefits and workers' compensation expense, as a percentage of revenues.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Results of Operations (Continued)

Six months ended June 30, 2011 and 2010 (Continued)

The decrease in direct payroll costs, as a percentage of revenues, from 35.5% for the second quarter of 2010 to 30.8% for the first six months of 2011 was primarily due to the increase in our mix of PEO services in the Company's customer base over the 2010 six-month period and the effect of each customer's unique mark-up percent.

Payroll taxes and benefits, as a percentage of revenues, for the six months ended June 30, 2011 was 41.9% compared to 37.8% for the comparable period of 2010. The percentage rate increase was largely due to the effect of significant growth in PEO services and to higher effective state unemployment tax rates in the majority of states in which the Company operates as compared to the same period of 2010.

Workers' compensation expense, as a percentage of revenues, increased from 13.1% in the first six months of 2010 to 14.3% in the first six months of 2011. Workers' compensation expense for the first six months of 2011 totaled \$20.7 million, compared to \$16.4 million for the first six months of 2010. The increase was primarily due to an increase in the number of injury claims incurred during the first six months of 2011.

SG&A expenses for the first six months of 2011 totaled approximately \$17.7 million, an increase of \$1.1 million or 6.4% over the first six months of 2010. The increase was primarily attributable to increases in management payroll, travel and legal expenses.

Other income for the first six months of 2011 was \$10.7 million compared to other income of \$665,000 for the first six months of 2010. The first six months of 2011 included the \$10.0 million of life insurance proceeds and higher investment income, as compared to the 2010 period.

The income tax rate for the first six months of 2011 was 19.9% which included a favorable benefit from the effect of the non-taxable \$10.0 million life insurance proceeds. The income tax rate for the first six months of 2010 was 32.1%. The first six months of 2010 included an additional benefit primarily from a reduction to a deferred tax asset allowance as sales of certain closed-end bond funds during the first six months of 2010 allowed the Company to apply current year capital losses to 2009 capital gains.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Factors Affecting Quarterly Results

The Company has historically experienced significant fluctuations in its quarterly operating results and expects such fluctuations to continue in the future. The Company's operating results may fluctuate due to a number of factors such as seasonality, wage limits on statutory payroll taxes, claims experience for workers' compensation, demand and competition for the Company's services and the effect of acquisitions. The Company's revenue levels may fluctuate from quarter to quarter primarily due to the impact of seasonality on its staffing services business and on certain of its PEO clients in the agriculture, food processing and construction-related industries. As a result, the Company may have greater revenues and net income in the third quarter of its fiscal year. Revenue levels in the fourth quarter may be affected by many customers' practice of operating on holiday-shortened schedules. Payroll taxes and benefits fluctuate with the level of direct payroll costs, but tend to represent a smaller percentage of revenues and direct payroll later in the Company's fiscal year as federal and state statutory wage limits for unemployment and social security taxes are exceeded on a per employee basis. Workers' compensation expense varies with both the frequency and severity of workplace injury claims reported during a quarter and the estimated future costs of such claims. Adverse loss development of prior period claims during a subsequent quarter may also contribute to the volatility in the Company's estimated workers' compensation expense.

Liquidity and Capital Resources

The Company's cash position for the six months ended June 30, 2011 decreased \$5.5 million from December 31, 2010, which compares to a decrease of \$19.2 million for the comparable period in 2010. The decrease in cash at June 30, 2011 as compared to December 31, 2010, was primarily due to net purchases of marketable securities of \$14.1 million and \$1.8 million used to pay cash dividends, offset in part by net income of \$9.0 million.

Net cash provided by operating activities for the six months ended June 30, 2011 amounted to \$12.5 million compared to \$1.6 million of net cash provided by operations for the comparable 2010 period. For the six months ended June 30, 2011, cash flow was principally provided by net income of \$9.0 million together with increases in accrued payroll, payroll taxes and benefits of \$22.8 million and increases in workers' compensation claims liabilities of \$1.8 million, partially offset by an increase in accounts receivable of \$22.1 million.

Net cash used in investing activities for the six months ended June 30, 2011 was \$15.2 million as compared to \$17.0 million of net cash used in investing activities for the similar 2010 period. For the 2011 period, cash from investing activities was principally used for the purchase of marketable securities totaling \$32.7 million and the purchases of restricted marketable securities of \$4.0 million, partially offset by the proceeds from the sales and maturities of marketable securities of \$18.6 million and \$3.4 million from the proceeds of restricted marketable securities. The transactions related to restricted marketable securities were scheduled maturities and the replacement of such securities held for workers' compensation surety deposit purposes. The Company presently has no material long-term capital commitments.

Net cash used in financing activities for the six months ended June 30, 2011 was \$2.7 million as compared to \$3.8 million for the similar 2010 period. For the 2011 period, the primary uses of cash for financing activities were the payment of regular quarterly cash dividends totaling \$1.8 million to holders of the Company's common stock and repurchases of the Company's common stock totaling \$923,000.

The Company's business strategy continues to focus on growth through the expansion of operations at existing offices, together with the selective acquisition of additional personnel-related business, both in its existing markets and other strategic geographic markets. The Company periodically evaluates proposals for various acquisition opportunities, but there can be no assurance that any additional transactions will be consummated.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Liquidity and Capital Resources (Continued)

The Company is a party to a Standby Letter of Credit Agreement dated as of June 30, 2009 (the "Credit Agreement") with its principal bank. The Credit Agreement provides for standby letters of credit as to which there were \$6.7 million outstanding at June 30, 2011 in connection with various surety deposit requirements for workers' compensation purposes.

Pursuant to the Credit Agreement, the Company is required to maintain compliance with the following covenants: (1) to maintain net income after taxes not less than \$1.00 (one dollar) on an annual basis, determined as of each fiscal year end; (2) to maintain liquid assets (defined as unencumbered cash, cash equivalents, and publicly traded and quoted marketable securities) having an aggregate fair market value at all times not less than \$10.0 million, determined as of the end of each fiscal quarter; and (3) to not borrow or permit to exist indebtedness (other than from or to the bank), or mortgage, pledge, grant, or permit to exist a security interest in, or a lien upon, all or any portion of the Company's assets now owned or hereafter acquired, except for purchase money indebtedness (and related security interests) which does not at any time exceed \$500,000. The Company was in compliance with all financial covenants at June 30, 2011.

Management expects that current liquid assets and the funds anticipated to be generated from operations will be sufficient in the aggregate to fund the Company's working capital needs for the next twelve months.

Inflation

Inflation generally has not been a significant factor in the Company's operations during the periods discussed above. The Company has taken into account the impact of escalating medical and other costs in establishing reserves for future expenses for self-insured workers' compensation claims.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Forward-Looking Information

Statements in this report which are not historical in nature, including discussion of economic conditions in the Company's market areas and effect on revenue levels, the potential for and effect of past and future acquisitions, the effect of changes in the Company's mix of services on gross margin, the adequacy of the Company's workers' compensation reserves and the effect of changes in estimate of its claims liabilities, the adequacy of the Company's allowance for doubtful accounts, the effect of the Company's formation and operation of two wholly owned, fully licensed captive insurance subsidiaries and becoming self-insured for certain business risks, the financial viability of the Company's excess insurance carriers, the effectiveness of the Company's management information systems, payment of future dividends, and the availability of financing and working capital to meet the Company's funding requirements, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company or industry to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors with respect to the Company include the ability to retain current customers and attract new customers, difficulties associated with integrating acquired businesses and clients into the Company's operations, economic trends in the Company's service areas, material deviations from expected future workers' compensation claims experience, the effect of changes in the workers' compensation regulatory environment in one or more of the Company's primary markets, collectibility of accounts receivable, the carrying values of deferred income tax assets and goodwill, which may be affected by the Company's future operating results, the availability of capital or letters of credit necessary to meet state-mandated surety deposit requirements for maintaining the Company's status as a qualified self-insured employer for workers' compensation coverage, and the use of \$70.2 million in cash and marketable securities, among others. The Company disclaims any obligation to update any such factors or to publicly announce the result of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's exposure to market risk for changes in interest rates primarily relates to its investment portfolio of liquid assets. As of June 30, 2011, the Company's investment portfolio consisted principally of approximately \$19.3 million in tax-exempt money market funds, \$21.3 million in tax-exempt municipal bonds with an average maturity of 137 days, and approximately \$28.8 million in corporate bonds. Based on the Company's overall interest exposure at June 30, 2011, a 100 basis point increase in market interest rates would not have a material effect on the fair value of the Company's investment portfolio of liquid assets or its results of operations because of the predominantly short maturities of the securities within the investment portfolio.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of June 30, 2011 the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company disclosure controls and procedures, as defined in Rule 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934. Based on the evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management as appropriate to allow timely decisions regarding required disclosure.

Item 4. Controls and Procedures (Continued)

Previously Reported Material Weakness in Internal Control over Financial Reporting

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. In connection with management's assessment of our internal control over financial reporting, we had identified a material weakness in our internal control over financial reporting as of December 31, 2010 as described below.

Previously Reported Material Weakness: The Company did not have effective controls to provide assurance as to the appropriate selection and implementation of accounting methods with respect to accounting for its legal fees incurred by its captive insurance subsidiary for the administration of workers' compensation claims. This material weakness resulted in the adjustment of workers' compensation claims liabilities, deferred taxes, workers' compensation expense (which is a component of cost of revenues), and income tax expense. The restatement of certain periods of the Company's consolidated financial statements is included in our Annual Report on Form 10-K for the year ended December 31, 2010 and in Item 1 of Part I of this report.

As a result of the material weakness in internal control over financial reporting described above, management concluded that the Company's internal control over financial reporting was not effective as of December 31, 2010 based on the criteria in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

For additional information regarding the restatements of certain of the Company's historical financial results and the material weakness identified by management, see Item 9A. Controls and Procedures in the Company's Annual Report on Form 10-K for the year ended December 31, 2010, filed on April 1, 2011 with the Securities and Exchange Commission.

Changes in Internal Control Over Financial Reporting

There have been no changes in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting, except for the remediation steps to address the material weakness in its internal control over financial reporting described above. Specifically, the following steps are being implemented:

Management has formalized the Company's process for reviewing, approving and updating its accounting policies;

Management has formalized the Company's process for reviewing and establishing appropriate accounting policies when forming a new subsidiary; and

Management has implemented steps to improve the industry specific accounting knowledge of the Company's accounting personnel.

Item 4. Controls and Procedures (Continued)

Changes in Internal Control Over Financial Reporting (Continued)

Under the direction of the Audit Committee, management will continue to review and make any changes it deems necessary to the overall design of the Company's internal control over financial reporting, including implementing improvements in policies and procedures.

We are committed to a strong internal control environment, and believe that, when fully implemented, these remediation actions will represent significant improvements in the Company's accounting function. The Company anticipates that it will complete its testing of the additional internal control processes designed to remediate this material weakness prior to the end of 2011. We will continue to assess the effectiveness of our remediation efforts in connection with management's future evaluations of internal control over financial reporting.

Part II Other Information

Item 1A. Risk Factors

There have been no material changes in our risk factors from those disclosed in our 2010 Annual Report on Form 10-K.

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

The following table summarizes information related to stock repurchases during the quarter ended June 30, 2011.

| Month | Total Number of Shares Repurchased | Average Price Paid Per Share | Total Number of Shares Repurchased as Part of Publicly Announced Plan (1) | Maximum Number of Shares that May Yet Be Repurchased Under the Plan (1) |
|-------|---|------------------------------------|--|--|
| April | 0 | \$ 0 | 0 | 1,543,600 |
| May | 0 | 0 | 0 | 1,543,600 |
| June | 61,398 | 14.13 | 61,398 | 1,482,200 |
| Total | 61,398 | | 61,398 | |

- (1) In November 2006, the Board adopted a stock repurchase program and authorized the repurchase of up to 500,000 shares of the Company's stock from time to time in open market purchases. In November 2007, the Board approved an increase in the authorized shares to be repurchased up to 1.0 million shares. In October 2008, the Board approved a second increase in the authorized shares to be repurchased up to 3.0 million shares.

Item 6. Exhibits

The exhibits filed with this report are listed in the Exhibit Index following the signature page of this report.

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.

BARRETT BUSINESS SERVICES, INC.

(Registrant)

Date: August 9, 2011

/s/ James D. Miller
James D. Miller
Vice President-Finance, Treasurer and Secretary
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

Exhibit

- 31.1 Certification of the Chief Executive Officer under Rule 13a-14(a).
- 31.2 Certification of the Chief Financial Officer under Rule 13a-14(a).
- 32 Certification pursuant to 18 U.S.C. Section 1350.
- 101. INS XBRL Instance Document *
- 101. SCH XBRL Taxonomy Extension Schema Document *
- 101. CAL XBRL Taxonomy Extension Calculation Linkbase Document *
- 101. LAB XBRL Taxonomy Extension Label Linkbase Document *
- 101. PRE XBRL Taxonomy Extension Presentation Linkbase Document *

* Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, or Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.