MAXIMUS INC
Form 10-Q
February 08, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

**Quarterly Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934**

For the quarterly period ended December 31, 2010

Commission File Number: 1-12997

MAXIMUS, INC.

(Exact name of registrant as specified in its charter)

Virginia (State or other jurisdiction of incorporation or organization)	**54-1000588** (I.R.S. Employer Identification No.)
11419 Sunset Hills Road **Reston, Virginia** (Address of principal executive offices)	**20190** (Zip Code)

(703) 251-8500

(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 x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

As of January 31, 2011, there were 17,169,621 shares of the registrant s common stock (no par value) outstanding.

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MAXIMUS, Inc.

Quarterly Report on Form 10-Q

For the Quarter Ended December 31, 2010

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Throughout this Quarterly Report on Form 10-Q, the terms Company , we, us, our and MAXIMUS refer to MAXIMUS, Inc. and its subsidiaries.

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PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements.

MAXIMUS, Inc.

CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)

	December 31, 2010 (unaudited)	September 30, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	$ 177,004	$ 155,321
Restricted cash	4,966	4,182
Accounts receivable billed, net of reserves of $2,088 and $1,845	114,586	136,260
Accounts receivable unbilled	18,797	17,245
Income taxes receivable	8,559	4,149
Deferred income taxes	14,848	13,290
Prepaid expenses and other current assets	24,682	25,702
Total current assets	363,442	356,149
Property and equipment, at cost	119,423	115,740
Less accumulated depreciation and amortization	(70,918)	(66,867)
Property and equipment, net	48,505	48,873
Capitalized software	38,537	35,648
Less accumulated amortization	(12,191)	(10,933)
Capitalized software, net	26,346	24,715
Deferred contract costs, net	7,320	6,708
Goodwill	72,189	71,251
Intangible assets, net	7,389	7,778
Deferred income taxes	425	1,844
Deferred compensation plan assets	8,878	8,317
Other assets, net	2,250	2,106
Total assets	$ 536,744	$ 527,741
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 53,638	$ 49,200
Accrued compensation and benefits	29,626	40,807
Deferred revenue	53,286	58,070
Acquisition-related contingent consideration	1,000	923
Income taxes payable	8,260	7,120
Other accrued liabilities	7,038	7,934
Liabilities of discontinued operations		634
Total current liabilities	152,848	164,688
Deferred revenue, less current portion	3,761	4,083

Long-term debt		1,452		1,411
Acquisition-related contingent consideration, less current portion		2,300		2,138
Income taxes payable, less current portion		1,823		1,793
Deferred income tax liability		5,924		4,946
Deferred compensation plan liabilities		11,459		9,893
Total liabilities		179,567		188,952
Shareholders equity:				
Common stock, no par value; 60,000,000 shares authorized; 27,612,647 and 27,487,725 shares issued and 17,164,447 and 17,174,141 shares outstanding at December 31, 2010 and September 30, 2010, at stated amount, respectively		360,198		352,696
Treasury stock, at cost;10,448,200 and 10,313,584 shares at December 31, 2010 and September 30, 2010, respectively		(367,733)		(359,366)
Accumulated other comprehensive income		18,459		14,530
Retained earnings		346,253		330,929
Total shareholders equity		357,177		338,789
Total liabilities and shareholders equity	$	536,744	$	527,741

See notes to unaudited consolidated financial statements.

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MAXIMUS, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended December 31, 2010	Three Months Ended December 31, 2009
Revenue	$ 214,114	$ 203,320
Cost of revenue	158,155	151,145
Gross profit	55,959	52,175
Selling, general and administrative expenses	28,667	27,429
Legal and settlement expense		686
Operating income from continuing operations	27,292	24,060
Interest and other income, net	491	99
Income from continuing operations before income taxes	27,783	24,159
Provision for income taxes	10,196	9,559
Income from continuing operations	17,587	14,600
Discontinued operations, net of income taxes:		
Loss from discontinued operations		(1,972)
Loss on disposal	(105)	
Loss from discontinued operations	(105)	(1,972)
Net income	$ 17,482	$ 12,628
Basic earnings (loss) per share (Note 7):		
Income from continuing operations	$ 1.02	$ 0.83
Loss from discontinued operations		(0.11)
Basic earnings per share	$ 1.02	$ 0.72
Diluted earnings (loss) per share (Note 7):		
Income from continuing operations	$ 0.99	$ 0.81
Loss from discontinued operations		(0.11)
Diluted earnings per share	$ 0.99	$ 0.70
Dividends paid per share	$ 0.12	$ 0.12
Weighted average shares outstanding:		
Basic	17,180	17,595
Diluted	17,710	18,039

See notes to unaudited consolidated financial statements.

MAXIMUS, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	Three Months Ended December 31, 2010	Three Months Ended December 31, 2009
Cash flows from operating activities:		
Net income	$ 17,482	$ 12,628
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss from discontinued operations	105	1,972
Depreciation and amortization	5,232	4,540
Deferred income taxes	990	(8,492)
Deferred interest income on note receivable		61
Non-cash equity based compensation	2,057	1,865
Change in assets and liabilities:		
Accounts receivable billed	22,145	9,349
Accounts receivable unbilled	(1,554)	(2,327)
Prepaid expenses and other current assets	1,041	1,042
Deferred contract costs	(580)	479
Other assets	(1,284)	(34)
Accounts payable	3,948	587
Accrued compensation and benefits	(11,553)	(2,035)
Deferred revenue	(5,270)	13,134
Income taxes	(3,470)	14,867
Other liabilities	1,092	1,251
Cash provided by operating activities continuing operations	30,381	48,887
Cash provided by (used in) operating activities discontinued operations	(739)	6,134
Cash provided by operating activities	29,642	55,021
Cash flows from investing activities:		
Proceeds from note receivable		217
Purchases of property and equipment	(2,407)	(3,938)
Capitalized software costs	(2,298)	(2,641)
Cash used in investing activities continuing operations	(4,705)	(6,362)
Cash used in investing activities discontinued operations		
Cash used in investing activities	(4,705)	(6,362)
Cash flows from financing activities:		
Employee stock transactions	4,329	1,004
Repurchases of common stock	(8,370)	(8,661)
Tax benefit due to option exercises and restricted stock units vesting	1,031	135
Cash dividends paid	(2,067)	(2,118)
Cash used in financing activities continuing operations	(5,077)	(9,640)
Cash used in financing activities discontinued operations		
Cash used in financing activities	(5,077)	(9,640)
Effect of exchange rate changes on cash and cash equivalents	1,823	106

Net increase in cash and cash equivalents		21,683		39,125
Cash and cash equivalents, beginning of period		155,321		87,815
Cash and cash equivalents, end of period	$	177,004	$	126,940

See notes to unaudited consolidated financial statements.

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MAXIMUS, Inc.

Notes to Unaudited Consolidated Financial Statements

For the Three Months Ended December 31, 2010 and 2009

In these Notes to Unaudited Consolidated Financial Statements, the terms the Company , MAXIMUS , us , we , or our refer to MAXIMUS, Inc. and its subsidiaries.

1. Organization and Basis of Presentation

General

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes 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. The results of operations for the three months ended December 31, 2010 are not necessarily indicative of the results that may be expected for the full fiscal year. The balance sheet at September 30, 2010 has been derived from the audited financial statements at that date but does not include all of the information and notes required by generally accepted accounting principles for complete financial statements.

These financial statements should be read in conjunction with the consolidated audited financial statements and the notes thereto at September 30, 2010 and 2009 and for each of the three years ended September 30, 2010, included in the Company s Annual Report on Form 10-K for the year ended September 30, 2010 filed with the Securities and Exchange Commission on November 19, 2010.

2. Recent Accounting Pronouncements

In September 2009, the FASB issued revised guidance for accounting for contracts that contain more than one contract element. The revised guidance establishes a selling price hierarchy for determining the selling price of each contract element. The guidance also expands the required disclosures. The Company adopted this guidance for all multiple-element arrangements entered into or significantly modified after October 1, 2010. The effect of this new guidance was not significant.

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3. Goodwill and Intangible Assets

The changes in goodwill for the three months ended December 31, 2010 are as follows (in thousands):

	Health Services	Human Services	Total
Balance as of September 30, 2010	$ 43,270	$ 27,981	$ 71,251
Foreign currency translation	221	717	938
Balance as of December 31, 2010	$ 43,491	$ 28,698	$ 72,189

The following table sets forth the components of intangible assets (in thousands):

	As of December 31, 2010			As of September 30, 2010		
	Cost	Accumulated Amortization	Intangible Assets, net	Cost	Accumulated Amortization	Intangible Assets, net
Technology-based intangible assets	$ 7,270	$ 3,777	$ 3,493	$ 7,160	$ 3,654	$ 3,506
Customer contracts and relationships	9,260	6,141	3,119	8,989	5,504	3,485
Non-compete arrangements	250	55	195	243	39	204
Trademark	640	58	582	622	39	583
Total	$ 17,420	$ 10,031	$ 7,389	$ 17,014	$ 9,236	$ 7,778

The intangible assets include $3.4 million of fully-amortized technology-based assets still in use by the Company. Excluding these assets, the Company s intangible assets have a weighted average remaining life of 6.4 years, comprising 7.6 years for technology-based intangible assets, 4.7 years for customer contracts and relationships, 3.1 years for non-compete arrangements and 9.1 years for the trademark. Amortization expense for the three months ended December 31, 2010 was $0.6 million. Future amortization expense is estimated as follows (in thousands):

Nine months ended September 30, 2011	$ 1,572
Year ended September 30, 2012	1,164
Year ended September 30, 2013	1,085
Year ended September 30, 2014	720
Year ended September 30, 2015	697
Thereafter	2,151
Total	$ 7,389

4. Fair Value Measurements

The Company is required to disclose the fair value of all assets and liabilities subject to fair value measurement and the nature of the valuation techniques, including their classification within the fair value hierarchy, utilized by the Company in performing these measurements.

The FASB provides a fair value framework which requires the categorization of assets and liabilities into three levels based upon the assumptions (or inputs) used to price the assets or liabilities. Level 1 provides the most reliable measure of fair value, whereas Level 3 generally requires significant management judgment. The three levels are defined as follows:

Level 1:	Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.
Level 2:	Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.
Level 3:	Unobservable inputs that reflect the reporting entity s own assumptions.

The Company s financial assets subject to fair value measurements and the necessary disclosures are as follows (in thousands):

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Description	Fair Value as of December 31, 2010	Fair Value Measurements as of December 31, 2010 Using Fair Value Hierarchy Level 1	Level 2	Level 3
Current portion of acquisition-related contingent consideration	$ (1,000)	$	$	$ (1,000)
Acquisition-related contingent consideration, less current portion	(2,300)			(2,300)
Deferred compensation plan liabilities	(11,459)		(11,459)	

The Company s deferred compensation plan liabilities are valued using a market approach, utilizing the value of the underlying investments to identify the fair value. Changes in deferred compensation plan liabilities are recorded in the income statement within Interest and other income, net .

The Company s only acquisition-related contingent consideration liability was incurred with the acquisition of DeltaWare Systems, Inc. in February 2010. The fair value of the acquisition-related contingent consideration liability was based on a probability-weighted approach derived from management s own estimates of profitability and sales targets. During the current period, management s estimates of DeltaWare s future profitability have been revised, with the result that an additional charge was recognized in the period. Foreign currency translation adjustments were recorded as a component of other comprehensive income.

The effect on the financial statements is summarized below (in thousands):

	Acquisition-related contingent consideration Current portion	Long-term portion	Total
Balance as of September 30, 2010	$ 923	$ 2,138	$ 3,061
Additional estimated consideration	50	100	150
Foreign currency translation	27	62	89
Balance as of December 31, 2010	$ 1,000	$ 2,300	$ 3,300

5. Commitments and Contingencies

Litigation

The Company is involved in various legal proceedings, including contract and employment claims, in the ordinary course of its business. The matters reported on below involve significant pending or potential claims against us.

In March 2009, a state Medicaid agency asserted a claim against MAXIMUS, related to a discontinued business line, in the amount of $2.3 million in connection with a contract MAXIMUS had through February 1, 2009 to provide Medicaid administrative claiming services to school districts in the state. MAXIMUS entered into separate agreements with the school districts under which MAXIMUS helped the districts prepare and submit claims to the state Medicaid agency which, in turn, submitted claims for reimbursement to the federal government. No legal action has been initiated. The state has asserted that its agreement with MAXIMUS requires the Company to reimburse the state for the amounts owed to the federal government. However, the Company s agreements with the school districts require them to reimburse MAXIMUS for such payments and therefore MAXIMUS believes the school districts are responsible for any amounts disallowed by the state Medicaid agency or the federal government. Accordingly, the Company believes its exposure in this matter is limited to its fees associated with this work and that the school districts will be responsible for the remainder. During the second quarter of fiscal 2009, MAXIMUS recorded a $0.7 million reduction of revenue reflecting the fees it earned under the contract. MAXIMUS has exited the federal healthcare claiming business and no longer provides the services at issue in this matter.

In August 2010, the Company received a draft audit report prepared on behalf of one of its former SchoolMAX customers. The SchoolMAX business line was sold as part of the divestiture of the MAXIMUS Education Systems division in 2008. The draft audit report recommends a refund of approximately $11.6 million primarily arising out of the alleged failure of MAXIMUS and the buyer of the division to observe the most favored customer pricing term of the contract. MAXIMUS believes the audit report is incorrect and that no amounts are owed as a refund. In February 2011, the client sent a letter to MAXIMUS and the buyer of the business initiating the dispute resolution process under the contract. The client reiterated some of the audit issues previously identified and also raised a number of issues pertaining to services and products delivered under the contract. The client alleges total damages in excess of $30 million. MAXIMUS and the buyer plan to contest all of the client's claims. The Company also believes that it is entitled to indemnification from the buyer of the business for claims pertaining to services and deliverables.

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Credit Facilities and Performance Bonds

The Company s Revolving Credit Agreement provides for a senior secured revolving credit facility, with SunTrust Bank as administrative agent, issuing bank and swingline lender, and a syndicate of other lenders (the Credit Facility). The Credit Facility provides for a $35.0 million revolving line of credit commitment, which may be used (i) for revolving loans, (ii) for swingline loans, subject to a sublimit of $5.0 million, and (iii) to request the issuance of letters of credit on the Company s behalf, subject to a sublimit of $25.0 million. The Company may request an increase in the commitment under the Credit Facility, such that the aggregate commitments under the Credit Facility shall at no time exceed $75.0 million. The credit available under the Credit Facility may be used, among other purposes, to refinance the Company s current indebtedness, to repurchase shares of the Company s capital stock and to finance the ongoing working capital, capital expenditure, and general corporate needs of the Company. The Credit Facility matures on January 25, 2013, at which time all outstanding borrowings must be repaid and all outstanding letters of credit must have been terminated or cash collateralized. At December 31, 2010, letters of credit totaling $11.3 million were outstanding under the Credit Facility.

Subject to applicable conditions, the Company may elect interest rates on its revolving borrowings calculated by reference to (i) the prime lending rate as announced by SunTrust Bank (or, if higher, the federal funds effective rate plus 0.50% or the one-month adjusted LIBOR) (a Base Rate Borrowing), or (ii) the reserve adjusted rate per annum equal to the offered rate for deposits in U.S. dollars for a one (1), two (2), three (3) or six (6) month period in the London Inter-Bank Market (a LIBOR Borrowing), and, in each case, plus an applicable margin that is determined by reference to the Company s then-current leverage ratio. For swingline borrowings, the Company will pay interest at the rate of interest for a one (1) month LIBOR Borrowing, plus the applicable margin, or at a rate to be separately agreed upon by the Company and the administrative agent.

The Credit Facility provides for the payment of specified fees and expenses, including commitment and letter of credit fees, and contains customary financial and other covenants that require the maintenance of certain ratios including a maximum leverage ratio and a minimum fixed charge coverage ratio. The Company was in compliance with all covenants in the amended Credit Facility as of December 31, 2010. The Company s obligations under the Credit Facility are guaranteed by certain of the Company s direct and indirect subsidiaries (collectively, the Guarantors) and are secured by substantially all of MAXIMUS and the Guarantors present and future tangible and intangible assets, including the capital stock of subsidiaries and other investment property.

The Company also has a loan agreement with the Atlantic Innovation Fund of Canada. This provides for a loan of up to 1.7 million Canadian Dollars, which must be used for specific technology-based research and development. The loan has no interest charge and is repayable in installments between 2012 and 2022. At December 31, 2010, $1.5 million (1.5 million Canadian Dollars) was outstanding under this agreement.

Certain contracts require us to provide a surety bond as a guarantee of performance. At December 31, 2010 and September 30, 2010, the Company had performance bond commitments totaling $31.3 million and $33.5 million, respectively. These bonds are typically renewed annually and remain in place until the contractual obligations have been satisfied. Although the triggering events vary from contract to contract, in general, we would only be liable for the amount of these guarantees in the event of default in our performance of our obligations under each contract, the probability of which we believe is remote.

Loss contract

During the period, the Company recorded a charge of $3.2 million on a fixed price contract. The Company has recorded a liability of $2.9 million related to the anticipated loss to be recorded on this contract. The revenue and profitability on this contract are based upon estimated costs to complete the project, which are inherently subject to risk. The contract is expected to be completed during the 2012 fiscal year.

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6. Legal and Settlement Expense

Legal and Settlement Expense consists of costs related to significant legal settlements, including future legal costs estimated to be incurred in connection with those matters.

Legal expenses of $686,000 for the three month period ended December 31, 2009 relate predominantly to costs incurred in resolving a dispute with one of the Company s subcontractors. There were no comparative costs in the three month period ended December 31, 2010.

7. Earnings Per Share

The following table sets forth the components of basic and diluted earnings per share (in thousands):

	Three Months Ended December 31, 2010	Three Months Ended December 31, 2009
Numerator:		
Income from continuing operations	$ 17,587	$ 14,600
Loss from discontinued operations	(105)	(1,972)
Net income	$ 17,482	$ 12,628
Denominator:		
Basic weighted average shares outstanding	17,180	17,595
Effect of dilutive securities:		
Employee stock options and unvested restricted stock units	530	444
Denominator for diluted earnings per share	17,710	18,039

The calculation of dilutive securities did not exclude any of the Company s vesting or exercisable stock options in either period shown.

8. Stock Repurchase Programs

Under resolutions adopted in July 2008 and September 2010, the Board of Di