

BARRETT BUSINESS SERVICES INC

Form 10-K

March 16, 2015

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

**FORM 10-K**

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2014

Commission File Number 0-21886

**BARRETT BUSINESS SERVICES, INC.**

(Exact name of registrant as specified in its charter)

Maryland	52-0812977
(State or other jurisdiction of	(IRS Employer
incorporation or organization)	Identification No.)
8100 NE Parkway Drive, Suite 200	
Vancouver, Washington	98662
(Address of principal executive offices)	(Zip Code)
(360) 828-0700	
(Registrant's telephone number, including area code)	

Securities registered pursuant to Section 12(b) of the Act:

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Title of each class	Name of each exchange on which registered
Common Stock, Par Value \$0.01 Per Share	The NASDAQ Stock Market LLC
Securities registered pursuant to Section 12(g) of the Act: None	

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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 for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 indicated by Exchange Act Rule 12b-2).

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 Act). Yes ☐ No ☒

State the aggregate market value of the common equity held by non-affiliates of the registrant: \$330,349,417 at June 30, 2014

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

Class	Outstanding at March 2, 2015
Common Stock, Par Value \$.01 Per Share	7,137,791 Shares

### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement for the 2015 Annual Meeting of Stockholders are hereby incorporated by reference into Part III of Form 10-K.

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**2014 ANNUAL REPORT ON FORM 10-K**

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**PART I**

**Item 1. BUSINESS**

***General***

**Company Background.** Barrett Business Services, Inc. ( BBSI, the Company, our or we ), is a leading provider of business management solutions for small-and mid-sized companies. The Company has developed a management platform that integrates a knowledge-based approach from the management consulting industry with tools from the human resource outsourcing industry. This platform, through the effective leveraging of human capital, assists our business owner clients in more effectively running their business. We believe this platform, delivered through a decentralized organizational structure, differentiates BBSI from our competitors. BBSI was incorporated in Maryland in 1965.

**Business Strategy.** Our strategy is to align local operations teams with the mission of small and mid-sized business owners, driving value to their business. To do so, BBSI:

partners with business owners to leverage their investment in human capital through a high-touch, results-oriented approach;

brings predictability to each client organization through a three-tiered management platform; and

enables business owners to focus on their core business by reducing organizational complexity and maximizing productivity.

**Business Organization.** We operate a decentralized delivery model using locally based teams, typically located within 50 miles of our client companies. We recruit senior level managers to oversee, develop and expand our business at the branch-office level. Additionally, we recruit professionals with expertise in human resources, risk management and workplace safety and various types of administration, including payroll, to field our client delivery teams. This structure fosters autonomous decision-making, allowing local teams of professionals to deliver plans that most closely align with the needs of each business owner client. It also assists us by incubating talent to support increased growth and capacity. We have clients with employees located in 22 states and the District of Columbia, through a network of 54 branch locations in California, Oregon, Washington, Idaho, Arizona, Nevada, Utah, Colorado, Maryland, Delaware and North Carolina. We also have several smaller recruiting locations in our general market areas, which are under the direction of a branch office.

BBSI believes that making significant investments in the best talent available allows us to leverage the value of this investment many times over. We motivate our management employees through a compensation package that includes a competitive base salary and the opportunity for profit sharing. At the branch level, profit sharing is in direct correlation to client performance, reinforcing a culture focused on achievement of client goals.

**Services Overview.** BBSI's core purpose is to advocate for business owners, particularly in the small-and mid-sized business segment. Our evolution from an entrepreneurially run company to a professionally managed organization has helped to form

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our view that all businesses experience inflection points at key stages of growth. The insights gained through our own growth, along with the trends we see in working with more than 3,000 companies each day, define our approach to guiding business owners through the challenges associated with being an employer.

BBSI's business teams align with each business owner client through a structured three-tiered progression. In doing so, business teams focus on the objectives of each business owner and deliver planning, guidance and resources in support of those objectives.

### ***Tier 1: Tactical Alignment***

The first stage focuses on the mutual setting of expectations and is essential to a successful client relationship. It begins with a process of assessment and discovery in which the business owners' business objectives, attitudes, and culture are aligned with BBSI's processes, controls and culture. This stage includes an implementation process, which addresses the administrative components of employment.

### ***Tier 2: Dynamic Relationship***

The second stage of the relationship emphasizes organizational development as a means of achieving each client's business objectives. There is a focus on process improvement, development of best practices, supervisor training and leadership development.

### ***Tier 3: Strategic Counsel***

With an emphasis on advocacy on behalf of the business owner, the third stage of the relationship is more strategic and forward-looking with a goal of cultivating an environment in which all efforts are directed by the mission and long-term objectives of the business owner.

In addition to serving as resource and guide, BBSI has the ability to provide workers' compensation coverage as a means of meeting statutory requirements and protecting our clients from employment-related injury claims. Through our internal claims managers and our third-party administrators, we provide claims management services for our co-employed clients. We work aggressively to manage and reduce job injury claims, identify fraudulent claims and structure optimal work programs, including modified duty employees.

### ***Categories of Services***

We report financial results in two categories of services: Professional Employer Services (PEO) and Staffing. During 2014, we supported in excess of 3,600 PEO clients and approximately 129,000 employees. This compares to more than 3,200 PEO clients and approximately 111,000 employees during 2013. See Item 7 of this Report for information regarding the percentages of total net revenues provided by our PEO and staffing services for each of the last three fiscal years.

**PEO.** We enter into a client services agreement to establish a co-employment relationship with each client company, assuming responsibility for payroll, payroll taxes, workers' compensation coverage and certain other administrative functions for the client's existing workforce. The client maintains physical care, custody and control of their workforce, including the authority to hire and terminate employees.

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**Staffing and Recruiting.** Our staffing services include on-demand or short-term staffing assignments, contract staffing, long-term or indefinite-term on-site management, and direct placement. Our recruiting experts maintain a deep network of professionals from which we source candidates. Through an assessment process, we gain an understanding of the short-and long-term needs of our clients, allowing us to identify and source the right talent for each position. We then conduct a rigorous screening process to help ensure a successful hire.

### ***Clients and Client Contracts***

Our business is typically characterized by long-term relationships that result in recurring revenue. Our client relationships are codified in a client services agreement, which typically provides for an initial term of one year with renewal for additional one-year periods but generally permits cancellation by either party upon 30 days' written notice. In addition, we may terminate the agreement at any time for specified breach of contract, including nonpayment or failure to follow our workplace safety recommendations. Our annual client retention rate is in excess of 90%. We do not include clients we have terminated in our retention calculation.

The client services agreement also provides for indemnification of us by the client against losses arising out of any default by the client under the agreement, including failure to comply with any employment-related, health and safety, or immigration laws or regulations. Our client service agreement requires clients in a co-employment arrangement to maintain comprehensive liability coverage in the amount of \$1.0 million for acts of their employees. Although no claims exceeding such policy limits have been paid by us to date, the possibility exists that claims for amounts in excess of sums available to us through indemnification or insurance may be asserted in the future, which could adversely affect profitability.

We have client services agreements with a diverse array of customers, including among others, electronics manufacturers, various light-manufacturing industries, agriculture-based companies, transportation and shipping enterprises, food processing, telecommunications, public utilities, general contractors in various construction-related fields, and professional services firms. None of our clients individually represented more than 1% of our total revenues in 2014.

### ***Market Opportunity***

As a company that aligns with the mission of business owners by providing resources and guidance to small and mid-size businesses, BBSI believes its growth is driven by the desire of business owners to focus on mission-critical functions, reduce complexity associated with the employment function, mitigate costs and maximize the investment in human capital. Our integrated management platform has enabled us to capitalize on these needs within the small to mid-size business sector.

The small and mid-sized business segment is particularly attractive because:

it is large, continues to grow and remains underserved by professional services companies;

it typically has fewer in-house resources than larger businesses and, as a result, is generally more dependent on external resources;

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we generally experience a relatively high client retention rate and lower client acquisition costs within this market segment; and

we have found that small to mid-size businesses are responsive to quality of service, ease-of-use, and responsiveness to clients needs when selecting a PEO or staffing services provider.

### ***Competition***

The business environment in which we operate is characterized by intense competition and fragmentation. BBSI is not aware of reliable statistics regarding the number of its competitors, but certain large, well-known companies typically compete with us in the same markets and also have greater financial and marketing resources than we do, including Automatic Data Processing, Inc., Manpower, Inc., Kelly Services, Inc., Insperity, Inc., TriNet, Group, Inc. and Paychex, Inc. We may face additional competition in the future from new entrants to the field, including other staffing services companies, payroll processing companies and insurance companies. The principal competitive factors in the business environment in which we operate are price and level of service.

We believe that our growth is attributable to our ability to provide small and mid-sized companies with the resources and knowledge base of a large employer delivered through a local operations team. Our level of integration with each client business provides us an additional competitive advantage.

### ***Sales and Marketing***

We believe our clients are our best advocates and powerful drivers of our brand awareness. We support our clients and foster advocacy through branch-based business teams. As such, sales and marketing efforts are led by area managers who lead teams responsible for client delivery and retention. Each integrated team is comprised of a client-facing Business Partner, HR Consultant, Risk Management Consultant, a Payroll Specialist and in some instances, a Recruiting Specialist. By developing business teams in our existing branches, we expect to see incremental growth in the markets where we currently do business, driven by our reputation and client referrals. BBSI's business development is the primary function of our area managers, and is focused on branch-level development of local business relationships. In some markets, our sales efforts are further supported by Business Development Managers.

On a regional and national level, we seek to expand and align our services to meet business demand, which may include opening additional offices to better support a client's geographic needs, or adding new business teams within an existing branch location. We believe our business teams serve a dual purpose: 1) Delivering high-quality guidance to our clients, thereby supporting client business growth and driving client referrals, and 2) Incubating talent at the branch level to support expansion into new markets.

Our business growth has three sources: referrals from existing clients, direct business-to-business sales efforts by our area managers, and an extensive referral network. Our referral partners include insurance brokers, financial advisors, attorneys, CPA's, and other business professionals who can facilitate an introduction to prospective clients. These partners, typically in exchange for a fee equal to a small percentage of payroll, facilitate introductions to business owners on our behalf.

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### ***Growth Strategy***

Our growth strategy is focused in the following areas:

Support, strengthen and expand branch office operations through the ongoing development of business units. We believe that strengthening and expanding the operations of each location is an efficient and effective means of increasing market share in the geographic areas in which we do business. Because we understand that successful and satisfied client companies are a powerful driver of brand awareness, we focus on creating and expanding business units within each branch that provide tactical and strategic guidance to our client base. As our presence in each market grows through the addition of branch business units, we believe market awareness of our reputation and services increases.

Enhance management information systems. We continue to invest in developing our information technology infrastructure, particularly in systems that allow increased engagement between our clients and their supporting business teams. We believe that this approach gives us a competitive advantage by allowing us to provide a high level of interaction with our small and medium-sized business clients on a cost-effective basis. Furthermore, we believe that our current technology platform is capable of supporting our planned development of new business units for the foreseeable future.

Penetrate new markets. We intend to open additional branch offices in new geographic markets as opportunities arise. We have developed a well-defined approach to geographic expansion, which will serve as a guide for entering new markets. We believe our decentralized organizational model built on teams of senior-level professionals allows us to incubate talent as we expand into new markets.

### ***Workers Compensation***

Through our client services agreement, we have the ability to provide workers compensation coverage to our clients. We provide this coverage through a variety of methods, all of which are subject to rigorous underwriting to assess financial stability, risk factors and cultural alignment related to safety and the client's desire to improve their operations. In providing this coverage, we are responsible for complying with applicable statutory requirements for workers compensation coverage. Additionally, risk mitigation is an important contributor to our principal goal of helping business owners operate their business more efficiently. It is in the mutual interests of the client and BBSI to commit to workplace safety and risk mitigation.

Elements of Workers Compensation System. State law (and for certain types of employees, federal law) generally mandates that an employer reimburse its employees for the costs of medical care and other specified benefits for injuries or illnesses, including catastrophic injuries and fatalities, incurred in the course and scope of employment. The benefits payable for various categories of claims are determined by state regulation and vary with the severity and nature of the injury or illness and other specified factors. In return for this guaranteed protection, workers compensation is an exclusive remedy and employees are generally precluded from seeking other damages from their employer for workplace injuries. Most states require employers to maintain workers compensation insurance or otherwise



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demonstrate financial responsibility to meet workers' compensation obligations to employees. In many states, employers who meet certain financial and other requirements are permitted to self-insure. See Regulatory and Legislative Issues below for a discussion of recent developments in California.

Self Insurance for Workers' Compensation. In August 1987, we became a self-insured employer for workers' compensation coverage in Oregon. We subsequently obtained self-insured employer status for workers' compensation in California, Delaware, Maryland and Colorado, as well as in Washington for our staffing and management employees. Regulations governing self-insured employers in each jurisdiction typically require the employer to maintain surety bonds, surety deposits of government securities, letters of credit or other financial instruments to cover workers' claims in the event the employer is unable to pay for such claims. Effective January 1, 2015, BBSI no longer maintains a certificate to self-insure in the state of California, and now maintains individual policies for all California-based clients. See Regulatory and Legislative Issues below for a discussion of recent developments in California.

To manage our financial exposure to catastrophic injuries and fatalities, we maintain excess workers' compensation insurance coverage. Our wholly owned, fully licensed captive insurance company incorporated in Arizona, Associated Insurance Company for Excess ( "AICE" ), provides us with excess workers' compensation coverage from \$1.0 million up to \$5.0 million per occurrence in the states of Oregon, California, Delaware and Washington. Additional excess workers' compensation insurance coverage is provided through annual policies issued by ACE Group ( "ACE" ) from \$5.0 million to \$15.0 million per occurrence, except for our Maryland and Colorado operations.

Our excess insurance policy in Maryland has a \$1.0 million retention with a \$25.0 million limit and our excess insurance policy in Colorado has a \$2.0 million retention and statutory limits on a per occurrence basis. This approach results in an effective per occurrence retention, on a consolidated basis, of \$5.0 million. This higher per occurrence retention may result in higher workers' compensation costs to us with a corresponding negative effect on our operating results. AICE provides us with access to an alternative mechanism for excess insurance coverage, as well as certain income tax benefits arising from the ability to accelerate the deduction, for tax purposes, of certain accruals for workers' compensation claims.

Additionally, we formed Ecole Insurance Company, a wholly owned fully licensed insurance company in Arizona ( "Ecole" ), to provide workers' compensation coverage to our employees working in Arizona, beginning with claims occurring on or after March 1, 2010. Additional reinsurance coverage for Ecole is provided by ACE from \$5.0 million to statutory limits per occurrence.

Claims Management. As a self-insured employer, our workers' compensation expense is tied directly to the incidence and severity of workplace injuries to our employees. We seek to contain our workers' compensation costs through an aggressive approach to claims management. We use managed-care systems to reduce medical costs and keep time-loss costs to a minimum by assigning injured workers, whenever possible, to short-term assignments which accommodate the workers' physical limitations. We believe that these

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assignments minimize both time actually lost from work and covered time-loss costs. We employ internal, professionally licensed claims adjusters and engage third-party claims administrators ( TPAs ) to provide the principal claims management expertise. Typical management procedures include performing thorough and prompt on-site investigations of claims filed by employees, working with physicians to encourage efficient medical management of cases, denying questionable claims and attempting to negotiate early settlements to eliminate future development of claims costs. We also maintain a corporate-wide pre-employment drug screening program and a mandatory post-injury drug test. The program is believed to have resulted in a reduction in the frequency of fraudulent claims and in accidents in which the use of illegal drugs appears to have been a contributing factor.

**Elements of Self-Insurance Costs.** The costs associated with our self-insured workers' compensation program include case reserves for reported claims, an additional expense provision for potential future increases in the cost of open injury claims (known as "adverse loss development") and claims incurred in prior periods but not reported (referred to as "IBNR"), fees payable to our TPAs, additional claims administration expenses, administrative fees payable to state workers' compensation regulatory agencies, legal fees, fees paid for business referrals, premiums for excess workers' compensation insurance, and costs associated with forming and operating our wholly owned, fully licensed captive insurance company for excess coverage. The state assessments are typically based on payroll amounts and, to a limited extent, the amount of permanent disability awards during the previous year. Excess insurance premiums are also based in part on the size and risk profile of our payroll and loss experience.

**Changes to Self-Insurance in California.** In September 2012, California Senate Bill 863 ( "SB 863" ), was signed into law. Under SB 863, the California Director of Self-Insurance was required not to issue certificates of consent to self-insure after January 1, 2013, to any employer engaged in the activities of a professional employer organization, a leasing employer, a temporary services employer or any employer the Director determines to be in the business of providing employees to other employers. Additionally, the Director was required to revoke any previously issued certificate of consent to self-insure in favor of any employer engaged in these types of activities not later than January 1, 2015. To address this issue, in February 2014, BBSI entered into an arrangement typically known as a "fronted" program with ACE. Under this arrangement, the risk of loss up to the first \$5.0 million per claim is retained by BBSI through an indemnity agreement, although ACE will be responsible for any claims BBSI is unable to satisfy. In addition, ACE continues to be BBSI's carrier for costs in excess of \$5.0 million per claim. During 2014, we transitioned all California-based clients and their employees to ACE policies prior to December 31, 2014 in compliance with SB 863. During 2015, we expect to incur increased costs associated with the fronted insurance program, as 2015 will represent the first full year of complete coverage.

### ***Workers' Compensation Claims Experience and Reserves***

We recognize our liability for the ultimate payment of incurred claims and claims adjustment expenses by accruing liabilities which represent estimates of future amounts necessary to pay claims and related expenses with respect to covered events that have occurred. When a claim involving a probable loss is reported, our internal claims management personnel or our TPA establishes a case reserve for the estimated amount of ultimate loss. The estimate reflects an informed judgment based on established case reserving practices.

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and the experience and knowledge of our claims management staff and the TPA regarding the nature and expected amount of the claim, as well as the estimated expenses of settling the claim, including legal and other fees and expenses of claims administration. The adequacy of such case reserves in part depends on the professional judgment of both our claims management staff and our TPA to properly and comprehensively evaluate the economic consequences of each claim. Our reserves include an additional component for both estimated future adverse loss development in excess of initial case reserves on open claims and for incurred but not reported claims (together IBNR) based upon actuarial estimates provided by the Company's independent actuary. Our reserves do not include an estimated provision for the incidence of unknown or unreported catastrophic claims.

As part of the case reserving process, historical data is reviewed and consideration is given to the anticipated effect of various factors, including known and anticipated legal developments, inflation and economic conditions. Reserve amounts are based on management's estimates, and as other data becomes available, these estimates are revised, which may result in increases or decreases in existing case reserves. Management's internal accrual process for workers' compensation expense is based upon the immediate recognition of an expense and the related liability at the time a claim occurs; the value ascribed to the expense and liability is based upon our internal claims management and the TPAs' estimate of ultimate claim cost coupled with a provision for estimated future development based upon an actuarial review performed by our independent actuary. We believe our total accrued workers' compensation claims liabilities at December 31, 2014 are adequate. It is possible, however, that our actual future workers' compensation obligations may exceed the amount of our accrued liabilities, with a corresponding negative effect on future earnings, due to such factors as unanticipated adverse loss development of known claims and, to a much lesser extent, of claims incurred but not reported.

Failure to successfully manage the severity and frequency of workplace injuries would result in increased workers' compensation expense and would have a negative effect, which may be substantial, on our operating results and financial condition. BBSI maintains clear guidelines for our area managers and risk management consultants, directly tying their continued employment to their diligence in understanding and addressing the risks of accident or injury associated with the industries in which client companies operate and in monitoring clients' compliance with workplace safety requirements. We have a policy of zero tolerance for avoidable workplace injuries. Each of our risk management consultants has the authority to cancel any client at any time based upon their assessment of their safe-work practices or philosophies.

### ***Employees and Employee Benefits***

At December 31, 2014, we had approximately 93,040 total employees, including approximately 10,280 staffing services employees, approximately 82,400 employees under our client service agreements, 515 managerial, sales and administrative employees, and 4 executive officers. The number of employees at any given time may vary significantly due to business conditions at customer or client companies. Substantially all of our managerial, sales and administrative employees have entered into a standard form of employment agreement which, among other provisions, contains covenants not to engage in certain activities in competition with us for 18 months following termination of employment and to maintain the confidentiality of certain proprietary information. We believe our employee relations are good.

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We offer various qualified employee benefit plans to our employees, including those employees for whom we are the administrative employer in a co-employment agreement who so elect. These qualified employee benefit plans include our 401(k) plan to which employees may begin making contributions upon reaching 21 years of age and completing 1,000 hours of service in any consecutive 12-month period. We may also make contributions to the 401(k) plan, which vest over six years and are subject to certain legal limits, at the sole discretion of our Board of Directors.

We make matching contributions to the 401(k) plan under a safe harbor provision, whereby we match 100% of contributions by management and staffing employees to the 401(k) plan up to 3% of each participating employee's annual compensation and 50% of the employee's contributions up to an additional 2% of annual compensation. We also offer a cafeteria plan under Section 125 of the Internal Revenue Code; and group health, life insurance and disability insurance plans. Generally, qualified employee benefit plans are subject to provisions of both the Internal Revenue Code and the Employee Retirement Income Security Act of 1974 (ERISA). In order to qualify for favorable tax treatment under the Internal Revenue Code, qualified plans must be established and maintained by an employer for the exclusive benefit of its employees.

### ***Regulatory and Legislative Issues***

**Business Operations.** We are subject to the laws and regulations of the jurisdictions within which we operate, including those governing self-insured employers under the workers' compensation systems in Oregon, Maryland, Delaware and Colorado, as well as in Washington for staffing and management employees. As a result of legislation in California related to our self-insurance program, we transitioned out of self-insurance in California during 2014 into an insured program with ACE. During the fourth quarter of 2014, the Company received confirmation from the Office of Self Insured Plans that BBSI was in full compliance with all regulatory collateral requirements for California self-insurance. See Workers' Compensation-Changes in Self-Insurance in California above. We are also subject to laws and regulations governing our two wholly owned, fully licensed insurance companies in Arizona. While the specific laws and regulations vary among these jurisdictions, they typically require some form of licensing and often have statutory requirements for workplace safety and notice of change in obligation of workers' compensation coverage in the event of contract termination. Although compliance with these requirements imposes some additional financial risk on us, particularly with respect to those clients who breach their payment obligation to us, such compliance has not had a material adverse effect on our business to date.

**Employee Benefit Plans.** Our operations are affected by numerous federal and state laws relating to labor, tax and employment matters. Through our client services agreement, we assume certain obligations and responsibilities as the administrative employer under federal and state laws. Because many of these federal and state laws were enacted prior to the development of nontraditional employment relationships, such as professional employer, temporary employment, and outsourcing arrangements, many of these laws do not specifically address the obligations and responsibilities of nontraditional employers. In addition, the definition of "employer" under these laws is not uniform.

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As an employer, we are subject to all federal statutes and regulations governing our employer-employee relationships. Subject to the discussion of risk factors below, we believe that our operations are in compliance in all material respects with applicable federal statutes and regulations.

### **Additional Information**

Our filings with the SEC, including our annual report on Form 10-K, quarterly reports on Form 10-Q, periodic reports on Form 8-K and amendments to these reports, are accessible free of charge at our website at <http://www.barrettbusiness.com> as soon as reasonably practicable after filing with the SEC. By making this reference to our website, we do not intend to incorporate into this report any information contained in the website. The website should not be considered part of this report.

The SEC maintains a website at <http://www.sec.gov> that contains reports, proxy and information statements, and other information regarding issuers with publicly traded securities, including the Company.

### **Item 1A. RISK FACTORS**

In addition to other information contained in this report, the following risk factors should be considered carefully in evaluating our business.

#### **Our workers' compensation loss reserves may be inadequate to cover our ultimate liability for workers' compensation costs.**

We maintain reserves (recorded as accrued liabilities on our balance sheet) to cover our estimated liabilities for our workers' compensation claims under our insurance arrangement with ACE in California, our self-insured status in Oregon, Delaware, Maryland and Colorado and our captive insurance subsidiary Ecole in Arizona. The determination of these reserves is based upon a number of factors, including current and historical claims activity, claims payment patterns and medical cost trends and developments in existing claims. Accordingly, reserves do not represent an exact calculation of liability. Reserves may be affected by both internal and external events, such as adverse developments on existing claims or changes in medical costs, medical condition of the claimant, claims handling procedures, administrative costs and legal fees, inflation, and legal trends and legislative changes. Reserves are adjusted from time to time to reflect new claims, claim developments, or systemic changes, and such adjustments are reflected in the results of the periods in which the reserves are changed. Our revenues include an additional component for both estimated future adverse loss development in excess of initial case reserves on open claims and for incurred but not reported claims based upon actuarial estimates provided by the Company's independent actuary. The estimated accrual does not include an estimated provision for the incidence of unknown catastrophic claims. Moreover, because of the uncertainties that surround estimating workers' compensation loss reserves, we cannot be certain that our reserves are adequate. If our reserves are insufficient to cover our actual losses, we would have to increase our reserves and incur charges to our earnings that could be material to our results of operations and financial condition. See Item 1. Business - Workers' Compensation above for additional information.

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**Our retention for workers' compensation claims is \$5.0 million per occurrence under our insurance arrangement with ACE in California as well as in the majority of our self-insured states.**

In view of the Company's favorable historical experience with large catastrophic claims and an opportunity to realize savings from lower excess workers' compensation insurance premiums, we maintain our retention at \$5.0 million per occurrence, except in Colorado and Maryland where our retention is at \$2.0 million and \$1.0 million per occurrence, respectively. Additionally, Ecole's retention is at \$5.0 million per occurrence for coverage in Arizona. Thus, the Company has financial risk for most workers' compensation claims under \$5.0 million, on a per occurrence basis. This level of per occurrence retention may result in higher workers' compensation costs to us with a corresponding negative effect on our operating results and financial condition.

**Adverse developments in the market for excess workers' compensation insurance could lead to increases in our costs.**

We are a state-approved self-insured employer for workers' compensation coverage in Oregon, Delaware, Maryland and Colorado, as well as in Washington for our staffing and management employees. To manage our financial exposure in the event of catastrophic injuries or fatalities, we maintain excess workers' compensation insurance with a per occurrence retention of \$5.0 million effective January 1, 2007, except in Colorado and Maryland where our retention is at \$2.0 million and \$1.0 million per occurrence, respectively. Additionally, Ecole's retention is at \$5.0 million per occurrence for coverage in Arizona. Changes in the market for excess workers' compensation insurance may lead to limited availability of such coverage, additional increases in our insurance costs or further increases in our self-insured retention, any of which may have a material adverse effect on our financial condition.

**Our ability to continue our business operations in California is dependent on maintaining workers' compensation insurance coverage.**

We recently renewed our workers' compensation insurance arrangement with ACE for our employees in California. The annual renewal extends through February 1, 2016, with the possibility of additional annual renewals. If ACE is unwilling or unable to renew our arrangement in the future, we would need to seek alternative coverage. If replacement coverage were unavailable or available only on significantly less favorable terms, our business and results of operations would be materially adversely affected.

**Our business is subject to risks associated with geographic market concentration.**

Our California operations accounted for approximately 77% of our total net revenues in 2014. As a result of the current importance of our California operations and anticipated continued growth from these operations, our profitability over the next several years is expected to be largely dependent on economic and regulatory conditions in California. If California experiences an economic downturn, or if the regulatory environment changes in a way that adversely affects our ability to do business or limits our competitive advantages, our profitability and growth prospects may be materially and adversely affected.

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### **Economic conditions, particularly in California, may impact our ability to attract new clients and cause our existing clients to reduce staffing levels or cease operations.**

Weak economic conditions typically have a negative impact on small-and mid-sized businesses, which make up the majority of our clients. In turn, these businesses could cut costs, including trimming employees from their payrolls, or ceasing operations altogether. These forces may result in decreased revenues due both to the downsizing of our current clients and difficulties in attracting new clients, and may also result in additional bad debt expense to the extent that existing clients cease operations.

### **We may be unable to draw on our revolving credit facility in the future.**

As discussed in more detail in Note 7 to the audited consolidated financial statements included in Item 15 of this Report, we maintain a credit agreement (the "Agreement") with our principal bank, Wells Fargo Bank, National Association (the "Bank"). The Agreement, which expires October 1, 2017, provides for a revolving credit facility with a borrowing capacity of up to \$14.0 million at December 31, 2014, to be used to finance working capital; there was no outstanding balance at that date. The Agreement also provides a term loan in the principal amount of \$40.0 million maturing December 31, 2016, which we used to fund our workers' compensation insurance reserves at December 31, 2014, as well as a standby letter of credit agreement providing for a total of approximately \$114.0 million in cash-secured letters of credit and a term loan with a balance of approximately \$5.1 million secured by our company office building in Vancouver, Washington.

If our business does not perform as expected, including if we generate less revenue than anticipated from our operations or encounter significant unexpected costs, we may fail to comply with the financial covenants under our credit facilities. If we do not comply with our financial covenants and we do not obtain a waiver or amendment from the Bank, the Bank may elect to cause all amounts owed to become immediately due and payable. In this event, we would seek to establish a replacement credit facility with one or more other lenders, including lenders with which we have an existing relationship, potentially at less desirable terms. There can be no guarantee that replacement financing would be available at commercially reasonable terms, if at all. Any of these risks and uncertainties could have a material adverse effect on our business, financial position, results of operations, and working capital.

### **If we are unable to maintain our brand image and corporate reputation, our business may suffer.**

Our success depends in part on our ability to maintain our reputation for providing excellent service to our customers. Service quality issues, actual or perceived, even when false or unfounded, could tarnish the image of our brand and may cause customers to use other companies. Also, adverse publicity surrounding labor relations, data breaches, securities class actions, and the like, or attempts to connect our Company to these types of issues, could negatively affect our overall reputation. Damage to our reputation could reduce demand for our services and thus have an adverse effect on our business, financial position and results of operations.

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### **Our staffing business is vulnerable to economic fluctuations.**

Demand for our staffing services is sensitive to changes in the level of economic activity in the regions in which we do business. As economic activity slows down, companies often reduce their use of temporary employees before undertaking layoffs of permanent staff, resulting in decreased demand for staffing services. During strong economic periods, on the other hand, we often experience shortages of qualified employees to meet customer needs.

### **Because we assume the obligation to make wage, tax and regulatory payments in respect of some employees, we are exposed to client credit risks.**

We generally assume responsibility for and manage the risks associated with our clients' employee payroll obligations, including liability for payment of salaries and wages (including payroll taxes), as well as group health and retirement benefits. These obligations are fixed, whether or not the client makes payments to us as required by our services agreement, which exposes us to credit risks. We attempt to mitigate this risk by invoicing our clients at the end of their specific payroll processing cycle. We also carefully monitor the timeliness of our clients' payments and impose strict credit standards on our customers. If we fail to successfully manage our credit risk, our results of operations and financial condition could be materially and adversely affected.

### **Increases in unemployment claims could raise our state and federal unemployment tax rates which we may not be able to pass on to our customers.**

During weak economic conditions in our markets, the level of unemployment claims tend to rise as a result of employee layoffs at our clients and lack of work in our temporary staffing pool. The rise in unemployment claims often results in higher state and federal unemployment tax rates which in most instances cannot be concurrently passed on to our customers either due to existing client services agreements or competitive pricing pressures. Increases in our state and federal unemployment tax rates could have a material adverse effect on our results of operations, particularly in the early part of the calendar year when effective payroll tax rates are at or near their maximum.

### **If we are determined not to be an employer under certain laws and regulations, our clients may stop using our services, and we may be subject to additional liabilities.**

We are the administrative employer in our co-employment relationships under the various laws and regulations of the Internal Revenue Service and the U.S. Department of Labor. If we are determined not to be the administrative employer under such laws and regulations and are therefore unable to assume our clients' obligations for employment and other taxes, our clients may be held jointly and severally liable for payment of such taxes. Some clients or prospective clients may view such potential liability as an unacceptable risk, discouraging current clients from continuing a relationship with us or prospective clients from entering into a new relationship with us. Any determination that we are not the administrative employer for purposes of ERISA could adversely affect our cafeteria benefits plan operated under Section 125 of the Internal Revenue Code and result in liabilities to us under the plan.



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### **We may be exposed to employment-related claims and costs and periodic litigation that could adversely affect our business and results of operations.**

We either co-employ employees in connection with our client services agreements or place our employees in our customers' workplace in connection with our staffing business. As such, we are subject to a number of risks inherent to our status as the administrative employer, including without limitation:

claims of misconduct or negligence on the part of our employees, discrimination or harassment claims against our employees, or claims by our employees of discrimination or harassment by our clients;

immigration-related claims;

claims relating to violations of wage, hour and other workplace regulations;

claims relating to employee benefits, entitlements to employee benefits, or errors in the calculation or administration of such benefits; and

possible claims relating to misuse of customer confidential information, misappropriation of assets or other similar claims.

If we experience significant incidents involving any of the above-described risk areas we could face substantial out-of-pocket losses, fines or negative publicity. In addition, such claims may give rise to litigation, which may be time consuming, distracting and costly, and could have a material adverse effect on our business. With respect to claims involving our co-employer relationships, although our client services agreement provides that the client will indemnify us for any liability attributable to the conduct of the client or its employees, we may not be able to enforce such contractual indemnification, or the client may not have sufficient assets to satisfy its obligations to us.

### **We are dependent upon technology services and if we experience damage, service interruptions or failures in our computer and telecommunications systems, our client relationships and our ability to attract new clients may be adversely affected.**

We rely extensively on our computer systems to manage our branch network, perform employment-related services, accounting and reporting, and summarize and analyze our financial results. Our systems are subject to damage or interruption from telecommunications failures, power-related outages, computer viruses and malicious attacks, security breaches and catastrophic events. If our systems are damaged or fail to function properly, we may incur substantial costs to repair or replace them, experience loss of critical data and interruptions or delays in our ability to manage our operations, and encounter a loss of client confidence. In addition, our clients' businesses may be adversely affected by any system or equipment failure or breach we experience. As a result, our relationships with our clients may be impaired, we may lose clients, our ability to attract new clients may be adversely affected and we could be exposed to contractual liability. We may invest in upgrades or replacements to our existing systems or additional security measures, each of which can involve substantial costs and risks relating to installation and implementation.

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**If our efforts to protect the security of personal information about our employees and clients are unsuccessful, we could be subject to costly government enforcement actions and private litigation and our reputation could suffer.**

The nature of our business involves the receipt, storage, and transmission of personal and proprietary information about thousands of employees and some clients. If we experience a significant data security breach or fail to detect and appropriately respond to a significant data security breach, we could be exposed to government enforcement actions and private litigation. In addition, our employees and clients could lose confidence in our ability to protect their personal and proprietary information, which could cause them to terminate their relationships with us. Any loss of confidence arising from a significant data security breach could hurt our reputation, further damaging our business.

**We operate in a complex regulatory environment, and failure to comply with applicable laws and regulations could adversely affect our business.**

Corporate human resource operations are subject to a broad range of complex and evolving laws and regulations, including those applicable to payroll practices, benefits administration, employment practices and privacy. Because our clients have employees in many states throughout the United States, we must perform our services in compliance with the legal and regulatory requirements of multiple jurisdictions. Some of these laws and regulations may be difficult to ascertain or interpret and may change from time to time. Violation of such laws and regulations could subject us to fines and penalties, damage our reputation, constitute a breach of our client agreements, impair our ability to obtain and renew required licenses, and decrease our profitability or competitiveness. If any of these effects were to occur, our operating results and financial condition could be adversely affected.

**Changes in government regulations may result in restrictions or prohibitions applicable to the provision of employment services or the imposition of additional licensing, regulatory or tax requirements.**

Our business is heavily regulated in most jurisdictions in which we operate. We cannot assure you that the states in which we conduct or seek to conduct business will not:

impose additional regulations that prohibit or restrict employment-related businesses like ours;

require additional licensing or add restrictions on existing licenses to provide employment-related services; or

increase taxes or make changes in the way in which taxes are calculated for providers of employment-related services.

Any changes in applicable laws and regulations may make it more difficult or expensive for us to do business, inhibit expansion of our business, or result in additional expenses that limit our profitability or decrease our ability to attract and retain clients.

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### **The tax status of our insurance subsidiaries could be challenged resulting in an acceleration of income tax payments.**

In conjunction with our workers' compensation program, we operate two wholly owned insurance subsidiaries, AICE and Ecole. We treat the two subsidiaries as insurance companies for federal income tax purposes, with respect to our consolidated federal income tax return. In the event the Internal Revenue Service ( IRS ) were to determine that the subsidiaries do not qualify as insurance companies, we could be required to make accelerated income tax payments to the IRS that we otherwise would have deferred until future periods.

### **We may find it difficult to expand our business into additional states due to varying state regulatory requirements.**

Future growth in our operations depends, in part, on our ability to offer our services to prospective clients in new states, which may subject us to different regulatory requirements and standards. In order to operate effectively in a new state, we must obtain all necessary regulatory approvals, adapt our procedures to that state's regulatory requirements and modify our service offerings to adapt to local market conditions. In the event that we expand into additional states, we may not be able to duplicate in other markets the financial performance experienced in our current markets.

### **Acquisitions subject us to various risks, including risks relating to selection and pricing of acquisition targets, integration of acquired companies into our business and assumption of unanticipated liabilities.**

We have completed 27 acquisitions since 1993 and may pursue additional acquisitions and investment opportunities. We cannot assure, however, that we will be able to identify or complete additional acquisitions. If we do pursue acquisitions, we may not realize the anticipated benefits of such acquisitions. Acquisitions involve many risks, including risks relating to the assumption of unforeseen liabilities of an acquired business, adverse accounting charges resulting from the acquisition, and difficulties in integrating acquired companies into our business, both from a cultural perspective, as well as with respect to personnel and client retention and technological integration. Acquired liabilities may be significant and may adversely affect our financial condition and results of operations. Our inability to successfully integrate acquired businesses may lead to increased costs, failure to generate expected returns, accounting charges, or even a total loss of amounts invested, any of which could have a material adverse effect on our financial condition and results of operations.

### **We face competition from a number of other companies.**

We face competition from various companies that may provide all or some of the services we offer. Our competitors include companies that are engaged in staffing services such as Kelly Services, Inc. and Manpower Inc., companies that are focused on co-employment, such as Insperity, Inc. and companies that primarily provide payroll processing services, such as Automatic Data Processing, Inc. and Paychex, Inc. We also face competition from information technology outsourcing firms and broad-based outsourcing and consulting firms that perform individual projects.

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Several of our existing or potential competitors have substantially greater financial, technical and marketing resources than we do, which may enable them to:

develop and expand their infrastructure and service offerings more quickly and achieve greater cost efficiencies;

invest in new technologies;

expand operations into new markets more rapidly;

devote greater resources to marketing;

compete for acquisitions more effectively and complete acquisitions more easily; and

aggressively price products and services and increase benefits in ways that we may not be able to match financially.

In order to compete effectively in our markets, we must target our potential clients carefully, continue to improve our efficiencies and the scope and quality of our services, and rely on our service quality, innovation, education and program clarity. If our competitive advantages are not compelling or sustainable, then we are unlikely to increase or sustain profits and our stock price could decline.

### **We are dependent upon certain key personnel and recruitment and retention of key employees may be difficult and expensive.**

We believe that the successful operation of our business is dependent upon our retention of the services of key personnel, including our Chief Executive Officer, other executive officers and area managers. We may not be able to retain all of our executives, senior managers and key personnel in light of competition for their services. If we lose the services of one of our executive officers or a significant number of our senior managers, our operations and profitability likely would be adversely affected.

### **We do not have an expansive in-house sales staff and therefore rely extensively on referral partners.**

We maintain a minimal internal professional sales force and we rely heavily on referral partners to provide referrals to new business, especially in California, although each area manager is expected to be an effective leader in business development, including marketing efforts and sales closures. In connection with these arrangements, we pay a fee to referral partners for new clients. As a result, we are dependent on firms and individuals that do not have an exclusive relationship with us. If we are unable to maintain these relationships, or if they increase their fees or lose confidence in our services, we could face declines in our business and additional costs and uncertainties as we attempt to hire and train an internal sales force.

### **We depend on attracting and retaining qualified employees; during periods of economic growth, our costs to do so increase and it becomes more difficult to attract and retain people.**

The success of our staffing services depends on our ability to attract and retain qualified employees for placement with our customers. Our ability to attract and retain

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qualified personnel could be impaired by rapid improvement in economic conditions resulting in lower unemployment and increases in compensation. During periods of economic growth, we face growing competition for retaining and recruiting qualified personnel, which in turn leads to greater advertising and recruiting costs and increased salary expenses. If we cannot attract and retain qualified employees, the quality of our services may deteriorate and our reputation and results of operations could be adversely affected.

**Our service agreements may be terminated on short notice, leaving us vulnerable to loss of a significant amount of customers in a short period of time, if business or regulatory conditions change or events occur that negatively affect our reputation.**

Our client services agreements are generally terminable on 30 days' notice by either us or the client. As a result, our clients may terminate their agreement with us at any time, making us particularly vulnerable to changing business or regulatory conditions or changes affecting our reputation or the reputation of our industry.

**Our industry has at times received negative publicity that, if it were to become more prevalent, could cause our business to decline.**

In the industries in which we compete, companies periodically have been tarnished by negative publicity or scandals from poor business judgment or even outright fraud. If we or our industry face negative publicity, customers' confidence in the use of temporary personnel or co-employed workers may deteriorate, and they may be unwilling to enter into or continue our staffing or co-employment relationships. If a negative perception were to prevail, it would be more difficult for us to attract and retain customers.

**Changes in state unemployment tax laws and regulations could adversely affect our business.**

In past years, there has been significant negative publicity relating to the use of staffing or PEO companies to shield employers from poor unemployment history and high unemployment taxes. New legislation enacted at the state or federal level to try to counter this perceived problem could have a material adverse effect on our business by limiting our ability to market our services or making our services less attractive to our customers and potential customers.

**We are, and in the future may be, subject to legal or administrative actions that could adversely affect our results of operations and our business.**

As described in more detail in Item 3 of this Report and in Note 13 to our audited consolidated financial statements included in Item 15 of this Report, three lawsuits purporting to be class actions brought on behalf of all of BBSI's stockholders have been filed in the United States District Court for the Western District of Washington against BBSI and BBSI's Chief Executive Officer and Chief Financial Officer. The actions allege violations of the federal securities laws based on claims arising from the decline in the market price for our common stock following announcement of a charge for increased workers compensation reserves expense in the 2014 third quarter. In addition, in February 2015, we received a letter from counsel from a stockholder threatening to commence a shareholder derivative action on

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behalf of the Company based on the same facts as the three lawsuits already filed, as well as that certain officers and directors sold shares of BBSI common stock while in possession of material non-public information.

The results of legal proceedings against us, including those described above, if decided adversely to us or to our directors or officers, could result in significant monetary damages or penalties or reputational harm, and could involve significant defense or other costs. We have entered into indemnification agreements with each of our directors and our corporate charter requires us to indemnify each of our officers and directors against all liabilities, losses, judgments, penalties, fines, settlements and reasonable expenses arising out of their actions in such capacities to the fullest extent permitted by Maryland law. Although we maintain insurance coverage in amounts and with deductibles that we believe are appropriate for our operations, our insurance coverage may not cover all claims that have been or may be brought against us, or continue to be available to us at a reasonable cost. As a result, we may be exposed to substantial uninsured liabilities, including pursuant to our indemnification obligations, which could adversely affect our business, prospects, results of operations and financial condition.

### **Maryland law and our Charter and bylaws contain provisions that could make the takeover of the Company more difficult.**

Certain provisions of Maryland law and our Charter and bylaws could have the effect of delaying or preventing a third party from acquiring the Company, even if a change in control would be beneficial to our stockholders. These provisions of our Charter and bylaws:

permit the Board of Directors to issue up to 500,000 shares of preferred stock with such rights and preferences, including voting rights, as the Board may establish, without further approval by the Company's stockholders, which could also adversely affect the voting power of holders of our common stock; and

vest the power to adopt, alter or repeal the Company's bylaws solely in the Board of Directors; the stockholders do not have that power.

In addition, the Company is subject to the Maryland control share act (the "Control Share Act"). Under the Control Share Act, a person (an "Acquiring Person") who acquires voting stock in a transaction (a "Control Share Acquisition") which results in its holding voting power within specified ranges cannot vote the shares it acquires in the Control Share Acquisition unless voting rights are accorded to such control shares by the holders of two-thirds of the outstanding voting shares, excluding the Acquiring Person and the Company's officers and directors who are also employees of the Company.

The Company is also subject to the provisions of Maryland law limiting the ability of certain Maryland corporations to engage in specified business combinations (the "Business Combination Act"). Subject to certain exceptions, the Business Combination Act prohibits a Maryland corporation from engaging in a business combination with a stockholder who, with its affiliates, owns 10% or more of the corporation's voting stock. These provisions will not apply to business combinations that are approved by the Board of Directors before the stockholder became an interested stockholder.

**Table of Contents****Item 1B. UNRESOLVED STAFF COMMENTS**

None.

**Item 2. PROPERTIES**

We operate through all 54 of our branch offices. The following table shows the number of locations in each state in which we operate. We also lease office space in other locations in our market areas which we use to recruit and place employees.

<b>Offices</b>	<b>Number of Branch Locations</b>
California	20
Oregon	11
Utah	5
Washington	5
Idaho	3
Arizona	2
Colorado	2
Maryland	2
North Carolina	2
Delaware	1
Nevada	1

We lease office space for our branch offices. At December 31, 2014, our leases had expiration dates ranging from less than one year to six years, with total minimum payments through 2020 of approximately \$10.7 million. Our corporate headquarters office in Vancouver, Washington occupies approximately 40 percent of the 63,500 square foot building we own.

**Item 3. LEGAL PROCEEDINGS**

On November 6, 2014, plaintiffs in *Michael Arciaga, et al. v. Barrett Business Services, Inc., et al.*, filed an action in the United States District Court for the Western District of Washington against BBSI and Michael L. Elich and James D. Miller, BBSI's Chief Executive Officer and Chief Financial Officer, respectively. The action purports to be a class action brought on behalf of all of BBSI's stockholders alleging violations of the federal securities laws. The claims arise from the decline in the market price for BBSI common stock following announcement of a charge for increased workers compensation reserves expense. The lawsuit seeks compensatory damages (in an amount to be determined at trial), plus interest, and costs and expenses (including attorney fees and expert fees).

On November 13, 2014, a second purported shareholder class action was filed in the United States District Court for the Western District of Washington, entitled *Christopher P. Carnes, et al. v. Barrett Business Services, Inc., et al.* The *Carnes* complaint names the same defendants as the *Arciaga* case and asserts similar claims for relief.

Similarly, on November 17, 2014, a third purported shareholder class action was filed in the United States District Court for the Western District of Washington, entitled *Shiva Stein, et al. v. Barrett Business Services, Inc., et al.* The *Stein* complaint names the same defendants as the *Arciaga* and *Carnes* cases and asserts similar claims for relief.

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On February 25, 2015, the court ordered consolidation of the three cases, and any new or other cases involving the same subject matter, into a single action for pretrial purposes. The court also appointed the Painters & Allied Trades District Council No. 35 Pension and Annuity Funds as the lead plaintiff. Discovery has not been undertaken as it is automatically stayed under the federal Private Securities Litigation Reform Act.

On February 27, 2015, BBSI received a letter from counsel for an alleged stockholder accusing each of the Company's directors and officers with having breached his fiduciary duties of loyalty and good faith based on the same facts as those alleged in the three lawsuits described above, as well as that certain officers and directors sold shares of BBSI common stock while in possession of material non-public information. The letter asserts that the Company has sustained and continues to sustain damages, including the costs and expenses incurred in connection with the Company's reserve strengthening process, reserve study and consultants, the cost of stock repurchases in October 2014, compensation paid to the Company's officers, and costs of negotiating the Company's credit facility with its principal lender. The letter demands that BBSI's Board of Directors take action against each of the Company's officers and directors to recover these damages and the proceeds of sales of stock by the officers and directors during 2013 and 2014. The letter states that if the Board does not take these actions within a reasonable period, the stockholder will commence a shareholder derivative action on behalf of the Company.

We intend to vigorously defend against the foregoing actions. We have not recorded any liabilities with respect to the claims in our audited consolidated financial statements included in Item 15 of this report. We believe that the claims are covered under our directors' and officers' liability insurance, and we have notified our insurance carriers of the claims. The insurers have responded by requesting additional information and by reserving their rights under the policies, including the right to deny coverage under various policy exclusions. Subject to their reservation of rights and the satisfaction of applicable deductibles, we expect to be reimbursed for substantially all legal fees relating to our defense of the claims.

**Item 4. MINE SAFETY DISCLOSURES**

Not Applicable

**EXECUTIVE OFFICERS OF THE REGISTRANT**

The following table identifies, as of March 16, 2015, each executive officer of the Company. Executive officers are elected annually and serve at the discretion of the Board of Directors.

<b>Name</b>	<b>Age</b>	<b>Principal Positions and Business Experience</b>	<b>Officer Since</b>
Michael L. Elich	49	President and Chief Executive Officer	2005
James D. Miller	51	Vice President-Finance, Treasurer and Secretary; Chief Financial Officer; Principal Accounting Officer	1994
Gregory R. Vaughn	59	Vice President and Assistant Secretary; Chief Operating Officer    Corporate Operations	1998
Gerald R. Blotz	45	Vice President, Chief Operating Officer    Field Operations	2014



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Michael L. Elich joined the Company in October 2001 as Director of Business Development. He was appointed Vice President and Chief Operating Officer in May 2005. He was appointed interim President and Chief Executive Officer in January 2011 upon the death of William W. Sherertz. Effective February 17, 2011, Mr. Elich was elected to serve on the Board of Directors and was made President and Chief Executive Officer. From 1995 to 2001, Mr. Elich served as Executive Vice President and Chief Operating Officer of Skills Resource Training Center, a staffing services company with offices in Oregon, Washington and Idaho that we acquired in 2004.

James D. Miller joined the Company in January 1994 as Controller. He was promoted to Vice President-Finance, Treasurer and Secretary, and Chief Financial Officer in June 2008. From 1991 to 1994, he was the Corporate Accounting Manager for Christensen Motor Yacht Corporation. Mr. Miller, a certified public accountant on inactive status, was employed by Price Waterhouse LLP, now known as PricewaterhouseCoopers LLP, from 1987 to 1991.

Gregory R. Vaughn joined the Company in July 1997 as Operations Manager. Mr. Vaughn was appointed Vice President in January 1998 and Chief Administrative Officer in February 2012. He was promoted to Chief Operating Officer-Corporate Operations in May 2014. Prior to joining Barrett, Mr. Vaughn was Chief Executive Officer of Insource America, Inc., a privately-held human resource management company headquartered in Portland, Oregon, for approximately one year. Mr. Vaughn has also held senior management positions with Sundial Time Systems, Inc., and Continental Information Systems, Inc. Previously, Mr. Vaughn was employed as a technology consultant by Price Waterhouse LLP, now known as PricewaterhouseCoopers LLP.

Gerald R. Blotz joined the Company in May 2002 as Area Manager of the San Jose branch office. Mr. Blotz was promoted to Vice President, Chief Operating Officer-Field Operations in May 2014. Prior to joining BBSI, Gerald was President and Chief Operating Officer of Protrades Connection, where he was instrumental in building Protrades to 44 offices in four states.

**Table of Contents****PART II****Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

Our common stock (the "Common Stock") trades on the Global Select Market segment of The Nasdaq Stock Market under the symbol "BBSI." At March 2, 2015, there were 23 stockholders of record and approximately 1,550 beneficial owners of the Common Stock.

The following table presents the high and low sales prices of the Common Stock and cash dividends paid for each quarterly period during the last two fiscal years, as reported by The Nasdaq Stock Market. The Company's debt covenants permit continuation of quarterly cash dividends up to \$0.22 per share so long as there is no default by the Company and payment would not cause a default. Any future determination as to the payment of dividends will be made at the discretion of the Board and will depend upon the Company's operating results, financial condition, capital requirements, general business conditions and such other factors as the Board deems relevant.

	High	Low	Cash Dividends Declared
<b>2013</b>			
First Quarter	\$ 53.27	\$ 38.15	\$ 0.13
Second Quarter	62.82	48.50	0.13
Third Quarter	73.49	48.08	0.13
Fourth Quarter	98.00	66.33	0.18
<b>2014</b>			
First Quarter	\$ 102.20	\$ 57.82	\$ 0.18
Second Quarter	63.19	41.96	0.18
Third Quarter	63.45	39.47	0.18
Fourth Quarter	45.38	18.25	0.22

The Company maintains a Board approved stock repurchase program which currently authorizes shares to be repurchased up to 3.0 million shares of the Company's stock from time to time in open market purchases. The following table summarizes information related to stock repurchases during the quarter ended December 31, 2014.

Month	Shares Repurchased	Average Price Per Share	Total Number of Shares Repurchased as Part of Publicly Announced Plan	Maximum Number of Shares that May Yet Be Repurchased Under the Plan
October	50,799	\$ 39.88	1,878,987	1,121,013
November	0	0	0	1,121,013
December	0	0	0	1,121,013
Total	50,799		1,878,987	

The following graph shows the cumulative total return at the dates indicated for the period from December 31, 2009, until December 31, 2014, for our Common Stock. The

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Nasdaq Composite Index, and a group of the Company's current peers in the staffing industry (the 2014 Peer Group). The 2014 Peer Group is comprised of five companies included in the peer group used to prepare the performance graph included in the Company's Form 10-K for the year ended December 31, 2014.

The stock performance graph has been prepared assuming that \$100 was invested on December 31, 2009, in our Common Stock, The Nasdaq Composite Index, and the 2014 Peer Group, and that dividends are reinvested. In accordance with the SEC's disclosure rules, the stockholder return for each company in the 2014 Peer Group indices has been weighted on the basis of market capitalization as of the beginning of each annual period shown. The stock price performance reflected in the graph may not be indicative of future price performance.

	12/09	12/10	12/11	12/12	12/13	12/14
<b>Barrett Business Services, Inc.</b>	<b>100.00</b>	<b>129.67</b>	<b>170.59</b>	<b>332.24</b>	<b>816.52</b>	<b>245.96</b>
<b>NASDAQ Composite</b>	<b>100.00</b>	<b>117.61</b>	<b>118.70</b>	<b>139.00</b>	<b>196.83</b>	<b>223.74</b>
<b>Peer Group</b>	<b>100.00</b>	<b>119.85</b>	<b>91.26</b>	<b>108.65</b>	<b>171.56</b>	<b>181.13</b>

**Members of Peer Group**

CDI Corp

Insperity Inc

Kelly Services Inc

Manpowergroup Inc

Robert Half International Inc

**Table of Contents****Item 6. SELECTED CONSOLIDATED FINANCIAL DATA**

The following selected consolidated financial data should be read in conjunction with the Company's financial statements and the accompanying notes listed in Item 8 of Part II, Financial Statements and Supplementary Data, and the information contained in Item 7 of Part II, Management's Discussion and Analysis of Financial Condition and Results of Operations. Historical results are not necessarily indicative of future results.

	Year Ended December 31,				
	2014	2013	2012	2011	2010
<b>(In thousands, except per share data)</b>					
Statement of operations:					
Revenues:					
Professional employer service fees	\$ 470,351	\$ 388,963	\$ 276,004	\$ 190,113	\$ 147,385
Staffing services	165,833	143,881	126,648	124,761	125,738
Total	636,184	532,844	402,652	314,874	273,123
Cost of revenues:					
Direct payroll costs	126,399	108,800	95,128	94,568	95,439
Payroll taxes and benefits	266,844	228,903	169,724	123,017	96,660
Workers' compensation	212,524	108,617	71,086	53,837	36,284
Total	605,767	446,320	335,938	271,422	228,383
Gross margin	30,417	86,524	66,714	43,452	44,740
Selling, general and administrative expenses	73,821	60,061	46,450	38,174	35,429
Depreciation and amortization	2,506	2,037	1,477	1,344	1,395
(Loss) income from operations	(45,910)	24,426	18,787	3,934	7,916
Other income (expense):					
Life insurance proceeds	0	0	0	10,000	0
Investment income, net	594	723	776	1,199	874
Interest expense	(173)	(238)	(76)	(25)	(25)
Other, net	152	(9)	(28)	47	1,162
Total	573	476	672	11,221	2,011
(Loss) income before income taxes	(45,337)	24,902	19,459	15,155	9,927
(Benefit from) provision for income taxes	(18,253)	7,010	6,328	837	2,574
Net (loss) income	(27,084)	17,892	13,131	14,318	7,353
Basic (loss) earnings per share	(3.78)	2.52	1.70	1.42	0.71
Weighted average number of basic shares outstanding	7,160	7,105	7,723	10,083	10,333
Diluted (loss) earnings per share	(3.78)	2.42	1.67	1.41	0.71
Weighted average number of diluted shares outstanding	7,160	7,397	7,863	10,150	10,372
Cash dividends per common share	0.76	0.57	0.46	0.38	0.33
Selected balance sheet data:					
Cash and marketable securities	62,431	119,253	72,394	81,844	61,356

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Working capital (deficit) surplus	(39,341)	64,421	28,142	49,639	44,563
Total assets	448,528	313,322	228,861	223,097	187,884
Long-term workers' compensation liabilities	161,933	76,603	45,266	30,596	21,847
Long-term debt, net of current portion	19,833	5,053	5,273	0	0
Stockholders' equity	38,658	72,553	53,896	101,655	95,365

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Management reached the conclusion in October 2014 that, based on actuarial methods, the estimate of workers' compensation liability should reflect a significant increase for the potential development of prior period claims. The Company recorded total workers' compensation claims expense of \$101.2 million during the third quarter of 2014, including a \$61.3 million change in estimate relating to prior period claims. For a detailed discussion, see Note 6 to the audited consolidated financial statements included in Item 15 of this Report.

## **Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **Overview**

The Company is a leading provider of business management solutions for small-and mid-sized companies. The Company has developed a management platform that integrates tools from the human resource outsourcing industry and knowledge-based approach from the management consulting industry. This platform, through the effective leveraging of human capital, assists our business owner clients in more effectively running their business.

We deliver the managerial resources and guidance of a large company to small and mid-sized businesses. Our professional employer service fees are generated from client services agreements with our clients; we enter into a co-employment arrangement in which we become the administrative employer and the client maintains care, custody and control of their operations. Revenues from client services agreements are recognized on a net basis in accordance with current accounting guidance for revenue recognition and principal/agent considerations. Consequently, service fee revenues represent the gross margin generated from our professional employer services after deducting the amounts invoiced to co-employed clients for direct payroll expenses such as salaries, wages, health insurance and employee out-of-pocket expenses incurred incidental to employment. These amounts are also excluded from cost of revenues. Our fees also include amounts invoiced to our clients for employer payroll-related taxes and workers' compensation coverage.

We generate staffing services revenues primarily from short-term staffing, contract staffing, on-site management and direct placement services. We recognize revenues from our staffing services for all amounts invoiced, including direct payroll, employer payroll-related taxes, workers compensation coverage and a service fee (equivalent to a mark-up percentage).

Through centralized operations at our headquarters in Vancouver, Washington, we prepare invoices weekly for our staffing services customers and following the end of each payroll processing cycle for clients under a client services agreement. We invoice our customers and clients as each payroll is processed. Payment terms for staffing customers are generally 30 days, while co-employed clients' invoices are generally due on the invoice date.

Our business is concentrated in California and we expect to continue to derive a majority of our revenues from this market in the future. Revenues generated in our California offices accounted for 77% of our total net revenues in 2014, 74% in 2013 and 69% in 2012. Consequently, any weakness in economic conditions or changes in the regulatory environments in California could have a material adverse effect on our financial results.

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Our cost of revenues is comprised of direct payroll costs for staffing services, employer payroll-related taxes and employee benefits and workers compensation. Direct payroll costs represent the gross payroll earned by staffing services employees based on salary or hourly wages. Payroll taxes and employee benefits consist of the employer's portion of Social Security and Medicare taxes, federal and state unemployment taxes, and staffing services employee reimbursements for materials, supplies and other expenses, which are paid by the customer.

Workers' compensation expense consists primarily of the costs associated with our self-insured workers' compensation program, such as claims reserves, claims administration fees, legal fees, state administrative agency fees and excess insurance costs for catastrophic injuries. We also maintain separate workers' compensation insurance policies for employees working in states where we are not self-insured.

The largest portion of workers' compensation expense is the cost of workplace injury claims. When an injury occurs and is reported to us, our respective independent TPA or our internal claims management personnel analyze the details of the injury and develop a case reserve, which becomes the estimate of the cost of the claim based on similar injuries and their professional judgment. We then record or accrue an expense and a corresponding liability based upon our estimate of the ultimate claim cost. As cash payments are made by our TPA against specific case reserves, the accrued liability is reduced by the corresponding payment amount. The TPA and our in-house claims administrators also review existing injury claims on an on-going basis and adjust the case reserves as new or additional information for each claim becomes available. Our reserve includes a provision both for future anticipated increases in costs (adverse loss development) of the claims reserves for open claims and for claims incurred but not reported related to prior and current periods (together IBNR). This provision for IBNR is based upon an actuarial estimate provided by our independent actuary. We believe our operational policies and internal claims reporting system help to limit the occurrence of unreported incurred claims.

Selling, general and administrative expenses represent both branch office and corporate-level operating expenses. Branch operating expenses consist primarily of branch office staff payroll and personnel related costs, advertising, rent, office supplies, professional and legal fees and branch incentive compensation. Corporate-level operating expenses consist primarily of executive and office staff payroll and personnel related costs, professional and legal fees, travel, occupancy costs, information systems costs and executive and corporate staff incentive compensation.

Depreciation and amortization represents depreciation of property and equipment and amortization of intangible assets consisting of the amortization of software costs, covenants not to compete, and if material, customer related intangibles. Property and equipment are depreciated using the straight-line method over their estimated useful lives, which generally range from two to thirty-nine years. Intangible assets are amortized using the straight-line method over their estimated useful lives, which range from two to ten years.

## **Critical Accounting Policies**

We have identified the following policies as critical to our business and the understanding of our results of operations. For a detailed discussion of the application of

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these and other accounting policies, see Note 1 to the audited consolidated financial statements included in Item 15 of this Report. Note that the preparation of this Annual Report on Form 10-K requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

**Self-Insured Workers' Compensation Reserves.** We are self-insured for workers' compensation coverage in a majority of our employee work sites in Oregon, Maryland, Delaware and Colorado and for staffing services and management employees only in Washington. We were self-insured in California through December 31, 2014 and now maintain individual policies for all California-based clients. Additionally, effective March 1, 2010, our employees working in Arizona were eligible for coverage through Ecole. The estimated liability for unsettled workers' compensation claims represents our best estimate, which includes an evaluation of information provided by our internal claims adjusters and our third-party claims administrators, coupled with management's use of an independent actuary. These elements serve as the basis for our overall estimate for workers' compensation claims liabilities, which include more specifically the following components: case reserve estimates for reported losses, plus additional amounts for estimated future development of reported claims and incurred but not reported claims (together IBNR). Our estimates also include 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.

Incurred but not reported ( IBNR ) is based upon an estimate of future claim payments beyond those considered in the specific case reserve estimates and claims arising from injuries that occurred during a particular time period on or prior to the balance sheet date. Therefore, IBNR is the compilation of the estimated ultimate losses for each accident year less amounts that have been paid and specific case reserves. IBNR reserves, unlike specific case reserves, do not apply to a specific claim, but rather apply to the entire body of claims arising from a specific time period. IBNR primarily provides for costs due to:

- 1) Future claim payments in excess of case reserves on recorded open claims;
- 2) Additional claim payments on closed claims; and
- 3) Claims that have been incurred but have not yet been reported to us.

Our workers' compensation claims liabilities do not represent an exact calculation of liability, but instead represent management's best estimate, generally utilizing actuarial expertise and projection techniques, at a given accounting date. The process of estimating unpaid claims and claim adjustment expense involves a high degree of judgment and is subject to a number of variables. These variables can be affected by both internal and external events, such as changes in claims handling and reserve estimation procedures, changes in individuals involved in the reserve estimation process, inflation, legal trends, and legislative changes.



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We use informed judgment throughout the process, derived from individual experiences and expertise applied to multiple sets of data and analysis. We consider all significant facts and circumstances known at the time loss reserves are established and as new facts and circumstances become known. Due to the inherent uncertainty underlying loss reserve estimates, including, but not limited to, the future settlement environment, final resolution of our estimated liability for our workers' compensation claims will likely be higher or lower than the related loss reserves at the reporting date. Therefore, actual paid losses, as specific claims are settled in the future, may be materially different in amount from our current loss reserves.

A basic premise in most actuarial analyses is that historical data and past patterns demonstrated in the incurred and paid historical data form a reasonable basis upon which to project future outcomes, absent a material change. To the extent a material change affecting the ultimate claim liability is known, such change is quantified to the extent possible through an analysis of internal company data and, if available and when appropriate, external data. Significant structural changes to the available data can materially impact the reserve estimation process. Actuaries exercise a considerable degree of judgment in the evaluation of these factors in their analysis of reserves. The application of actuarial judgment is unavoidable when faced with material uncertainty. Different actuaries may choose different assumptions when faced with such uncertainty, based on their individual backgrounds, professional experiences and the context in which they are reviewing the reserves. Hence, the estimates selected by different actuaries may differ materially from each other.

We believe that the amounts recorded for our estimated liabilities, which are based upon facts and other trends associated with the Company's historical universe of claims data, are reasonable and objective. Nevertheless, it is possible that adjustments to such estimates may be required in future periods if the development of claim costs varies materially from our estimates and such adjustments, if necessary, could be material to results of operations.

**Safety Incentives Liability.** Our accrued safety incentives represent cash incentives paid to certain clients under our client services agreement for maintaining safe-work practices in order to minimize workplace injuries. 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 expected payout as determined by historical incentive payment trends. The safety incentive expense is netted against PEO revenues on our consolidated statements of operations.

**Allowance for Doubtful Accounts.** We are required to make estimates of the collectability of accounts receivables. Management analyzes historical bad debts, customer concentrations, customer creditworthiness, current economic trends and changes in the customers' payment tendencies when evaluating the adequacy of the allowance for doubtful accounts. If the financial condition of our customers deteriorates, resulting in an impairment of their ability to make payments, additional allowances may be required.

**Goodwill.** We assess the recoverability of goodwill annually and whenever events or changes in circumstances indicate that the carrying value might be impaired. Factors that are

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considered include significant underperformance relative to expected historical or projected future operating results, significant negative industry trends and significant change in the manner of use of the acquired assets. Management's current assessment of the carrying value of goodwill indicates there was no impairment as of December 31, 2014. If these estimates or their related assumptions change in the future, we may be required to record impairment charges for these assets whenever events or circumstances occur indicating that goodwill might be impaired.

**Investments in Marketable Securities.** We consider available evidence in evaluating potential impairment of our investments, including the duration and extent to which fair value is less than cost and our ability and intent to hold the investment. Investments in securities classified as trading are reported at fair value, with unrealized gains or losses reported in other income in our consolidated statements of operations. Investments in securities classified as available-for-sale are reported at fair value, with unrealized gains or losses reported net of tax in accumulated other comprehensive (loss) income in stockholders' equity. In the event a loss on our available-for-sale investments is determined to be other-than-temporary, the loss will be recognized in our statement of operations. Investments in securities classified as held-to-maturity are reported at amortized cost.

**Income Taxes.** Our income taxes are accounted for using an asset and liability approach. This requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial statement and tax basis of assets and liabilities at the applicable tax rates. The determination of our provision for income taxes requires significant judgment, the use of estimates, and the interpretation and application of complex tax laws. Significant judgment is required in assessing the timing and amounts of deductible and taxable items and the probability of sustaining uncertain tax positions. The impact of uncertain tax positions would be recorded in our financial statements only after determining a more-likely-than-not probability that the uncertain tax positions would withstand challenge, if any, from taxing authorities. At December 31, 2014, we had deferred income tax assets of \$23.0 million and deferred tax liabilities of \$15.4 million for net deferred income tax assets of \$7.6 million. We assess the realization of the deferred income tax assets as significant changes in circumstances may require adjustments during future periods. The amount of the deferred income tax assets actually realized could vary, if there are differences in the timing or amount of future reversals of existing deferred income tax assets or changes in the actual amounts of future taxable income as compared to operating forecasts. If our operating forecast is determined to no longer be reliable due to uncertain market conditions, our long-term forecast may require reassessment. As a result, in the future, a valuation allowance may be required to be established for all or a portion of the deferred income tax assets. Such a valuation allowance could have a significant effect on our future results of operations and financial position.

## **Recent Accounting Pronouncements**

For a discussion of recent accounting pronouncements and their potential effect on the Company's results of operations and financial condition, refer to Note 1 in the Notes to the Consolidated Financial Statements beginning at page [F-8] of this Annual Report on Form 10-K.

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### **Forward-Looking Information**

Statements in this Item or in Items 1 and 1A of 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 acquisitions, the effect of changes in the Company's mix of services on gross margin, continued retention of customers following price increases, the adequacy of the Company's workers' compensation reserves and the effect of changes in estimate of its claims liabilities on its workers' compensation liability, the effect of changes in its reserving practices and claims management process on its actuarial estimates and workers' compensation reserves, the ability of the Company to generate sufficient taxable income in the future to utilize its deferred tax assets, the effect of changes in the interest rate environment on the value of the Company's investment securities and long-term debt, 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 insurance subsidiaries and becoming self-insured for certain business risks, the operation and cost of the Company's fronted insurance program with ACE in California, 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 Company's ability to retain current customers and attract new clients, economic trends in the Company's service areas, the potential for 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, difficulties associated with integrating acquired businesses and clients into the Company's operations, collectability 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 effect of conditions in the global capital markets on the Company's investment portfolio and the availability of capital, borrowing capacity on the Company's revolving credit facility, 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 or its fronted insurance program, 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.

**Table of Contents****Results of Operations**

The following table sets forth the percentages of total revenues represented by selected items in the Company's Consolidated Statements of Operations for the years ended December 31, 2014, 2013 and 2012, included in Item 15 of this report. References to the Notes to Financial Statements appearing below are to the notes to the Company's Consolidated Financial Statements included in Item 15 of this report.

	Percentage of Total Net Revenues Year Ended December 31,		
	2014	2013	2012
<b>Revenues:</b>			
Professional employer service fees	73.9%	73.0%	68.5%
Staffing services	26.1	27.0	31.5
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>Cost of revenues:</b>			
Direct payroll costs	19.9	20.4	23.6
Payroll taxes and benefits	41.9	43.0	42.1
Workers' compensation	33.4	20.4	17.7
<b>Total</b>	<b>95.2</b>	<b>83.8</b>	<b>83.4</b>
Gross margin	4.8	16.2	16.6
Selling, general and administrative expenses	11.6	11.2	11.5
Depreciation and amortization	0.4	0.4	0.4
(Loss) income from operations	(7.2)	4.6	4.7
Other income	0.1	0.1	0.1
(Loss) income before income taxes	(7.1)	4.7	4.8
(Benefit from) provision for income taxes	(2.8)	1.3	1.6
<b>Net (loss) income</b>	<b>(4.3)%</b>	<b>3.4%</b>	<b>3.2%</b>

We report PEO revenues on a net basis because we are not the primary obligor for the services provided by our co-employed clients to their customers pursuant to our client service agreements. We present for comparison purposes the gross revenues and cost of revenues information for the years ended December 31, 2014 and 2013 set forth in the table below. Although not in accordance with generally accepted accounting principles in the United States (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.

The presentation of revenues on a net basis and the relative contributions of staffing and PEO services revenues can create volatility in our gross margin percentage. The general impact of fluctuations in our revenue mix is described below.

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

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.



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reported in cost of sales. While staffing relationships typically have higher margins than co-employment relationships, an increase in staffing revenues and related costs presented at gross dilutes the impact of the net PEO services revenue on gross margin percentage.

(in thousands)	Year Ended December 31,	
	2014	2013
<b>Revenues:</b>		
Professional employer services	\$ 3,191,229	\$ 2,665,714
Staffing services	165,833	143,881
 Total revenues	 3,357,062	 2,809,595
 <b>Cost of revenues:</b>		
Direct payroll costs	2,827,732	2,369,282
Payroll taxes and benefits	266,844	228,903
Workers compensation	232,069	124,886
 Total cost of revenues	 3,326,645	 2,723,071
 Gross margin	 \$ 30,417	 \$ 86,524

A reconciliation of non-GAAP gross revenues to net revenues is as follows for the years ended December 31, 2014 and 2013 (in thousands):

	Gross Revenue Reporting Method		Reclassification		Net Revenue Reporting Method	
	2014	2013	2014	2013	2014	2013
<b>Revenues:</b>						
Professional employer services	\$ 3,191,229	\$ 2,665,714	\$ (2,720,878)	\$ (2,276,751)	\$ 470,351	\$ 388,963
Staffing services	165,833	143,881	0	0	165,833	143,881
 Total revenues	 \$ 3,357,062	 \$ 2,809,595	 \$ (2,720,878)	 \$ (2,276,751)	 \$ 636,184	 \$ 532,844
 <b>Cost of revenues:</b>	 \$ 3,326,645	 \$ 2,723,071	 \$ (2,720,878)	 \$ (2,276,751)	 \$ 605,767	 \$ 446,320

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

**Years Ended December 31, 2014 and 2013**

Net loss for 2014 amounted to \$27.1 million as compared to net income of \$17.9 million for 2013. Net loss in 2014 was primarily driven by the Company's recording of an incremental \$61.3 million to its self-insured workers' compensation reserve as a result of a change in estimate relating to prior period claims during the third quarter of 2014. Diluted loss per share for 2014 was \$3.78 compared to a diluted income per share of \$2.42 for 2013.

Revenues for 2014 totaled \$636.2 million, an increase of approximately \$103.3 million or 19.4%, which reflects an increase in both the Company's professional employer service fee revenue and staffing services revenue. Professional employer service fee revenue increased approximately \$81.4 million or 20.9% over 2013, primarily from continued strength

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in our referral channels as business from new customers during 2014 nearly doubled our lost business from former customers. Professional employer service revenue from continuing customers grew 8.9% on a year-over-year basis, primarily resulting from increases in employee headcount and hours worked. Staffing services revenue increased approximately \$22.0 million or 15.3% over 2013 due to growth in new customers as well as the addition of new business, partially offset by lost business from former customers. Approximately 77% and 74%, respectively, of our total net revenues during 2014 and 2013 was attributable to our California operations.

During 2014, the Company served approximately 3,665 co-employment clients, which compares to approximately 3,200 co-employment clients during 2013. During 2014, the Company served approximately 1,825 staffing services customers, which compares to 1,870 during 2013.

Gross margin for 2014 totaled approximately \$30.4 million, which represented a decrease of \$56.1 million or 64.8% from 2013, primarily due to an increase in workers' compensation expense as a percentage of revenues, partially offset by an increase in revenues of 19.4% and a decline in payroll taxes and benefits and direct payroll costs as a percentage of revenues. The gross margin percent decreased from 16.2% of revenues for 2013 to 4.8% for 2014.

Workers' compensation expense, in terms of dollars and as a percentage of revenues, increased from \$108.6 million or 20.4% in 2013 to \$212.5 million or 33.4% in 2014. The percentage rate increase was primarily due to the Company's recording of an incremental \$61.3 million to its self-insured workers' compensation reserve as a result of a change in estimate relating to prior period claims at September 30, 2014.

The Company has provided a total of \$216.0 million and \$112.4 million at December 31, 2014 and 2013, respectively, as an estimated future liability for unsettled workers' compensation claims liabilities. The estimated liability for unsettled workers' compensation claims represents management's best estimate based upon an actuarial valuation provided by a third party actuary at December 31, 2014 and 2013. 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.

We have undertaken a number of steps during the past two years to improve our workers' compensation claims administration practices. These steps include hiring additional claim administrators in response to our business growth, and working to close litigated claims more quickly.

Beginning in late 2013, as part of our efforts to improve our claims handling practices, the Company initiated a specific case reserve study on its open workers' compensation claims with injury dates in 2012 and earlier. The specific case reserve study resulted in moving dollars from the general IBNR reserve for unreported claims and future loss development of known claims into specific case reserves for individual claims. This

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process was intended to provide management with a more accurate estimate of the ultimate total cost of each claim at a detailed level. Management believes that this change in process provides better information to our claims management personnel to evaluate and close historical and future claims at lower ultimate total costs than our historical practices.

Additionally, in mid-2013, the Company initiated a change to its individual claim handling practices by recording specific case reserves on new claims at amounts that include all of the anticipated future costs and working to close claims more quickly with the goal of reducing the ultimate total cost of the claims. Previously, the Company had litigated claims more often, but determined that this practice often resulted in a higher total cost to resolve claims.

While management believes that the changes in the claims handling process are having the intended result of lowering the ultimate total cost per claim, we became aware, during the second quarter of 2014, that these combined initiatives were causing a disruption of the historical incurred and paid trends within our claims data from an actuarial perspective.

In May 2014, the Company engaged an actuarial consultant to assist management in studying selected historical claims experience and the impact of the change in its claims handling process. During the third quarter of 2014, the Company engaged a new actuary to assist management in determining its best estimate of the Company's workers' compensation liability. Based on the work of the new actuary and a thorough review of the Company's claims handling practices and the results of the work performed by the actuarial consultant engaged during the second quarter of 2014, management reached the conclusion in October 2014 that, based on actuarial methods, the estimate of workers' compensation liability should reflect a significant increase for the potential development of prior period claims. We believe this change in estimate resulted primarily from the structural changes to the available claims data described above and generated a total workers' compensation claims expense accrual of \$101.2 million for the third quarter of 2014, including a \$61.3 million change in estimate relating to prior period claims. Management's primary considerations in arriving at its estimate of workers' compensation liability include the significant increase in the Company's business in recent years, the potential for unexpected future adverse development of open claims, and the increasing complexity and uncertainty surrounding healthcare costs.

In September 2012, California Senate Bill 863 ( SB 863 ) was signed into law. Under SB 863, the California Director of Self-Insurance was ordered not to issue certificates of consent to self-insure after January 1, 2013 to any employer engaged in the activities of a professional employer organization, a leasing employer, a temporary services employer or any employer the Director determines to be in the business of providing employees to other employers. Additionally, the Director was required to revoke any previously issued certificate of consent to self-insure in favor of any employer engaged in these types of activities not later than January 1, 2015. To address this issue, BBSI entered into an arrangement typically known as a fronted program with ACE Group. Under this arrangement, the risk of loss up to the first \$5.0 million per claim is retained by BBSI through an indemnity agreement, although ACE is responsible for any claims BBSI is unable to satisfy. In addition, ACE continues to be BBSI's carrier for costs in excess of \$5.0 million per claim. All of BBSI's California clients were transitioned to ACE policies prior to the December 31, 2014 deadline. We expect to offset the increased costs of the fronted program and the increase in the loss accrual rate described above through price increases to selected customers.



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The decrease in payroll taxes and benefits, as a percentage of revenues, from 43.0% for 2013 to 41.9% for 2014, was primarily due to optimizing the use of prior wages applied against the state unemployment taxable wage basis as new PEO customers are brought on board and to a slight rise in the overall average wage rates which allowed the tax ceilings to be reached sooner in 2014 as compared to 2013. The decrease in direct payroll costs, as a percentage of revenues, from 20.4% for 2013 to 19.9% for 2014 was primarily due to the increase in our mix of PEO services in the Company's customer base compared to 2013 and the effect of each customer's unique mark-up percent. We expect gross margin as a percentage of total revenues to continue to be influenced by fluctuations in the mix between staffing and PEO services, as well as changes to our estimates for workers' compensation claims liabilities, as necessary.

Selling, general and administrative (SG&A) expenses consist of compensation and other expenses relating to the operation of our headquarters and our branch offices and the marketing of our services. SG&A expenses for 2014 amounted to approximately \$73.8 million, an increase of \$13.8 million or 22.9% over 2013. The increase was primarily attributable to an increase in management payroll, information technology (IT) expenses, and other variable expense components within SG&A to support our business growth. The increased IT expenses relate to projects designed to enhance access and delivery of information to the field as well as to improve efficiencies over time. SG&A expenses, as a percentage of revenues, increased from 11.2% in 2013 to 11.6% in 2014.

Other income for 2014 was \$573,000 compared to other income of \$476,000 for 2013. Other income for 2014 was primarily attributable to investment income earned on the Company's cash and marketable securities.

Our effective income tax rate for 2014 was (40.3)% reflecting our loss from operations, as compared to 28.2% for 2013. Our income tax rate typically differs from the federal statutory tax rate of 35% primarily due to federal employment tax credits and state tax expense, net of federal benefit. See Note 10 in the Notes to the Consolidated Financial Statements on page F-26 of this Annual Report on Form 10-K regarding income taxes; for additional information.

The Company has established a valuation allowance for certain deferred tax assets due to uncertainties regarding the Company's ability to generate future taxable investment gains in order to utilize certain investment impairment losses and investment loss carry forwards for tax purposes. The realization of a significant portion of net deferred tax assets is based in part on our estimates of the timing of reversals of certain temporary differences and on the generation of taxable income before such reversals. At December 31, 2014, we maintained a valuation allowance for approximately \$1.1 million of federal and state tax benefits that are not expected to be utilized.

Under ASC 740, Income Taxes, management evaluates the realizability of the deferred tax assets on a quarterly basis under a more-likely than not standard. As part of this evaluation, management reviews all evidence both positive and negative to determine if a valuation allowance is needed. One component of this analysis is to determine whether the Company was in a cumulative loss position for the most recent 12 quarters. Despite the increase to the workers' compensation reserve in the third quarter of 2014, the Company was in a cumulative income position for the 12 quarters ended December 31, 2014.

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Management's review of positive evidence included the existence of federal and California taxable income in eligible carryback years, reversal of temporary items and projection of future taxable income. The projection of future taxable income was a significant factor in management's determination that no additional valuation allowance was required at December 31, 2014. Management's projections of taxable income are based on the existence of signed annual contracts with the Company's PEO customer base, objective evidence that the Company's customers are retained at a rate in excess of 90% over long periods, and objective evidence that recent price increases are being accepted by the Company's customer base.

Management has continued to improve the Company's procedures in many areas of its self-insured workers' compensation program over the past two years; see Note 6 to the audited consolidated financial statements included in Item 15 of this Report. The results of these efforts have improved management's ability to project workers' compensation expense. Management will monitor the need for an additional valuation allowance at each quarter in the future and, if the negative evidence outweighs the positive evidence, an allowance will be recorded.

### **Years Ended December 31, 2013 and 2012**

Net income for 2013 amounted to \$17.9 million, as compared to net income of \$13.1 million for 2012. Net income in 2013 was primarily driven by a 32.3% increase in revenues. Diluted income per share for 2013 was \$2.42 compared to a diluted income per share of \$1.67 for 2012. 2013 reflected nearly 500,000 fewer diluted common shares outstanding compared to 2012 primarily due to the Company's repurchase of approximately 2.5 million shares from the Estate of William W. Sherertz, as well as 500,000 shares from Nancy Sherertz, on March 28, 2012.

Revenues for 2013 totaled \$532.8 million, an increase of approximately \$130.2 million or 32.3%, which reflects an increase in both the Company's PEO service fee revenue and staffing services revenue. PEO service fee revenue increased approximately \$113.0 million or 40.9% over 2012 primarily due to growth in new customers as co-employment based business from new customers during 2013 tripled our lost PEO business from former customers. PEO service revenue from continuing customers grew 10.2% on a year-over-year basis, primarily resulting from increases in employee headcount and hours worked. Staffing services revenue increased approximately \$17.2 million or 13.6% over 2012 due to growth in new customers, as well as an increase in revenue from existing customers. Approximately 74% and 69%, respectively, of our total net revenues during 2013 and 2012 was attributable to our California operations.

During 2013, the Company served approximately 3,200 co-employment clients, which compares to approximately 2,910 co-employment clients during 2012. During 2013, the Company served approximately 1,870 staffing service customers, which compares to 1,850 during 2012.

Gross margin for 2013 totaled approximately \$86.5 million, which represented an increase of \$19.8 million or 29.7% over 2012, primarily due to the 32.3% increase in revenues.

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and a decline in direct payroll costs as a percentage of revenues, partially offset by higher payroll taxes and benefits and workers' compensation expense as a percentage of revenues. The gross margin percent decreased from 16.6% of revenues for 2012 to 16.2% for 2013. The increase in payroll taxes and benefits, as a percentage of revenues, from 42.1% for 2012 to 43.0% for 2013, was principally due to a relative shift in business mix to PEO services, with payroll taxes and benefits presented at gross cost, while 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 operated in 2013 as compared to 2012. Workers' compensation expense for 2013 totaled \$108.6 million, which compares to \$71.1 million for 2012. Workers' compensation expense, as a percent of revenues, increased from 17.7% in 2012 to 20.4% in 2013. The increase in the percentage rate was primarily driven by an increase in the provision for claim costs related to current year claims and increases in the estimated costs to close prior year claims and higher insurance broker commissions resulting from increased workers' compensation insurance rates. The decrease in direct payroll costs, as a percentage of revenues, from 23.6% for 2012 to 20.4% for 2013 was primarily due to the increase in our mix of PEO services in the Company's customer base compared to 2012 and the effect of each customer's unique mark-up percent.

SG&A expenses for 2013 amounted to approximately \$60.1 million, an increase of \$13.6 million or 29.3% over 2012. The increase was primarily attributable to an increase in management payroll and other variable expense components within SG&A to support our business growth and to higher incentive pay based on increased branch performance. SG&A expenses, as a percentage of revenues, decreased from 11.5% in 2012 to 11.2% in 2013.

Other income for 2013 was \$476,000 compared to other income of \$672,000 for 2012. Other income for 2013 was primarily attributable to investment income earned on the Company's cash and marketable securities.

Our effective income tax rate for 2013 was 28.2%, as compared to 32.5% for 2012. Our income tax rate typically differs from the statutory tax rate of 39.0% primarily due to federal and state employment tax credits.

## **Fluctuations in Quarterly Operating Results**

We have historically experienced significant fluctuations in our quarterly operating results and expect such fluctuations to continue in the future. Our 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 for our services and competition and the effect of acquisitions. Payroll taxes, as a component of cost of revenues, generally decline throughout a calendar year as the applicable statutory wage bases for federal and state unemployment taxes and Social Security taxes are exceeded on a per employee basis. Our revenue levels may be higher in the third quarter due to the effect of increased business activity of our customers' businesses in the agriculture, food processing and forest products-related industries. In addition, revenues in the fourth quarter may be affected by many customers' practice of operating on holiday-shortened schedules. 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. In addition, adverse loss development of prior period claims during a subsequent quarter may also contribute to the volatility in the Company's estimated worker's compensation expense.

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### **Liquidity and Capital Resources**

The Company's cash position of \$11.5 million at December 31, 2014 decreased \$82.0 million compared to December 31, 2013, which compares to an increase of \$47.8 million for the year ended December 31, 2013. The decrease in cash at December 31, 2014, as compared to December 31, 2013, was primarily due to a net loss of \$27.1 million, purchases of restricted certificates of deposits of \$101.5 million, net purchases of \$51.1 million of restricted marketable securities, net purchases of \$25.2 million of marketable securities, increases in trade accounts receivable, income taxes receivable and deferred income taxes of \$38.0 million, and dividends paid of \$5.4 million, partially offset by increases in workers' compensation claims liabilities of \$103.5 million, accrued payroll, payroll taxes and related benefits of \$27.6 million, and proceeds of \$40.0 million from the issuance of long-term debt.

Net cash provided by operating activities for 2014 amounted to \$69.6 million, as compared to net cash provided by operating activities of \$70.2 million for 2013. For 2014, cash flow was primarily provided by an increase in workers' compensation claims liabilities of \$103.5 million and accrued payroll, payroll taxes and related benefits of \$27.6 million, partially offset by a net loss of \$27.1 million, and increases in trade accounts receivable of \$17.0 million, income taxes receivable of \$11.4 million and deferred income taxes of \$9.5 million.

Net cash used in investing activities totaled \$182.5 million for 2014, compared to net cash used in investing activities of \$17.4 million for 2013. For 2014, cash used in investing activities was primarily used for purchases of restricted certificates of deposits of \$101.5 million, purchases of restricted marketable securities of \$61.6 million, purchases of marketable securities of \$38.4 million, and purchases of property and equipment of \$4.6 million, partially offset by proceeds from sales and maturities of marketable securities of \$13.2 million and proceeds from maturities of restricted marketable securities of \$10.5 million. The Company presently has no material long-term capital commitments.

The Company's investment policy strictly defines the types and quantities of investments that can be made by its investment brokers. The general parameters of our investment policy are as follows:

We make investments in highly rated instruments to reduce our investment risk. Short-term instruments (maturity of less than one year) must be obligations of issuers rated A2/P2 or better by two National Recognized Statistical Rating Organizations. Long-term instruments (maturities greater than one year) must be obligations of issuers rated BBB-/Baa3 or better by two National Recognized Statistical Rating Organizations.

No more than 5% of our investment portfolio is invested in any one issuer (excluding U.S. Treasury obligations and Federal Agency obligations including Government Sponsored Enterprises).

To monitor our overall investment risk and to assess the fair values of assets within our investment portfolio, we review our investment portfolio on a quarterly basis for significant unrealized gains or losses. We define significant to be in excess of 5% of cost basis. When we identify significant unrealized gains or losses, we inquire as to the reasons with our investment advisors.

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Net cash provided by financing activities for 2014 was \$30.9 million compared to net cash used in financing activities of \$5.0 million for 2013. For 2014 the primary sources of cash provided by financing activities was \$40.0 million from the issuance of long-term debt, partially offset by the payment of regular quarterly cash dividends totaling \$5.4 million to holders of the Company's common stock and the repurchase of common stock for \$3.7 million.

The Company's business strategy continues to focus on growth through the expansion of operations at existing branch offices, together with the possibility of selective acquisition of additional personnel-related businesses, 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.

As disclosed in Note 7 to the Consolidated Financial Statements in this Report, effective December 29, 2014, the Company entered into a new credit agreement (the "Agreement") with its principal bank, Wells Fargo Bank, National Association (the "Bank"). The Agreement, provides for a \$40.0 million term loan maturing December 31, 2016, as well as a \$14.0 million revolving credit line, with a \$5.0 million sublimit for unsecured standby letters of credit. The Company had no outstanding borrowings on its revolving credit line at December 31, 2014. The Agreement also provides for an increase to a total of \$114.3 million in cash-secured letters of credit to satisfy collateral requirements associated with various surety deposit requirements for workers' compensation purposes in the state of California. In conjunction with the letter of credit, the Company posted \$114.3 million of certificates of deposit with Wells Fargo as collateral and is included in long-term assets on the consolidated balance sheet. The Agreement includes a non-refundable commitment fee of \$400,000, which is reported within prepaid expenses and other on the Company's consolidated balance sheet. The fee will be amortized to interest expense ratably over the term of the loan.

The \$40.0 million term loan with the Bank requires payments of \$3.0 million on June 30, 2015, \$7.0 million on September 30, 2015, \$15.0 million on December 31, 2015, \$5.0 million on June 30, 2016 and \$5.0 million on September 30, 2016. The term loan bears interest at the one month LIBOR plus 4.0%.

Advances under the revolving credit facility bear interest, as selected by the Company of either (a) a daily floating rate of one month LIBOR plus 2% or (b) a fixed rate of LIBOR plus 2.0%. The Agreement also provides for an unused commitment fee of 0.35% per year on the average daily unused amount of the revolving credit facility, and a fee of 1.75% of the face amount of each letter of credit.

The states of California, Oregon, Maryland, Washington, Delaware and Colorado require us to maintain specified investment balances or other financial instruments, totaling \$198.5 million at December 31, 2014 to cover potential workers compensation claims losses related to the Company's status as a self-insured employer. In partial satisfaction of these requirements, at December 31, 2014, we have provided surety bonds and standby letters of credit totaling \$194.9 million. The State of California requires the Company to maintain a surety deposit of \$190.6 million (which is included in the total \$194.9 million of surety bonds and standby letters of credit), which the Company satisfied through the posting of third party issued surety bonds, backed by a total of \$114.3 million in letters of credit. In conjunction with these letters of credit, the Company posted \$114.3 million of certificates of deposit with Wells Fargo as collateral.

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Management expects future amounts of the certificates of deposit and the letters of credit to decrease as a result of a declining self-insured liability as the Company's ability to self-insure in California ended December 31, 2014. Consequently, management expects the Company's working capital position to improve in future quarters as the related collateral requirements ease.

The credit facility is collateralized by the Company's accounts receivable and other rights to receive payment, general intangibles, inventory and equipment.

The Agreement requires the satisfaction of certain financial covenants as follows:

minimum Fixed Charge Coverage ratio of no less than 1.5:1.0, measured quarterly on a rolling four-quarter basis; and

ratio of restricted and unrestricted cash and marketable securities to workers' compensation and safety incentive liabilities of at least 1.0:1.0, measured quarterly;

The Agreement includes certain additional covenants as follows:

capital expenditures may not exceed a total of \$5.0 million in 2015 and of \$4.0 million in 2016 without the Bank's prior approval;

prohibition on incurring additional indebtedness without the prior approval of the Bank, other than up to \$200,000 per year in purchase money financing and the aggregate of all purchase money indebtedness does not exceed \$400,000 at any time;

prohibition on repurchases of the Company's common stock;

continuation of quarterly cash dividends up to \$0.22 per share so long as there is no default by the Company and payment would not cause a default.

The Agreement also contains customary events of default. If an event of default under the Agreement occurs and is continuing, the Bank may declare any outstanding obligations under the Agreement to be immediately due and payable. The Company was in compliance with all applicable financial covenants at December 31, 2014.

Additionally, the Company maintains a term loan with the Bank with a current balance of approximately \$5.1 million secured by the Company's corporate office building in Vancouver, Washington. The term loan requires payment of monthly installments of \$18,375, bearing interest at the one month LIBOR plus 2.25%, with the unpaid principal balance due November 1, 2017.

The Company is self-insured for certain business insurance risks such as general liability, errors and omissions and umbrella coverage. Management may explore in the future whether to pursue other vehicles to provide coverage including coverages provided by the Company's captive insurance companies.

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

**Table of Contents****Contractual Obligations**

The Company's contractual obligations as of December 31, 2014, including commitments for future payments under non-cancelable lease arrangements, long-term workers' compensation liabilities for catastrophic injuries, long-term debt, and other long-term liabilities, are summarized below:

(in thousands)	Total	Payments Due by Period			
		Less than 1 year	1 - 3 years	4 - 5 years	After 5 years
Operating leases	\$ 10,684	\$ 3,502	\$ 5,107	\$ 2,015	\$ 60
Long-term workers' compensation claims liabilities for catastrophic injuries	271	53	59	51	108
Long-term debt	45,053	25,220	19,833	0	0
Total contractual cash obligations	\$ 56,008	\$ 28,775	\$ 24,999	\$ 2,066	\$ 168

**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 7A. 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 and its outstanding borrowings on its line of credit and long-term debt. As of December 31, 2014, the Company's investment portfolio consisted principally of approximately \$137.6 million in certificates of deposit, \$50.1 million in money market funds, \$21.7 million in variable rate demand notes, \$8.2 million in municipal bonds and \$5.7 million in corporate bonds. The Company's outstanding long-term debt totaled approximately \$45.1 million at December 31, 2014. Based on the Company's overall interest exposure at December 31, 2014, 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, its outstanding borrowings or its results of operations because of the predominantly short maturities of the securities within the investment portfolio and the relative size of the outstanding borrowings.

**Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The financial statements and notes thereto required by this item begin on page F-1 of this report, as listed in Item 15.

**Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

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### **Item 9A. CONTROLS AND PROCEDURES**

#### **Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e) as of December 31, 2014 in connection with the filing of this Annual Report on Form 10-K. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of December 31, 2014, our disclosure controls and procedures were effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in rules and forms of the SEC and is accumulated and communicated to our management as appropriate to allow timely decisions regarding required disclosure.

#### **Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining for our Company adequate internal control over financial reporting as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2014. This evaluation was based on the framework established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ( COSO ).

Based upon this evaluation and the criteria noted above, management has concluded that, as of December 31, 2014, our internal control over financial reporting was effective.

The effectiveness of our internal control over financial reporting as of December 31, 2014 has been audited by Moss Adams LLP, the Company's independent registered public accounting firm, as stated in their report which appears on page F-1 of Item 15 in this Annual Report on Form 10-K.

#### **Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting during the fourth quarter of 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### **Inherent Limitations**

Control systems, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control systems objectives are being met. Further, the design of any control systems must reflect the fact that there are resource constraints, and the benefits of all controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our Company have been detected. These inherent limitations include the realities that judgments in decision making can be faulty and that breakdowns can occur because of simple errors or mistakes. Control systems can also be circumvented by the individual acts of some persons,



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by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

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**Item 9B. OTHER INFORMATION**

None.

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**PART III**

**Item 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Information required by this Item 10 concerning directors and executive officers of the Company appears under the heading Executive Officers of the Registrant on page 19 of this report or is incorporated into this report by reference to the Company's definitive Proxy Statement for its 2015 Annual Meeting of Stockholders to be filed within 120 days of the Company's fiscal year end of December 31, 2014 (the Proxy Statement). The additional required information is included under the following headings of the Proxy Statement; Item 1 Election of Directors, Stock Ownership by Principal Stockholders and Management Section 16(a) Beneficial Ownership Reporting Compliance, and Code of Ethics.

**Audit Committee**

The Company has a separately-designated standing audit committee established in accordance with Section 3(a)(58)(A) of the Exchange Act known as the Audit and Compliance Committee. The members of the Audit and Compliance Committee are Thomas J. Carley, chairman, James B. Hicks, Ph.D., and Roger L. Johnson, each of whom is independent as that term is used in Nasdaq listing standards applicable to the Company.

**Audit Committee Financial Expert**

The Company's Board of Directors has determined that Thomas J. Carley, an audit committee member, qualifies as an audit committee financial expert as defined by Item 407(d)(5) of Regulation S-K under the Exchange Act and is independent as that term is defined for audit committee members in Nasdaq listing standards applicable to the Company.

**Item 11. EXECUTIVE COMPENSATION**

Information required by this Item 11 concerning executive and director compensation and participation of compensation committee members is incorporated into this report by reference to the Proxy Statement, in which required information is included under the headings Director Compensation for 2014 and Executive Compensation.

**Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information required by this Item 12 concerning the security ownership of certain beneficial owners and management is incorporated into this report by reference to the Proxy Statement, in which required information is set forth under the headings Stock Ownership of Principal Stockholders and Management Beneficial Ownership Table and Additional Equity Compensation Plan Information.

**Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

Information required by this Item 13 concerning certain relationships and related transactions and director independence is incorporated into this report by reference to the

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Proxy Statement, in which required information is included under the headings Item 1 Election of Directors and Related Person Transactions.

**Item 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

Information required by this Item 14 concerning fees paid to our accountants is incorporated into this report by reference to the Proxy Statement, in which required information is included under the heading Matters Relating to Our Independent Registered Public Accounting Firm.

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**PART IV**

**Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

**Financial Statements and Schedules**

The Financial Statements, together with the report thereon of Moss Adams LLP, are included on the pages indicated below:

	<b>Page</b>
<u>Report of Independent Registered Public Accounting Firm Moss Adams LLP</u>	F-1
<u>Consolidated Balance Sheets as of December 31, 2014 and 2013</u>	F-3
<u>Consolidated Statements of Operations for the Years Ended December 31, 2014, 2013 and 2012</u>	F-4
<u>Consolidated Statements of Comprehensive (Loss) Income for the Years Ended December 31, 2014, 2013 and 2012</u>	F-5
<u>Consolidated Statements of Stockholders Equity for the Years Ended December 31, 2014, 2013 and 2012</u>	F-6
<u>Consolidated Statements of Cash Flows for the Years Ended December 31, 2014, 2013 and 2012</u>	F-7
<u>Notes to Consolidated Financial Statements</u>	F-8

No schedules are required to be filed herewith.

**Exhibits**

Exhibits are listed in the Exhibit Index that follows the signature page of this report.

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders

Barrett Business Services, Inc.

We have audited the accompanying consolidated balance sheets of Barrett Business Services, Inc. and subsidiaries ( the Company ) as of December 31, 2014 and 2013, and the related consolidated statements of operations, comprehensive (loss) income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2014. We also have audited the Company's internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting located in Item 9A. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with the authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Barrett Business Services, Inc. and subsidiaries as of December 31, 2014 and 2013, and the consolidated results of its operations and its cash flows for

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each of the three years in the period ended December 31, 2014, in conformity with generally accepted accounting principles in the United States of America. Also in our opinion, Barrett Business Services, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

/s/ Moss Adams LLP

Portland, Oregon

March 16, 2015

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**Table of Contents****Barrett Business Services, Inc.**

## Consolidated Balance Sheets

December 31, 2014 and 2013

(In Thousands, Except Par Value)

	2014	2013
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 11,544	\$ 93,557
Marketable securities	29,957	19,787
Trade accounts receivable, net	102,627	85,586
Income taxes receivable	11,421	0
Prepaid expenses and other	3,813	3,026
Restricted marketable securities and workers' compensation deposits	3,776	0
Deferred income taxes	15,791	8,929
Total current assets	178,929	210,885
Marketable securities	20,930	5,909
Property, equipment and software, net	22,675	20,549
Restricted certificates of deposit	114,335	12,789
Restricted marketable securities and workers' compensation deposits	58,533	11,205
Other assets	1,881	1,864
Workers' compensation receivables for insured losses and recoveries	3,425	2,301
Goodwill	47,820	47,820
	\$ 448,528	\$ 313,322
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$ 25,220	\$ 220
Accounts payable	2,719	3,252
Accrued payroll, payroll taxes and related benefits	120,133	92,516
Income taxes payable	0	1,236
Other accrued liabilities	1,917	313
Workers' compensation claims liabilities	54,049	35,841
Safety incentives liability	14,232	13,086
Total current liabilities	218,270	146,464
Long-term workers' compensation claims liabilities	161,933	76,603
Long-term debt	19,833	5,053
Deferred income taxes	8,159	10,787
Customer deposits and other long-term liabilities	1,675	1,862
Commitments and contingencies (Notes 7, 9 and 13)		
Stockholders' equity:		
Common stock, \$.01 par value; 20,500 shares authorized, 7,126 and 7,165 shares issued and outstanding	71	72
Additional paid-in capital	4,410	5,781
Accumulated other comprehensive loss	(23)	(26)
Retained earnings	34,200	66,726



38,658	72,553
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\$ 448,528	\$ 313,322
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The accompanying notes are an integral part of these financial statements.

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**Table of Contents****Barrett Business Services, Inc.**

## Consolidated Statements of Operations

Years Ended December 31, 2014, 2013 and 2012

(In Thousands, Except Per Share Amounts)

	2014	2013	2012
Revenues:			
Professional employer service fees	470,351	388,963	276,004
Staffing services	165,833	143,881	126,648
	636,184	532,844	402,652
Cost of revenues:			
Direct payroll costs	126,399	108,800	95,128
Payroll taxes and benefits	266,844	228,903	169,724
Workers compensation	212,524	108,617	71,086
	605,767	446,320	335,938
Gross margin	30,417	86,524	66,714
Selling, general and administrative expenses	73,821	60,061	46,450
Depreciation and amortization	2,506	2,037	1,477
(Loss) income from operations	(45,910)	24,426	18,787
Other income (expense):			
Investment income	594	723	776
Interest expense	(173)	(238)	(76)
Other	152	(9)	(28)
	573	476	672
(Loss) income before income taxes	(45,337)	24,902	19,459
(Benefit from) provision for income taxes	(18,253)	7,010	6,328
Net (loss) income	(27,084)	17,892	13,131
Basic (loss) earnings per share	(3.78)	2.52	1.70
Weighted average number of basic shares outstanding	7,160	7,105	7,723
Diluted (loss) earnings per share	(3.78)	2.42	1.67
Weighted average number of diluted shares outstanding	7,160	7,397	7,863
Cash dividends per common share	0.76	0.57	0.46

The accompanying notes are an integral part of these financial statements.

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**Barrett Business Services, Inc.**

Consolidated Statements of Comprehensive (Loss) Income

Years Ended December 31, 2014, 2013 and 2012

(In Thousands)

	For the year ended December 31,		
	2014	2013	2012
Net (loss) income	(27,084)	17,892	\$ 13,131
Unrealized gains (losses) on marketable securities, net of tax of \$3, (\$31), and \$36 in 2014, 2013 and 2012, respectively	3	(49)	57
Comprehensive (loss) income	\$ (27,081)	\$ 17,843	\$ 13,188

The accompanying notes are an integral part of these financial statements.

**Table of Contents****Barrett Business Services, Inc.**

## Consolidated Statements of Stockholders' Equity

Years Ended December 31, 2014, 2013 and 2012

(In Thousands)

	Common Stock		Additional	Accumulated Other Comprehensive	Retained	Total
	Shares	Amount	Paid-in Capital	(Loss) Income	Earnings	
Balance, December 31, 2011	9,871	\$ 99	\$ 20,943	\$ (34)	\$ 80,647	101,655
Common stock issued on exercise of options	132	1	1,844	0	0	1,845
Share based compensation expense, net of tax	0	0	695	0	0	695
Excess tax benefits from share-based compensation	0	0	295	0	0	295
Company repurchase of common stock	(2,986)	(30)	(22,864)	0	(37,338)	(60,232)
Cash dividends on common stock	0	0	0	0	(3,550)	(3,550)
Unrealized holding gains on marketable securities, net of tax	0	0	0	57	0	57
Net income	0	0	0	0	13,131	13,131
Balance, December 31, 2012	7,017	\$ 70	\$ 913	\$ 23	\$ 52,890	\$ 53,896
Common stock issued on exercise of options and vesting of restricted stock units	148	2	1,858	0	0	1,860
Common stock repurchased on vesting of restricted stock units	0	0	(89)	0	0	(89)
Share based compensation expense, net of tax	0	0	1,016	0	0	1,016
Excess tax benefits from share-based compensation	0	0	2,083	0	0	2,083
Cash dividends on common stock	0	0	0	0	(4,056)	(4,056)
Unrealized holding losses on marketable securities, net of tax	0	0	0	(49)	0	(49)
Net income	0	0	0	0	17,892	17,892
Balance, December 31, 2013	7,165	\$ 72	\$ 5,781	\$ (26)	\$ 66,726	\$ 72,553
Common stock issued on exercise of options and vesting of restricted stock units	56	0	434	0	0	\$ 434
Common stock repurchased on vesting of restricted stock units	(8)	0	(407)	0	0	\$ (407)
Share based compensation expense, net of tax	0	0	1,699	0	0	\$ 1,699
Excess tax benefits from share-based compensation	0	0	578	0	0	\$ 578
Company repurchase of common stock	(87)	(1)	(3,675)	0	0	\$ (3,676)
Cash dividends on common stock	0	0	0	0	(5,442)	\$ (5,442)
Unrealized holding gains on marketable securities, net of tax	0	0	0	3	0	\$ 3
Net loss	0	0	0	0	(27,084)	\$ (27,084)
Balance, December 31, 2014	7,126	\$ 71	\$ 4,410	(23)	\$ 34,200	\$ 38,658

The accompanying notes are an integral part of these financial statements.

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**Table of Contents****Barrett Business Services, Inc.**

## Consolidated Statements of Cash Flows

Years Ended December 31, 2014, 2013 and 2012

(In Thousands)

	2014	2013	2012
Cash flows from operating activities:			
Net (loss) income	\$ (27,084)	\$ 17,892	\$ 13,131
Reconciliations of net (loss) income to net cash provided by operating activities:			
Depreciation and amortization	2,506	2,037	1,477
Losses (gains) recognized on marketable securities	3	(1)	(4)
Gain recognized on sale and leaseback	0	(60)	(122)
Deferred income taxes	(9,487)	(632)	301
Share based compensation	1,699	1,016	695
Excess tax benefit from share-based compensation	(578)	(2,083)	(295)
Changes in certain assets and liabilities:			
Trade accounts receivable, net	(17,041)	(21,665)	(17,401)
Income taxes receivable	(11,421)	0	4,133
Prepaid expenses and other	(387)	1,828	1,043
Accounts payable	(533)	1,257	356
Accrued payroll, payroll taxes and related benefits	27,617	22,948	17,228
Other accrued liabilities	1,604	7	6
Income taxes payable	(658)	3,047	567
Workers compensation claims liabilities	103,538	41,880	20,663
Safety incentives liability	1,146	3,244	3,521
Customer deposits, long-term liabilities and other assets, net	(1,328)	(519)	358
Net cash provided by operating activities	69,596	70,196	45,657
Cash flows from investing activities:			
Purchase of property and equipment	(4,632)	(4,097)	(3,712)
Proceeds from sales and maturities of marketable securities	13,241	60,850	39,190
Purchase of marketable securities	(38,434)	(59,917)	(33,539)
Proceeds from maturities of restricted certificates of deposit	0	63,944	0
Purchase of restricted certificates of deposit	(101,546)	(76,733)	0
Proceeds from maturities of restricted marketable securities	10,524	9,918	10,796
Purchase of restricted marketable securities	(61,628)	(11,397)	(10,599)
Net cash (used in) provided by investing activities	(182,475)	(17,432)	2,136
Cash flows from financing activities:			
Proceeds from credit-line borrowings	6,242	132,664	50,229
Payments on credit-line borrowings	(6,242)	(137,196)	(45,697)
Proceeds from the issuance of long-term debt	40,000	0	5,512
Commitment fee from the issuance of long-term debt	(400)	0	0
Payments on long-term debt	(220)	(220)	(19)
Repurchase of common stock	(3,676)	0	(25,432)
Common stock repurchased on vesting of restricted stock units	(407)	(89)	0
Redemption of mandatorily redeemable preferred stock	0	0	(34,800)
Dividends paid	(5,443)	(4,056)	(3,550)
Proceeds from the exercise of stock options and vesting of restricted stock units	434	1,860	1,845
Excess tax benefit from share-based compensation	578	2,083	295
Net cash provided by (used in) financing activities	30,866	(4,954)	(51,617)

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Net (decrease) increase in cash and cash equivalents	(82,013)	47,810	(3,824)
Cash and cash equivalents, beginning of year	93,557	45,747	49,571
Cash and cash equivalents, end of year	11,544	93,557	45,747
<b>Supplemental schedule of noncash financing activities:</b>			
Issuance of mandatorily redeemable preferred stock	\$ 0	\$ 0	\$ 34,800

The accompanying notes are an integral part of these financial statements.

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# **Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements

### **1. Summary of Operations and Significant Accounting Policies**

#### **Nature of operations**

Barrett Business Services, Inc. ( "BBSI", the "Company" ), is a leading provider of business management solutions for small-and mid-sized companies. The Company has developed a management platform that integrates a knowledge-based approach from the management consulting industry with tools from the human resource outsourcing industry. This platform, through the effective leveraging of human capital, assists our business owner clients in more effectively running their business. We believe this platform, delivered through a decentralized organizational structure, differentiates BBSI from our competitors. The Company operates through a network of branch offices throughout California, Oregon, Washington, Idaho, Arizona, Nevada, Utah, Colorado, Maryland, Delaware and North Carolina. Approximately 77%, 74% and 69%, respectively, of our revenue during 2014, 2013 and 2012 was attributable to our California operations. BBSI was incorporated in Maryland in 1965.

The Company operates a wholly owned captive insurance company, Associated Insurance Company for Excess ( "AICE" ). AICE is a fully licensed captive insurance company holding a certificate of authority from the Arizona Department of Insurance. The purpose of AICE is twofold: (1) to provide access to more competitive and cost effective insurance markets and (2) to provide additional flexibility in cost effective risk management. The captive handles the Company's workers' compensation claims occurring on or after January 1, 2007. AICE provides excess workers' compensation coverage from \$1.0 million up to \$5.0 million per occurrence in the states of California, Oregon, Delaware and Washington. AICE also provides general liability insurance coverage for BBSI.

The Company also operates 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 beginning with claims occurring on or after March 1, 2010. The restricted capital used to capitalize the insurance company was approximately \$6.1 million and is included in restricted marketable securities and workers' compensation deposits in our consolidated balance sheets.

#### **Principles of consolidation**

The accompanying financial statements are prepared on a consolidated basis. All significant intercompany account balances and transactions between BBSI, AICE, Ecole and BBS I, LLC, the aircraft subsidiary which owns an aircraft for management's operational travel needs, have been eliminated in consolidation.

#### **Reportable Segment**

The Company has one principal operating and reporting segment. The chief operating decision maker (currently our Chief Executive Officer) regularly reviews the financial information of our business at a consolidated level in deciding how to allocate resources and assessing performance.

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# **Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

### **1. Summary of Operations and Significant Accounting Policies (Continued)**

#### **Revenue recognition**

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

#### **Cost of revenues**

Our cost of revenues for PEO services includes employer payroll related taxes and workers' compensation. Our cost of revenues for staffing services is comprised of direct payroll costs, employer payroll related taxes, employee benefits, and workers' compensation. Direct payroll costs represent the gross payroll earned by staffing services employees based on salary or hourly wages. Payroll taxes and employee benefits consist of the employer's portion of Social Security and Medicare taxes, federal and state unemployment taxes, and staffing services employee reimbursements for materials, supplies and other expenses, which are paid by our customer. Workers' compensation costs consist primarily of the costs associated with our self-insured workers' compensation program, such as claims reserves, claims administration fees, legal fees, state administrative agency fees and excess insurance premiums for catastrophic injuries.

We maintain separate workers' compensation insurance policies for employees working in states where the Company is not self-insured. Safety incentives represent cash incentives paid to certain client companies engaged in a client services agreement, for maintaining safe-work practices in order to minimize workplace injuries. The incentive is based on a percentage of annual payroll and is paid annually to clients who meet predetermined workers' compensation claims cost objectives.

#### **Cash and cash equivalents**

We consider non-restricted short-term investments, which are highly liquid, readily convertible into cash, and have original maturities of less than three months, to be cash

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**1. Summary of Operations and Significant Accounting Policies (Continued)**

equivalents for purposes of the consolidated statements of cash flows. A substantial portion of the Company's cash and cash equivalents is invested in tax-exempt money market funds managed by the Company's principal bank. The Company maintains cash balances in bank accounts that normally exceed FDIC insured limits. The Company has not experienced any losses related to its cash concentration.

**Marketable securities**

As of December 31, 2014, the Company's marketable securities consisted of tax-exempt municipal securities, U.S. Treasuries, variable rate demand notes (VRDN) and corporate bonds. We determine the appropriate classification for certain investments in debt securities, and classify our marketable securities as trading or available-for-sale. The Company classifies municipal securities, U.S. Treasuries, VRDN, and 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 (loss) income in stockholders' equity. Management considers available evidence in evaluating potential impairment of investments, including the duration and extent to which fair value is less than cost and the Company's ability and intent to hold the investments. In the event a loss is determined to be other-than-temporary, the loss will be recognized in the consolidated statements of operations.

**Restricted marketable securities**

At December 31, 2014 and 2013, restricted marketable securities consisted of money market funds held in trust, U.S. Treasuries, municipal debt instruments, and corporate debt instruments with maturities generally from 180 days to two years (see Note 3, Note 4 and Note 6). At December 31, 2014 and 2013, the approximate fair value of restricted marketable securities equaled their approximate amortized cost. Restricted marketable securities have been categorized 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 (loss) income in stockholders' equity. Realized gains and losses on sales of restricted marketable securities are included in other income (expense) on our consolidated statements of operations.

**Allowance for doubtful accounts**

We must make estimates of the collectability of our accounts receivable for services provided to our customers. Our management analyzes historical bad debts, customer concentrations, customer credit-worthiness, current economic conditions, and changes in customers' payment trends when evaluating the adequacy of the allowance for doubtful accounts. If the financial condition of our customers deteriorates, resulting in an impairment of their ability to make payments, additional allowances may be required.

**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**1. Summary of Operations and Significant Accounting Policies (Continued)**

Our allowance for doubtful accounts activity is summarized as follows (in thousands):

	2014	2013	2012
Balance at January 1,			
Allowance for doubtful accounts	\$ 242	\$ 381	\$ 452
Charges to expense	103	300	195
Write-offs of uncollectible accounts, net of recoveries	(54)	(439)	(266)
Balance at December 31,			
Allowance for doubtful accounts	\$ 291	\$ 242	\$ 381

**Income taxes**

Our income taxes are accounted for using an asset and liability approach. This requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial statement and tax basis of assets and liabilities at the applicable tax rates. A valuation allowance is recorded against deferred tax assets if, based on the weight of the available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. The factors used to assess the likelihood of realization include the Company's forecast of the reversal of temporary differences, future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Failure to achieve forecasted taxable income in applicable tax jurisdictions could affect the ultimate realization of deferred tax assets and could result in an increase in the Company's effective tax rate on future earnings.

The determination of our provision for income taxes requires significant judgment, the use of estimates, and the interpretation and application of complex tax laws. Significant judgment is required in assessing the timing and amounts of deductible and taxable items and the probability of sustaining uncertain tax positions. The Company recognizes the tax benefit from uncertain tax positions if it is more likely than not that the tax positions will be sustained on examination by the tax authorities, based on the technical merits of the position. The tax benefit is measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. As facts and circumstances change, we reassess these probabilities and would record any changes in the consolidated financial statements as appropriate. The Company recognizes interest and penalties related to unrecognized tax benefits in income tax expense.

**Business combinations**

We account for business combinations using the acquisition method of accounting. Transaction costs incurred in connection with a business combination are expensed as incurred. Changes in deferred tax asset valuation allowances and acquired income tax uncertainties after the measurement period are recognized in earnings.

**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**1. Summary of Operations and Significant Accounting Policies (Continued)****Goodwill and intangible assets**

Goodwill is recorded as the difference, if any, between the aggregate consideration paid for a business combination and the fair value of the net assets acquired. Goodwill is not amortized, but is evaluated for impairment annually, or more frequently if indicators of impairment are present or changes in circumstances suggest that impairment may exist. The Company has one reporting unit and evaluates the carrying value of goodwill annually at December 31. No impairment has been recognized in the periods presented.

Our intangible assets with definite lives are amortized on a straight-line basis over their estimated economic useful lives.

**Property, equipment and software**

Property, equipment and software are stated at cost. Expenditures for maintenance and repairs are charged to operating expense as incurred and expenditures for additions and improvements are capitalized. The cost of assets sold or otherwise disposed of and the related accumulated depreciation are eliminated from the accounts, and any resulting gain or loss is reflected in the consolidated statements of operations.

Depreciation of property, equipment and software is calculated using either straight-line or accelerated methods over estimated useful lives of the related assets or lease terms, as follows:

	<b>Years</b>
Buildings	39
Office furniture and fixtures	7
Computer hardware and software	3-10
Aircraft	20
Leasehold improvements	Shorter of lease term or estimated useful life

**Impairment of long-lived assets**

Long-lived assets, such as property, equipment and software and acquired intangibles, subject to amortization, are reviewed for impairment annually, or whenever events or changes in circumstances indicate that the remaining estimated useful life may warrant revision or that the carrying amount of an asset may not be recoverable. Some of the events or changes in circumstances that would trigger an impairment review include, but are not limited to, significant under-performance relative to expected and/or historical results (such as two years of significant sales declines or two years of significant negative operating cash flows), significant negative industry or economic trends, or knowledge of transactions involving the sale of similar property at amounts below the carrying value.

Assets are grouped for recognition and measurement of impairment at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets. If the carrying amount of an asset group exceeds the estimated, undiscounted

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**1. Summary of Operations and Significant Accounting Policies (Continued)**

future cash flows expected to be generated by the asset, then an impairment charge is recognized to the extent the carrying amount exceeds the asset's fair value. In determining fair value, management considers current results, trends, future prospects, and other economic factors.

**Workers' compensation claims liabilities**

The estimated liability for unsettled workers' compensation claims represents an evaluation of information provided by our internal claims adjusters and our third-party administrators for workers' compensation claims, coupled with an actuarial estimate of future cost development of reported claims and incurred but not reported claims (together, IBNR) provided by the Company's independent actuary. Included in the claims liabilities are case reserve estimates for reported losses, plus additional amounts for estimated future development of reported claims and incurred but not reported claims as well as estimates 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.

The Company's independent actuary provides management with an estimate of the current portion and long-term portion of our total workers' compensation claims. The current portion represents the best estimate of 2014 and prior year claims expected to be paid out in 2015. The Company will also pay out a portion of the 2015 claims during 2015.

Our workers' compensation claims liabilities do not represent an exact calculation of liability, but instead represent management's best estimate, generally utilizing actuarial expertise and projection techniques, at a given accounting date. The process of estimating unpaid claims and claim adjustment expense involves a high degree of judgment and is subject to a number of variables. These variables can be affected by both internal and external events such as changes in claims handling and reserve estimation procedures, changes in individuals involved in the reserve estimation process, inflation, legal trends and legislative changes.

We use informed judgment throughout the process, derived from individual experiences and expertise applied to multiple sets of data and analysis. We consider all significant facts and circumstances known at the time loss reserves are established and as new facts and circumstances become known. Due to the inherent uncertainty underlying loss reserve estimates including, but not limited to, the future settlement environment, final resolution of our estimated liability for our workers' compensation claims will likely be higher or lower than the related loss reserves at the reporting date. Therefore, actual paid losses, as specific claims are settled in the future, may be materially different in amount from our current loss reserves.

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# **Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

### **1. Summary of Operations and Significant Accounting Policies (Continued)**

A basic premise in most actuarial analyses is that historical data and past patterns demonstrated in the incurred and paid historical data form a reasonable basis upon which to project future outcomes, absent a material change. To the extent a material change affecting the ultimate claim liability is known, such change is quantified to the extent possible through an analysis of internal Company data and, if available and when appropriate, external data. Significant structural changes to the available data can materially impact the reserve estimation process. Actuaries exercise a considerable degree of judgment in the evaluation of these factors in their analysis of reserves. The application of actuarial judgment is unavoidable when faced with material uncertainty. Different actuaries may choose different assumptions when faced with such uncertainty, based on their individual backgrounds, professional experiences and the context in which they are reviewing the reserves. Hence, the estimates selected by different actuaries may differ materially from each other.

#### **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. 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 contract year-to-date payroll and the then-current amount of the customer's estimated workers' compensation claims reserves as established by us and our third party administrator 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.

#### **Customer deposits**

We require deposits from certain PEO customers to cover a portion of our accounts receivable due from such customers in the event of default of payment.

#### **Comprehensive (loss) income**

Comprehensive (loss) income includes all changes in equity during a period except those that resulted from investments by or distributions to the Company's stockholders.

Other comprehensive (loss) income refers to revenues, expenses, gains and losses that under generally accepted accounting principles are included in comprehensive (loss) income, but excluded from net (loss) income as these amounts are recorded directly as an adjustment to stockholders' equity. Our other comprehensive (loss) income is comprised of unrealized holding gains and losses on our available for sale marketable securities.

**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**1. Summary of Operations and Significant Accounting Policies (Continued)****Statements of cash flows**

Interest paid during 2014, 2013 and 2012 did not materially differ from interest expense.

Income taxes paid by the Company in 2014, 2013 and 2012 totaled \$3.3 million, \$9.0 million and \$3.3 million, respectively.

**Basic and diluted earnings per share**

Basic earnings per share are computed based on the weighted average number of common shares outstanding for each year using the treasury method. Diluted earnings per share reflect the potential effects of the exercise of outstanding stock options. Basic and diluted shares outstanding are summarized as follows (in thousands):

	<b>Year Ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
Weighted average number of basic shares outstanding	7,160	7,105	7,723
Effect of dilutive securities	0	292	140
Weighted average number of diluted shares outstanding	7,160	7,397	7,863

As a result of the net loss for the year ended December 31, 2014, 227,000 potential common shares have been excluded from the calculation of diluted loss per share because their effect would be anti-dilutive.

**Reclassifications**

Certain prior year amounts have been reclassified to conform to the 2014 presentation. Such reclassifications had no impact on the Company's financial condition, operating results, cash flows, working capital or stockholder's equity.

**Accounting estimates**

The preparation of our consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Estimates are used for carrying values of marketable securities, allowance for doubtful accounts, deferred income taxes, carrying values for goodwill and property and equipment, accrued workers' compensation liabilities and safety incentive liabilities. Actual results may or may not differ from such estimates.





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# Barrett Business Services, Inc.

## Notes to Consolidated Financial Statements (Continued)

### 1. Summary of Operations and Significant Accounting Policies (Continued)

#### Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) 2014-09 *Revenue from Contracts with Customers*, which will supersede nearly all existing revenue recognition guidance under U.S. GAAP. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard is effective for the Company on January 1, 2017. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. The Company has not yet selected a transition method or determined the effect of the standard on its ongoing financial reporting.

In September 2014, the FASB issued new accounting guidance on disclosure of uncertainties about an entity's ability to continue as a going concern. The new guidance requires an entity's management to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued, and if so, disclose that fact. Management is also required to evaluate and disclose whether its plans alleviate that doubt. The guidance is effective for us in 2017 and will be applicable to both annual and interim reporting periods. We do not expect the adoption of this guidance to have an impact on our consolidated financial statements.

### 2. Stock Repurchase

Effective March 28, 2012, the Company repurchased 2,485,929 shares of the Company's common stock held by the Estate of William W. Sherertz and 500,000 common shares held by Nancy Sherertz. Mr. Sherertz, a founder and former president and CEO of the Company, died January 20, 2011. Nancy Sherertz is also a founder of the Company. The common shares were repurchased at a price of \$20 per share, representing total consideration of \$59.7 million. The Company used a combination of \$24.9 million in cash and issued 34,800 shares of Series A Nonconvertible, Non-Voting Redeemable Preferred Stock with a liquidation preference of \$1,000 per share. Additionally, the Company incurred professional and legal fees totaling \$514,000 related to the transaction.

Effective September 21, 2012, the Company redeemed all of the outstanding shares of its Series A Nonconvertible, Non-Voting Redeemable Preferred Stock for \$34.8 million using a combination of cash on hand and availability under a new revolving credit facility provided by its principal bank. By redeeming the preferred stock within six months of issuance, the Company avoided having to pay a 5% semi-annual dividend of approximately \$870,000 due September 28, 2012.

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**3. Fair Value of Financial Instruments and Concentration of Credit Risk**

All of our financial instruments are recognized in our consolidated balance sheet. Carrying values approximate fair value of most financial assets and liabilities. The fair value of restricted marketable securities consisting primarily of certificates of deposits, money market funds, municipal bonds, U.S. treasury bills and corporate bonds is recorded at amortized cost, which approximates fair value for similar instruments. The interest rates on our restricted marketable security investments approximate current market rates for these types of investments; therefore, the recorded value of the restricted marketable securities approximates fair value.

Financial instruments that potentially subject us to concentration of credit risk consist primarily of temporary cash investments, marketable securities, restricted marketable securities and trade accounts receivable. We limit investment of temporary cash investments and marketable securities to financial institutions with high credit ratings, corporate bonds and to investments in governmental debt instruments. Credit risk on trade receivables is minimized as a result of the large and diverse nature of our customer base.

At December 31, 2014, we had significant concentrations of credit risk as follows:

Marketable securities \$137.6 million, at fair value, in certificates of deposit.

Marketable securities \$50.1 million, at fair value, in money market funds.

Marketable securities \$21.7 million, at fair value, in VRDN.

Marketable securities \$8.2 million, at fair value, in municipal bonds.

Marketable securities \$5.7 million, at fair value, in corporate bonds.

**4. Fair Value Measurement**

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

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

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

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**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**4. Fair Value Measurement (Continued)**

In determining the fair value of our financial assets, the Company predominately uses the market approach. In determining the fair value of all its certificates of deposit, money market funds, U.S. treasuries, municipal bonds, corporate bonds, and variable rate demand notes classified as Level 2, the Company utilizes the non-binding quotes provided by our three investment brokers. We receive one non-binding broker quote for each financial asset as of the balance sheet date. To value the Level 2 assets, our investment brokers use proprietary multi-dimensional pricing models that include a variety of inputs, including quoted prices for identical or similar assets in active markets, quoted prices for identical or similar assets in markets that are not active, interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks and default rates that are observable at commonly quoted intervals. 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 (in thousands):

	December 31, 2014			December 31, 2013			
		Gross Unrealized Gains (Losses)	Recorded Basis		Gross Unrealized (Losses)	Recorded Basis	Fair Value Category
	Cost			Cost			
Current:							
Available-for-sale:							
VRDN	\$ 21,670	\$ 0	\$ 21,670	\$ 10,000	\$ 0	\$ 10,000	2
Certificates of deposit	8,330	(43)	8,287	0	0	0	2
Corporate bonds	0	0	0	9,800	(13)	9,787	2
	\$ 30,000	\$ (43)	\$ 29,957	\$ 19,800	\$ (13)	\$ 19,787	
Long term:							
Available-for-sale:							
Municipal bonds	\$ 3,843	\$ 7	\$ 3,850	\$ 4,074	\$ (17)	\$ 4,057	2
Corporate bonds	2,153	(3)	2,150	1,879	(27)	1,852	2
Certificates of deposit	14,944	(14)	14,930	0	0	0	2
	\$ 20,940	\$ (10)	\$ 20,930	\$ 5,953	\$ (44)	\$ 5,909	

Table of Contents**Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**4. 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):

	December 31, 2014			December 31, 2013			
		Gross Unrealized Gains (Losses)	Recorded Basis		Gross Unrealized Gains	Recorded Basis	Fair Value Category
	Cost			Cost			
Current:							
Available-for-sale:							
Money market funds held in trust	\$ 3,776	\$ 0	\$ 3,776	\$ 0	\$ 0	\$ 0	2
	\$ 3,776	\$ 0	\$ 3,776	\$ 0	\$ 0	\$ 0	
Long term:							
Available-for-sale:							
Money market funds held in trust	\$ 46,310	\$ 0	\$ 46,310	\$ 0	\$ 0	\$ 0	2
Municipal bonds	4,352	21	4,373	4,742	10	4,752	2
Corporate bonds	3,540	(3)	3,537	2,849	5	2,854	2
U.S. treasuries	3,963	0	3,963	2,787	0	2,787	1
	\$ 58,165	\$ 18	\$ 58,183	\$ 10,378	\$ 15	\$ 10,393	

The Company's long term restricted certificates of deposit are summarized as follows (in thousands):

	December 31, 2014			December 31, 2013			
		Gross Unrealized Gains	Recorded Basis		Gross Unrealized Gains	Recorded Basis	Fair Value Category
	Cost			Cost			
Restricted certificates of deposit	\$ 114,335	\$ 0	\$ 114,335	\$ 12,789	\$ 0	\$ 12,789	2

**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**5. Property, Equipment and Software**

Property, equipment and software consist of the following (in thousands):

	<b>December 31,</b>	
	<b>2014</b>	<b>2013</b>
Buildings	\$ 13,004	\$ 11,158
Office furniture and fixtures	6,706	5,548
Computer hardware and software	12,949	11,396
Aircraft	4,668	4,617
	37,327	32,719
Less accumulated depreciation and amortization	(16,142)	(13,660)
	21,185	19,059
Land	1,490	1,490
	\$ 22,675	\$ 20,549

**6. Workers Compensation Claims**

The Company is a self-insured employer with respect to workers compensation coverage for all of its employees (including employees co-employed through our client service agreements) working in California, Oregon, Maryland, Delaware and Colorado, except as described below. The Company's ability to self-insure in California ended on December 31, 2014, as described in more detail below. 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, the Company operates a wholly owned fully licensed insurance company, Ecole Insurance Company (Ecole), in Arizona to provide workers compensation coverage to our employees in Arizona.

To manage our financial exposure, in the event of catastrophic injuries or fatalities, the Company maintains 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 \$2.0 million, respectively. AICE maintains excess workers compensation insurance coverage with ACE Group (ACE), between \$5.0 million and \$15.0 million per occurrence, except in Maryland, where coverage with ACE is between \$1.0 million and \$25.0 million per occurrence, and in Colorado, where the coverage with ACE is between \$2.0 million and statutory limits per occurrence. Prior to December 1, 2012, similar excess workers compensation coverage was through American International Group. The Company continues to evaluate the financial capacity of its insurers to assess the recoverability of the related insurer receivables.

The Company has provided a total of \$216.0 million and \$112.4 million at December 31, 2014 and 2013, respectively, as an estimated future liability for unsettled workers compensation claims liabilities. The estimated liability for unsettled workers

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**6. Workers Compensation Claims (Continued)**

compensation claims represents management's best estimate based upon an actuarial valuation provided by a third party actuary at December 31, 2014 and 2013. 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.

Our workers' compensation claims liabilities do not represent an exact calculation of liability, but instead represent management's best estimate, generally utilizing actuarial expertise and projection techniques, at a given accounting date. The process of estimating unpaid claims and claim adjustment expense involves a high degree of judgment and is subject to a number of variables. These variables can be affected by both internal and external events such as changes in claims handling procedures, changes in individuals involved in the reserve estimation process, legal trends and legislative changes.

We have undertaken a number of steps during the past two years to improve our workers' compensation claims administration practices. These steps include hiring additional claim administrators in response to our business growth, and working to close litigated claims more quickly.

Beginning in late 2013, as part of our efforts to improve our claims handling practices, the Company initiated a specific case reserve study on its open workers' compensation claims with injury dates in 2012 and earlier. The specific case reserve study resulted in moving dollars from the general reserve of incurred but not reported claims and future loss development into specific case reserves for individual claims. This process was intended to provide management with a more accurate estimate of the ultimate total cost of each claim at a detailed level. Additionally, in mid-2013, the Company initiated a change to its individual claim handling practices by recording specific case reserves on new claims at amounts that include all of the anticipated future costs and working to close claims more quickly with the goal of reducing the ultimate cost of the claims.

In May 2014, the Company engaged an actuarial consultant to assist management in studying selected historical claims experience and the impact of the change in its claims handling process. During the third quarter of 2014, the Company engaged a new actuary to assist management in determining its best estimate of the Company's workers' compensation liability. Based on the work of the new actuary and a thorough review of the Company's claims handling practices and the results of the work performed by the actuarial consultant engaged during the second quarter of 2014, management reached the conclusion in October 2014 that, based on actuarial methods, the estimate of workers' compensation liability should reflect a significant increase for the potential development of prior period claims. The Company recorded total workers' compensation



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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**6. Workers Compensation Claims (Continued)**

claims expense of \$101.2 million during the third quarter of 2014, including a \$61.3 million change in estimate relating to prior period claims. Management's primary considerations in arriving at its estimate of workers' compensation liability include the significant increase in the Company's business in recent years, the potential for unexpected future adverse development of open claims, and the increasing complexity and uncertainty surrounding healthcare costs.

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 \$781,000 and \$768,000 at December 31, 2014 and 2013, respectively.

Liabilities incurred for work-related employee fatalities and for severely injured workers, as determined by the state in which the accident occurred, are recorded either at an agreed lump-sum settlement amount or the net present value of future fixed and determinable payments over the actuarially determined remaining life expectancy of the beneficiary, discounted at a rate that approximates a long-term, high-quality corporate bond rate. We present our accrued liabilities for workers' compensation claims on a gross basis along with a corresponding receivable from our insurers, as we are the primary obligor for payment of the related insured claims.

At December 31, 2014, our long-term workers' compensation claims liabilities in the accompanying consolidated balance sheet included \$271,000 for work-related fatalities. The aggregate undiscounted payout amount related to the catastrophic injuries and fatalities is \$360,000. The discount rates applied to the discounted liabilities range from 4.25% to 9.00%. These rates represented the then-current rates for high quality long-term debt securities available at the date of loss with maturities equal to the length of the payout period to the beneficiaries. The actuarially determined payout periods to the beneficiaries range from 7 to 32 years.

In February 2014, the Company entered into a workers' compensation insurance arrangement with ACE to provide coverage to BBSI employees in California beginning in the first quarter of 2014. The current agreement is effective through January 2016 with the potential for annual renewals thereafter.

The arrangement, typically known as a fronted program, provides BBSI a licensed, admitted insurance carrier in California to issue policies on behalf of BBSI without the intention of transferring any of the worker's compensation risk for the first \$5.0 million per claim. The risk of loss up to the first \$5.0 million per claim is retained by BBSI through an indemnity agreement.

During the first quarter of 2014, the Company made an initial deposit of \$20.0 million into a trust account established between the Company and ACE related to the new ACE fronted insurance program. The Company began making monthly payments in April 2014.

**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**6. Workers Compensation Claims (Continued)**

into the trust account to be set aside for the payment of future claims. The balance in the trust account as of December 31, 2014 totaled \$50.1 million. The trust account balance is included as a component of the current and long-term restricted marketable securities and workers compensation deposits in the accompanying consolidated balance sheet.

The states of California, Oregon, Maryland, Washington, Delaware and Colorado require us to maintain specified investment balances or other financial instruments, totaling \$198.5 million at December 31, 2014 and \$72.9 million at December 31, 2013, to cover potential claims losses. In partial satisfaction of these requirements, at December 31, 2014, we have provided surety bonds and standby letters of credit totaling \$194.9 million. The investments are included in restricted marketable securities and workers compensation deposits in the accompanying consolidated balance sheets. During the fourth quarter of 2014, the state of California increased the Company's surety deposit requirement to \$190.6 million (which is included in the total \$194.9 million of surety bonds and standby letters of credit), which the Company satisfied through the posting of third party issued surety bonds which are backed by a \$114.3 million letter of credit. In conjunction with this letter of credit, the Company posted \$114.3 million of certificates of deposit with Wells Fargo as collateral, this amount is included in long-term assets on the consolidated balance sheet.

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

	<b>Year Ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
Balance at January 1,			
Workers compensation claims liabilities	\$ 112,444	\$ 70,564	\$ 51,193
Claims expense accrual:			
Current year	97,883	63,822	38,386
Prior years	67,101	23,445	12,344
	164,984	87,267	50,730
Claims payments related to:			
Current year	13,183	10,586	6,746
Prior years	48,263	34,801	24,613
	61,446	45,387	31,359
Balance at December 31,			
Workers compensation claims liabilities	\$ 215,982	\$ 112,444	\$ 70,564
Incurred but not reported (IBNR)	\$ 113,984	\$ 69,611	\$ 47,992

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**7. Revolving Credit Facility and Long-Term Debt**

Effective December 29, 2014, the Company entered into a new credit agreement (the "Agreement") with its principal bank, Wells Fargo Bank, National Association (the "Bank"). The Agreement provides for a \$40.0 million term loan maturing December 31, 2016, as well as a \$14.0 million revolving credit line, with a \$5.0 million sublimit for unsecured standby letters of credit. The Company had no outstanding borrowings on its revolving credit line at December 31, 2014. The Agreement also provides for an increase to a total of \$114.3 million in cash-secured letters of credit to satisfy collateral requirements associated with various surety deposit requirements for workers' compensation purposes in the state of California. In conjunction with this letter of credit, the Company posted \$114.3 million of certificates of deposit with Wells Fargo as collateral, which is included in long-term assets on the consolidated balance sheet. The Agreement includes a non-refundable commitment fee of \$400,000, which is reported within prepaid expenses and other on the Company's consolidated balance sheet. The fee will be amortized to interest expense ratably over the term of the loan.

The \$40.0 million term loan with the Bank requires payments of \$3.0 million on June 30, 2015, \$7.0 million on September 30, 2015, \$15.0 million on December 31, 2015, \$5.0 million on June 30, 2016 and \$5.0 million on September 30, 2016. The term loan bears interest at the one month LIBOR plus 4.0%.

Advances under the revolving credit facility bear interest as selected by the Company of either (a) a daily floating rate of one month LIBOR plus 2% or (b) a fixed rate of LIBOR plus 2.0%. The Agreement also provides for an unused commitment fee of 0.35% per year on the average daily unused amount of the revolving credit facility, and a fee of 1.75% of the face amount of each letter of credit.

The credit facility is collateralized by the Company's accounts receivable and other rights to receive payment, general intangibles, inventory and equipment.

The Agreement requires the satisfaction of certain financial covenants as follows:

minimum Fixed Charge Coverage ratio of no less than 1.5:1.0, measured quarterly on a rolling four-quarter basis; and

ratio of restricted and unrestricted cash and marketable securities to workers' compensation and safety incentive liabilities of at least 1.0:1.0, measured quarterly;

The Agreement includes certain additional covenants as follows:

capital expenditures may not exceed a total of \$5.0 million in 2015 and a total of \$4.0 million in 2016 without the Bank's prior approval;

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**7. Revolving Credit Facility and Long-Term Debt (Continued)**

prohibition on incurring additional indebtedness without the prior approval of the Bank, other than up to \$200,000 per year in purchase money financing and the aggregate of all purchase money indebtedness does not exceed \$400,000 at any time;

prohibition on repurchases of the Company's common stock; and

continuation of quarterly cash dividends up to \$0.22 per share so long as there is no default by the Company and payment would not cause a default.

The Agreement also contains customary events of default. If an event of default under the Agreement occurs and is continuing, the Bank may declare any outstanding obligations under the Agreement to be immediately due and payable. The Company was in compliance with all applicable financial covenants at December 31, 2014.

Additionally, the Company maintains a term loan with the Bank with a current balance of approximately \$5.1 million secured by the Company's corporate office building in Vancouver, Washington. The term loan requires payment of monthly installments of \$18,375, bearing interest at the one month LIBOR plus 2.25%, with the unpaid principal balance due November 1, 2017.

**8. 401(k) Savings Plan**

We have a Section 401(k) Retirement Savings Plan for the benefit of our eligible employees. All staffing and management employees 21 years of age or older become eligible to participate in the savings plan upon completion of 1,000 hours of service in any consecutive 12-month period following the initial date of employment. Employees covered under a PEO arrangement may participate in the plan at the sole discretion of the PEO client. The determination of discretionary Company contributions to the plan, if any, is at the sole discretion of our Board of Directors. No discretionary Company contributions were made to the plan for the years ended December 31, 2014, 2013 and 2012.

We make matching contributions to the 401(k) plan under a safe harbor provision, whereby the Company matches 100% of contributions by management and staffing employees up to 3% of each participating employee's annual compensation; and 50% of the employee's contributions up to an additional 2% of annual compensation. We made \$885,000, \$734,000 and \$610,000 in matching contributions during 2014, 2013 and 2012, respectively. Participants' interests in Company safe harbor contributions to the plan are fully vested when made.

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## Notes to Consolidated Financial Statements (Continued)

**9. Commitments and Contingencies****Lease commitments**

We lease office space for our branch offices under operating lease agreements that require minimum annual payments as follows (in thousands):

<b>Year ending</b>	
<b>December 31,</b>	
2015	\$ 3,502
2016	2,874
2017	2,233
2018	1,349
2019	666
2020	60
Thereafter	0
	\$ 10,684

Rent expense was approximately \$3.7 million, \$3.2 million, and \$2.8 million for the years ended December 31, 2014, 2013 and 2012, respectively.

**10. Income Taxes**

The provision for income taxes from continuing operations is as follows (in thousands):

	<b>Year ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
<b>Current:</b>			
Federal	\$ (8,022)	\$ 6,386	\$ 5,378
State	(741)	1,225	685
	(8,763)	7,611	6,063
<b>Deferred:</b>			
Federal	(10,237)	(519)	341
State	747	(82)	(76)
	(9,490)	(601)	265
<b>Total (benefit) provision</b>	<b>\$ (18,253)</b>	<b>\$ 7,010</b>	<b>\$ 6,328</b>



**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**10. Income Taxes (Continued)**

Deferred income tax assets and liabilities are comprised of the following components (in thousands):

	<b>December 31,</b>	
	<b>2014</b>	<b>2013</b>
Gross deferred income tax assets:		
Workers' compensation claims liabilities	\$ 12,168	\$ 6,985
Safety incentives payable	3,782	3,529
Allowance for doubtful accounts	118	94
Tax effect of unrealized losses, net	856	959
Alternative minimum tax credit carryforward	1,840	0
State credit carryforward	969	805
State loss carryforward	568	0
Workers' opportunity tax credit and EZ credit carryforward	3,162	0
Other	605	504
	24,068	12,876
Less valuation allowance	1,078	1,763
	22,990	11,113
Gross deferred income tax liabilities:		
Tax depreciation in excess of book depreciation	(3,770)	(2,793)
Tax amortization of goodwill	(11,588)	(10,178)
	(15,358)	(12,971)
Net deferred income tax assets (liabilities)	\$ 7,632	\$ (1,858)

The effective tax rate for continuing operations differed from the U.S. statutory federal tax rate due to the following:

	<b>Year ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
Statutory federal tax rate	(35.0)%	35.0%	35.0%
State taxes, net of federal benefit	.2	3.4	.4
Valuation allowance on capital loss carryforward and state tax credit carryforward	(.2)	(.4)	2.3
Adjustment for final positions on filed returns	(.7)	(1.5)	(.3)
Non deductible expenses and other, net	2.2	.8	4.4
Federal tax-exempt interest income	(.2)	(.2)	(.4)
Federal and state tax credits	(6.6)	(8.9)	(8.9)

(40.3)%

28.2%

32.5%

The Company has established a valuation allowance for certain deferred tax assets due to uncertainties regarding the Company's ability to generate future taxable investment gains in order to utilize certain investment impairment losses and investment loss carry

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**10. Income Taxes (Continued)**

forwards for tax purposes. The realization of a significant portion of net deferred tax assets is based in part on our estimates of the timing of reversals of certain temporary differences and on the generation of taxable income before such reversals. At December 31, 2014, we maintained a valuation allowance for approximately \$1.1 million of federal and state tax benefits that are not expected to be utilized.

Under ASC 740, Income Taxes, management evaluates the realizability of the deferred tax assets on a quarterly basis under a more-likely than not standard. As part of this evaluation, management reviews all evidence both positive and negative to determine if a valuation allowance is needed. One component of this analysis is to determine whether the Company was in a cumulative loss position for the most recent 12 quarters. Despite the increase to the workers' compensation reserve in the third quarter of 2014, the Company was in a cumulative income position for the 12 quarters ended December 31, 2014.

Management's review of positive evidence included the existence of federal and California taxable income in eligible carryback years, reversal of temporary items, and projection of future taxable income. The projection of future taxable income was a significant factor in management's determination that no additional valuation allowance was required at December 31, 2014. Management's projections of taxable income are based on the existence of signed annual contracts with the Company's PEO customer base, objective evidence that the Company's customers are retained at a high rate over long periods, and objective evidence that recent price increase initiatives are being accepted by the Company's customer base.

Management has continued to improve the Company's procedures in many areas of its self-insured workers' compensation program over the past two years as described in Note 6. The results of these efforts have improved management's ability to project workers' compensation expense. Management will monitor the need for an additional valuation allowance at each quarter in the future and, if the negative evidence outweighs the positive evidence, an allowance will be recorded.

The Company is subject to Income taxes in U.S. federal and multiple state and local tax jurisdictions. In the major jurisdictions where the Company operates, it is generally no longer subject to income tax examinations by tax authorities for years before 2010. As of December 31, 2014 and 2013, the Company had no unrecognized tax benefits.

A portion of the consolidated income the Company generates is not subject to state income tax. Depending on the percentage of this income to total consolidated income, the Company's state effective rate can fluctuate from expectations. As a result of the mix of income subject to state income tax, total state tax expense decreased by approximately \$4,000, \$284,000 and \$498,000 in 2014, 2013 and 2012, respectively.

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**10. Income Taxes (Continued)**

At December 31, 2014, the Company had capital loss carry forward of approximately \$2.1 million. The carry forward will expire unless utilized in tax years on or before December 31, 2015. At December 31, 2014, the Company had federal general business tax credit carry forwards of approximately \$3.2 million. The carry forwards will expire unless utilized in tax years on or before December 31, 2024. The Company also had an alternative minimum tax credit carry forward of approximately \$1.8 million. The credit carry forward has an indefinite life and will not expire until utilized.

At December 31, 2014, the Company had state tax credit carry forwards of approximately \$1.5 million. The carryforwards expire unless utilized in tax years on or before December 31, 2024. At December 31, 2014, the Company had a California net operating loss carry forward of approximately \$6.7 million. The carry forward will expire unless utilized in tax years on or before December 31, 2034. In addition, the Company had a total of approximately \$3.9 million in net operating loss carry forwards from other states that will expire unless utilized in tax years between December 31, 2021 and December 31, 2034.

**11. Stock Incentive Plans**

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 stock-based awards 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 December 31, 2014, there were option awards covering 367,533 shares outstanding under the 2009 Plan, together with the 2003 Plan and its predecessor, the 1993 Stock Incentive Plan. Outstanding options under all the plans generally expire ten years after the date of grant. Options are generally exercisable in four equal annual installments beginning one year after the date of grant. At December 31, 2014, there are 126,846 restricted stock units outstanding.

The Company recognizes compensation expense for options awarded under its stock incentive plans based on the grant-date fair value. Compensation expense is attributed to earnings using the straight-line method over the requisite service period.

Table of Contents**Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**11. Stock Incentive Plans (Continued)**

A summary of the status of the Company's stock options at December 31, 2014, 2013 and 2012, together with changes during the periods then ended, is presented below:

	<b>Number of options</b>	<b>Weighted average exercise price</b>
Outstanding at December 31, 2011	671,294	
Options granted at market price	7,500	17.55
Options exercised	(131,997)	13.98
Options cancelled	(8,100)	13.85
Outstanding at December 31, 2012	538,697	
Options exercised	(138,298)	13.53
Outstanding at December 31, 2013	400,399	
Options exercised	(32,866)	13.24
Outstanding at December 31, 2014	367,533	
Available for grant at December 31, 2014	481,999	

The following tables presents information on stock options exercised and outstanding:

	<b>Year Ended December 31,</b>	
<b>(in thousands, except share data)</b>	<b>2014</b>	<b>2013</b>
Intrinsic value of options exercised in the period	\$ 1,025	\$ 6,089

<b>(\$ in thousands, except share data)</b>	<b>Number of Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term (Years)</b>	<b>Aggregate Intrinsic Value</b>
Stock options:				
Outstanding December 31, 2014	367,533	\$ 15.22	5.25	\$ 4,478
Exercisable at December 31, 2014	221,059	14.45	4.55	2,847

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.



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## Notes to Consolidated Financial Statements (Continued)

**11. Stock Incentive Plans (Continued)**

The fair value of stock option awards as determined under the Black-Scholes option-pricing model was estimated with the following weighted-average assumptions:

	<b>2012</b>
Expected volatility	65.9%
Risk free interest rate	2.9%
Expected dividend yield	2.5%
Expected term	7.3 years
Weighted average fair value per share	\$ 9.08

There were no options granted during 2014 or 2013. There were no options granted during 2012 below market price.

During 2014, 2013 and 2012, the Company granted 69,371, 44,970 and 47,500 restricted stock units at a weighted average grant date fair value of \$50.47, \$50.28 and \$21.44 per share, respectively, which represented the closing price of the Company's stock on the date of grant. The restricted stock units vest in four equal annual installments beginning one year following the date of grant.

The following table presents restricted stock unit activity:

	<b>Units</b>	<b>Weighted Average Grant Date Fair Value</b>
Non-vested at December 31, 2011	0	\$ 0.00
Granted	47,500	21.44
Non-vested at December 31, 2012	47,500	21.44
Granted	44,970	50.28
Vested	(10,302)	21.44
Cancelled/Forfeited	(1,573)	21.44
Non-vested at December 31, 2013	80,595	37.53
Granted	69,371	50.47
Vested	(15,253)	33.40
Cancelled/Forfeited	(7,867)	34.90
Non-vested at December 31, 2014	126,846	44.99

[Table of Contents](#)**Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**11. Stock Incentive Plans (Continued)**

The following table summarizes stock-based compensation expense related to stock option and restricted stock unit awards (in thousands):

	<b>Year Ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
Stock-based compensation expense included in selling, general and administrative expenses	\$ 1,699	\$ 1,016	\$ 695
Deferred income taxes	675	404	272
Stock-based compensation expense related to stock options and restricted stock units, net of tax	\$ 1,024	\$ 612	\$ 423

As of December 31, 2014, unrecognized compensation expense related to stock options and restricted stock units was \$5.6 million with a weighted average remaining contractual period of 3.15 years.

The following table summarizes information about stock options outstanding at December 31, 2014:

<b>Exercise price range</b>	<b>Options outstanding</b>		<b>Weighted-average remaining contractual life (years)</b>	<b>Options exercisable</b>	
	<b>Number of shares</b>	<b>Weighted-average exercise price</b>		<b>Exercisable at December 31, 2014</b>	<b>Weighted-average exercise price</b>
\$2.01 - \$ 2.58	2,250	\$ 2.29	Indefinite	2,250	\$ 2.29
8.82 - 17.55	365,283	15.29	5.3	218,809	14.57
	367,533	15.22		221,059	14.45

**12. Stock Repurchase Program**

The Company maintains a stock repurchase program approved by the Board of Directors, which authorizes the repurchase of shares from time to time in open market purchases. The repurchase program currently allows for the repurchase of approximately 1.1 million additional shares as of December 31, 2014.

During 2014, we repurchased 87,200 shares at a weighted average price of \$42.16. No share repurchases were made under the repurchase program during 2013 and 2012.

### **13. Litigation**

On November 6, 2014, plaintiffs in *Michael Arciaga, et al. v. Barrett Business Services, Inc., et al.*, filed an action in the United States District Court for the Western District of Washington against the Company and Michael L. Elich and James D. Miller, the Company's Chief Executive Officer and Chief Financial Officer, respectively. The action

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**Barrett Business Services, Inc.**

Notes to Consolidated Financial Statements (Continued)

**13. Litigation (Continued)**

purports to be a class action brought on behalf of all Company stockholders alleging violations of the federal securities laws. The claims arise from the decline in the market price for the Company's common stock following announcement of a charge for increased workers compensation reserves expense. The lawsuit seeks compensatory damages (in an amount to be determined at trial), plus interest, and costs and expenses (including attorney fees and expert fees).

On November 13, 2014, a second purported shareholder class action was filed in the United States District Court for the Western District of Washington, entitled *Christopher P. Carnes, et al. v. Barrett Business Services, Inc., et al.* The *Carnes* complaint names the same defendants as the *Arciaga* case and asserts similar claims for relief.

Similarly, on November 17, 2014, a third purported shareholder class action was filed in the United States District Court for the Western District of Washington, entitled *Shiva Stein, et al. v. Barrett Business Services, Inc., et al.* The *Stein* complaint names the same defendants as the *Arciaga* and *Carnes* cases and asserts similar claims for relief.

On February 25, 2015, the court ordered consolidation of the three cases, and any new or other cases involving the same subject matter, into a single action for pretrial purposes. The court also appointed the Painters & Allied Trades District Council No. 35 Pension and Annuity Funds as the lead plaintiff. Discovery has not been undertaken as it is automatically stayed under the federal Private Securities Litigation Reform Act.

On February 27, 2015, the Company received a letter from counsel for an alleged stockholder accusing each of the Company's directors and officers with having breached his fiduciary duties of loyalty and good faith based on the same facts as those alleged in the three lawsuits described above, as well as that certain officers and directors sold shares of the Company's stock while in possession of material non-public information. The letter asserts that the Company has sustained and continues to sustain damages, including the costs and expenses incurred in connection with the Company's reserve strengthening process, reserve study and consultants, the cost of stock repurchases in October 2014, compensation paid to the Company's officers, and costs of negotiating the Company's credit facility with its principal lender. The letter demands that the Company's Board of Directors take action against each of the Company's officers and directors to recover these damages and the proceeds of sales of stock by the officers and directors during 2013 and 2014. The letter states that if the Board does not take these actions within a reasonable period, the stockholder will commence a shareholder derivative action on behalf of the Company.

Management is unable to estimate the probability, or the potential range, of loss arising from these legal actions.



**Table of Contents****Barrett Business Services, Inc.**

## Notes to Consolidated Financial Statements (Continued)

**13. Litigation (Continued)**

The Company is subject to other legal proceedings and claims, which arise in the ordinary course of our business. In the opinion of management, the amount of ultimate liability with respect to currently pending or threatened actions is not expected to materially affect the consolidated financial position or results of operations of the Company.

**14. Quarterly Financial Information (Unaudited)**

(in thousands, except per share amounts and market price per share)

	<b>First Quarter</b>	<b>Second Quarter</b>	<b>Third Quarter</b>	<b>Fourth Quarter</b>
Year ended December 31, 2014				
Revenues	\$ 135,140	\$ 151,069	\$ 174,959	\$ 175,016
Cost of revenues	125,834	121,217	217,741	140,975
Net (loss) income	(3,583)	7,283	(37,818)	7,034
Basic (loss) earnings per share	(0.50)	1.02	(5.27)	0.99
Diluted (loss) earnings per share	(0.50)	0.98	(5.27)	0.97
Common stock market prices:				
High	102.20	63.19	63.45	45.38
Low	57.82	41.96	39.47	18.25
Year ended December 31, 2013				
Revenues	\$ 111,551	\$ 128,798	\$ 147,971	\$ 144,524
Cost of revenues	103,240	105,072	117,785	120,223
Net (loss) income	(2,549)	5,886	8,994	5,561
Basic (loss) earnings per share	(0.36)	0.83	1.26	0.78
Diluted (loss) earnings per share	(0.36)	0.80	1.21	0.74
Common stock market prices:				
High	53.27	62.82	73.49	98.00
Low	38.15	48.50	48.08	66.33

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**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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: March 16, 2015

By: /s/ James D. Miller  
James D. Miller  
Vice President-Finance, Treasurer and Secretary

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities indicated on the 16th day of March, 2015.

Principal Executive Officer and Director:

/s/ Michael L. Elich President and Chief Executive

Michael L. Elich Officer and Director

Principal Financial and Accounting Officer:

/s/ James D. Miller Vice President-Finance, Treasurer and

James D. Miller Secretary

Majority of Directors:

/s/ Thomas J. Carley Director

Thomas J. Carley

/s/ James B. Hicks Director

James B. Hicks, Ph.D.

/s/ Roger L. Johnson Director

Roger L. Johnson

/s/ Jon L. Justesen Director

Jon L. Justesen

/s/ Anthony Meeker Chairman of the Board and Director

Anthony Meeker

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**EXHIBIT INDEX\*\***

- 3.1 Charter of the Registrant, as amended, through March 27, 2012. Incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2012.
  - 3.2 Bylaws of the Registrant, as amended effective February 3, 2014. Incorporated by reference to Exhibit 3.2 to the Registrant's Current Report on Form 8-K filed on February 7, 2014.
  - 4.1 Credit Agreement dated as of December 29, 2014, between the Registrant and Wells Fargo Bank, National Association ( "Wells Fargo" ). Incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on January 5, 2015.
  - 4.2 Revolving Line of Credit Note dated December 29, 2014, of the Registrant. Incorporated by reference to Exhibit 10.5 to the Registrant's Current Report on Form 8-K filed on January 5, 2015.
  - 4.3 Term Note dated November 1, 2012, of the Registrant. Incorporated by reference to Exhibit 4.4 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2012 (the "2012 Third Quarter 10-Q" ).
  - 4.4 First Modification to Term Note dated December 29, 2014, of the Registrant. Incorporated by reference to Exhibit 10.3 to the Registrant's Current Report on Form 8-K filed on January 5, 2015.
  - 4.5 Term Note 2 dated December 29, 2014, between the Registrant and Wells Fargo. Incorporated by reference to Exhibit 10.4 to the Registrant's Current Report on Form 8-K filed on January 5, 2015.
  - 4.6 Security Agreement: Specific Rights to Payment dated as of June 14, 2013, between the Registrant and Wells Fargo. Incorporated by reference to Exhibit 4.2 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013.
  - 4.7 Second Amended and Restated Third Party Security Agreement: Specific Rights to Payment dated as December 29, 2014, between Associated Insurance Company for Excess and Wells Fargo.
  - 4.8 Standby Letter of Credit Agreement dated as of September 18, 2012 between the Registrant and Wells Fargo. Incorporated by reference to Exhibit 4.3 to the 2012 Third Quarter 10-Q.
- The Registrant has incurred additional long-term indebtedness as to which the amount involved is less than 10 percent of the Registrant's total assets. The Registrant agrees to furnish copies of the instruments relating to such indebtedness to the Commission upon request.
- 10.1 Second Amended and Restated 1993 Stock Incentive Plan of the Registrant. Incorporated by reference to Exhibit 10.1 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2001.\*
  - 10.2 2003 Stock Incentive Plan of the Registrant (the "2003 Plan" ). Incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2003.\*

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10.3	Form of Incentive Stock Option Agreement under the 2003 Plan. Incorporated by reference to Exhibit 10.11 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2003 (the 2003 10-K ).*
10.4	Form of Nonqualified Stock Option Agreement under the 2003 Plan. Incorporated by reference to Exhibit 10.12 to the 2003 10-K.*
10.5	Form of Incentive Stock Option Agreement relating to July 2005 option grants under the 2003 Plan. Incorporated by reference to Exhibit 10.11 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2005 (the 2005 10-K ).*
10.6	Form of Nonqualified Stock Option Agreement relating to July 2005 option grants under the 2003 Plan. Incorporated by reference to Exhibit 10.12 to the 2005 10-K.*
10.7	Form of Annual Director Option Agreement for July 2005 option grants under the 2003 Plan. Incorporated by reference to Exhibit 10.14 to the 2005 10-K.*
10.8	Form of Incentive Stock Option Award Agreement relating to January 2009 option grants under the 2003 Plan. Incorporated by reference to Exhibit 10.16 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2008 (the 2008 10-K ).*
10.9	Form of Employee Nonqualified Stock Option Award Agreement relating to January 2009 option grants under the 2003 Plan. Incorporated by reference to Exhibit 10.17 to the 2008 10-K.*
10.10	Form of Non-Employee Director Option Award Agreement relating to January 2009 option grants under the 2003 Plan. Incorporated by reference to Exhibit 10.18 to the 2008 10-K.*
10.11	2009 Stock Incentive Plan of the Registrant (the 2009 Plan ). Incorporated by reference to Exhibit 10.2 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2009.*
10.12	Form of Incentive Stock Option Award Agreement under the 2009 Plan. Incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2010 (the 2010 First Quarter 10-Q ).*
10.13	Form of Employee Nonqualified Stock Option Award Agreement under the 2009 Plan. Incorporated by reference to Exhibit 10.2 to the 2010 First Quarter 10-Q.*
10.14	Form of Non-Employee Director Nonqualified Stock Option Award Agreement under the 2009 Plan. Incorporated by reference to Exhibit 10.3 to the 2010 First Quarter 10-Q.*
10.15	Employment Agreement between the Registrant and Michael L. Elich, dated September 25, 2001. Incorporated by reference to Exhibit 10.17 to the Registrant's Registration Statement on Form S-2 (Registration No. 333-126496) filed July 11, 2005.*
10.16	Summary of compensatory arrangements for non-employee directors of the Registrant. Incorporated by reference to Exhibit 10.16 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2013 (the 2013 10-K ).*
10.17	Form of Incentive Stock Option Award Agreement under the Registrant's 2009 Stock Incentive Plan (the 2009 Plan ). Incorporated by reference to Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2011 (the 2011 First Quarter 10-Q ).*

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10.18	Form of Employee Nonqualified Stock Option Award Agreement under the 2009 Plan. Incorporated by reference to Exhibit 10.2 to the 2011 First Quarter 10-Q.*
10.19	Form of Non-Employee Director Nonqualified Stock Option Award Agreement under the 2009 Plan. Incorporated by reference to Exhibit 10.3 to the 2011 First Quarter 10-Q.*
10.20	Change in Control Employment Agreement between the Registrant and Michael L. Elich, dated April 12, 2011. Incorporated by reference to Exhibit 10.4 to the 2011 First Quarter 10-Q.*
10.21	Change in Control Employment Agreement between the Registrant and Gregory R. Vaughn, dated April 12, 2011. Incorporated by reference to Exhibit 10.5 to the 2011 First Quarter 10-Q.*
10.22	Change in Control Employment Agreement between the Registrant and James D. Miller, dated April 12, 2011. Incorporated by reference to Exhibit 10.6 to the 2011 First Quarter 10-Q.*
10.23	Form of Indemnification Agreement with each outside director of Barrett Business Services, Inc. Incorporated by reference to Exhibit 10.1 to the registrant's Current Report on Form 8-K filed April 16, 2012.
10.24	Form of Employee Restricted Stock Units Award Agreement under the 2009 Plan. Incorporated by reference to Exhibit 10.1 to the 2012 Third Quarter 10-Q.*
10.25	Form of Non-Employee Director Restricted Stock Units Award Agreement under the 2009 Plan. Incorporated by reference to Exhibit 10.2 to the 2012 Third Quarter 10-Q.*
10.26	Death Benefit Agreement entered into by the Registrant and Michael L. Elich effective January 1, 2014. Incorporated by reference to Exhibit 10.27 to the 2013 10-K.*
10.27	Death Benefit Agreement entered into by the Registrant and Gregory R. Vaughn effective January 1, 2014. Incorporated by reference to Exhibit 10.28 to the 2013 10-K.*
10.28	Death Benefit Agreement entered into by the Registrant and James D. Miller effective January 1, 2014. Incorporated by reference to Exhibit 10.29 to the 2013 10-K.*
10.29	Barrett Business Services, Inc. Annual Cash Incentive Award Plan, Incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on March 13, 2014.*
21.	Subsidiaries of the Registrant.
23.1	Consent of Moss Adams LLP, Independent Registered Public Accounting Firm.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a).
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a).
32.	Certification pursuant to 18 U.S.C. Section 1350.
99.1	Description of Capital Stock. Incorporated by reference to Exhibit 99.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012.

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101.	INS XBRL Instance Document
101.	SCH XBRL Taxonomy Extension Schema Document
101.	CAL XBRL Taxonomy Extension Calculation Linkbase Document
101.	DEF XBRL Taxonomy Extension Definition Linkbase Document
101.	LAB XBRL Taxonomy Extension Label Linkbase Document
101.	PRE XBRL Taxonomy Extension Presentation Linkbase Document

\* Denotes a management contract or a compensatory plan or arrangement.

\*\* Except as otherwise indicated, the SEC File Number for all exhibits is 000-21866.