

PRGX GLOBAL, INC.  
Form 10-K  
March 13, 2013  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2012

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-28000

**PRGX Global, Inc.**

(Exact name of registrant as specified in its charter)

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**Georgia**  
(State or other jurisdiction of  
incorporation or organization)

**58-2213805**  
(I.R.S. Employer  
Identification No.)

**600 Galleria Parkway**  
**Suite 100**

**Atlanta, Georgia**  
(Address of principal executive offices)

**30339-5986**  
(Zip Code)

**Registrant's telephone number, including area code: (770) 779-3900**

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

<b>Title of each class</b>	<b>Name of each exchange on which registered</b>
<b>Common Stock, No Par Value</b>	<b>The NASDAQ Stock Market LLC (The Nasdaq Global Select Market)</b>
<b>Preferred Stock Purchase Rights</b>	<b>The NASDAQ Stock Market LLC (The Nasdaq Global Select Market)</b>

**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

**Note** Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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

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

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Large accelerated filer  Accelerated filer   
Non-accelerated filer  Small reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

The aggregate market value, as of June 30, 2012, of common shares of the registrant held by non-affiliates of the registrant was approximately \$167.5 million, based upon the last sales price reported that date on The Nasdaq Global Select Market of \$7.95 per share. (Aggregate market value is estimated solely for the purposes of this report and shall not be construed as an admission for the purposes of determining affiliate status.)

Common shares of the registrant outstanding as of February 27, 2013 were 28,562,575.

**Documents Incorporated by Reference**

Part III: Portions of Registrant's Proxy Statement relating to the Company's 2013 Annual Meeting of Shareholders.

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**Cautionary Statement Regarding Forward-Looking Statements**

The following discussion includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are at times identified by words such as plans, intends, expects, or anticipates and words of similar effect and include statements regarding the Company's financial and operating plans and goals. These forward-looking statements include any statements that cannot be assessed until the occurrence of a future event or events. Except as otherwise indicated or unless the context otherwise requires, PRGX, we, us, our and the Company refer to PRGX Global, Inc. and its subsidiaries.

These forward-looking statements are subject to risks, uncertainties and other factors, including but not limited to those discussed herein and below under Item 1A **Risk Factors**. Many of these risks are outside of our control and could cause actual results to differ materially from the results discussed in the forward-looking statements. Factors that could lead to material changes in our performance may include, but are not limited to:

our ability to successfully execute our recovery audit growth strategy;

our continued dependence on our largest clients for significant revenue;

changes to Medicare and Medicaid recovery audit contractor ( RAC ) programs and our role in the national Medicare RAC program, the results of operations of which are included in our Healthcare Claims Recovery Audit business;

changes to revenue from our Medicare audit recovery work due to a number of pressures and uncertainties affecting Medicare spending generally and over which we have little or no control;

revenue that does not meet expectations or justify costs incurred;

our ability to develop material sources of new revenue in addition to revenue from our core accounts payable recovery audit services; changes in the market for our services;

client and vendor bankruptcies and financial difficulties;

our ability to retain and attract qualified personnel;

our inability to protect and maintain the competitive advantage of our proprietary technology and intellectual property rights;

our reliance on operations outside the U.S. for a significant portion of our revenue;

the highly competitive environments in which our recovery audit services and Profit Optimization services businesses operate and the resulting pricing pressure on those businesses;

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our ability to integrate recent and future acquisitions;

our ability to realize operational cost savings and the transformation severance and related expenses we may incur to generate these savings;

uncertainty in the global credit markets;

our ability to maintain compliance with our financial covenants;

a cyber-security incident involving the misappropriation, loss or unauthorized disclosure or use of confidential information of our clients;

effects of changes in accounting policies, standards, guidelines or principles; or

terrorist acts, acts of war and other factors over which we have little or no control.

Any forward-looking statement speaks only as of the date on which such statement is made, and, except as required by law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time and it is not possible for management to predict all such factors.

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**PART I**

**ITEM 1. Business**

PRGX Global, Inc., together with its subsidiaries, is an analytics-powered information and professional services firm based in the United States of America ( U.S. ). PRGX Global, Inc. was incorporated in the State of Georgia in 1996. At the heart of our client services portfolio is the core capability of mining client data to deliver actionable insights. Actionable insights allow our clients to improve their financial performance by reducing costs, improving business processes and increasing profitability. In 2010, we rebranded the Company as PRGX and adopted the tagline Discover Your Hidden Profits.

We currently provide services to clients in approximately 40 countries, and conduct our operations through three reportable segments: Recovery Audit Services Americas, Recovery Audit Services Europe/Asia-Pacific and New Services. The Recovery Audit Services Americas segment represents recovery audit services (other than Healthcare Claims Recovery Audit services) we provide in the U.S., Canada and Latin America. The Recovery Audit Services Europe/Asia-Pacific segment represents recovery audit services (other than Healthcare Claims Recovery Audit services) we provide in Europe, Asia and the Pacific region. The New Services segment represents Healthcare Claims Recovery Audit services and our Profit Optimization services (formerly referred to as analytics and advisory services). We report the unallocated portion of corporate selling, general and administrative expenses not specifically attributable to the three reportable segments in Corporate Support. For additional financial information relating to our reporting segments, see *Note 2 Operating Segments and Related Information* of our Consolidated Financial Statements included in Item 8 of this Form 10-K.

Our core business is recovery audit, a service based on the mining of a tremendous amount of our clients purchasing data, looking for overpayments to their third-party suppliers. Most of our large retail clients in mature geographic markets employ their own internal staff to audit and recover overpayments to suppliers, engaging us as a supplement to this internal function. For other clients, including some large and mid-size retailers and our commercial (non-retail) clients, we serve as the complete outsourced provider of this standard function. We process over 2.1 million client files each year, including purchase orders, receipt and shipment data, invoices, payables data and point of sales data, and, at any point in time, have over six petabytes of client data available for analysis.

Our Healthcare Claims Recovery Audit services involve the identification of overpayments and underpayments made to healthcare providers such as hospitals and physicians practices. We identify such improper payments by using various methods, including proprietary methods which are comparable to the proprietary techniques we developed through many years of performing other types of recovery audits involving massive volumes of transaction data. Auditing medical claims data requires that we maintain a staff of healthcare professionals with in-depth expertise in healthcare procedures and billing processes.

Our Profit Optimization services target client functional and process areas where we have established expertise, enabling us to provide services to senior finance executives to optimize working capital, reduce enterprise costs, transform the finance function and improve corporate performance. Recovery audit services operate in a mindset of continuous improvement, i.e., reporting on the over-payment categories and their root causes. Our Profit Optimization services teams are well-positioned to help clients resolve many of the root causes of errors identified as part of our recovery audit services. These teams also enhance our client value propositions relating to spend analytics and sourcing/procurement excellence. We use the data from our clients to create spend reporting at the line-item level of detail, a capability that many of our clients do not possess in-house. This information enables us to assist clients with supplier rationalization, collaborative purchasing, strategic sourcing and procurement transformation, all of which can dramatically enhance the clients bottom lines.

We provide certain of our insights through web-based technologies using the SaaS (software as a service) delivery model. Our SaaS model uses a periodic license fee allowing clients to tailor service levels such as frequency of data refresh and scope of reporting outputs. Our range of software-based solutions extends to fraud prevention and compliance reporting, control monitoring and contract management. As our clients data volumes and complexity levels continue to grow, we are using our deep data management experience to incubate new actionable insight solutions in retail and healthcare, as well as to develop custom analytics services. Taken together, our software capability and solutions provide multiple routes to helping our clients achieve greater profitability.

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### **The PRGX Strategy and Client Value Propositions**

During 2009, our executive management team performed an extensive review of our competitive advantages and marketplace opportunities and developed a revised business strategy for growth. The five components of this growth strategy are:

1. grow the accounts payable recovery audit business;
2. trailblaze accountability in healthcare;
3. expand data mining for profitability;
4. broaden our services footprint; and
5. build a strong team with a high-performance culture.

These elements of our growth strategy represent our plans to reinvigorate our core business while significantly expanding our services portfolio. The go-to-market strategy is built on a competency foundation that includes data mining, audit/forensics capabilities, finance and procure-to-pay business process expertise, and a proprietary business intelligence platform. We now refer to these as our core capabilities of Audit, Analytics and Advice. We believe that we can combine these core capabilities effectively to discover and deliver hidden profits for our clients, enabling the creation of a new service category in the professional services marketplace: *Profit Discovery*.

We have identified five major routes to discover profits for clients, each of which we refer to as a Client Value Proposition, or CVP. These CVPs represent our services portfolio, and we discuss them within the descriptions of the various planks of our growth strategy below.

#### *Grow the Accounts Payable Recovery Audit Business*

The **Grow the Accounts Payable Recovery Audit Business** component of our business strategy is focused on expanding our traditional stronghold in recovery audit in the retail industry, along with a renewed focus on profitably delivering recovery audit services to non-retail (or what we internally refer to as commercial ) clients.

To facilitate growth in the accounts payable recovery audit market, we have reintroduced a dedicated sales force. In addition, we have increased our focus on the quality of our client relationships and management of our existing client accounts. We also have established alliance agreements with several third-party service providers to allow us to offer our clients a comprehensive suite of recovery audit services beyond accounts payable to include tax, real estate, and telecommunications audits. The new service offerings made possible by these alliance partners broaden the scope of audits with existing clients, and we expect them to help us establish new client relationships and business opportunities around the globe. With a keen focus on business development and audit strategy, we succeeded in growing our recovery audit business in 2011 for the first year-over-year increase in revenue since 2002. Although our revenue from this business declined slightly in 2012, we believe we will grow recovery audit revenue in 2013.

**Next-Generation Recovery Audit**, one of our five Client Value Propositions, aims to build on these improvements by delivering a better recovery audit service to our clients. We completed the initial development of our Next-Generation Recovery Audit business model and implemented it in several client teams in 2011. Through this model, we are introducing innovation in best practices for recovery audit, increasing the quality and consistency of service and implementing sophisticated central data storage, audit technologies and tools. These improvements also enabled us to lower our cost of delivering our services in both 2011 and 2012, and we believe that we will realize further improvements in 2013.

Key to serving clients more efficiently and cost-effectively under our Next-Generation Recovery Audit service delivery model is success in our offshoring initiative. In 2010, we established our operations in Pune, India, and now have over 220 employees in India, providing business analytics, information technology and other support services to our client teams in other parts of the world. This initiative was a key factor in



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improving our Recovery Audit Services Americas gross margins from 43.9% in 2011 to 47.2% in 2012. Also, by lowering our cost of delivery, we are significantly expanding the addressable target market for our recovery audit services. Historically, much of our recovery audit focus has been on clients in the retail industry due to the enormous volumes of transactions engaged in by these clients. With the improvements in our service delivery model that we are building into Next-Generation Recovery Audit, we believe we can compete more effectively in our core retail market, and also can profitably expand our service offerings to industries such as manufacturing, energy, financial institutions and

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transportation and logistics. We further enhanced our capabilities in this area with our December 2011 acquisition of Business Strategy, Inc. (BSI). We acquired BSI for the scale and efficiencies we believe it will deliver to us in the commercial recovery audit arena. Building on this acquisition, we created a world-class shared service center in Grand Rapids, Michigan.

### *Trailblaze Accountability in Healthcare*

The primary focus of our Healthcare Claims Recovery Audit services to date has been the auditing of Medicare spending as part of the legislatively mandated Medicare recovery audit contractor (RAC) program of the Centers for Medicare and Medicaid Services (CMS), the federal agency that administers the Medicare program. From March 2005 through March 2008, we were one of three recovery audit contractors that participated in CMS's Medicare RAC demonstration project. Under the demonstration project, we were responsible for auditing Medicare spending in the State of California. Under CMS's national Medicare RAC program, we are operating as a subcontractor in three of the national Medicare RAC program's four geographic regions. The principal services we provide as part of the Medicare RAC program involve the identification of overpayments and underpayments made by Medicare to healthcare providers, such as hospitals and physicians' practices. We identify such improper payments by using various methods, including proprietary methods that are comparable to the proprietary techniques we developed through many years of performing other types of recovery audits involving massive volumes of transaction data.

Our second Client Value Proposition, **Healthcare Claims Recovery Audit**, drives our growth strategy in healthcare to execute with excellence our role in the Medicare RAC program, and leverage our healthcare services infrastructure to expand recovery audit services to other healthcare payers. We have invested heavily in the infrastructure and tools required to execute our Medicare RAC program subcontracts and believe much of this infrastructure can be applied to the audit of medical claims paid by other healthcare payers.

As a result of health care reform in the U.S., as reflected in the Patient Protection and Affordable Care Act, which became law in 2010, recovery auditing of medical claims is now mandated for state Medicaid programs. As the opportunities to serve these state Medicaid programs emerge, we are focusing our efforts on opportunities where our capabilities are a good match for the scope and administration of a state's Medicaid program. With these filters in place, we have selectively competed in a number of state Medicaid procurements. We were awarded the Medicaid RAC contracts for Mississippi, Rhode Island and the District of Columbia and have begun associated audit activities.

In addition to audits of medical claims under the Medicare and Medicaid programs, we believe that private payers, including health insurance companies, represent a significant opportunity for our recovery audit services, and that we are well-positioned to further grow our Healthcare Claims Recovery Audit business by focusing on the private payer market. We currently are focusing our sales capabilities on the numerous opportunities for sales of healthcare claims recovery auditing on behalf of government entities and plan to expand this focus to include private payers and self-insured employers.

### *Expand Data Mining for Profitability*

In 2010, we launched Profit Optimization, an integrated set of analytics and advisory services across drivers of client profitability other than the recovery of overpayments. Our current Profit Optimization CVPs are Spend Optimization, Fraud Prevention & Compliance, and Profit Performance Optimization. We continue to enhance our client value proposition around spend analytics and sourcing/procurement excellence. In our third CVP, **Spend Optimization**, we analyze line-item purchasing detail and provide insights from that analysis to our clients. This information enables our clients to better manage their businesses by improving their ability to bundle their spend dollars, source their direct and indirect goods globally, negotiate better terms with their suppliers and vendors, organize their procurement organizations and implement better internal processes and controls.

Our fourth CVP, **Fraud Prevention & Compliance**, leverages the unique insights we gain from working closely with our clients in finance, audit and loss prevention and the sophisticated proprietary audit tools we use to mine clients' data to discover where there is a risk of fraud or abuse. Through these services, we help clients protect their organization's assets, and our reports document and record their proactive efforts to develop an effective fraud management program that anticipates, prevents, detects and remedies fraud and abuse.

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### *Broaden Our Services Footprint*

Senior executives of complex organizations regularly require external help to identify and maximize profit improvement opportunities. Our Profit Optimization services combine data analytics with deep functional expertise and a practical hands-on approach to help these client executives improve their operating margins.

**Profit Performance Optimization**, our fifth CVP, leverages these capabilities and our long-standing client relationships by providing services including working capital optimization, corporate performance management, enterprise cost reduction and finance transformation to senior finance executives. These services focus on improving the profitability of our clients' procure-to-pay cycle and on merchandise optimization.

### *Build a Strong Team with a High-Performance Culture*

The final element of our strategy is to become a magnet for global talent and expertise relevant to our service lines and operations. As part of our overall transformation, we are building a culture of results-oriented performance and collaboration, and an environment that promotes innovation and knowledge sharing. This transformation is crucial to ensure that we capture, understand, and deploy the very best practices consistently across every client globally. In addition, we have maintained our increased focus on recruiting. The success of our growth strategy is predicated on continuously improving the capabilities of our client-facing personnel who identify the levers to add to clients' profitability and effectively position all of our service offerings.

### *Update on Our Strategy Execution*

We now have completed two years since the implementation of our growth strategy, and we are encouraged by the success we have achieved to date. In 2011, our accounts payable recovery audit business generated the first year-over-year increase in revenue since 2002. This revenue declined slightly in 2012, but our cost of revenue declined by a greater amount, resulting in incremental gross profit of \$4.2 million in 2012 compared to 2011. These improvements in financial performance over the last two years occurred while we were making significant investments in our accounts payable recovery audit segments, including re-implementing a sales force, establishing and expanding offshore capabilities, completing strategic acquisitions and developing and refining our Next-Generation Recovery Audit service delivery model. We will continue to drive toward increasing our revenue and lowering our costs as a percentage of revenue in accounts payable recovery audit.

Our Healthcare Claims Recovery Audit business grew significantly from 2010 to 2012, and generated positive adjusted earnings before interest, taxes, depreciation and amortization in 2012. This unit more than doubled its revenue in 2012, and we anticipate that we will continue to improve our operating results in this service line in 2013.

We also invested in our Profit Optimization services business over the past three years, both organically and through acquisitions. We have acquired, developed and improved the tools we use in performing these services. The acquisitions we completed in this area also helped us to broaden our services footprint and provide extensive services to our clients and prospective clients. We believe our recent success in adding new clients and improving client retention rates in our recovery audit businesses is due in part to these additional service offerings, although these benefits are not reflected in the New Services segment.

Collectively, these changes reflect our transformation from essentially a one-product, one-industry provider to an analytics-powered information and professional services firm. We believe that Profit Discovery, our combination of audit, analytics and advisory capabilities, represents a new category of business services that will enable us to provide greater value to our existing clients and to expand our reach into new clients and industries.

### **The Recovery Audit Industry and PRGX**

Many businesses and government agencies generate substantial volumes of payment transactions involving multiple vendors, numerous discounts and allowances, fluctuating prices and complex pricing arrangements or rate structures. Although these entities correctly process the vast majority of payment transactions, errors occur in a small percentage of transactions. These errors include, but are not limited to, missed or inaccurate discounts, allowances and rebates, vendor pricing errors, erroneous coding and duplicate payments. In the aggregate, these transaction errors can represent significant amounts of reduced cash flow and lost profits for these entities. Many factors contribute to the errors, including communication failures between the purchasing and accounts payable departments, complex pricing arrangements or rate structures, personnel turnover and changes in information and accounting systems.



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Recovery auditing is a business service focused on finding overpayments created by these errors. We are the leading worldwide provider of recovery audit services, principally to large businesses and government agencies having numerous payment transactions and complex purchasing/payment environments. These businesses and agencies include:

retailers such as discount, department, specialty, grocery and drug stores, and wholesalers who sell to these retailers;

business enterprises other than retailers, such as manufacturers, financial services firms, and pharmaceutical companies;

healthcare payers, both private sector health insurance companies and state and federal government payers such as CMS; and

federal and state government agencies other than government healthcare payers.

Under virtually all of our recovery audit contracts, we receive a percentage of overpayments and other savings that we identify and that our clients recover or realize. We generate the substantial majority of our revenue from accounts payable recovery audit services that we provide to retail clients. These audit services typically recur annually and are the most extensive of our recovery audit services, focusing on numerous recovery categories related to procurement and payment activities, as well as client/vendor promotions and allowances. These audits typically entail comprehensive and customized data acquisition from the client, frequently including purchasing, receiving, point-of-sale, pricing and deal documentation, emails, and payment data. Recovery audits for larger retail clients often require year-round on-site work by multi-auditor teams.

In addition to these retail clients, we also provide accounts payable recovery audit services to clients in other industries. We typically refer to these clients as our commercial clients. Services to these types of clients tend to be either periodic (typically, every two to three years) or rotational in nature with different divisions of a given client being audited in pre-arranged periodic sequences, and are typically relatively short in duration. Accordingly, the revenue we derive from a given commercial client may change markedly from year to year.

The recovery audit services we provide to our retail and commercial clients involve the identification of overpayments relating to purchases. We also provide recovery audit services relating to healthcare claims which involve the identification of overpayments and underpayments made by healthcare payers to healthcare providers, such as hospitals and physicians' practices. Auditing medical claims data requires in-depth expertise in healthcare procedures and billing processes. Due to the different expertise necessary to provide such services, we include the results of our operations of Healthcare Claims Recovery Audit services in our New Services segment rather than in one of our two recovery audit services segments.

Some organizations (primarily large retailers) maintain internal recovery audit departments to recover certain types of payment errors and identify opportunities to reduce costs. Despite having such internal resources, many companies also retain independent recovery audit firms, such as PRGX, due to their specialized knowledge and focused technologies. In the U.S., Canada, the United Kingdom and France, large retailers routinely engage independent recovery audit firms as a standard business practice. In other countries, large retailers and many other types of businesses also engage independent recovery audit firms, but this practice is less common.

As businesses have evolved, PRGX and the recovery audit industry have evolved with them, innovating processes, error identification tools, and claim types to maximize recoveries. The following are a number of factors significantly impacting the recovery audit industry:

*Data Capture and Availability.* Businesses increasingly are using technology to manage complex procurement and accounts payable systems and realize greater operating efficiencies. Many businesses worldwide communicate with vendors electronically—whether by Electronic Data Interchange (EDI) or the Internet—to exchange inventory and sales data, transmit purchase orders, submit invoices, forward shipping and receiving information and remit payments. These systems capture more detailed data and enable the cost effective review of more transactions by recovery auditors.

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*Increased Role of Email Documentation in Client Transaction Data.* Clients and vendors increasingly document transaction terms in email correspondence that is not integrated into their financial systems and increases opportunities for errors. To efficiently identify these errors, recovery audit firms must use sophisticated tools that are able to ingest and search through massive volumes of emails to identify potential errors that then are investigated by the auditors. A comprehensive recovery audit requires the effective use of email search tools and techniques.

*Increasing Number of Auditable Claim Categories.* Traditionally, the recovery audit industry identified simple, or disbursement, claim types such as the duplicate payment of invoices. Enhancements to accounts payable software, particularly large enterprise software solutions used by many large companies, have reduced the extent to which these companies make simple disbursement errors. However, the introduction of creative vendor discount programs, complex pricing arrangements and activity-based incentives has led to an increase in auditable transactions and potential sources of error. These transactions are complicated to audit, as the underlying transaction data is difficult to access and recognizing mistakes is complex. Recovery audit firms such as PRGX with significant industry-specific expertise and sophisticated technology are best equipped to audit these complicated, or contract compliance, claim categories.

*Globalization.* As the operations of major retailers and other business enterprises become increasingly global, they often seek service providers with a global reach.

*Consolidation in the Retail Industry.* Retailer consolidation continues in both the U.S. and internationally. As retailers grow larger, vendors become more reliant on a smaller number of retailer customers, and, as a result, the balance of power favors retailers rather than their vendors. This dynamic creates an environment that allows retailers to assert overpayment claims more easily.

*Significant Promotional Activity.* Trade promotion spending is substantial within the retail trade and significant sums are being spent in categories with numerous transactions and a high potential for errors, such as scan downs, or discounts at the point of sale. Because of the high volume of trade promotion within retail, there are significant opportunities for mistakes and, therefore, auditable claims.

*Move Toward Standard Auditing Practices.* Increasingly, our clients vendors are insisting on the satisfaction of certain conditions, such as clearer post-audit procedures, better documentation and electronic communication of claims, before accepting the validity of a claim.

We expect the evolution of the recovery audit industry to continue. In particular, we expect that the industry will continue to move towards the electronic capture and presentation of data, more automated, centralized processing and faster approvals and deductions of claims.

### **Clients**

PRGX provides its services principally to large and mid-sized businesses and government agencies having numerous payment transactions and complex procurement environments. Retailers continue to constitute the largest part of our client and revenue base. Our five largest clients contributed approximately 28.2% of our revenue in 2012, 30.2% in 2011 and 31.3% in 2010. Wal-Mart Stores, Inc. (and its affiliated companies) accounted for approximately 10.2% of our revenue in 2011 and 12.1% in 2010. No client accounted for 10% or more of total revenue in 2012.

### **Client Contracts**

PRGX provides services to its clients pursuant to contracts. Our compensation under recovery audit service contracts generally is stated as a stipulated percentage of improper payments or other savings recovered for or realized by clients. Recovery audit clients generally recover claims by either (a) taking credits against outstanding payables or future purchases from the involved vendors or service providers, or (b) receiving refund checks directly from those vendors or service providers. Industry practice generally dictates the manner in which a client receives a recovery audit claim. In many cases, we must satisfy client-specific procedural guidelines before we can submit recovery audit claims for client approval. For services such as Profit Optimization services, client contracts often provide for compensation to us in the form of a flat fee, fee rate per hour, or a fee per other unit of service.

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Most of our contracts provide that the client may terminate the contract without cause prior to the completion of the term of the agreement by providing relatively short prior written notice of termination. In addition to being subject to termination for material default, our Medicare RAC program subcontracts are subject to termination or

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partial termination for convenience to the extent all or any portion of the work covered by the associated Medicare RAC prime contract is eliminated by CMS, or to the extent our performance of the subcontract results in an organizational conflict of interest that is not mitigated or able to be mitigated after joint consultation among CMS, the Medicare RAC prime contractor and PRGX. See Management's Discussion and Analysis of Financial Condition and Results of Operations included in Item 7 of this Form 10-K for recent developments related to the Medicare RAC program.

## **Technology**

PRGX uses advanced, proprietary information systems and processes and a large-scale technology infrastructure to conduct its audits of clients payment transactions. Because of the ever-increasing volume and complexity of the transactions of our clients, we believe that our proprietary technology and processes serve as important competitive advantages over both our principal competitors and our clients' in-house internal recovery audit functions. To sustain these competitive advantages, we continually invest in technology initiatives to deliver innovative solutions that improve both the effectiveness and efficiency of our services.

We aim our data acquisition, data processing and data management methodologies at maximizing efficiencies and productivity and maintaining the highest standards of transaction auditing accuracy. At the beginning of a typical recovery audit engagement, we use a dedicated staff of data acquisition specialists and proprietary tools to acquire a wide array of transaction data from the client for the time period under review. We typically receive this data by secured electronic transmissions, digital media or paper. For paper-based data, we use a custom, proprietary imaging technology to scan the paper into electronic format. Upon receipt of the data, we secure, catalogue, back up and convert it into standard, readable formats using third party and proprietary tools.

Our technology professionals clean and map massive volumes of client data, primarily using high performance database and storage technologies, into standardized layouts at one of our data processing facilities. We also generate statistical reports to verify the completeness and accuracy of the data.

We then process the data using proprietary algorithms (business rules) leveraging over thirty years' experience to help uncover patterns or potential problems in clients' various transactional streams. We deliver this data with a high probability of transaction errors to our auditors who, using our proprietary audit software, sort, filter and search the data to validate and identify actual transaction errors. We also maintain a secure database of audit information with the ability to query on multiple variables, including claim categories, industry codes, vendors and audit years, to facilitate the identification of additional recovery opportunities and provide recommendations for process improvements to clients.

Once we identify and validate transaction errors, we present the information to clients for approval and submission to vendors as claims. We offer a web-based claim presentation and collaboration tool, which uses proprietary imaging technology to help the client view, approve and submit claims to vendors.

In providing our spend analytics services, we use proprietary algorithms and technologies to clean and classify a client's vendor spend data down to the line item level. We then are able to present this information to the client as a multi-dimensional data cube over a web-based interface. We believe these proprietary algorithms and technologies provide us with a competitive advantage over many of our competitors.

## **Auditor Hiring, Training and Compensation**

Many of our auditors and specialists formerly held finance-related management positions in the industries we serve. Training provided in the field by our experienced auditors enables newly hired auditors to develop and refine their auditing skills and improve productivity. Additionally, we provide training for auditors utilizing self-paced media such as specialized computer-based training modules. We periodically upgrade our training programs based on feedback from auditors and changing industry protocols. Many of our auditors and specialists participate in one of our incentive compensation plans that link compensation of the auditor or specialist to audit performance.

## **Proprietary Rights**

From time to time, we develop new software and methodologies that replace or enhance existing proprietary software and methodologies. We rely primarily on trade secret and copyright protection for our proprietary software



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and other proprietary information. We consider the costs associated with these activities to be research and development costs and expense them as incurred. However, we capitalize the costs incurred for the development of computer software that will be sold, leased, or otherwise marketed or that will be used in our operations beginning when technological feasibility has been established. Research and development costs, including the amortization of amounts previously capitalized, were \$4.0 million in 2012, \$3.4 million in 2011 and \$3.2 million in 2010.

We own or have rights to various trademarks, trade names and copyrights, including U.S. and foreign registered trademarks and trade names and U.S. registered copyrights, that are valuable assets and important to our business. We monitor the status of our copyright and trademark registrations to maintain them in force and renew them as appropriate. The duration of our active trademark registrations varies based upon the relevant statutes in the applicable jurisdiction, but generally endure for as long as they are used. The duration of our active copyright registrations similarly varies based on the relevant statutes in the applicable jurisdiction, but generally endure for the full statutory period. Our trademarks and trade names are of significant importance and include, but are not limited to, the following: PRGX®, Discover Your Hidden Profits®, PRG-Schultz®, imDex®, SureF!nd®; Profit Discovery , AuditPro , DirectF!nd , claimDex , GET ; PRGX APTrax , PRGX AuditTrax PRGX ClaimTrax , PRGX MailTrax , PRGX FraudTrax , PRGX MerchTrax , and PRGX SpendTrax .

## **Competition**

### *Accounts Payable Recovery Audit*

We believe that the principal providers of domestic and international accounts payable recovery audit services in major markets worldwide consist of PRGX, one substantial competitor, and numerous other smaller competitors. The smaller recovery audit firms generally do not possess multi-country service capabilities and do not have the centralized resources or broad client base required to support the technology investments necessary to provide comprehensive recovery audit services for large, complex accounts payable systems. These smaller firms, therefore, are less equipped to audit large, data-intensive purchasing and accounts payable systems. In addition, many of these firms have limited resources and may lack the experience and knowledge of national promotions, seasonal allowances and current recovery audit practices. As a result, we believe that compared to most other firms providing accounts payable recovery audit services, PRGX has competitive advantages based on its national and international presence, well-trained and experienced professionals, and advanced technology.

While we believe that PRGX has the greatest depth and breadth of audit expertise, data and technology capabilities, scale and global presence in the industry, we face competition from the following:

*Client Internal Recovery Audit Departments.* A number of large retailers (particularly those in the discount, grocery and drug sectors) have developed an internal recovery audit process to review transactions prior to turning them over to external recovery audit firms. Regardless of the level of recoveries made by internal recovery audit departments, we have observed that virtually all large retail clients retain at least one (primary), and sometimes two (primary and secondary), external recovery audit firms to capture errors not identified by their internal recovery audit departments.

*Other Accounts Payable Recovery Audit Firms.* The competitive landscape in the recovery audit industry is comprised of:

Full-service accounts payable recovery audit firms. We believe that only one company other than PRGX offers a full suite of U.S. and international recovery audit services;

A large number of smaller accounts payable recovery firms which have a limited client base and which use less sophisticated tools to mine disbursement claim categories at low contingency rates. These firms are most common in the U.S. market. Competition in most international markets, if any, typically comes from small niche providers;

Firms that offer a hybrid of audit software tools and training for use by internal audit departments, or general accounts payable process improvement enablers; and

Firms with specialized skills focused on recovery audit services for discrete sectors such as sales and use tax or real estate.



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*Other Providers of Recovery Audit Services.* The major international accounting firms provide recovery audit services; however, we believe their practices tend to be primarily focused on tax-related services.

### *Healthcare Claims Recovery Audit Services*

A number of national and regional private payers have developed their own post-payment recovery audit capabilities. Nevertheless, these private payers typically also retain or engage one or more third party post payment audit service providers. The competitive landscape in Healthcare Claims Recovery Audit services includes:

Firms that provide recovery audit services across multiple industries including healthcare;

Firms that provide healthcare IT solutions and services to both the government and private payers; and

Firms that contract with federal and state governments integrity programs.

### *Profit Optimization Services*

Our Profit Optimization services business faces competition from regional and local consulting firms; privately and publicly held worldwide and national firms; large, well-known ERP software vendors; procurement-specific software providers and smaller, very specialized analytics providers. These businesses compete generally on the basis of the range, quality and cost of the services and products provided to clients. We believe that we differentiate ourselves from our competitors by virtue of synergies with our analytics capabilities and our direct channel to existing accounts payable recovery audit clients.

## **Regulation**

Various aspects of our business, including, without limitation, our data acquisition, processing and reporting protocols, are subject to extensive and frequently changing governmental regulation in both the U.S. and internationally. These regulations include extensive data protection and privacy requirements. In the U.S., we are subject to the provisions of the Health Insurance Portability and Accountability Act of 1996 ( HIPAA ) with respect to our Healthcare Claims Recovery Audit work. Internationally, we must comply with the European Data Protection Directive that various members of the European Union have implemented, as well as with data protection laws that exist in many of the other countries where we have a presence. Failure to comply with such regulations may, depending on the nature of the noncompliance, result in the termination or loss of contracts, the imposition of contractual damages, civil sanctions, damage to our reputation or in certain circumstances, criminal penalties.

## **Employees**

As of January 31, 2013, PRGX had approximately 1,700 employees, of whom approximately 760 were in the U.S. The majority of our employees are involved in the audit function. None of our employees are covered by a collective bargaining agreement, and we believe our employee relations are satisfactory.

## **Website**

PRGX makes available free of charge on its website, [www.prgx.com](http://www.prgx.com), its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports. PRGX makes all filings with the Securities and Exchange Commission available on its website no later than the close of business on the date the filing was made. In addition, investors can access our filings with the Securities and Exchange Commission at [www.sec.gov](http://www.sec.gov).

We also post certain corporate governance materials, including our Board of Directors committee charters and our Code of Conduct and Code of Ethics For Senior Financial Officers, on our website under the heading Corporate Governance on the Investors page. From time to time, we may update the corporate governance materials on our website as necessary to comply with rules issued by the SEC or NASDAQ, or as desirable to further the continued effective and efficient governance of our company.



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**ITEM 1A. Risk Factors**

***Revenue from our accounts payable recovery audit business declined for several years through 2010. We must successfully execute our recovery audit growth strategy in order to increase our revenue, and must lower our cost of delivery in order to maintain profitability.***

Over time, our clients tend to resolve recurring transaction processing deficiencies. In addition, many of our clients have an internal staff that audits the transactions before we do. As the skills, experience and resources of our clients' internal recovery audit staffs improve, they will identify many overpayments themselves and reduce some of our audit recovery opportunities. Based on these and other factors, including competitive rate pressures and loss of clients from time to time, without improved audit execution and acquisition of new clients, we believe that our accounts payable recovery audit business will experience revenue declines and may incur losses.

***We depend on our largest clients for significant revenue, so losing a major client could adversely affect our revenue and liquidity.***

We generate a significant portion of our revenue from our largest clients. Our five largest clients collectively accounted for approximately 28.2% of our annual revenue in 2012, 30.2% in 2011 and 31.3% in 2010. Wal-Mart Stores Inc. (and its affiliated companies) accounted for approximately 10.2% of our total revenue in 2011 and 12.1% in 2010. No client accounted for 10% or more of total revenue in 2012. If we lose any of our major clients, our results of operations and liquidity could be materially and adversely affected.

Although we continually seek to diversify our client base, we may be unable to offset the effects of an adverse change in one of our key client relationships. For example, if our existing clients elect not to renew their contracts with us at the expiration of the current terms of those contracts, or reduce the services they purchase thereunder, our recurring revenue base will be reduced, which could have a material adverse effect on our results of operations. In addition, we could lose clients if they cancel their agreements with us, if we fail to win a competitive bid at the time of contract renewal, if the financial condition of any of our clients deteriorates or if our clients are acquired by, or acquire, companies with which we do not have contracts, any of which could materially and adversely affect our results of operations.

***Our growth strategy may not be successful.***

As discussed in Item 1 "The PRGX Strategy," our objectives are to build on our position as the leading worldwide provider of recovery audit services and to develop and grow our Profit Optimization and Healthcare Claims Recovery Audit services businesses. Our strategic plan to achieve these objectives focuses on efforts designed to maintain our dedicated focus on clients and rekindle our growth. These efforts are ongoing, and the results of the strategy will not be known until sometime in the future. Successful execution of our strategy requires sustained management focus, organization and coordination over time, as well as success in building relationships with third parties. If we are unable to execute our strategy successfully, our results of operations and cash flows could be adversely affected. In addition, execution of our strategy will require material investments and additional costs that may not yield incremental revenue and improved financial performance as planned.

***Our acquisitions, investments, partnerships and strategic alliances may require significant resources and/or result in significant unanticipated losses, costs or liabilities.***

Acquisitions have contributed to our growth. Although we cannot predict our rate of growth as the result of acquisitions with complete accuracy, we believe that additional acquisitions, investments and strategic alliances will be important to our growth strategy.

We may finance future acquisitions by issuing additional equity and/or debt. The issuance of additional equity in connection with any such transaction could be substantially dilutive to existing shareholders. The issuance of additional debt could increase our leverage substantially. In addition, announcement or implementation of future transactions by us or others could have a material effect on the price of our common stock. We could face financial risks associated with incurring additional debt, particularly if the debt results in significant incremental leverage. Additional debt may reduce our liquidity, curtail our access to financing markets, impact our standing with credit agencies and increase the cash flow required for debt service. Any incremental debt incurred to finance an acquisition could also place significant constraints on the operation of our business.

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Furthermore, any future acquisitions of businesses or facilities could entail a number of additional risks, including:

problems with effective integration of acquired operations;

the inability to maintain key pre-acquisition business relationships;

increased operating costs;

the diversion of our management team from its other operations;

problems with regulatory agencies;

exposure to unanticipated liabilities;

difficulties in realizing projected efficiencies, synergies and cost savings; and

changes in our credit rating and financing costs.

***The terms of our credit facility place restrictions on us, which create risks of default and reduce our flexibility.***

Our current credit facility contains a number of affirmative, negative, and financial covenants that limit our ability to take certain actions and require us to comply with specified financial ratios and other performance covenants. No assurance can be provided that we will not violate the covenants of our secured credit facility in the future. If we are unable to comply with our financial covenants in the future, our lenders could pursue their contractual remedies under the credit facility, including requiring the immediate repayment in full of all amounts outstanding, if any. Additionally, we cannot be certain that, if the lenders demanded immediate repayment of any amounts outstanding, we would be able to secure adequate or timely replacement financing on acceptable terms or at all.

Our ability to make payments due on our debt will depend upon our future operating performance, which is subject to general economic and competitive conditions and to financial, business and other factors, many of which we cannot control. If the cash flow from our operating activities is insufficient to make these payments, we may take actions such as delaying or reducing capital expenditures, attempting to restructure or refinance our debt, selling assets or operations or seeking additional equity capital. Some or all of these actions may not be sufficient to allow us to service our debt obligations and we could be required to file for bankruptcy. Further, we may be unable to take any of these actions on satisfactory terms, in a timely manner or at all. In addition, our credit agreements may limit our ability to take several of these actions. Our failure to generate sufficient funds to pay our debts or to undertake any of these actions successfully could materially and adversely affect our business, results of operations and financial condition.

***We have incurred and will continue to incur significant costs in establishing the necessary resources to provide services for Medicare, Medicaid and other healthcare claims audit recovery work.***

We have expended substantial resources in connection with preparing for and providing healthcare claims recovery audit services, including those under CMS's Medicare RAC program. We continue to incur significant costs relating to our healthcare claims recovery audit services business, including our participation as a subcontractor in the national Medicare RAC program. In addition, as a result of the complex regulations governing many healthcare payments and recoupments, including a multi-layered scheme for provider appeals of overpayment determinations under the Medicare RAC program, the terms of the Company's Medicare RAC subcontracts and the complexity of Medicare and other healthcare data, systems and processes, generally, it is more difficult and takes longer to achieve recoveries from healthcare claims recovery auditing than in other areas of our recovery audit business.

*Our participation in the Medicare recovery audit program is as a subcontractor, and, consequently, is subject to being reduced or eliminated should our subcontracts be terminated or should the prime contractors with whom we have contracted have their prime contracts with CMS terminated or should those contracts expire.*

Under CMS's Medicare recovery audit contractor program, we are participating as a subcontractor in three of the program's four geographic regions. Accordingly, we have entered into three separate subcontracts with the prime contractors and are not directly contracting with CMS. Under these circumstances, we generally bear the risk that the prime contractors will not meet their performance obligations to CMS under the prime contract, that the prime

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contractors will not pay us amounts due under the subcontracts and that the prime contractors will seek to terminate our subcontracts or otherwise minimize our role in the Medicare RAC program. Furthermore, the failure of a prime contractor to perform its obligations to CMS could result in the termination of the associated contract with CMS, which would, in turn, result in the termination of our subcontract. Additionally, based on recent developments, we believe CMS has agreed with the prime contractors to allow the prime contracts to expire in August 2013, subject to extension by CMS to allow for a transition period to the new RAC contracts. Should the prime contracts expire in August 2013, our RAC subcontracts will also expire at that time, subject to any additional extensions by CMS in connection with a transition to the new RAC contracts. The termination or expiration of any of these subcontracts or the failure of the prime contractors to make required payments to us could have a material adverse effect on our business, financial condition and results of operations.

***Recovery auditing of Medicare and Medicaid spending is subject to a number of pressures and uncertainties that could impact our future opportunities and revenue from this business.***

As contrasted with recovery audit services provided to our retail and commercial clients, recovery auditing of Medicare and Medicaid spending is legislatively mandated and is subject to, among other things, the efforts of healthcare providers and provider associations, including political pressures, to end or severely limit the Medicare and Medicaid recovery audit programs. We expect these efforts and political pressures to be ongoing throughout the life of these programs. If federally mandated recovery audit programs are significantly limited or delayed, subjected to burdensome or commercially challenging requirements, terms and/or conditions, or altogether terminated, our future revenue, operating results and financial condition could be materially and adversely affected.

***The prime contracts for the Medicare recovery audit program are expected to expire in August 2013, subject to an extension by CMS to allow for a transition period to the new RAC contracts, and we may not be selected to receive any prime contracts or subcontracts during the re-bid process.***

We currently serve as a subcontractor to the prime contractor on three of the four prime contracts in the Medicare RAC program. Based on recent developments, we believe CMS has agreed with the prime contractors to allow the prime contracts to expire in August 2013, subject to extension by CMS to allow for a transition period to the new RAC contracts. Should the prime contracts expire in August 2013, our RAC subcontracts will also expire at that time, subject to any additional extensions by CMS in connection with the transition to new RAC contracts, and contracts for the performance of future Medicare RAC services will be subject to a bidding process administered by CMS. CMS issued a request for proposals in connection with the re-bidding for the RAC contracts, and the proposals are due by March 27, 2013. CMS is expected to award the RAC contracts to more than one contractor and divide the country into geographic regions for contracting purposes. We will be competing to participate in the RAC program as a prime contractor through the bidding process. While we believe we are well-positioned to compete in the bidding process, there are no assurances that we will receive any contract when the new Medicare RAC contracts are ultimately awarded. The failure to receive any of these contracts could have a material adverse effect on our business, financial condition and results of operations.

***We may be unable to protect and maintain the competitive advantage of our proprietary technology and intellectual property rights.***

Our operations could be materially and adversely affected if we are not able to protect our proprietary software, audit techniques and methodologies, and other proprietary intellectual property rights. We rely on a combination of trade secret and copyright laws, nondisclosure and other contractual arrangements and technical measures to protect our proprietary rights. Although we presently hold U.S. and foreign registered trademarks and U.S. registered copyrights on certain of our proprietary technology, we may be unable to obtain similar protection on our other intellectual property. In addition, our foreign registered trademarks may not receive the same enforcement protection as our U.S. registered trademarks.

Additionally, to protect our confidential and trade secret information, we generally enter into nondisclosure agreements with our employees, consultants, clients and potential clients. We also limit access to, and distribution of, our proprietary information. Nevertheless, we may be unable to deter misappropriation or unauthorized dissemination of our proprietary information, detect unauthorized use and take appropriate steps to enforce our intellectual property rights. In spite of the level of care taken to protect our intellectual property, there is no guarantee that our sensitive proprietary information will not be improperly accessed or that our competitors will not independently develop technologies that are substantially equivalent or superior to our technology. Moreover,



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although we are not aware of any infringement of our services and products on the intellectual property rights of others, we also are subject to the risk that someone else will assert a claim against us in the future for violating their intellectual property rights.

***Cyber-security incidents, including data security breaches or computer viruses, could harm our business by disrupting our delivery of services, damaging our reputation or exposing us to liability.***

We receive, process, store and transmit, often electronically, the confidential data of our clients and others. Unauthorized access to our computer systems or stored data could result in the theft or improper disclosure of confidential information, the deletion or modification of records or could cause interruptions in our operations. These cyber-security risks increase when we transmit information from one location to another, including transmissions over the Internet or other electronic networks. Despite implemented security measures, our facilities, systems and procedures, and those of our third-party service providers, may be vulnerable to security breaches, acts of vandalism, software viruses, misplaced or lost data, programming and/or human errors or other similar events which may disrupt our delivery of services or expose the confidential information of our clients and others. Any security breach involving the misappropriation, loss or other unauthorized disclosure or use of confidential information of our clients or others, whether by us or a third party, could (i) subject us to civil and criminal penalties, (ii) have a negative impact on our reputation, (iii) expose us to liability to our clients, third parties or government authorities, and (iv) cause our present and potential clients to choose another service provider. Any of these developments could have a material adverse effect on our business, results of operations and financial condition.

***Operational failures in our data processing facilities could harm our business and reputation.***

An interruption of data processing services caused by damage or destruction of our facilities or a failure of our data processing equipment could result in a loss of clients, difficulties in obtaining new clients and a reduction in revenue. In addition, we also may be liable to third parties or our clients because of such interruption. These risks would increase with longer service interruptions. Despite any disaster recovery and business continuity plans and precautions we have implemented (including insurance) to protect against the effects of service delivery interruptions, such interruptions could result in a material adverse effect on our business, results of operations and financial condition.

***Our investment of substantial capital in information technology systems, and a failure to successfully implement such systems could adversely affect our business.***

We have invested and continue to invest substantial amounts in the development and implementation of information technology systems. Although investments are carefully planned, there can be no assurance that such systems will justify the related investments. If we fail to realize the benefits expected from our information technology system investments, or if we fail to do so within the envisioned timeframe, it could have an adverse effect on our results of operations and financial condition.

***Client and vendor bankruptcies and financial difficulties could reduce our earnings.***

Our clients generally operate in intensely competitive environments and, accordingly, bankruptcy filings by our clients are not uncommon. Bankruptcy filings by our large clients or the significant vendors who supply them or unexpectedly large vendor claim chargebacks lodged against one or more of our larger clients could have a materially adverse effect on our financial condition and results of operations. Similarly, our inability to collect our accounts receivable due to other financial difficulties of one or more of our large clients could adversely affect our financial condition and results of operations.

Recent economic conditions which have adversely impacted the retail industry in the U.K and Europe may continue to have a negative impact on our revenue. Since we generally audit our clients' purchases up to 15 months in arrears, we cannot yet determine if we have experienced the full impact of the recent economic downturn on our business and revenue. Specifically, client liquidity and the liquidity of client vendors can have a significant impact on claim production, the claim approval process, and the ability of clients to offset or otherwise make recoveries from their vendors.

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If a client files for bankruptcy, we could be subject to an action to recover certain payments received in the 90 days prior to the bankruptcy filing known as preference payments. If we are unsuccessful in defending against such claims, we would be required to make unbudgeted cash payments which could strain our financial liquidity, and our earnings would be reduced.

***Our failure to retain the services of key members of our management team and highly skilled personnel could adversely impact our operations and financial performance.***

Our future success depends largely on the efforts and skills of our management team, including our executive officers and other key employees. As such, we have entered into employment agreements with key members of our management team. While these employment agreements include limits on the ability of key employees to directly compete with us in the future, nothing prevents them from leaving our company. We also do not maintain key person life insurance policies on any of our executive officers or other key employees. Thus, we may have to incur costs to replace such employees if we were to lose their services, and our ability to execute our business strategy could be impaired if we are unable to replace such employees in a timely manner.

In addition, it is especially challenging to attract and retain highly qualified skilled auditors and other professionals in an industry where competition for skilled personnel is intense. Accordingly, our future performance also depends, in part, on the ability of our management team to work together effectively, manage our workforce, and retain highly qualified personnel.

***We rely on operations outside the U.S. for a significant portion of our revenue and are increasingly dependent on operations outside the U.S. for supporting our operations globally.***

Operations outside the U.S. generated approximately 40.4% of our annual revenue in 2012, 47.3% in 2011 and 49.7% in 2010. These international operations are subject to numerous risks, including:

greater exposure to the possibility of economic instability, the disruption of operations from labor and political disturbances, expropriation or war in the international markets we serve;

difficulties in staffing and managing foreign operations and in collecting accounts receivable;

fluctuations in currency exchange rates, particularly weaknesses in the British pound, the euro, the Canadian dollar, the Mexican peso, the Brazilian real and other currencies of countries in which we transact business, which could result in currency translations that materially reduce our revenue and earnings;

costs associated with adapting our services to our foreign clients' needs;

unexpected changes in regulatory requirements and laws;

expenses and legal restrictions associated with transferring earnings from our foreign subsidiaries to us;

difficulties complying with a variety of foreign laws and regulations, such as those relating to data content retention, privacy and employee welfare;

business interruptions due to widespread disease, potential terrorist activities, or other catastrophes;

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reduced or limited protection of our intellectual property rights;

longer accounts receivable cycles; and

competition with large or state-owned enterprises or regulations that effectively limit our operations and favor local competitors.

Because we expect a significant portion of our revenue to continue to come from operations outside the U.S., and expect to continue transitioning certain of our operations to locations outside the U.S., the occurrence of any of these events could materially and adversely affect our business, financial condition and results of operations.

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In 2012, our European operations accounted for approximately 23.6% of our consolidated revenue. There have been continuing concerns and uncertainties regarding the stability of the European economies. A decline in the economic conditions in Europe may materially and adversely affect our operations both in Europe and on a consolidated basis.

Furthermore, in 2010 we began transitioning certain of our core data processing and other functions to locations outside the U.S., including India, where 12% of our employees were located at December 31, 2012. While our operations in India have been key to serving clients more efficiently and cost-effectively under our Next-Generation Recovery Audit service delivery model, India has from time to time experienced instances of civil unrest and hostilities with Pakistan. In recent years, there have been military confrontations between India and Pakistan in the region of Kashmir and along the India-Pakistan border as well as terrorist activity in several major Indian cities. Although the relations between the two countries generally have been improving, military activity or terrorist attacks in the future could adversely affect the Indian economy by disrupting communications and making travel more difficult, which may have a material adverse effect on our ability to deliver services from India. Disruption in our Indian operations could materially and adversely affect our profitability and our ability to execute our growth strategy.

***Our Next-Generation Recovery Audit, Healthcare Claims Recovery Audit and Profit Optimization services businesses operate in highly competitive environments and are subject to pricing pressure.***

The environment in which our business operates is highly competitive, with numerous other recovery audit firms and other service providers. In addition, many of our recovery audit clients have developed their own internal recovery audit capabilities. As a result of competition among the providers of these services and the availability of certain recovery audit services from clients' internal audit departments, our business is subject to intense price pressure. In addition, our Healthcare Claims Recovery Audit services business currently is involved in a very competitive process of bidding for a new contract under the Medicare RAC program. We may not be awarded a region to audit, or may be awarded a region at a lower contingency rate than we currently earn. Our Profit Optimization services business also has numerous competitors varying in size, market strength and specialization, many of whom have established and well-known franchises and brands. Intense price competition faced by all of our service lines could negatively impact our profit margins and have a potential adverse effect on our business, financial condition and results of operations.

***Our client contracts generally contain provisions under which the client may terminate our services prior to the completion of the agreement.***

Many of our client contracts provide that the client may terminate the contract without cause prior to the end of the term of the agreement by providing us with relatively short prior written notice of the termination. As a result, the existence of contractual relationships with our clients is not an assurance that we will continue to provide services for our clients through the entire terms of their respective agreements. If clients representing a significant portion of our revenue terminated their agreements unexpectedly, we may not, in the short-term, be able to replace the revenue and earnings from such contracts and this would have a material adverse effect on our operations and financial results. In addition, client contract terminations also could harm our reputation within the industry which could negatively impact our ability to obtain new clients.

***Our charges to earnings resulting from acquisition, restructuring and integration costs may materially adversely affect the market value of our common stock.***

We account for the completion of our acquisitions using the purchase method of accounting. We allocate the total estimated purchase prices to net tangible assets, amortizable intangible assets and indefinite-lived intangible assets, and based on their fair values as of the date of completion of the acquisitions, record the excess of the purchase price over those fair values as goodwill. Our financial results, including earnings per share, could be adversely affected by a number of financial adjustments required in purchase accounting including the following:

we will incur additional amortization expense over the estimated useful lives of certain of the intangible assets acquired in connection with acquisitions during such estimated useful lives;

we will incur additional depreciation expense as a result of recording purchased tangible assets; and

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to the extent the value of goodwill or intangible assets becomes impaired, we may be required to incur material charges relating to the impairment of those assets.

***Our failure to comply with applicable governmental privacy laws and regulations could substantially impact our business, operations and financial condition.***

We are subject to extensive and evolving federal, state and foreign privacy laws and regulations. Changes in privacy laws or regulations or new interpretations of existing laws or regulations could have a substantial effect on our operating methods and costs. Failure to comply with such regulations could result in the termination or loss of contracts, the imposition of contractual damages, civil sanctions, damage to the Company's reputation, or in certain circumstances, criminal penalties, any of which could have a material adverse effect on our results of operations, financial condition, business and prospects. Determining compliance with such regulations is complicated by the fact that many of these laws and regulations have not been fully interpreted by governing regulatory authorities or the courts, and many of the provisions of such laws and regulations are open to a wide range of interpretations. There can be no assurance that we are or have been in compliance with all applicable existing laws and regulations or that we will be able to comply with new laws or regulations.

***The ownership change that occurred as a result of our 2006 exchange offer limits our ability to use our net operating losses.***

We have substantial tax loss and credit carry-forwards for U.S. federal income tax purposes. On March 17, 2006, as a result of the closing of its exchange offer, the Company experienced an ownership change as defined under Section 382 of the Internal Revenue Code ( IRC ). This ownership change resulted in an annual IRC Section 382 limitation that limits the use of certain tax attribute carry-forwards. Of the \$78.6 million of U.S. federal net loss carry-forwards available to the Company, \$17.8 million of the loss carry-forwards are subject to an annual usage limitation of \$1.4 million. We believe that such limitations and the loss of these carry-forwards may significantly increase our projected future tax liability.

We currently are in the process of determining if we experienced an ownership change subsequent to March 17, 2006, but have not yet completed this analysis. Based on preliminary calculations we have made with the assistance of external advisors, we believe that any additional limitations on the usage of our loss carry-forwards that would be imposed if an additional ownership change has occurred would be minimal. We do not believe that an additional ownership change would have a material adverse impact on our financial position, results of operations or cash flows.

***Certain of our tax positions may be subject to challenge by the Internal Revenue Service and other tax authorities, and if successful, these challenges could increase our future tax liabilities and expense.***

For U.S. federal income tax purposes, as well as local country tax purposes in the jurisdictions where we operate, from time to time we take positions under provisions of applicable tax law that are subject to varying interpretations. Certain of our tax positions may be subject to challenge by the applicable taxing authorities, including, in the U.S., the Internal Revenue Service. If our tax positions are successfully challenged, our future tax liabilities and expense could significantly increase.

While we believe that our tax positions are proper based on applicable law and we believe that it is more likely than not that we would prevail with respect to challenges to these positions, we can make no assurances that we would prevail if our positions are challenged or that business economics would justify the mounting of a legal defense against such challenges. If our tax positions are successfully challenged by the U.S. or non-U.S. taxing authorities, it could increase our future tax liabilities and expense and have a material adverse impact on our financial position, results of operations and cash flows.

***We may have exposure to additional income tax liabilities or additional costs if the U.S. government changes certain U.S. tax rules or other laws applicable to U.S. corporations doing business in foreign jurisdictions.***

We are a U.S. corporation that conducts business both in the U.S. and in foreign jurisdictions. As part of the ongoing discussions regarding the federal budget and the federal debt ceiling, various proposals have been made that may negatively impact U.S. corporations doing business in foreign jurisdictions, including proposals for comprehensive tax reform. While the scope of future changes remains unclear, proposed changes might include

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limiting the ability of U.S. corporations to deduct certain expenses attributable to offshore earnings, modifying the foreign tax credit rules and taxing currently certain transfers of intangible assets offshore or imposing other economic disincentives to doing business outside of the U.S. The enactment of some or all of these proposals could increase the Company's effective tax rate or otherwise adversely affect our profitability.

***Future impairment of goodwill, other intangible assets and long-lived assets would reduce our future earnings.***

As of December 31, 2012, the Company's goodwill and other intangible assets totaled \$32.1 million. We must perform periodic assessments to determine whether some portion, or all, of our goodwill, intangible assets and other long-lived assets are impaired. Future impairment testing could result in a determination that our goodwill, other intangible assets or our long-lived assets have been impaired. Future adverse changes in the business environment or in our ability to perform audits successfully and compete effectively in our markets or the discontinuation of our use of certain of our intangible or other long-lived assets could result in impairment which could materially adversely impact future earnings.

***Claims under our self-insurance program may differ from our estimates, which could materially impact our results of operations.***

We use a combination of insurance and self-insurance plans to provide for the potential liabilities for healthcare benefits for our employees. We estimate the liabilities associated with the risks that we retain by considering historical claims experience, demographic factors, severity factors and other actuarial assumptions. Our results could be materially impacted by claims and other expenses related to such plans if future occurrences and claims differ from these assumptions and historical trends.

***Our articles of incorporation, bylaws, shareholder rights plan and Georgia law may inhibit a change of control that shareholders may favor.***

Our articles of incorporation, bylaws and Georgia law contain provisions that may delay, deter or inhibit a future acquisition of PRGX that is not approved by our Board of Directors. This could occur even if our shareholders receive attractive offers for their shares or if a substantial number, or even a majority, of our shareholders believe the takeover is in their best interest. These provisions are intended to encourage any person interested in acquiring us to negotiate with and obtain the approval of our Board of Directors in connection with the transaction. Provisions that could delay, deter or inhibit a future acquisition include the following:

a classified Board of Directors;

the requirement that our shareholders may only remove directors for cause;

specified requirements for calling special meetings of shareholders;

the ability of the Board of Directors to consider the interests of various constituencies, including our employees, clients and creditors and the local community, in making decisions; and

the ability of the Board of Directors to issue shares of preferred stock with such designations, powers, preferences and rights as it determines, without any further vote or action by our shareholders.

In addition, we have in place a poison pill shareholders' rights plan that could trigger a dilutive issuance of common stock upon substantial purchases of our common stock by a third party that are not approved by the Board of Directors. These provisions also could discourage bids for our shares of common stock at a premium and could have a material adverse effect on the market price of our common stock.

***Our stock price has been and may continue to be volatile.***

Our common stock is currently traded on The Nasdaq Global Select Market. The trading price of our common stock has been and may continue to be subject to large fluctuations. For example, for the year ended December 31, 2012, our stock traded as high as \$8.85 per share and as low as \$5.29 per share. Our stock price may increase or decrease in response to a number of events and factors, including:

future announcements concerning us, key clients or competitors;

quarterly variations in operating results and liquidity;

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changes in financial estimates and recommendations by securities analysts;

developments with respect to technology or litigation;

changes in applicable laws and regulations;

the operating and stock price performance of other companies that investors may deem comparable to our company;

acquisitions and financings; and

sales and purchases of our stock by insiders.

Fluctuations in the stock market, generally, also impact the volatility of our stock price. Finally, general economic conditions and stock market movements may adversely affect the price of our common stock, regardless of our operating performance.

**ITEM 1B. Unresolved Staff Comments**

None.

**ITEM 2. Properties**

Our principal executive offices are located in approximately 132,000 square feet of office space in Atlanta, Georgia. We lease this space under an agreement expiring on December 31, 2014. We have subleased approximately 58,000 square feet of our principal executive office space to independent third parties. Our various operating units lease numerous other parcels of operating space in the various countries in which we currently conduct our business.

Excluding the lease for our principal executive offices, the majority of our real property leases are individually less than five years in duration. See *Note 6* of Notes to Consolidated Financial Statements included in Item 8 of this Form 10-K.

**ITEM 3. Legal Proceedings**

On December 16, 2011, an employee of our wholly owned subsidiary PRGX USA, Inc., filed a lawsuit in the U.S. District Court for the District of Minnesota (Civil Action No. 0:11-CV-03631-PJS-FLN) alleging that PRGX USA, Inc. failed to pay overtime wages to the Plaintiff and other similarly situated individuals as required by the Fair Labor Standards Act (FLSA). In this collective action, the Plaintiff sought an unspecified amount of monetary damages and costs, including attorneys' fees. We filed an Answer denying all of the asserted claims on January 31, 2012, and the parties then conducted limited discovery. In August 2012, the parties reached an agreement to settle the case for \$135,000, which includes the plaintiffs' attorney fees, and all of the plaintiffs have approved the settlement. The settlement received court approval on November 19, 2012 and the case has been dismissed.

In addition, we are party to a variety of other legal proceedings arising in the normal course of business. While the results of these proceedings cannot be predicted with certainty, management believes that the final outcome of these proceedings will not have a material adverse effect on our financial position or results of operations.

**ITEM 4. Mine Safety Disclosures**

Not applicable.



**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 is traded under the symbol PRGX on The Nasdaq Global Select Market (Nasdaq). The Company has not paid cash dividends on its common stock since it became a public company in 1996 and does not intend to pay cash dividends in the foreseeable future. Moreover, restrictive covenants included in our secured credit facility specifically prohibit payment of cash dividends and limit the amount of our common stock that we may repurchase to \$1.0 million on an annual basis. As of February 27, 2013, there were 178 holders of record of our common stock and management believes there were approximately 3,000 beneficial holders. The following table sets forth, for the quarters indicated, the range of high and low sales prices for the Company's common stock as reported by Nasdaq during 2012 and 2011.

<b>2012 Calendar Quarter</b>	<b>High</b>	<b>Low</b>
1st Quarter	\$ 6.50	\$ 5.29
2nd Quarter	8.07	5.66
3rd Quarter	8.85	7.00
4th Quarter	8.60	5.93

<b>2011 Calendar Quarter</b>	<b>High</b>	<b>Low</b>
1st Quarter	\$ 6.64	\$ 5.41
2nd Quarter	8.39	5.99
3rd Quarter	7.42	4.48
4th Quarter	6.23	4.07

**Issuer Purchases of Equity Securities**

A summary of our repurchases of our common stock during the fourth quarter ended December 31, 2012 is set forth below.

<b>2012</b>	<b>Total Number of Shares Purchased (a)</b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (millions of dollars)</b>
October 1 - October 31	1,081	\$ 7.45		\$
November 1 - November 30		\$		\$
December 1 - December 31		\$		\$
	1,081	\$ 7.45		\$

- (a) All shares reported during the quarter were surrendered by an employee to satisfy tax withholding obligations upon vesting of restricted stock.



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Set forth below is a line graph presentation comparing the cumulative shareholder return on our common stock, on an indexed basis, against cumulative total returns of The Nasdaq Composite Index and the RDG Technology Composite Index. The graph assumes that the value of the investment in the common stock in each index was \$100 on December 31, 2007 and shows total return on investment for the period beginning December 31, 2007 through December 31, 2012, assuming reinvestment of any dividends. Notwithstanding anything to the contrary set forth in any of the Company's filings under the Securities Act of 1933 or the Securities Exchange Act of 1934 that might incorporate future filings, including this Annual Report on Form 10-K, in whole or in part, the Performance Graph presented below shall not be incorporated by reference into any such filings.

**Cumulative Total Return**

	12/07	12/08	12/09	12/10	12/11	12/12
<b>PRGX Global, Inc.</b>	<b>100.00</b>	<b>47.61</b>	<b>68.96</b>	<b>73.86</b>	<b>69.43</b>	<b>75.26</b>
<b>NASDAQ Composite</b>	<b>100.00</b>	<b>59.03</b>	<b>82.25</b>	<b>97.32</b>	<b>98.63</b>	<b>110.78</b>
<b>RDG Technology Composite</b>	<b>100.00</b>	<b>56.89</b>	<b>91.53</b>	<b>103.10</b>	<b>103.14</b>	<b>117.75</b>

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The following table sets forth selected consolidated financial data for the Company as of and for each of the five years in the period ended December 31, 2012. The following data reflects the business acquisitions that we have completed through December 31, 2012. We have included the results of operations for these acquired businesses in our results of operations since the date of their acquisitions. We have derived this historical consolidated financial data from our Consolidated Financial Statements and Notes thereto, which have been audited by our Independent Registered Public Accounting Firm. The Consolidated Balance Sheets as of December 31, 2012 and 2011, and the related Consolidated Statements of Income, Comprehensive Income, Shareholders' Equity and Cash Flows for each of the years in the three-year period ended December 31, 2012 and the report of the Independent Registered Public Accounting Firm thereon are included in Item 8 of this Form 10-K.

The data presented below should be read in conjunction with the Consolidated Financial Statements and Notes thereto included elsewhere in this Form 10-K and other financial information appearing elsewhere in this Form 10-K, including **Management's Discussion and Analysis of Financial Condition and Results of Operations**.

	2012	Years Ended December 31,			2008
		2011	2010	2009	
	(In thousands, except per share data)				
<b>Statements of Income Data:</b>					
Revenue	\$ 208,503	\$ 203,117	\$ 184,081	\$ 179,583	\$ 195,706
Operating expenses:					
Cost of revenue	134,390	137,482	126,069	115,064	124,997
Selling, general and administrative expenses	52,527	49,102	40,735	40,390	36,455
Depreciation of property and equipment	7,084	5,401	4,903	3,505	2,991
Amortization of intangible assets	7,224	4,991	4,131	3,227	2,203
Total operating expenses	201,225	196,976	175,838	162,186	166,646
Operating income	7,278	6,141	8,243	17,397	29,060
Gain on bargain purchase, net (1)				(2,388)	
Foreign currency transaction (gains) losses on short-term intercompany balances	(377)	417	422	(1,595)	3,283
Interest expense, net	966	1,616	1,305	3,025	3,245
Loss on debt extinguishment and financial restructuring			1,381		
Earnings before income taxes	6,689	4,108	5,135	18,355	22,532
Income tax expense (2)	1,297	1,292	1,882	3,028	3,502
Net earnings	\$ 5,392	\$ 2,816	\$ 3,253	\$ 15,327	\$ 19,030
Basic earnings per common share	\$ 0.21	\$ 0.11	\$ 0.14	\$ 0.67	\$ 0.87
Diluted earnings per common share	\$ 0.21	\$ 0.11	\$ 0.13	\$ 0.65	\$ 0.83

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	2012	2011	December 31, 2010	2009	2008
	(In thousands)				
<b>Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 37,806	\$ 20,337	\$ 18,448	\$ 33,026	\$ 26,688
Working capital	37,445	16,319	17,678	18,479	10,512
Total assets	143,586	126,413	106,321	110,513	98,783
Long-term debt, excluding current installments	3,000	6,000	9,000	11,070	14,331
Total shareholders' equity	\$ 84,652	\$ 59,090	\$ 48,843	\$ 41,439	\$ 22,710

- (1) In July 2009, we acquired the business and certain assets of First Audit Partners LLP. The excess of the fair value of assets acquired over the purchase price resulted in a gain on bargain purchase for this acquisition.
- (2) The low effective tax rate relative to the U.S. federal statutory rate in 2012 is attributable to recognition of certain previously unrecognized tax benefits. Low effective tax rates in 2009 and 2008 are primarily attributable to reductions in the deferred tax asset valuation allowance. See *Note 1 (i)* and *Note 7* of Notes to Consolidated Financial Statements included in Item 8 of this Form 10-K.

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**ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

**Introduction**

We conduct our operations through three reportable segments: Recovery Audit Services Americas, Recovery Audit Services Europe/Asia-Pacific and New Services. The Recovery Audit Services Americas segment represents recovery audit services (other than Healthcare Claims Recovery Audit services) we provide in the U.S., Canada and Latin America. The Recovery Audit Services Europe/Asia-Pacific segment represents recovery audit services (other than Healthcare Claims Recovery Audit services) we provide in Europe, Asia and the Pacific region. The New Services segment includes Profit Optimization services as well as Healthcare Claims Recovery Audit services. We include the unallocated portion of corporate selling, general and administrative expenses not specifically attributable to the three operating segments in Corporate Support.

Recovery auditing is a business service focused on finding overpayments created by errors in payment transactions, such as missed or inaccurate discounts, allowances and rebates, vendor pricing errors, erroneous coding and duplicate payments. Generally, we earn our recovery audit revenue by identifying overpayments made by our clients, assisting our clients in recovering the overpayments from their vendors, and collecting a specified percentage of the recoveries from our clients as our fee. The fee percentage we earn is based on specific contracts with our clients that generally also specify: (a) time periods covered by the audit; (b) the nature and extent of services we are to provide; and (c) the client's responsibilities to assist and cooperate with us. Clients generally recover claims by either taking credits against outstanding payables or future purchases from the relevant vendors, or receiving refund checks directly from those vendors. The manner in which a claim is recovered by a client is often dictated by industry practice. In addition, many clients establish client-specific procedural guidelines that we must satisfy prior to submitting claims for client approval. For some services we provide, such as certain of our Profit Optimization services, we earn our compensation in the form of a flat fee, a fee per hour, or a fee per other unit of service.

We earn the vast majority of our recovery audit revenue from clients in the retail industry due to many factors, including the high volume of transactions and the complicated pricing and allowance programs typical in this industry. Changes in consumer spending associated with economic fluctuations generally impact our recovery audit revenue to a lesser degree than they affect individual retailers due to several factors, including:

**Diverse client base** our clients include a diverse mix of discounters, grocery, pharmacy, department and other stores that tend to be impacted to varying degrees by general economic fluctuations, and even in opposite directions from each other depending on their position in the market and their market segment;

**Motivation** when our clients experience a downturn, they frequently are more motivated to use our services to recover prior overpayments to make up for relatively weaker financial performance in their own business operations;

**Nature of claims** the relationship between the dollar amount of recovery audit claims identified and client purchases is non-linear. Claim volumes are generally impacted by purchase volumes, but a number of other factors may have an even more significant impact on claim volumes, including new items being purchased, changes in discount, rebate, marketing allowance and similar programs offered by vendors and changes in a client's or a vendor's information processing systems; and

**Timing** the client purchase data on which we perform our recovery audit services is historical data that typically reflects transactions between our clients and their vendors that took place 3 to 15 months prior to the data being provided to us for audit. As a result, we generally experience a delayed impact from economic changes that varies by client and the impact may be positive or negative depending on the individual clients' circumstances.

While the net impact of the economic environment on our recovery audit revenue is difficult to determine or predict, we believe that for the foreseeable future, our revenue will remain at a level that will not have a significant adverse impact on our liquidity, and we have taken steps to mitigate any adverse impact of an economic downturn on our revenue and overall financial health. These steps include devoting substantial efforts to develop a lower cost service delivery model to enable us to more cost effectively serve our clients. Further, we continue to pursue our



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ongoing growth strategy to expand our business beyond our core recovery audit services to retailers by growing the portion of our business that provides recovery audit services to enterprises other than retailers and growing our New Services segment which includes our Healthcare Claims Recovery Audit services and our Profit Optimization services. Our Healthcare Claims Recovery Audit services include services we provide as a participant in the Medicare RAC program.

**Results of Operations**

The following table sets forth the percentage of revenue represented by certain items in our Consolidated Statements of Income for the periods indicated:

	Years Ended December 31,		
	2012	2011	2010
<b>Statements of Income Data:</b>			
Revenue	100.0%	100.0%	100.0%
Operating expenses:			
Cost of revenue	64.5	67.7	68.5
Selling, general and administrative expenses	25.2	24.2	22.1
Depreciation of property and equipment	3.4	2.7	2.7
Amortization of intangible assets	3.4	2.4	2.2
Total operating expenses	96.5	97.0	95.5
Operating income	3.5	3.0	4.5
Foreign currency transaction (gains) losses on short-term intercompany balances	(0.2)	0.2	0.2
Interest expense, net	0.5	0.8	0.7
Loss on debt extinguishment			0.8
Earnings before income taxes	3.2	2.0	2.8
Income tax expense	0.6	0.6	1.0
Net earnings	2.6%	1.4%	1.8%

*Revenue.* Revenue was as follows (in thousands):

	Years Ended December 31,		
	2012	2011	2010
Recovery Audit Services Americas	\$ 121,638	\$ 115,807	\$ 115,156
Recovery Audit Services Europe/Asia-Pacific	53,783	61,570	57,590
New Services	33,082	25,740	11,335
Total	\$ 208,503	\$ 203,117	\$ 184,081

Total revenue increased by \$5.4 million, or 2.7%, in 2012 and \$19.0 million, or 10.3%, in 2011. Below is a discussion of our revenue for our three reportable segments.

Recovery Audit Services Americas revenue increased by 5.0% in 2012 and increased by 0.6% in 2011. We experience changes in our reported revenue based on the strength of the U.S. dollar relative to foreign currencies. Changes in the value of the U.S. dollar relative to currencies in Canada and Latin America negatively impacted reported revenue in 2012 and positively impacted reported revenue in 2011. On a constant dollar basis, adjusted for changes in foreign exchange ( FX ) rates, 2012 revenue increased by 6.4% compared to an increase of 5.0% as reported, and



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2011 revenue decreased by 0.5% compared to an increase of 0.6% as reported.

The increases in our Recovery Audit Services Americas revenue in 2012 and 2011 were due to a number of factors. Revenue increased 1.6% in 2012 and 7.7% in 2011 due to new clients, new geographic territories for existing clients and a promotion from secondary auditor to primary auditor at a significant client in 2011. Revenue from existing clients decreased 1.4% in 2012 and increased 1.6% in 2011. The decrease in 2012 is due primarily to one significant client for which 2011 included an audit of purchases from multiple years for one area and 2012

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included an audit of purchases for one year, as well as increased findings by this client's internal staff that reduced the opportunity available to us. Revenue from new clients we gained through our acquisition of Business Strategy, Inc. (BSI) in December 2011 added another 7.1% in 2012 and 0.6% in 2011 to our revenue. These increases were offset primarily by discontinued clients and, to a lesser extent, demotions from primary auditor to secondary auditor and from restrictions on claim types imposed by certain clients.

Although we generated year over year increases in revenue in this segment for both 2012 and 2011, we experienced declining revenue in this segment in years prior to 2011 due to reduced liquidity of our clients' vendors, competitive rate pressures, client attrition, and the impact of our clients developing and strengthening their own internal audit capabilities as a substitute for our services. To address these issues, offset their impact and generate growth in this segment, we began implementing several growth strategies in late 2009. We reinstated a sales function in 2010, resulting in a significant increase in our client count in the past two years. We continue to implement our service delivery model transformation designed to make our recovery audit process more cost efficient and effective. We expanded the use of our new service delivery platform in 2012, and are planning to continue the expansion in 2013. We also are providing greater value to our existing and potential clients by offering adjacent services in the procure-to-pay value chain and to the CFO suite, and by capitalizing on our existing data mining and related competencies. While we are encouraged by some of our recent successes, we can provide no assurances that we will be able to build on them in the future or that we will be able to sustain our current revenue levels in this segment.

**Recovery Audit Services – Europe/Asia-Pacific** revenue decreased by 12.6% in 2012 and increased by 6.9% in 2011. The changes in the strength of the U.S. dollar relative to foreign currencies in Europe, Asia and Australia negatively impacted reported revenue in 2012 but positively impacted reported revenue in 2011. On a constant dollar basis, adjusted for changes in FX rates, 2012 revenue decreased by 10.0% compared to a decrease of 12.6% as reported, and 2011 revenue increased by 1.5% compared to an increase of 6.9% as reported. Revenue increased 4.8% in 2012 and 6.0% in 2011 due to new clients and new geographic territories for existing clients. Revenue from existing clients decreased 5.9% in 2012 and 2.0% in 2011, resulting primarily from fewer individually significant claims at continuing clients in 2012 than were generated in 2011, and audits of special claim concepts that positively impacted 2011 to a greater degree than 2012. The remaining net decrease is due to discontinued clients and lower revenue from cyclical clients, which generally include commercial companies for which we complete the audits in a relatively short period of time, and then have several quarters with no revenue while we are between audits. As in our Recovery Audit Services – Americas segment, we experience competitive and other pressures in this segment, but to a lesser degree due to the smaller number of competitors with global capabilities. We intend to execute the same strategic initiatives for this segment as we are executing in the Recovery Audit Services – Americas segment.

**New Services** revenue increased by 28.5% in 2012 and increased by 127.1% in 2011. Our Healthcare Claims Recovery Audit business more than doubled its revenue in both years. Our Profit Optimization revenue also more than doubled in 2011, but declined approximately 15% in 2012. Approximately 40% of the 2011 increase in New Services revenue is attributable to incremental revenue associated with our acquisitions of Etesius Limited (Etesius) in February 2010 and TJG Holdings LLC (TJG) in November 2010. The remaining 2011 increase resulted from organic growth.

We currently serve as a subcontractor to the prime contractor on three of the four prime contracts in the Medicare RAC program. Based on recent developments, we believe CMS has agreed with the prime contractors to allow the prime contracts to expire in August 2013, subject to extension by CMS to allow for a transition period to the new RAC contracts. Should the prime contracts expire in August 2013, our RAC subcontracts will also expire at that time, subject to any additional extensions by CMS in connection with the transition to new RAC contracts, and contracts for the performance of future Medicare RAC services will be subject to a bidding process administered by CMS. CMS issued a request for proposals in connection with the re-bidding for the RAC contracts, and the proposals are due by March 27, 2013. CMS is expected to award the RAC contracts to more than one contractor and divide the country into geographic regions for contracting purposes. We will be competing to participate in the RAC program as a prime contractor through the bidding process. While we believe we are well-positioned to compete in the bidding process, there are no assurances that we will receive any contract when the new Medicare RAC contracts are ultimately awarded.

Growth in our Profit Optimization business was very strong through the first half of 2011, but revenue declined in the second half of the year compared to the first half of 2011. As part of our continuing investment in our New

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Services segment, we changed the leadership and realigned this organization in 2012. Profit Optimization revenue stabilized in 2012, and we anticipate that it will return to growth in 2013.

*Cost of Revenue ( COR )*. COR consists principally of commissions and other forms of variable compensation we pay to our auditors based primarily upon the level of overpayment recoveries and/or profit margins derived therefrom, fixed auditor salaries, compensation paid to various types of hourly support staff, and salaried operational and client service managers for our recovery audit and Profit Optimization services businesses. COR also includes other direct and indirect costs incurred by these personnel, including office rent, travel and entertainment, telephone, utilities, maintenance and supplies and clerical assistance. A significant portion of the components comprising COR is variable and will increase or decrease with increases or decreases in revenue. Beginning in 2011, we reclassified depreciation and amortization to present them separately from COR and selling, general and administrative expenses ( SG&A ). The COR and SG&A expenses presented below for 2010 reflect these reclassifications.

COR expenses were as follows (in thousands):

		Years Ended December 31,		
		2012	2011	2010
Recovery Audit Services	Americas	\$ 64,205	\$ 64,946	\$ 67,744
Recovery Audit Services	Europe/Asia-Pacific	41,715	47,105	44,200
New Services		28,470	25,431	14,125
Total		\$ 134,390	\$ 137,482	\$ 126,069

COR as a percentage of revenue for Recovery Audit Services Americas was 52.8% in 2012, 56.1% in 2011 and 58.8% in 2010. We invested in our various growth and other strategic initiatives, and included significant portions of these costs in Recovery Audit Services Americas COR in 2010. Although we continued to make these investments in subsequent years, we began to realize the benefits of the investments and were able to increase revenue and still reduce COR by 1.1% in 2012 and 4.1% in 2011, respectively. We continue to implement additional facets of our strategic initiatives, and believe we will continue to reduce COR as a percentage of revenue in 2013.

COR as a percentage of revenue for Recovery Audit Services Europe/Asia-Pacific was 77.6% in 2012, 76.5% in 2011 and 76.7% in 2010. The slight changes in the gross margins in these periods primarily resulted from changes in the mix of audit revenue and from changes in our methods of providing audit services in Europe. We subcontract a portion of our audit services in Europe to third-party audit firms, which we refer to as the associate model. We generally earn a lower gross margin from associate model audits than we earn from audits we perform ourselves, which we refer to as employee model audits. We migrated several of the larger audits to an employee model in 2011 and 2012. In an associate migration, we generally transfer all of the employees of the associate entity to PRGX, and continue to service the related clients with the same personnel after the associate migration as were providing services prior to the associate migration. We intend for the associate migrations to provide more standardization and centralization of our audit procedures, thereby increasing client service while also decreasing costs. Generally, revenue remains unchanged as a result of an associate migration, and expenses change from a fixed percentage of revenue to a variable amount based on employee and related costs. In 2012, the benefits we anticipated from these associate migrations were diminished by the revenue declines in this segment. In 2011 as compared to 2010, we generated a greater percentage of our revenue in this segment from associate model audits, which changed the mix of our revenue and negatively impacted our gross margins. Although we incur some increased costs during this migration process, we expect that the migrations ultimately will result in higher gross margins for this segment and for the Company as a whole.

The higher COR as a percentage of revenue for Recovery Audit Services Europe/Asia-Pacific (77.6% for 2012) compared to Recovery Audit Services Americas (52.8% for 2012) is due primarily to differences in service delivery models, scale and geographic fragmentation. The Recovery Audit Services Europe/Asia-Pacific segment generally serves fewer clients in each geographic market and generates lower revenue per client than those served by the Company's Recovery Audit Services Americas segment.

New Services COR relates primarily to costs of Profit Optimization services and costs associated with services we provide under the Medicare RAC program subcontracts portion of our Healthcare Claims Recovery Audit business. New Services revenue exceeded COR by \$4.6 million in 2012 and \$0.3 million in 2011, but COR exceeded revenue by \$2.8 million in 2010 primarily due to our investments in the Medicare RAC program as well as our investments in our Profit Optimization services capabilities.



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*Selling, General and Administrative Expenses ( SG&A ).* SG&A expenses of the Recovery Audit and New Services segments include the expenses of sales and marketing activities, information technology services and allocated corporate data center costs, human resources, legal, accounting, administration, foreign currency transaction gains and losses other than those relating to short-term intercompany balances, and gains and losses on asset disposals. Corporate Support SG&A represents the unallocated portion of SG&A expenses which are not specifically attributable to our segment activities and include the expenses of information technology services, the corporate data center, human resources, legal, accounting, treasury, administration and stock-based compensation charges.

SG&A expenses were as follows (in thousands):

		<b>Years Ended December 31,</b>		
		<b>2012</b>	<b>2011</b>	<b>2010</b>
Recovery Audit Services	Americas	\$ 19,882	\$ 18,479	\$ 16,448
Recovery Audit Services	Europe/Asia-Pacific	4,980	4,627	4,764
New Services		5,497	4,907	2,608
Subtotal for segments		30,359	28,013	23,820
Corporate support		22,168	21,089	16,915
Total		\$ 52,527	\$ 49,102	\$ 40,735

Recovery Audit Services Americas SG&A increased 7.6% in 2012 and 12.3% in 2011. These increases resulted primarily from costs incurred in connection with the execution of our growth strategies. The 2012 increase also includes incremental expenses resulting from our December 2011 BSI acquisition and costs relating to an overtime wages claim. The 2011 increase also includes greater incentive compensation accruals and some incremental expenses resulting from the BSI acquisition.

Recovery Audit Services Europe/Asia-Pacific SG&A increased 7.6% in 2012 and decreased 2.9% in 2011. The 2012 increase resulted primarily from severance charges and provisions for bad debts, partially offset by a reduction in a business acquisition obligation resulting from decreased revenue and profitability generated by the acquired business. Although incentive compensation accruals increased in 2011, most other SG&A expenses decreased in 2011, resulting in the 2.9% decrease from 2010.

New Services SG&A increased 12.0% in 2012 and 88.2% in 2011. The increase in 2012 primarily resulted from our continuing efforts to improve our processes and develop new tools for use in our Healthcare Claims Recovery Audit business. The acquisitions of Etesius and TJG in 2010 resulted in increased expenses in 2011 due to the inclusion of the acquired entities for the full year in 2011. In addition, during 2011, we hired additional resources for both our Profit Optimization business and our Healthcare Claims Recovery Audit business and incurred additional SG&A expenses associated with the additional personnel.

Corporate Support SG&A includes stock-based compensation charges of \$6.3 million in 2012, \$5.1 million in 2011 and \$4.0 million in 2010. Excluding stock-based compensation charges, Corporate Support SG&A decreased 0.9% in 2012 and increased 23.7% in 2011. The increase in 2011 is due to higher incentive compensation accruals relative to the decreased incentive compensation accruals in 2010, costs associated with the BSI acquisition, and higher sales and marketing expenses associated with our renewed focus on revenue growth and client retention.

*Depreciation of property and equipment.* Depreciation of property and equipment was as follows (in thousands):

		<b>Years Ended December 31,</b>		
		<b>2012</b>	<b>2011</b>	<b>2010</b>
Recovery Audit Services	Americas	\$ 4,651	\$ 3,491	\$ 3,442
Recovery Audit Services	Europe/Asia-Pacific	322	417	354
New Services		2,111	1,493	1,107
Total		\$ 7,084	\$ 5,401	\$ 4,903

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The increases in depreciation in the Recovery Audit Services Americas segment relate primarily to improvements we made to our IT infrastructure as well as depreciation relating to capitalized software development costs. The increase in depreciation in the New Services segment in 2012 is due primarily to an increase in the

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depreciation of capitalized software development costs and the 2011 increase is due to software we purchased in the Etesius acquisition in 2010 for which 2011 included a full year of depreciation.

*Amortization of intangible assets.* Amortization of intangible assets was as follows (in thousands):

		Years Ended December 31,		
		2012	2011	2010
Recovery Audit Services	Americas	\$ 4,355	\$ 2,467	\$ 2,427
Recovery Audit Services	Europe/Asia-Pacific	2,062	1,665	1,403
New Services		807	859	301
Total		\$ 7,224	\$ 4,991	\$ 4,131

The increase in amortization expense in our recovery audit services segments is due to the amortization of intangible assets recorded in connection with our recent acquisitions. These acquisitions include the December 2011 acquisition of BSI in Recovery Audit Services Americas, the 2011 and 2012 associate migrations in Recovery Audit Services Europe / Asia Pacific. The increase in amortization expense in our New Services segment from 2010 to 2011 is due to the amortization of intangible assets recorded in connection with the February 2010 acquisition of Etesius and the November 2010 acquisition of TJG. We anticipate that, absent our completing additional acquisitions in 2013, amortization expense will decrease in 2013 due to the declining rate of amortization relating to the 2011 and prior acquisitions and the completion of substantially all amortization resulting from the associate migrations we completed in 2011 and 2012.

*Foreign Currency Transaction (Gains) Losses on Short-Term Intercompany Balances.* Foreign currency transaction gains and losses on short-term intercompany balances result from fluctuations in the exchange rates for the foreign currencies and the U.S. dollar. Substantial changes from period to period in foreign currency exchange rates may significantly impact the amount of such gains and losses. The strengthening of the U.S. dollar relative to other currencies results in recorded losses on short-term intercompany balances receivable from our foreign subsidiaries while the relative weakening of the U.S. dollar results in recorded gains.

In 2011 and 2010, the local currencies of certain of our foreign subsidiaries with significant short-term intercompany balances weakened relative to the U.S. dollar, resulting in recorded losses of \$0.4 million in both years. The U.S. dollar generally weakened relative to those foreign currencies in 2012, resulting in our recording net foreign currency transaction gains on short-term intercompany balances of \$0.4 million for the year.

*Interest Expense, net and Loss on Extinguishment of Debt.* Net interest expense was \$1.0 million in 2012, \$1.6 million in 2011 and \$1.3 million in 2010. We also recorded a \$1.4 million loss on extinguishment of debt in 2010. In January 2010, we entered into a new credit facility with SunTrust Bank and repaid our prior term loan from Ableco LLC in full (see Secured Credit Facility below for additional information regarding this transaction). The loss on extinguishment of debt consists of the write-off of the unamortized deferred loan costs associated with the prior credit facility. The interest rate on the new credit facility is based on the one-month LIBOR rate, plus an applicable margin of from 2.25% to 3.5% per annum. The interest rate in effect at December 31, 2012 under the new credit facility was approximately 2.71%, while the prior credit facility bore a minimum interest rate of 9.75%. The increase in net interest expense in 2011 was primarily due to interest expense associated with business acquisition obligations and uncertain tax positions. The decrease in 2012 was due to the reversal of \$0.8 million of interest accruals made in previous years for interest on uncertain tax positions, as described in more detail under *Income Tax Expense* below.

*Income Tax Expense.* Our reported effective tax rates on earnings approximated 19.4% in 2012, 31.5% in 2011 and 36.7% in 2010. Reported income tax expense in each year primarily results from taxes on the income of foreign subsidiaries. The effective tax rates generally are less than the expected tax rate primarily due to reductions of the Company's deferred tax asset valuation allowance. The 2011 effective tax rate reflects a higher base rate due to taxes on earnings from foreign subsidiaries and additional accruals for uncertain tax positions in a foreign jurisdiction, partially offset by the reduction of a portion of the valuation allowance on deferred tax assets resulting from the additional deferred tax liabilities that we recorded in connection with the BSI acquisition and the reversal of a portion of the valuation allowance attributable to the deferred tax assets of a foreign subsidiary. The lower effective tax rate in 2012 reflects the reversal of \$0.4 million of the accruals made in previous years for uncertain tax positions.

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Together with the reversal of interest expense accruals described above, the total reduction to our reserves for uncertain tax positions in 2012 was \$1.2 million. We initially established these reserves based on estimates we made in prior years of the potential liability we may incur should certain domestic and foreign tax jurisdictions perform audits of our books and records and determine that we owe additional taxes, for which they may also assess penalty and interest amounts. We increased the reserves for additional estimated interest in subsequent years to reflect the additional time from when the estimated potential taxes may have been due. In 2012, we adjusted our estimates for several reasons, including the expiration of the statute of limitations for certain of these taxes in several states and in two foreign jurisdictions, completion of an audit by a foreign jurisdiction that resulted in a lower tax assessment than we had estimated, and the imposition of limitations on our potential liability resulting from our beginning the voluntary disclosure agreement process with one state.

As of the end of the past three years, management determined that based on all available evidence, deferred tax asset valuation allowances of \$49.1 million in 2012, \$52.0 million in 2011 and \$54.8 million in 2010 were appropriate. We recorded reductions in the deferred tax asset valuation allowance of \$1.7 million in 2011 and \$1.2 million in 2010 as a result of the deferred tax liabilities that we recorded relating to business acquisitions. The remaining reduction in each of the three years was due primarily to lower net deferred tax assets for which we recorded a portion of the valuation allowance. We expensed or impaired a significant amount of intangible assets in previous years for financial reporting purposes. For income tax reporting purposes, we continue to deduct the amortization of these intangible assets over their tax lives, generally 15 years. The excess of tax amortization over amortization for financial reporting purposes is reducing the related deferred tax asset each year, resulting in lower deferred tax assets and a lower related valuation allowance, although increases in our net operating losses have partially offset this impact in recent years. This reduction in deferred tax assets related to intangible assets was \$5.7 million in 2012, \$5.8 million in 2011 and \$6.1 million in 2010, and we currently project this effect to continue at these elevated levels through 2013 before declining in subsequent years.

As of December 31, 2012, we had approximately \$78.6 million of U.S. federal loss carry-forwards available to reduce future U.S. federal taxable income. The U.S. federal loss carry-forwards expire through 2032. As of December 31, 2012, we had approximately \$91.3 million of state loss carry-forwards available to reduce future state taxable income. The state loss carry-forwards expire to varying degrees between 2017 and 2032 and are subject to certain limitations.

On March 17, 2006, the Company experienced an ownership change as defined under Section 382 of the Internal Revenue Code ( IRC ). This ownership change resulted in an annual IRC Section 382 limitation that limits the use of certain tax attribute carry-forwards. Of the \$78.6 million of U.S. federal loss carry-forwards available to the Company, \$17.8 million of the loss carry-forwards are subject to an annual usage limitation of \$1.4 million.

**Liquidity and Capital Resources**

As of December 31, 2012, we had \$37.8 million in cash and cash equivalents and no borrowings under the revolver portion of our credit facility. The revolver had approximately \$8.1 million of calculated availability for borrowings at the end of 2012. The Company was in compliance with the covenants in its SunTrust credit facility as of December 31, 2012.

The \$37.8 million in cash and cash equivalents includes \$24.8 million held in the U.S., \$4.5 million held in Canada, and \$8.5 million held in other foreign jurisdictions, primarily in the United Kingdom, France, and Brazil. Certain foreign jurisdictions restrict the amount of cash that can be transferred to the U.S. or impose taxes and penalties on such transfers of cash. To the extent we have excess cash in foreign locations that could be used in, or is needed by, our operations in the U.S., we may incur significant penalties and/or taxes to repatriate these funds. Generally, we have not provided deferred taxes on the undistributed earnings of international subsidiaries as we consider these earnings to be permanently reinvested. However, we do not consider the earnings of our Canadian subsidiary to be permanently invested, and have provided deferred taxes relating to the potential repatriation of the funds held in Canada.



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*Operating Activities.* Net cash provided by operating activities was \$18.8 million in 2012, \$19.3 million in 2011 and \$3.5 million in 2010. These amounts consist of two components, specifically, net earnings adjusted for certain non-cash items (such as depreciation, amortization, stock-based compensation expense, and deferred income taxes) and changes in assets and liabilities, primarily working capital, as follows:

	Years Ended December 31,		
	2012	2011	2010
Net earnings	\$ 5,392	\$ 2,816	\$ 3,253
Adjustments for certain non-cash items	19,667	13,945	13,636
	25,059	16,761	16,889
Changes in operating assets and liabilities	(6,216)	2,532	(13,420)
Net cash provided by operating activities	\$ 18,843	\$ 19,293	\$ 3,469

Net earnings adjusted for certain non-cash items, primarily depreciation, amortization and stock-based compensation expense, increased \$8.3 million in 2012 as compared to 2011. This increase compared to 2011 was offset primarily by the impact of the change in accounts payable and incentive compensation accruals between 2010 and 2011, which resulted in the positive change in operating assets and liabilities in 2011. These incentive compensation accruals were low at the end of 2010 and higher in 2011, thereby generating cash from working capital changes in 2011. The 2012 accruals were more consistent with the 2011 levels, thus not resulting in a comparable benefit in 2012.

The \$15.8 million improvement in cash provided by operating activities in 2011 compared to 2010 was due to changes in assets and liabilities, primarily working capital. The 2011 improvement relates primarily to changes in accounts payable and compensation accruals as we used cash in 2010 to pay the 2009 accruals, required less cash in 2011 to pay the lower 2010 incentive compensation accruals, and increased these accruals again in 2011. These changes in accounts payable and compensation accruals resulted in \$17.2 million less cash used for working capital, which was partially offset by \$2.1 million of additional cash used to fund the net increase in billed and unbilled receivables. This increase in billed and unbilled receivables is due primarily to our increase in revenue from our participation in the Medicare RAC program, for which we generally cannot invoice until the cash is collected by the prime contractors for whom we operate as a subcontractor. The increase in unbilled receivables was also due to increases in revenue from recovery audit clients for which we have agreed not to invoice the clients until a later date even though we have already earned the related revenue.

We include an itemization of these changes in our Consolidated Statements of Cash Flows included in Part II, Item 8 of this Form 10-K.

We have one client, Wal-Mart Stores Inc., that accounted for 10% or more of our annual revenue in 2011 and 2010. The loss of this client would negatively impact our operating cash flows and would potentially have a material adverse impact on the Company's liquidity.

*Investing Activities and Depreciation and Amortization Expense.* Depreciation and amortization expense was \$14.3 million in 2012, \$10.4 million in 2011 and \$9.0 million in 2010. Net cash used for capital expenditures was \$7.9 million in 2012, \$8.3 million in 2011 and \$6.9 million in 2010. These capital expenditures primarily related to investments we made to upgrade our information technology infrastructure, develop our Next-Generation Recovery Audit service delivery model and develop software relating to our participation in the Medicare RAC program.

Capital expenditures are discretionary and we currently expect future capital expenditures to decline slightly from 2012 levels. Although we continue to enhance our Next-Generation Recovery Audit service delivery model and our Healthcare Claims Recovery Audit systems, we expect that these projects will require less development in 2013 than they did in 2011 and 2012. We may alter our capital expenditure plans should we experience changes in our operating results which cause us to adjust our operating plans.

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### *Business Acquisitions*

We made several business acquisitions over the past few years, each of which is discussed more fully in *Note 12 Business Acquisitions* in *Notes to Consolidated Financial Statements* in Part II, Item 8 of this Form 10-K. Following is a summary of business acquisition activities impacting our liquidity and capital resources in the past three years.

In July 2009, we acquired the business and certain assets of First Audit Partners LLP ( *FAP* ), a privately-held European provider of recovery audit services based in Cambridge, United Kingdom, for a purchase price valued at \$5.8 million. The purchase price included an initial cash payment of \$1.6 million that we paid in July 2009. We made the first of two deferred payments required as part of the *FAP* acquisition in January 2010 in the amount of £0.5 million (\$0.8 million) and the second payment of £0.8 million (\$1.3 million) in July 2010. Additional variable consideration may be due based on the operating results generated by the acquired business over a four year period from the date of acquisition. From the acquisition date to December 31, 2012, we paid £1.1 million (\$1.7 million) of the earn-out and recorded accretion and other adjustments of the liability of \$1.3 million, resulting in an earn-out payable of \$0.9 million as of December 31, 2012.

In February 2010, we acquired all of the issued and outstanding capital stock of Etesius Limited, a privately-held European provider of purchasing and payables technologies and spend analytics based in Chelmsford, United Kingdom for a purchase price valued at \$3.1 million. The purchase price included an initial cash payment of \$2.8 million and a \$0.3 million payment for obligations on behalf of Etesius shareholders that we paid in February 2010 as well as deferred payments of \$1.2 million over four years from the date of the acquisition. We also may be required to make additional payments of up to \$3.8 million over a four-year period if the financial performance of this service line meets certain targets. These payments would be to Etesius employees that we hired in connection with the acquisition. We will not be obligated to make the deferred and earn-out payments to these employees if they resign or are terminated under certain circumstances. We therefore are recognizing the accrual of the deferred payments as compensation expense. From the acquisition date to December 31, 2012, we paid \$0.2 million of the deferred payments. An additional \$1.0 million will be due through February 2014 unless there is a termination of employment of these employees under certain circumstances. We have not paid or accrued any earn-out payments as of December 31, 2012.

In November 2010, we acquired the business and certain assets of TJG Holdings LLC ( *TJG* ), a privately-held provider of finance and procurement operations improvement services based in Chicago, Illinois for a purchase price valued at \$3.7 million. The purchase price included an initial cash payment of \$2.3 million that we paid in November 2010. Additional payments of up to a maximum of \$1.9 million may be due to the sellers in four semi-annual payments if certain performance targets are met. We recorded \$1.4 million as the estimated fair value of these payments at the acquisition date. From the acquisition date to December 31, 2012, we paid \$1.8 million of the earn-out and recorded accretion and other adjustments of the liability of \$0.4 million, resulting in an earn-out payable of less than \$0.1 million as of December 31, 2012.

In December 2011, we acquired Business Strategy, Inc. and substantially all of the assets of an affiliated company (collectively *BSI* ), both based in Grand Rapids, Michigan, for a purchase price valued at \$11.9 million. *BSI* was a provider of recovery audit and related procure-to-pay process improvement services for commercial clients, and a provider of customized software solutions and outsourcing solutions to improve back office payment processes. The purchase price included an initial cash payment of \$2.8 million and 640,614 shares of our common stock having a value of \$3.7 million. An additional payment of approximately \$0.8 million was made in the first half of 2012 for working capital received in excess of a specified minimum level. Additional variable consideration of up to \$5.5 million, payable via a combination of cash and shares of our common stock, may be due based on the performance of the acquired businesses over a two year period from the date of acquisition. We may also be required to pay additional consideration of up to \$8.0 million, payable in cash over a period of two years, based on certain net cash fee receipts from a particular recovery audit claim at a specific client. We recorded an additional \$4.9 million payable based on management's estimate of the fair value of the variable consideration payable. From the acquisition date to December 31, 2012, we paid \$0.7 million of deferred consideration, \$0.4 million of the earn-out liability and recorded accretion and other adjustments to the earn-out liability of \$0.8 million, resulting in an earn-out payable of \$4.9 million as of December 31, 2012.

We also acquired the assets of several third-party audit firms to which we had subcontracted a portion of our audit services in our Recovery Audit Services Europe/Asia-Pacific segment. These 2012 associate migrations

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included CRC Management Consultants LLP ( CRC ) in January 2012 for a purchase price valued at \$1.0 million; QFS Ltd ( QFS ) in June 2012 for a purchase price valued at \$0.4 million; and Nordic Profit Provider AB ( NPP ) in November 2012 for a purchase price valued at \$0.1 million. We completed an additional associate migration in May 2011 for a purchase price valued at \$0.7 million.

*Financing Activities and Interest Expense.* Net cash provided by financing activities was \$7.8 million in 2012. Net cash used in financing activities was \$5.4 million in 2011 and \$3.5 million in 2010. The net cash provided by financing activities in 2012 included net proceeds of \$14.7 million from our follow-on public offering in December 2012, which we describe in more detail below. Also, we entered into a new credit facility in January 2010, which we describe in more detail below. We used the \$15.0 million term loan proceeds to repay the remaining \$14.1 million of outstanding principal under our prior term loan and to pay \$0.5 million in loan costs incurred in connection with the new credit facility. We made mandatory principal payments totaling \$3.0 million on the new credit facility in each of 2012, 2011 and 2010. We paid \$2.8 million in 2012, \$1.7 million in 2011, and \$0.4 million in 2010 of deferred acquisition consideration, and also repurchased \$1.6 million in 2012, \$1.1 million in 2011, and \$0.2 million in 2010 of stock from employees to allow them to satisfy their tax withholding obligations in connection with the vesting of restricted stock and restricted stock units.

*Secured Credit Facility*

On January 19, 2010, we entered into a four-year revolving credit and term loan agreement with SunTrust Bank ( SunTrust ). We used substantially all the funds from the SunTrust term loan to repay in full the \$14.1 million outstanding under our then-existing Ableco LLC term loan. The SunTrust credit facility consists of a \$15.0 million committed revolving credit facility and a \$15.0 million term loan. The SunTrust credit facility is guaranteed by the Company and its domestic subsidiaries and is secured by substantially all of our assets. Amounts available for borrowing under the SunTrust revolver are based on our eligible accounts receivable and other factors. Borrowing availability under the SunTrust revolver at December 31, 2012 was \$8.1 million. We had no borrowings outstanding under the SunTrust revolver as of December 31, 2012.

The SunTrust term loan requires quarterly principal payments of \$0.8 million from March 2010 through December 2013, and a final principal payment of \$3.0 million in January 2014. The loan agreement requires mandatory prepayments with the net cash proceeds from certain asset sales, equity offerings and insurance proceeds received by the Company. In connection with our equity offering in December 2012 (see *Common Stock Offering* below), we obtained a waiver of the requirement to prepay the loan from SunTrust that enabled us to retain the net proceeds from the offering. The loan agreement also requires an additional annual prepayment contingently payable in April of each year based on excess cash flow ( ECF ) if our leverage ratio as defined in the agreement exceeds a certain threshold. Our leverage ratio has remained below the threshold and ECF payments have not been required in any year, and we do not anticipate one being required in 2013.

Interest on both the revolver and term loan are payable monthly and accrued at an index rate based on the one-month LIBOR rate, plus an applicable margin as determined by the loan agreement. The applicable interest rate margin varies from 2.25% per annum to 3.5% per annum, depending on our consolidated leverage ratio, and is determined in accordance with a pricing grid under the SunTrust loan agreement. The applicable margin was 2.5% and the interest rate was approximately 2.71% at December 31, 2012. We also must pay a commitment fee of 0.5% per annum, payable quarterly, on the unused portion of the \$15.0 million SunTrust revolving credit facility.

The SunTrust credit facility includes customary affirmative, negative, and financial covenants binding on the Company, including delivery of financial statements and other reports, maintenance of existence, and transactions with affiliates. The negative covenants limit the ability of the Company, among other things, to incur debt, incur liens, make investments, sell assets, repurchase shares of its capital stock or declare or pay dividends on its capital stock. The financial covenants included in the SunTrust credit facility, among other things, limit the amount of capital expenditures the Company can make, set forth maximum leverage and net funded debt ratios for the Company and a minimum fixed charge coverage ratio, and also require the Company to maintain minimum consolidated earnings before interest, taxes, depreciation and amortization. In addition, the SunTrust credit facility includes customary events of default.

In September 2010 we entered into an amendment of the SunTrust credit facility that lowered the required minimum adjusted EBITDA and fixed charge coverage ratio through December 31, 2010. In October 2010 we entered into an interest rate swap agreement with SunTrust that limits our exposure to increases in the one-month LIBOR rate. In October 2011 we entered into an amendment of the SunTrust credit facility that increased our capital expenditure limits for 2011 and 2012.

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We believe that we will have sufficient borrowing capacity and cash generated from operations to fund our capital and operational needs for at least the next twelve months.

*Common Stock Offering*

On December 11, 2012, we closed our public offering of 6,249,234 shares of our common stock, which consisted of 2,500,000 shares sold by us and 3,749,234 shares sold by certain selling shareholders, at a price to the public of \$6.39 per share. The net proceeds to us from the public offering, after deducting underwriting discounts and commissions and offering expenses, were \$14.7 million. We intend to use the net proceeds from the public offering for working capital and general corporate purposes, including potential acquisitions. We did not receive any proceeds from the sale of shares by the selling shareholders. In addition, the underwriters elected to exercise an overallotment option for an additional 687,385 shares, and we completed the sale of these additional shares on January 8, 2013. The net proceeds to us from the exercise of the overallotment option, after deducting underwriting discounts and commission and offering expenses, were \$4.1 million.

*Contractual Obligations and Other Commitments*

As discussed in *Notes to Consolidated Financial Statements* included in Item 8 of this Form 10-K, the Company has certain contractual obligations and other commitments. A summary of those commitments as of December 31, 2012 is as follows:

	Payments Due by Period (in thousands)				More Than 5 Years
	Total	Less Than 1 Year	1-3 Years	3-5 Years	
<b>Contractual obligations</b>					
Long-term debt obligations (1)	\$ 6,000	\$ 3,000	\$ 3,000	\$	\$
Interest and commitment fee on Secured Credit Facility (2)	215	207	8		
Operating lease obligations	18,539	8,127	8,965	1,447	
Payments to Messrs. Cook and Toma (3)	927	60	126	133	608
Purchase price payments for business acquisitions (4)	6,697	4,218	2,479		
Expected interest and compensation relating to business acquisition obligations (5)	955	856	99		
Severance	971	971			
<b>Total</b>	<b>\$ 34,304</b>	<b>\$ 17,439</b>	<b>\$ 14,677</b>	<b>\$ 1,580</b>	<b>\$ 608</b>

- (1) Excludes variable rate interest (LIBOR plus 2.25% to 3.50% per annum) payable monthly. For an estimate of interest due on the loan see footnote (2).
- (2) Represents the estimated commitment fee and interest due on the Secured Credit Facility using the interest rate as of December 31, 2012 and assuming no borrowings on the revolver. See Note 5 of the Notes to Consolidated Financial Statements for additional information regarding the Credit Agreement.
- (3) Represents estimated reimbursements payable for healthcare costs incurred by these former executives.
- (4) Represents the estimated present value of deferred payments relating to our acquisitions of FAP, Etesius, TJG and BSI see *Business Acquisitions* above. These amounts generally represent the estimated present value of the variable consideration which may be due based on cash flows generated by the acquired business over the next few years. Certain of the obligations are denominated in British pounds sterling. The U.S. dollar amounts included above are based on December 31, 2012 foreign exchange rates.
- (5) Represents the estimated interest and compensation expense to be incurred to increase the present value amounts for business acquisition obligations listed above to the estimated payment amounts.

As of December 31, 2012, our liabilities for uncertain tax positions were \$2.2 million, which are classified as current. We are unable to reasonably estimate the timing of future cash flows related to such amounts as the timing is dependent on examinations by taxing authorities.

*2006 Management Incentive Plan*

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At the annual meeting of shareholders held on August 11, 2006, the shareholders of the Company approved a proposal granting authorization to issue up to 2.1 million shares of our common stock under the 2006 Management Incentive Plan ( 2006 MIP ). At Performance Unit settlement dates, participants are issued that number of shares of

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Company common stock equal to 60% of the number of Performance Units being settled, and are paid in cash an amount equal to 40% of the fair market value of that number of shares of common stock equal to the number of Performance Units being settled. Prior to 2012, Performance Units were only granted in 2006 and 2007, and the last of such units were settled in May 2011. No Performance Units were outstanding as of December 31, 2011.

On June 19, 2012, seven senior officers of the Company were granted 154,264 Performance Units under the 2006 MIP, comprising all remaining available awards under the plan. The awards had an aggregate grant date fair value of \$1.2 million and vest ratably over three years.

All Performance Units must be settled before April 30, 2016. We recognized compensation expense of \$0.2 million in 2012 and less than \$0.1 million in both 2011 and 2010 related to these 2006 MIP Performance Unit awards. We determined the amount of compensation expense recognized on the assumption that none of the Performance Unit awards will be forfeited.

Cash payments relating to these MIP awards were \$0.1 million in 2011 and \$0.6 million in 2010. There was no cash payment in 2012 for the MIP awards.

### ***Off Balance Sheet Arrangements***

As of December 31, 2012, the Company did not have any material off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of the SEC's Regulation S-K.

### **Critical Accounting Policies**

We describe our significant accounting policies in *Note 1* of Notes to Consolidated Financial Statements included in Item 8 of this Form 10-K. However, certain of our accounting policies are particularly important to the portrayal of our financial position and results of operations and require the application of significant judgment by management. As a result, they are subject to an inherent degree of uncertainty. We consider accounting policies that involve the use of estimates that meet both of the following criteria to be critical accounting policies. First, the accounting estimate requires us to make assumptions about matters that are highly uncertain at the time that the accounting estimate is made. Second, alternative estimates in the current period, or changes in the estimate that are reasonably likely in future periods, would have a material impact on the presentation of our financial condition, changes in financial condition or results of operations.

In addition to estimates that meet the critical estimate criteria, we also make many other accounting estimates in preparing our consolidated financial statements and related disclosures. All estimates, whether or not deemed critical, affect reported amounts of assets, liabilities, revenue and expenses, as well as disclosures of contingent assets and liabilities. On an on-going basis, we evaluate our estimates and judgments, including those related to revenue recognition, refund liabilities, accounts receivable allowance for doubtful accounts, goodwill and other intangible assets and income taxes. We base our estimates and judgments on historical experience, information available prior to the issuance of the consolidated financial statements and on various other factors that we believe to be reasonable under the circumstances. This information forms the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Materially different results can occur as circumstances change and additional information becomes known, including changes in those estimates not deemed critical.

We believe the following critical accounting policies, among others, involve our more significant estimates and judgments we used in the preparation of our consolidated financial statements. We have discussed the development and selection of accounting estimates, including those deemed critical, and the associated disclosures in this Form 10-K with the audit committee of the Board of Directors.

*Revenue Recognition.* We generally recognize revenue on the accrual basis except with respect to an insignificant number of our international units where we recognize revenue on the cash basis. We generally recognize revenue for a contractually specified percentage of amounts recovered when we have determined that our clients have received economic value (generally through credits taken against existing accounts payable due to the involved vendors or refund checks received from those vendors), and when we have met the following criteria: (a) persuasive evidence of an arrangement exists; (b) services have been rendered; (c) the fee billed to the client is fixed or determinable; and (d) collectability is reasonably assured.

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Additionally, for purposes of determining appropriate timing of recognition and for internal control purposes, we rely on customary business practices and processes for documenting that the criteria described in (a) through (d) above have been met. Such customary business practices and processes may vary significantly by client. On occasion, it is possible that a transaction has met all of the revenue recognition criteria described above but we do not recognize revenue, unless we can otherwise determine that criteria (a) through (d) above have been met, because our customary business practices and processes specific to that client have not been completed. The determination that we have met each of the aforementioned criteria, particularly the determination of the timing of economic benefit received by the client and the determination that collectability is reasonably assured, requires the application of significant judgment by management and a misapplication of this judgment could result in inappropriate recognition of revenue.

During the third quarter of 2011, we changed the point at which we recognize revenue for our Healthcare Claims Recovery Audit services within our New Services segment based on our gaining sufficient experience with auditing such claims. We now recognize revenue without formal client sign-off provided that we can objectively demonstrate that the acceptance criteria specified by the client are satisfied. This change resulted in a \$1.4 million increase in revenue, a \$0.4 million increase in net earnings and a \$0.02 increase in basic and diluted earnings per common share in 2011.

*Unbilled Receivables & Refund Liabilities.* Unbilled receivables relate to claims for which our clients have received economic value but for which we contractually have agreed not to invoice the clients. These unbilled receivables arise when a portion of our fee is deferred at the time of the initial invoice. At a later date (which can be up to a year after the original invoice, or a year after completion of the audit period), we invoice the unbilled receivable amount. Notwithstanding the deferred due date, our clients acknowledge that we have earned this unbilled receivable at the time of the original invoice, but have agreed to defer billing the client for the related services. Unbilled receivables also arise in our Healthcare Claims Recovery Audit services as we generally cannot invoice the prime contractors for whom we operate as a subcontractor under the Medicare RAC program until cash is collected by the prime contractors.

Refund liabilities result from reductions in the economic value previously received by our clients with respect to vendor claims identified by us and for which we previously have recognized revenue. We satisfy such refund liabilities either by offsets to amounts otherwise due from clients or by cash refunds to clients. We compute the estimate of our refund liabilities at any given time based on actual historical refund data.

We record periodic changes in unbilled receivables and refund liabilities as adjustments to revenue.

During the fourth quarter of 2010, we revised our estimate of expected refund rates of unbilled receivables in our Recovery Audit Services Americas operating segment. We obtained sufficient historical data on our realization of paybacks from unbilled receivables that enabled us to make this change to our method of calculating this estimate. The impact of this change resulted in a \$0.2 million increase in fourth quarter 2010 net earnings, or less than \$0.01 per basic and diluted share. We do not expect that this change in estimate will have a material impact on our net earnings in future periods.

*Goodwill and Other Intangible Assets.* We assess the recoverability of our goodwill and other intangible assets during the fourth quarter of each year, or sooner if events or changes in circumstances indicate that the carrying amount may exceed its fair value. For our goodwill impairment testing in the fourth quarter of 2011, we implemented Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) Update No. 2011-08 and elected to assess qualitative factors prior to performing the two-step process utilized in this testing. Under the new guidance, we are not required to calculate the fair value of our reporting units that hold goodwill unless we determine that it is more likely than not that the fair value of these reporting units is less than their carrying values. In this analysis, we considered a number of factors, including changes in our legal, business and regulatory climates, changes in competition or key personnel, macroeconomic factors impacting our company or our clients, our recent financial performance and expectations of future performance and other pertinent factors. We also utilized this methodology in 2012. Based on these analyses, we determined that it was not necessary for us to perform the two-step process, and we did not record an impairment charge in 2011 or 2012. We last used independent business valuation professionals to calculate the fair value of our reporting units that hold goodwill in the fourth quarter of 2010, but have performed internal calculations in 2011 and 2012.

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In 2012, we recorded a purchase price adjustment for our acquisition of BSI, which led to a reduction of goodwill of \$0.2 million. In connection with the associate migrations we completed in 2012, we recorded additional goodwill of \$0.7 million and additional intangible assets of \$0.2 million consisting of non-compete agreements. In connection with the business acquisitions we completed in 2011, we recorded additional goodwill of \$8.0 million and additional intangible assets of \$4.1 million consisting primarily of customer relationships, non-compete agreements and trademarks. In connection with the business acquisitions we completed in 2010, we recorded additional goodwill of \$0.6 million and additional intangible assets of \$3.9 million consisting primarily of customer relationships, non-compete agreements and trade names. We determined these amounts based on estimates we made and on valuation reports we obtained from third parties. We generally use accelerated amortization methods for customer relationships and trade names, and straight-line amortization for non-compete agreements.

*Income Taxes.* Our effective tax rate is based on historical and anticipated future taxable income, statutory tax rates and tax planning opportunities available to us in the various jurisdictions in which we operate. Significant judgment is required in determining the effective tax rate and in evaluating our tax positions. Tax regulations require items to be included in the tax returns at different times than the items are reflected in the financial statements. As a result, our effective tax rate reflected in our Consolidated Financial Statements included in Item 8 of this Form 10-K is different than that reported in our tax returns. Some of these differences are permanent, such as expenses that are not deductible on our tax returns, and some are temporary differences, such as depreciation expense. Temporary differences create deferred tax assets and liabilities. Deferred tax assets generally represent items that can be used as a tax deduction or credit in our tax returns in future years for which we have already recorded the tax benefit in our Consolidated Statements of Income. We establish valuation allowances to reduce net deferred tax assets to the amounts that we believe are more likely than not to be realized. We adjust these valuation allowances in light of changing facts and circumstances. Deferred tax liabilities generally represent tax expense recognized in our consolidated financial statements for which payment has been deferred, or expense for which a deduction has already been taken on our tax returns but has not yet been recognized as an expense in our consolidated financial statements.

We reduce our deferred tax assets by a valuation allowance if it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences are deductible. In determining the amount of valuation allowance to record, we consider all available positive and negative evidence affecting specific deferred tax assets, including our past and anticipated future performance, the reversal of deferred tax liabilities, the length of carry-back and carry-forward periods, and the implementation of tax planning strategies. Objective positive evidence is necessary to support a conclusion that a valuation allowance is not needed for all or a portion of deferred tax assets when significant negative evidence exists. Cumulative tax losses in recent years are the most compelling form of negative evidence we considered in this determination.

As a result of our review of the deferred tax assets in 2011, we released a portion of our valuation allowance relating to a foreign subsidiary, and recorded \$0.5 million of tax benefit in the fourth quarter of 2011. Also in the fourth quarter of 2011, management recorded the initial purchase accounting entries for the December 2011 acquisition of BSI. As a part of this process, we recorded a \$1.7 million reduction in the deferred tax asset valuation allowance that resulted from the deferred tax liabilities that we recorded relating to the acquisition. This reduction was accounted for as an income tax benefit in the fourth quarter of 2011.

We apply a more-likely-than-not recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We refer to U.S. generally accepted accounting principles ( GAAP ) for guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. Our policy for recording interest and penalties associated with tax positions is to record such items as a component of earnings before income taxes. As a part of an ongoing Canadian tax audit, we continue to defend our tax position related to the valuation of an intercompany transaction. We recognized \$0.6 million of additional tax expense in the fourth quarter of 2011 to reflect our estimate of the potential tax due based on our continuing discussions with the Canadian tax authorities. In the fourth quarter of 2012, we reduced our tax expense by \$0.4 million and our interest expense by \$0.8 million to reflect adjustments to our estimates for



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uncertain tax positions. We adjusted our estimates for several reasons, including the expiration of the statute of limitations for certain of these taxes in several states and in two foreign jurisdictions, completion of an audit by a foreign jurisdiction that resulted in a lower tax assessment than we had estimated, and the imposition of limitations on our potential liability resulting from our beginning the voluntary disclosure agreement process with one state.

*Stock-Based Compensation.* We account for awards of equity instruments issued to employees under the fair value method of accounting and recognize such amounts in our Consolidated Statements of Income. We measure compensation cost for all stock-based awards at fair value on the date of grant and recognize compensation expense using the straight-line method over the service period over which we expect the awards to vest. We recognize compensation costs for awards with performance conditions based on the probable outcome of the performance conditions. We accrue compensation cost if we believe it is probable that the performance condition(s) will be achieved and do not accrue compensation cost if we believe it is not probable that the performance condition(s) will be achieved.

We estimate the fair value of all time-vested options as of the date of grant using the Black-Scholes option valuation model, which was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. Option valuation models require the input of highly subjective assumptions, including the expected stock price volatility.

We estimate the fair value of awards of restricted shares and nonvested shares as being equal to the market value of the common stock on the date of the award. We classify our share-based payments as either liability-classified awards or as equity-classified awards. We remeasure liability-classified awards to fair value at each balance sheet date until the award is settled. We measure equity-classified awards at their grant date fair value and do not subsequently remeasure them. We have classified our share-based payments which are settled in our common stock as equity-classified awards and our share-based payments that are settled in cash as liability-classified awards. Compensation costs related to equity-classified awards generally are equal to the grant-date fair value of the award amortized over the vesting period of the award. The liability for liability-classified awards generally is equal to the fair value of the award as of the balance sheet date multiplied by the percentage vested at the time. We charge (or credit) the change in the liability amount from one balance sheet date to another to compensation expense.

Stock-based compensation expense was \$6.3 million in 2012, \$5.1 million in 2011 and \$4.0 million in 2010. We discuss stock-based compensation in more detail in *Note 1(l)* and *Note 11* of Notes to Consolidated Financial Statements included in Item 8 of this Form 10-K.

## **New Accounting Standards**

No new accounting standards have been issued by the FASB and included in the ASC that PRGX has not yet adopted that we expect will have a significant impact on the Company's financial statements.

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**ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk**

*Foreign Currency Market Risk.* Our reporting currency is the U.S. dollar although we transact business in various foreign locations and currencies. As a result, our financial results could be significantly affected by factors such as changes in foreign currency exchange rates, or weak economic conditions in the foreign markets in which we provide our services. Our operating results are exposed to changes in exchange rates between the U.S. dollar and the currencies of the other countries in which we operate. When the U.S. dollar strengthens against other currencies, the value of foreign functional currency revenue decreases. When the U.S. dollar weakens, the value of the foreign functional currency revenue increases. Overall, we are a net receiver of currencies other than the U.S. dollar and, as such, benefit from a weaker dollar. We therefore are adversely affected by a stronger dollar relative to major currencies worldwide. In 2012, we recognized \$11.6 million of operating income from operations located outside the U.S., virtually all of which we accounted for originally in currencies other than the U.S. dollar. Upon translation into U.S. dollars, such operating income would increase or decrease, assuming a hypothetical 10% change in weighted-average foreign currency exchange rates against the U.S. dollar, by approximately \$1.2 million. We do not have any arrangements in place currently to hedge our foreign currency risk.

*Interest Rate Risk.* Our interest income and expense are sensitive to changes in the general level of U.S. interest rates. In this regard, changes in U.S. interest rates affect the interest earned on our cash equivalents as well as interest paid on our debt. We had \$6.0 million outstanding under a term loan and \$8.1 million of calculated borrowing availability under our revolving credit facility as of December 31, 2012, but had no amounts drawn under the revolving credit facility as of that date. Interest on both the revolver and the term loan are payable monthly and accrue at an index rate using the one-month LIBOR rate plus an applicable margin as determined by the loan agreement. The applicable interest rate margin varies from 2.25% per annum to 3.5% per annum and was 2.71% at December 31, 2012. Assuming full utilization of the revolving credit facility, a hypothetical 100 basis point change in interest rates applicable to the revolver would result in an approximate \$0.1 million change in annual pre-tax income. A hypothetical 100 basis point change in interest rates applicable to the term loan would result in an approximate \$0.1 million change in annual pre-tax income.

In order to mitigate some of this interest rate risk, we entered into an interest rate swap agreement with SunTrust Bank in October 2010 under which we pay additional interest on a notional amount of \$3.8 million through December 31, 2013 to the extent that the one-month LIBOR rate is below 1.23%, and receive payments from SunTrust Bank to the extent the index exceeds this level. The notional amount is equal to the final two payments due under the term loan in December 2013 and January 2014. Currently, LIBOR is below 1.23% and we are paying a minimal amount of additional interest under this agreement. Should LIBOR rates increase above the 1.23% level, we will incur additional interest expense on all of the amounts outstanding under our credit facility, but will offset a portion of this additional expense with the income we earn from the swap agreement.

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**ITEM 8. Financial Statements and Supplementary Data**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

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<u>Consolidated Statements of Comprehensive Income for the Years ended December 31, 2012, 2011 and 2010</u>	41
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**Report of Independent Registered Public Accounting Firm**

Board of Directors and Shareholders

PRGX Global, Inc.

Atlanta, Georgia

We have audited the accompanying consolidated balance sheets of PRGX Global, Inc. and subsidiaries (the Company) as of December 31, 2012 and 2011 and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2012. In connection with our audits of the financial statements, we have also audited the financial statement schedule listed in the accompanying index. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements and schedule. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of PRGX Global, Inc. and subsidiaries at December 31, 2012 and 2011, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2012, in conformity with accounting principles generally accepted in the United States of America.

Also, in our opinion, the financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 13, 2013 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Atlanta, Georgia

March 13, 2013

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**PRGX GLOBAL, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**

(In thousands, except per share data)

	Years Ended December 31,		
	2012	2011	2010
Revenue	\$ 208,503	\$ 203,117	\$ 184,081
Operating expenses:			
Cost of revenue	134,390	137,482	126,069
Selling, general and administrative expenses	52,527	49,102	40,735
Depreciation of property and equipment	7,084	5,401	4,903
Amortization of intangible assets	7,224	4,991	4,131
Total operating expenses	201,225	196,976	175,838
Operating income	7,278	6,141	8,243
Foreign currency transaction (gains) losses on short-term intercompany balances	(377)	417	422
Interest expense	(1,116)	(1,904)	(1,451)
Interest income	150	288	146
Loss on debt extinguishment (Note 5)			(1,381)
Earnings before income taxes	6,689	4,108	5,135
Income tax expense (Note 7)	1,297	1,292	1,882
Net earnings	\$ 5,392	\$ 2,816	\$ 3,253
Basic earnings per common share (Note 3)	\$ 0.21	\$ 0.11	\$ 0.14
Diluted earnings per common share (Note 3)	\$ 0.21	\$ 0.11	\$ 0.13
Weighted-average common shares outstanding (Note 3):			
Basic	25,566	24,634	23,906
Diluted	26,137	25,029	24,144

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(In thousands)

	Years Ended December 31,		
	2012	2011	2010
Net earnings	\$ 5,392	\$ 2,816	\$ 3,253
Foreign currency translation adjustments	363	(519)	380

Comprehensive income	\$ 5,755	\$ 2,297	\$ 3,633
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*See accompanying Notes to Consolidated Financial Statements.*

**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

(In thousands, except share and per share data)

	December 31,	
	2012	2011
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 37,806	\$ 20,337
Restricted cash	65	64
Receivables:		
Contract receivables, less allowances of \$1,693 in 2012 and \$811 in 2011:		
Billed	32,626	30,583
Unbilled	12,501	10,041
	45,127	40,624
Employee advances and miscellaneous receivables, less allowances of \$538 in 2012 and \$272 in 2011	1,352	1,591
<b>Total receivables</b>	<b>46,479</b>	<b>42,215</b>
Prepaid expenses and other current assets	3,801	5,571
Deferred income taxes ( <i>Note 7</i> )	52	23
<b>Total current assets</b>	<b>88,203</b>	<b>68,210</b>
Property and equipment:		
Computer and other equipment	25,320	24,993
Furniture and fixtures	3,022	2,980
Leasehold improvements	3,270	3,066
Software	25,312	19,753
	56,924	50,792
Less accumulated depreciation and amortization	(37,350)	(32,206)
<b>Property and equipment, net</b>	<b>19,574</b>	<b>18,586</b>
Goodwill ( <i>Note 4</i> )	13,669	12,946
Intangible assets, less accumulated amortization of \$27,720 in 2012 and \$22,116 in 2011 ( <i>Note 4</i> )	18,399	23,406
Unbilled receivables	1,391	1,672
Deferred loan costs, net of accumulated amortization ( <i>Note 5</i> )	193	376
Deferred income taxes ( <i>Note 7</i> )	1,552	831
Other assets	605	386
	\$ 143,586	\$ 126,413
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 14,136	\$ 15,035
Accrued payroll and related expenses	20,874	21,920
Refund liabilities	6,979	6,746
Deferred revenue	1,551	1,688

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Current portions of debt <i>(Note 5)</i>	3,000	3,000
Business acquisition obligations <i>(Note 12)</i>	4,218	3,502
Total current liabilities	50,758	51,891
Long-term debt <i>(Note 5)</i>	3,000	6,000
Noncurrent business acquisition obligations <i>(Note 12)</i>	2,479	5,604
Refund liabilities	1,159	1,000
Other long-term liabilities	1,538	2,828
Total liabilities	58,934	67,323
Commitments and contingencies <i>(Notes 2, 5, 6, 9 and 10)</i>		
Shareholders' equity <i>(Notes 10 and 12):</i>		
Common stock, no par value; \$.01 stated value per share. Authorized 50,000,000 shares; 27,893,132 shares issued and outstanding in 2012 and 25,108,754 shares issued and outstanding in 2011	279	251
Additional paid-in capital	594,045	574,266
Accumulated deficit	(513,200)	(518,592)
Accumulated other comprehensive income	3,528	3,165
Total shareholders' equity	84,652	59,090
	\$ 143,586	\$ 126,413

*See accompanying Notes to Consolidated Financial Statements.*



**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY**

Years Ended December 31, 2012, 2011 and 2010

(In thousands, except share data)

	Common Stock		Additional	Accumulated	Accumulated	Total
	Shares	Amount	Paid-In	Deficit	Other	Shareholders
			Capital		Comprehensive	Equity
					Income	
<b>Balance at December 31, 2009</b>	23,272,892	\$ 233	\$ 562,563	\$ (524,661)	\$ 3,304	\$ 41,439
Net earnings				3,253		3,253
Foreign currency translation adjustments					380	380
Issuances of common stock:						
Restricted share awards	560,460	6	(6)			
Restricted shares remitted by employees for taxes	(28,547)		(214)			(214)
Stock option exercises	38,633		109			109
2006 MIP Performance Unit settlements	134,490	1	(1)			
Forfeited restricted share awards	(45,154)	(1)	1			
Stock-based compensation expense			3,876			3,876
<b>Balance at December 31, 2010</b>	23,932,774	239	566,328	(521,408)	3,684	48,843
Net earnings				2,816		2,816
Foreign currency translation adjustments					(519)	(519)
Issuances of common stock:						
Restricted share awards	694,030	7	(7)			
Shares issued for acquisition	640,614	6	3,716			3,722
Restricted shares remitted by employees for taxes	(132,974)	(1)	(1,062)			(1,063)
Stock option exercises	116,073	1	352			353
2006 MIP Performance Unit settlements	26,898					
Forfeited restricted share awards	(168,661)	(1)	1			
Stock-based compensation expense			4,938			4,938
<b>Balance at December 31, 2011</b>	25,108,754	251	574,266	(518,592)	3,165	59,090
Net earnings				5,392		5,392
Foreign currency translation adjustments					363	363
Issuances of common stock:						
Restricted share awards	500,128	5	(5)			
Shares issued for stock offering	2,500,000	25	14,657			14,682
Restricted shares remitted by employees for taxes	(161,514)	(2)	(1,603)			(1,605)
Stock option exercises	141,849	2	557			559
Forfeited restricted share awards	(196,085)	(2)	2			
Stock-based compensation expense			6,171			6,171
<b>Balance at December 31, 2012</b>	27,893,132	\$ 279	\$ 594,045	\$ (513,200)	\$ 3,528	\$ 84,652

See accompanying Notes to Consolidated Financial Statements.

**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

	Years Ended December 31,		
	2012	2011	2010
<b>Cash flows from operating activities:</b>			
Net earnings	\$ 5,392	\$ 2,816	\$ 3,253
<b>Adjustments to reconcile earnings from operations to net cash provided by operating activities:</b>			
Depreciation and amortization	14,308	10,392	9,034
Amortization of debt discount, premium and deferred loan costs	183	188	1,539
Stock-based compensation expense	6,321	5,093	3,980
Loss on disposals of property, plant and equipment, net	31	6	15
Foreign currency transaction (gains) losses on short-term intercompany balances	(377)	417	422
Deferred income taxes	(799)	(2,151)	(1,354)
<b>Changes in operating assets and liabilities, net of business acquisitions:</b>			
Restricted cash	(1)		193
Billed receivables	(1,598)	1,717	(1,757)
Unbilled receivables	(2,179)	(5,419)	(320)
Prepaid expenses and other current assets	693	(718)	(1,400)
Other assets	(179)	(455)	56
Accounts payable and accrued expenses	(1,125)	110	(2,529)
Accrued payroll and related expenses	(1,258)	8,289	(6,255)
Refund liabilities	392	(837)	(39)
Deferred revenue	(157)	(338)	(139)
Noncurrent compensation obligations	345	432	(707)
Other long-term liabilities	(1,149)	(249)	(523)
<b>Net cash provided by operating activities</b>	<b>18,843</b>	<b>19,293</b>	<b>3,469</b>
<b>Cash flows from investing activities:</b>			
Business acquisitions, net of cash acquired	(1,542)	(3,155)	(7,741)
Purchases of property and equipment, net of disposal proceeds	(7,931)	(8,287)	(6,934)
<b>Net cash used in investing activities</b>	<b>(9,473)</b>	<b>(11,442)</b>	<b>(14,675)</b>
<b>Cash flows from financing activities:</b>			
Repayments of former credit facility (Note 5)			(14,070)
Repayments of long-term debt and capital lease obligations	(3,000)	(3,000)	(3,260)
Proceeds from term loan (Note 5)			15,000
Payments for deferred loan costs		(6)	(666)
Payments of deferred acquisition consideration	(2,837)	(1,694)	(409)
Net proceeds from issuance of common stock	14,682		
Restricted stock remitted by employees for taxes	(1,605)	(1,063)	(214)
Proceeds from stock option exercises	559	353	109
<b>Net cash provided by (used in) financing activities</b>	<b>7,799</b>	<b>(5,410)</b>	<b>(3,510)</b>
<b>Effect of exchange rates on cash and cash equivalents</b>	<b>300</b>	<b>(552)</b>	<b>138</b>
<b>Net change in cash and cash equivalents</b>	<b>17,469</b>	<b>1,889</b>	<b>(14,578)</b>

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Cash and cash equivalents at beginning of year	20,337	18,448	33,026
Cash and cash equivalents at end of year	\$ 37,806	\$ 20,337	\$ 18,448
<b>Supplemental cash flow statement information:</b>			
Cash paid during the year for interest	\$ 340	\$ 422	\$ 570
Cash paid during the year for income taxes, net of refunds received	\$ 2,730	\$ 4,235	\$ 2,743
Deferred and contingent business acquisition consideration ( <i>Note 12</i> )	\$ 189	\$ 5,643	\$ 1,638

*See accompanying Notes to Consolidated Financial Statements.*

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**PRGX GLOBAL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***(a) Description of Business and Basis of Presentation***

*Description of Business*

The principal business of PRGX Global, Inc. and subsidiaries is providing recovery audit services to large businesses and government agencies having numerous payment transactions. PRGX Global, Inc. also provides Profit Optimization services, including analytics and advisory services, to a similar client base. These businesses include, but are not limited to:

retailers such as discount, department, specialty, grocery and drug stores;

business enterprises other than retailers such as manufacturers, financial services firms, and pharmaceutical companies;

healthcare payers, both private sector health insurance companies and state and federal government payers such as the Centers for Medicare and Medicaid Services ( CMS ); and

federal and state government agencies.

Except as otherwise indicated or unless the context otherwise requires, PRGX, we, us, our and the Company refer to PRGX Global, Inc. and subsidiaries. PRGX currently provides services to clients in approximately 40 countries.

*Basis of Presentation*

The consolidated financial statements include the financial statements of the Company and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Certain reclassifications have been made to the 2011 financial statements to conform to the presentations adopted in 2012.

Management of the Company has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with U.S. generally accepted accounting principles ( GAAP ). Actual results could differ from those estimates.

***(b) Revenue Recognition, Unbilled Receivables and Refund Liabilities***

We base our revenue on specific contracts with our clients. These contracts generally specify: (a) time periods covered by the audit; (b) nature and extent of audit services we are to provide; (c) the client's duties in assisting and cooperating with us; and (d) fees payable to us, generally expressed as a specified percentage of the amounts recovered by the client resulting from overpayment claims identified. Clients generally recover claims either by taking credits against outstanding payables or future purchases from the involved vendors, or receiving refund checks directly from those vendors. The manner in which a claim is recovered by a client often is dictated by industry practice. In addition, many clients establish specific procedural guidelines that we must satisfy prior to submitting claims for client approval, and these guidelines are unique to each client. For some services we provide, we earn our compensation in the form of a flat fee, a fee per hour, or a fee per other unit of service.

We generally recognize revenue on the accrual basis except with respect to an insignificant number of our international units where we recognize revenue on the cash basis. We generally recognize revenue for a contractually specified percentage of amounts recovered when we have determined that our clients have received economic value (generally through credits taken against existing accounts payable due to the

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involved vendors or refund checks received from those vendors) and when we have met the following criteria: (a) persuasive evidence of an arrangement exists; (b) services have been rendered; (c) the fee billed to the client is fixed or determinable; and (d) collectability is reasonably assured. In certain limited circumstances, we will invoice a client prior to meeting all four of these criteria; in such cases, we defer the revenue until we meet all of the criteria. Additionally,

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for purposes of determining appropriate timing of recognition and for internal control purposes, we rely on customary business practices and processes for documenting that we have met the criteria described in (a) through (d) above. Such customary business practices and processes may vary significantly by client. On occasion, it is possible that a transaction has met all of the revenue recognition criteria described above but we do not recognize revenue, unless we can otherwise determine that criteria (a) through (d) above have been met, because our customary business practices and processes specific to that client have not been completed.

Historically, there has been a certain amount of revenue with respect to which, even though we had met the requirements of our revenue recognition policy, our clients' vendors ultimately have rejected the claims underlying the revenue. In that case, our clients may request a refund or offset of such amount even though we may have collected fees. We record any such refunds as a reduction of revenue. We provide refund liabilities for these reductions in the economic value previously received by our clients with respect to vendor claims we identified and for which we previously have recognized revenue. We compute an estimate of our refund liabilities at any given time based on actual historical refund data.

During the fourth quarter of 2010, we revised our estimate of expected refund rates of unbilled receivables in our Recovery Audit Services Americas operating segment. We obtained sufficient historical data on our realization of paybacks from unbilled receivables that enabled us to make this change to our method of calculating this estimate. The impact of this change in estimate resulted in a \$0.2 million increase in fourth quarter 2010 net earnings, or less than \$0.01 per basic and diluted share. We believe that this change represents an improvement in our method for determining this estimate.

During the third quarter of 2011, we changed the point at which we recognize revenue for our Healthcare Claims Recovery Audit services within our New Services segment based on our gaining sufficient experience with auditing such claims. We now recognize revenue without formal client sign-off provided that we can objectively demonstrate that the acceptance criteria specified by the client are satisfied. This change resulted in a \$1.4 million increase in revenue, a \$0.4 million increase in net earnings and a \$0.02 increase in basic and diluted earnings per common share in 2011.

Unbilled receivables relate to claims for which clients have received economic value but for which we contractually have agreed not to submit an invoice to the clients at such time. Unbilled receivables arise when a portion of our fee is deferred at the time of the initial invoice. At a later date (which can be up to a year after original invoice, and at other times a year after completion of the audit period), we invoice the unbilled receivable amount. Notwithstanding the deferred due date, our clients acknowledge that we have earned this unbilled receivable at the time of the original invoice, but have agreed to defer billing the client for the related services. Unbilled receivables also arise in our Healthcare Claims Recovery Audit services as we generally cannot invoice the prime contractors for whom we operate as a subcontractor under the Medicare RAC program until cash is collected by the prime contractors.

We record periodic changes in unbilled receivables and refund liabilities as adjustments to revenue.

We derive a relatively small portion of revenue on a fee-for-service basis whereby billing is based upon a flat fee, a fee per hour, or a fee per other unit of service. We recognize revenue for these types of services as we provide and invoice for them, and when criteria (a) through (d) as set forth above are met.

***(c) Cash and Cash Equivalents***

Cash and cash equivalents include all cash balances and highly liquid investments with an initial maturity of three months or less from date of purchase. We place our temporary cash investments with high credit quality financial institutions. At times, certain investments may be in excess of the Federal Deposit Insurance Corporation ( FDIC ) insurance limit or otherwise may not be covered by FDIC insurance.

Our cash and cash equivalents included short-term investments of approximately \$25.1 million as of December 31, 2012 and \$8.2 million as of December 31, 2011, of which approximately \$1.6 million and \$2.7 million, respectively, were held at banks outside of the United States, primarily in Brazil.



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***(d) Fair Value of Financial Instruments***

We state cash equivalents at cost, which approximates fair market value. The carrying values for receivables from clients, unbilled services, accounts payable, deferred revenue and other accrued liabilities reasonably approximate fair market value due to the nature of the financial instrument and the short term maturity of these items.

We recorded bank debt of \$6.0 million as of December 31, 2012 and \$9.0 million as of December 31, 2011 at the unpaid balances as of those dates based on the effective borrowing rates and repayment terms when originated. This debt is subject to variable rate terms, and we believe that its fair value is approximately equal to its carrying value. We consider the factors used in determining the fair value of this debt to be Level 3 inputs (significant unobservable inputs).

We recorded business acquisition obligations of \$6.7 million as of December 31, 2012 and \$9.1 million as of December 31, 2011 representing the fair value of deferred consideration and earn-out payments estimated to be due as of those dates. We determine the estimated fair values based on our projections of future revenue and profits or other factors used in the calculation of the ultimate payment to be made. The discount rate that we use to value the liability is based on specific business risk, cost of capital, and other factors. We consider these factors to be Level 3 inputs (significant unobservable inputs).

***(e) Property and Equipment***

We report property and equipment at cost or estimated fair value at acquisition date and depreciate them over their estimated useful lives using the straight-line method. During the second quarter of 2010, we revised our estimate of the useful lives of certain fixed assets used for the purpose of calculating depreciation expense based on a review of our planned fixed asset replacement cycle. Our revised useful lives for fixed assets are three years for computer laptops, four years for desktops, five years for IT server, storage and network equipment, five years for furniture and fixtures and three years for purchased software. We continue to amortize leasehold improvements using the straight-line method over the shorter of the lease term or ten years. The impact of the change in estimate was a reduction in depreciation expense of approximately \$0.6 million in 2010. Depreciation expense was \$7.1 million in 2012, \$5.4 million in 2011 and \$4.9 million in 2010.

We review the carrying value of property and equipment for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, we will recognize an impairment loss equal to the amount by which the carrying value exceeds the fair value of the asset. No impairment charges were necessary in the three years ended December 31, 2012.

***(f) Software Development Costs***

We capitalize a portion of the costs we incur related to our internal development of software that we use in our operations and amortize these costs using the straight-line method over the expected useful lives of three to seven years.

We also capitalize a portion of the costs we incur related to our internal development of software that we intend to market to others. We amortize these costs over the products' estimated economic lives, which typically are three years, beginning when the underlying products are available for general release to clients. We review the carrying value of capitalized software development costs for impairment whenever events and circumstances indicate that the carrying value of the asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, we will recognize an impairment loss equal to the amount by which the carrying value exceeds the fair value of the asset. No impairment charges were necessary in the three years ended December 31, 2012. We consider these software development activities to be research and development costs and expense them as incurred. However, we capitalize the costs incurred for the development of computer software that will be sold, leased, or otherwise marketed or that will be used in our operations beginning when technological feasibility has been established. Research and development costs, including the amortization of amounts previously capitalized, were \$4.0 million in 2012, \$3.4 million in 2011 and \$3.2 million in 2010.





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***(g) Goodwill and Intangible Assets***

Goodwill represents the excess of the purchase price over the estimated fair market value of net identifiable assets of acquired businesses. We evaluate the recoverability of goodwill in the fourth quarter of each year or sooner if events or changes in circumstances indicate that the carrying amount may exceed its fair value. This evaluation has two steps. The first step identifies potential impairments by comparing the fair value of the reporting unit with its carrying value, including goodwill. If the calculated fair value of a reporting unit exceeds the carrying value, goodwill is not impaired, and the second step is not necessary. If the carrying value of a reporting unit exceeds the fair value, the second step calculates the possible impairment loss by comparing the implied fair value of goodwill with the carrying value. If the fair value is less than the carrying value, we would record an impairment charge.

We implemented Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) Update No. 2011-08 in 2011 and elected to assess qualitative factors in both 2011 and 2012 prior to performing the two-step process described above. Under the new guidance, we are not required to calculate the fair value of our reporting units that hold goodwill unless we determine that it is more likely than not that the fair value of these reporting units is less than their carrying values. In this analysis, we considered a number of factors, including changes in our legal, business and regulatory climates, changes in competition or key personnel, macroeconomic factors impacting our company or our clients, our recent financial performance and expectations of future performance and other pertinent factors. Based on these analyses, we determined that it was not necessary for us to perform the two-step process. We last used independent business valuation professionals to estimate fair value in the fourth quarter of 2010 and determined that fair value exceeded carrying value for all relevant reporting units. No impairment charges were necessary in the three years ended December 31, 2012.

***(h) Direct Expenses and Deferred Costs***

We typically expense direct expenses that we incur during the course of recovery audit and delivery of Profit Optimization services as incurred. For certain implementation and set-up costs associated with our fee for service revenue that we earn over an extended period of time, we defer the related direct and incremental costs and recognize them as expenses over the life of the underlying contract.

In addition, we incur significant personnel and other costs when performing recovery audit services to certain healthcare organizations. The process of documenting that we have met our revenue recognition criteria as described in *(b) Revenue Recognition, Unbilled Receivables and Refund Liabilities* above is extensive and generally is completed from three months to a year after we substantially have completed our services. We defer these costs and recognize them as expenses when we record the related revenue. We had deferred \$0.9 million of these costs as of December 31, 2012 and \$1.1 million as of December 31, 2011 and reflected them as Prepaid expenses and other current assets in our Consolidated Balance Sheets.

***(i) Income Taxes***

We account for income taxes under the asset and liability method. We recognize deferred tax assets and liabilities for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. We measure deferred tax assets and liabilities using enacted tax rates we expect to apply to taxable income in the years in which we expect to recover or settle those temporary differences. We recognize the effect on the deferred tax assets and liabilities of a change in tax rates in income in the period that includes the enactment date.

We reduce our deferred tax assets by a valuation allowance if it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences are deductible. In determining the amount of valuation allowance to record, we consider all available positive and negative evidence

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affecting specific deferred tax assets, including our past and anticipated future performance, the reversal of deferred tax liabilities, the length of carry-back and carry-forward periods and the implementation of tax planning strategies. Objective positive evidence is necessary to support a conclusion that a valuation allowance is not needed for all or a portion of deferred tax assets when significant negative evidence exists. Cumulative losses for tax reporting purposes in recent years are the most compelling form of negative evidence we considered in this determination.

We apply a more-likely-than-not recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We refer to GAAP for guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. In accordance with FASB ASC 740, our policy for recording interest and penalties associated with tax positions is to record such items as a component of earnings before income taxes.

***(j) Foreign Currency***

We use the local currency as the functional currency in the majority of the countries in which we conduct business outside of the United States. We translate the assets and liabilities denominated in foreign currencies into U.S. dollars at the current rates of exchange at the balance sheet date. We include the translation gains and losses as a separate component of shareholders' equity and in the determination of comprehensive income. We translate revenue and expenses in foreign currencies at the weighted average exchange rates for the period. We separately state the foreign currency transaction gains and losses on short-term intercompany balances in the Consolidated Statements of Income. We include all other realized and unrealized foreign currency transaction gains (losses) in Selling, general and administrative expenses.

***(k) Earnings Per Common Share***

We compute basic earnings per common share by dividing net earnings available to common shareholders by the weighted-average number of shares of common stock outstanding during the period. We compute diluted earnings per common share by dividing net earnings available to common shareholders by the sum of (1) the weighted-average number of shares of common stock outstanding during the period, (2) the dilutive effect of the assumed exercise of stock options using the treasury stock method, and (3) the dilutive effect of other potentially dilutive securities. We exclude the potential dilutive effect of stock options and convertible instruments from the determination of diluted earnings per share if the effect of including them would be antidilutive.

***(l) Stock-Based Compensation***

We account for awards of equity instruments issued to employees under the fair value method of accounting and recognize such amounts in our Consolidated Statements of Income. We measure compensation cost for all stock-based awards at fair value on the date of grant and recognize compensation expense in our Consolidated Statements of Income using the straight-line method over the service period over which we expect the awards to vest. We recognize compensation costs for awards with performance conditions based on the probable outcome of the performance conditions. We accrue compensation cost if we believe it is probable that the performance condition(s) will be achieved and do not accrue compensation cost if we believe it is not probable that the performance condition(s) will be achieved.

We estimate the fair value of all time-vested options as of the date of grant using the Black-Scholes option valuation model, which was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. Option valuation models require the input of highly subjective assumptions, including the expected stock price volatility.

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For time-vested option grants that resulted in compensation expense recognition, we used the following assumptions in our Black-Scholes valuation models:

	Years Ended December 31,					
	2012		2011		2010	
Risk-free interest rates	0.33%	0.83%	0.86%	2.30%	0.80%	2.65%
Dividend yields						
Volatility factor of expected market price	.530	.710	.732	.797	.795	1.036
Weighted-average expected term of option	3.8	5 years	3.7	5 years	3.9	4.9 years
Forfeiture rate						

We estimate the fair value of awards of restricted shares and nonvested shares as being equal to the market value of the common stock on the date of the award. We classify our share-based payments as either liability-classified awards or as equity-classified awards. We remeasure liability-classified awards to fair value at each balance sheet date until the award is settled. We measure equity-classified awards at their grant date fair value and do not subsequently remeasure them. We have classified our share-based payments which are settled in our common stock as equity-classified awards and our share-based payments that are settled in cash as liability-classified awards. Compensation costs related to equity-classified awards generally are equal to the fair value of the award at grant-date amortized over the vesting period of the award. The liability for liability-classified awards generally is equal to the fair value of the award as of the balance sheet date multiplied by the percentage vested at the time. We record the change in the liability amount from one balance sheet date to another to compensation expense.

**(m) Comprehensive Income**

Consolidated comprehensive income consists of consolidated net earnings and foreign currency translation adjustments. We present the calculation of consolidated comprehensive income in the accompanying Consolidated Statements of Comprehensive Income.

**(n) Segment Reporting**

We report our operating segment information in three segments: Recovery Audit Services Americas; Recovery Audit Services Europe / Asia Pacific; and New Services. We include the unallocated portion of corporate selling, general and administrative expenses not specifically attributable to our three segments in Corporate Support. Our business segments reflect the internal reporting that our Chief Executive Officer, who is our chief operating decision maker, uses for the purpose of making decisions about allocating resources and assessing performance. Our management, including our Chief Executive Officer, uses what we internally refer to as Adjusted EBITDA as the primary measure of profit or loss for purposes of assessing the operating performance of all operating segments. We define Adjusted EBITDA as earnings from continuing operations before interest, taxes, depreciation and amortization ( EBITDA ) as adjusted for unusual and other significant items that management views as distorting the operating results of the various segments from period to period.

EBITDA and Adjusted EBITDA are not financial measures determined in accordance with GAAP. Such non-GAAP financial measures do not measure the profit or loss of the reportable segments in accordance with GAAP. Given that we use Adjusted EBITDA as our primary measure of segment performance, GAAP rules on segment reporting require that we include this non-GAAP measure in our discussion of our operating segments. We also must reconcile Adjusted EBITDA to our operating results presented on a GAAP basis. We provide this reconciliation in Note 2 to these consolidated financial statements along with other information about our reportable segments. We do not intend the reconciling items to be, nor should they be, interpreted as non-recurring or extraordinary, or in any manner be deemed as adjustments made in accordance with GAAP. Because Adjusted EBITDA is not a financial measure determined in accordance with GAAP, it may not be comparable to other similarly titled measures of other companies.

**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(o) New Accounting Standards**

No new accounting standards have been issued by the FASB and included in the ASC that PRGX has not yet adopted that we expect will have a significant impact on the Company's financial statements.

**(2) OPERATING SEGMENTS AND RELATED INFORMATION**

We conduct our operations through three reportable segments:

**Recovery Audit Services – Americas** represents recovery audit services (other than Healthcare Claims Recovery Audit services) we provide in the U.S., Canada and Latin America.

**Recovery Audit Services – Europe/Asia-Pacific** represents recovery audit services (other than Healthcare Claims Recovery Audit services) we provide in Europe, Asia and the Pacific region.

**New Services** includes Profit Optimization services (formerly referred to as analytics and advisory services) and Healthcare Claims Recovery Audit services.

We include the unallocated portion of corporate selling, general and administrative expenses not specifically attributable to the three reportable segments in **Corporate Support**.

We evaluate the performance of our operating segments based upon revenue and measures of profit or loss we refer to as EBITDA and Adjusted EBITDA. We define Adjusted EBITDA as earnings from continuing operations before interest and taxes (EBIT), adjusted for depreciation and amortization (EBITDA), and then adjusted for unusual and other significant items that management views as distorting the operating results of the various segments from period to period. Such adjustments include restructuring charges, stock-based compensation, bargain purchase gains, acquisition transaction costs and acquisition obligations classified as compensation, intangible asset impairment charges, certain litigation costs and litigation settlements, severance charges and foreign currency transaction gains and losses on short-term intercompany balances viewed by management as individually or collectively significant. We do not have any inter-segment revenue. Segment information for the years ended December 31, 2012, 2011 and 2010 and segment asset information as of December 31, 2012 and 2011 (in thousands) is as follows:

	Recovery Audit Services Americas	Recovery Audit Services Europe/Asia- Pacific	New Services	Corporate Support	Total
<b>2012</b>					
Revenue	\$ 121,638	\$ 53,783	\$ 33,082	\$	\$ 208,503
Net earnings					\$ 5,392
Income tax expense					1,297
Interest expense, net					966
EBIT	\$ 28,589	\$ 5,035	\$ (3,803)	\$ (22,166)	7,655
Depreciation of property and equipment	4,651	322	2,111		7,084
Amortization of intangible assets	4,355	2,062	807		7,224
EBITDA	37,595	7,419	(885)	(22,166)	21,963

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Foreign currency transaction gains on short-term intercompany balances	(44)	(331)		(2)	(377)
Acquisition obligations classified as compensation			382		382
Transformation severance and related expenses	493	1,156	394	64	2,107
Wage claim costs	577		407		984
Stock-based compensation				6,321	6,321
Adjusted EBITDA	\$ 38,621	\$ 8,244	\$ 298	\$ (15,783)	\$ 31,380

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<b>2012</b>	<b>Recovery Audit Services Americas</b>	<b>Recovery Audit Services Europe/Asia- Pacific</b>	<b>New Services</b>	<b>Corporate Support</b>	<b>Total</b>
Capital expenditures	\$ 5,699	\$ 846	\$ 1,386	\$	\$ 7,931
Allocated assets	\$ 57,722	\$ 17,893	\$ 25,126	\$	\$ 100,741
<b>Unallocated assets:</b>					
Cash and cash equivalents				37,806	37,806
Restricted cash				65	65
Deferred loan costs				193	193
Deferred income taxes				1,604	1,604
Prepaid expenses and other assets				3,177	3,177
<b>Total assets</b>	<b>\$ 57,722</b>	<b>\$ 17,893</b>	<b>\$ 25,126</b>	<b>\$ 42,845</b>	<b>\$ 143,586</b>

<b>2011</b>	<b>Recovery Audit Services Americas</b>	<b>Recovery Audit Services Europe/Asia- Pacific</b>	<b>New Services</b>	<b>Corporate Support</b>	<b>Total</b>
Revenue	\$ 115,807	\$ 61,570	\$ 25,740	\$	\$ 203,117
Net earnings					\$ 2,816
Income tax expense					1,292
Interest expense, net					1,616
EBIT	\$ 26,280	\$ 7,484	\$ (6,951)	\$ (21,089)	5,724
Depreciation of property and equipment	3,491	417	1,493		5,401
Amortization of intangible assets	2,467	1,665	859		4,991
EBITDA	32,238	9,566	(4,599)	(21,089)	16,116
Foreign currency transaction losses on short-term intercompany balances	144	272	1		417
Acquisition transaction costs and acquisition obligations classified as compensation			440	360	800
Transformation severance and related expenses	1,465	566			2,031
Stock-based compensation				5,093	5,093
<b>Adjusted EBITDA</b>	<b>\$ 33,847</b>	<b>\$ 10,404</b>	<b>\$ (4,158)</b>	<b>\$ (15,636)</b>	<b>\$ 24,457</b>
Capital expenditures	\$ 5,459	\$ 1,041	\$ 1,787	\$	\$ 8,287
Allocated assets	\$ 62,702	\$ 20,308	\$ 17,316	\$	\$ 100,326

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Unallocated assets:							
Cash and cash equivalents						20,337	20,337
Restricted cash						64	64
Deferred loan costs						376	376
Deferred income taxes						854	854
Prepaid expenses and other assets						4,456	4,456
Total assets	\$	62,702	\$	20,308	\$	17,316	\$ 26,087 \$ 126,413



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<b>2010</b>	<b>Recovery Audit Services Americas</b>	<b>Recovery Audit Services Europe/Asia- Pacific</b>	<b>New Services</b>	<b>Corporate Support</b>	<b>Total</b>
Revenue	\$ 115,156	\$ 57,590	\$ 11,335	\$	\$ 184,081
Net earnings					\$ 3,253
Income tax expense					1,882
Interest expense, net					1,305
Loss on debt extinguishment					1,381
EBIT	\$ 25,062	\$ 6,478	\$ (6,804)	\$ (16,915)	7,821
Depreciation of property and equipment	3,442	354	1,107		4,903
Amortization of intangible assets	2,427	1,403	301		4,131
EBITDA	30,931	8,235	(5,396)	(16,915)	16,855
Foreign currency transaction (gains) losses on short-term intercompany balances	33	391	(2)		422
Acquisition transaction costs and acquisition obligations classified as compensation			371		371
Stock-based compensation				3,980	3,980
Adjusted EBITDA	\$ 30,964	\$ 8,626	\$ (5,027)	\$ (12,935)	\$ 21,628
Capital expenditures	\$ 5,674	\$ 329	\$ 931	\$	\$ 6,934

The following table presents revenue by country based on the location of clients served (in thousands):

	<b>Years Ended December 31,</b>		
	<b>2012</b>	<b>2011</b>	<b>2010</b>
United States	\$ 124,302	\$ 107,072	\$ 92,574
United Kingdom	30,437	36,123	31,422
Canada	17,007	20,200	22,141
France	11,330	13,425	12,231
Brazil	5,919	5,718	5,128
Mexico	4,877	4,836	3,950
Australia	2,467	1,299	1,690
Sweden	1,753	2,145	1,460
Spain	1,252	1,901	2,065
Czech Republic	1,110	706	654
New Zealand	984	1,111	738
Ireland	954	776	1,024
Other	6,111	7,805	9,004
	\$ 208,503	\$ 203,117	\$ 184,081

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The following table presents long-lived assets by country based on the location of the asset (in thousands):

	December 31,	
	2012	2011
United States	\$ 42,629	\$ 46,083
United Kingdom	8,328	8,792
All Other	1,483	1,073
	\$ 52,440	\$ 55,948

Wal-Mart Stores Inc. (and its affiliated companies) accounted for approximately 10.2% of total revenue in 2011 and 12.1% in 2010. We recorded this revenue primarily in the Recovery Audit Services Americas Segment. No client accounted for 10% or more of total revenue in 2012.

**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(3) EARNINGS PER COMMON SHARE**

The following tables set forth the computations of basic and diluted earnings per common share (in thousands, except per share data).

	Years Ended December 31,		
	2012	2011	2010
<b><u>Basic earnings per common share:</u></b>			
Numerator:			
Net earnings	\$ 5,392	\$ 2,816	\$ 3,253
Denominator:			
Weighted-average common shares outstanding	\$ 25,566	\$ 24,634	\$ 23,906
Basic earnings per common share	\$ 0.21	\$ 0.11	\$ 0.14
<b><u>Diluted earnings per common share:</u></b>			
Numerator:			
Net earnings	\$ 5,392	\$ 2,816	\$ 3,253
Denominator:			
Weighted-average common shares outstanding	\$ 25,566	\$ 24,634	\$ 23,906
Incremental shares from stock-based compensation plans	571	395	238
Denominator for diluted earnings per common share	\$ 26,137	\$ 25,029	\$ 24,144
Diluted earnings per common share	\$ 0.21	\$ 0.11	\$ 0.13

Weighted average shares outstanding excludes anti-dilutive shares underlying options that totaled 1.6 million shares in 2012, 1.5 million shares in 2011 and 1.7 million shares in 2010. The number of common shares we used in the basic and diluted earnings per common share computations include nonvested restricted shares of 0.9 million in 2012, 1.2 million in 2011 and 1.2 million in 2010, and nonvested restricted share units that we consider to be participating securities of 0.2 million in 2012, 0.2 million in 2011 and 0.3 million in 2010.

On December 11, 2012, we closed a public offering of 6,249,234 shares of our common stock, which consisted of 2,500,000 shares sold by us and 3,749,234 shares sold by certain selling shareholders, at a price to the public of \$6.39 per share. The net proceeds to us from the public offering, after deducting underwriting discounts and commissions and offering expenses, were \$14.7 million. We intend to use the net proceeds from the public offering for working capital and general corporate purposes, including potential acquisitions. We did not receive any proceeds from the sale of shares by the selling shareholders. In addition, the underwriters elected to exercise an overallotment option for an additional 687,385 shares, and completed the additional sale on January 8, 2013. The net proceeds to us from the overallotment, after deducting underwriting discounts and commission and offering expenses were \$4.1 million.

**(4) GOODWILL AND INTANGIBLE ASSETS***(a) Goodwill*

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We evaluate the recoverability of goodwill in the fourth quarter of each year or sooner if events or changes in circumstances indicate that the carrying amount may exceed its fair value. These analyses did not result in an impairment charge during the periods presented.

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Goodwill by reportable segments was as follows (in thousands):

	December 31,	
	2012	2011
Recovery Audit Services Americas	\$ 12,177	\$ 12,177
Recovery Audit Services Europe/Asia-Pacific	896	173
New Services	596	596
 Total	 \$ 13,669	 \$ 12,946

We initially recorded goodwill of \$7.8 million in our Recovery Audit Services Americas segment in conjunction with our December 2011 acquisition of Business Strategy, Inc. ( BSI ) (see *Note 12 Business Acquisitions* below). We recorded purchase price adjustments in 2012 of \$0.2 million that reduced the BSI goodwill to \$7.6 million and recorded this change retroactively to 2011. We also recorded additions to goodwill of \$0.7 million and \$0.2 million in our Recovery Audit Services Europe Asia/Pacific segment in 2012 and 2011, respectively, relating to our acquisitions in 2012 of two third-party audit firms to which we had subcontracted a portion of our audit services ( associate migrations ) and our completion of one associate migration in 2011. There were no changes in goodwill in our New Services segment during 2012 and 2011.

**(b) Intangible Assets**

Intangible assets consist principally of amounts we assigned to customer relationships, trademarks, non-compete agreements and trade names in conjunction with business acquisitions. Changes in intangible assets in 2012 related primarily to the completion of two associate migrations, CRC Management Consultants LLP ( CRC ) and QFS Ltd ( QFS ). Changes in intangible assets in 2011 related primarily to our December 2011 BSI acquisition and an associate migration. *Note 12 Business Acquisitions* below includes a more detailed description of the acquisitions in both 2012 and 2011. Intangible assets associated with CRC, QFS and the 2011 associate migration are denominated in British pounds sterling and are subject to movements in foreign currency rates ( FX adjustments ). We present the amounts below in United States dollars utilizing foreign currency exchange rates as of December 31, 2012.

As of January 21, 2010, the Company changed its trade name from PRG-Schultz International, Inc. to PRGX Global, Inc. and is using the previous trade name only in limited circumstances. We intend to maintain the legal rights to the former name but, for accounting purposes, have reclassified the intangible asset associated with this trade name from an indefinite lived intangible asset to one with a definite life and began amortizing the trade name in January 2010.

Amortization expense relating to intangible assets was \$5.4 million in 2012, \$4.6 million in 2011 and \$4.0 million in 2010. As of December 31, 2012 and based on our current amortization methods, we project amortization expense relating to intangible assets for the next five years will be \$4.9 million in 2013, \$3.6 million in 2014, \$2.7 million in 2015, \$1.7 million in 2016 and \$1.4 million in 2017. We generally use accelerated amortization methods for customer relationships and trade names, and straight-line amortization for non-compete agreements.

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Changes in noncurrent intangible assets during 2012 and 2011 were as follows (in thousands):

	Customer Relationships	Trademarks	Non-compete Agreements	Trade Names	Total
<b>Gross carrying amount:</b>					
Balance, January 1, 2011	\$ 36,505	\$ 505	\$ 1,553	\$ 2,865	\$ 41,428
Associate migration			98		98
Acquisition of BSI	2,836	555	650		4,041
FX adjustments and other	(35)	(2)	(8)		(45)
Balance, December 31, 2011	39,306	1,058	2,293	2,865	45,522
Acquisition of CRC			128		128
Acquisition of QFS			43		43
FX adjustments and other	359	23	44		426
Balance, December 31, 2012	\$ 39,665	\$ 1,081	\$ 2,508	\$ 2,865	\$ 46,119
<b>Accumulated amortization:</b>					
Balance, January 1, 2011	\$ (16,609)	\$ (123)	\$ (274)	\$ (567)	\$ (17,573)
Amortization expense	(3,236)	(104)	(519)	(747)	(4,606)
FX adjustments and other	52	3	8		63
Balance, December 31, 2011	(19,793)	(224)	(785)	(1,314)	(22,116)
Amortization expense	(3,692)	(238)	(751)	(713)	(5,394)
FX adjustments and other	(170)	(11)	(29)		(210)
Balance, December 31, 2012	\$ (23,655)	\$ (473)	\$ (1,565)	\$ (2,027)	\$ (27,720)
<b>Net carrying amount:</b>					
Balance, December 31, 2011	\$ 19,513	\$ 834	\$ 1,508	\$ 1,551	\$ 23,406
Balance, December 31, 2012	\$ 16,010	\$ 608	\$ 943	\$ 838	\$ 18,399
Estimated useful life (years)	6 20 years	6 years	1 5 years	4 5 years	

**(5) DEBT**

Long-term debt consisted of the following (in thousands):

	December 31, 2012	December 31, 2011
SunTrust term loan due quarterly through January 2014	\$ 6,000	\$ 9,000

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Less current portion	3,000	3,000
Noncurrent portion	\$ 3,000	\$ 6,000

On January 19, 2010, we entered into a four-year revolving credit and term loan agreement with SunTrust Bank ( SunTrust ). The SunTrust credit facility consists of a \$15.0 million committed revolving credit facility and a \$15.0 million term loan. The SunTrust credit facility is guaranteed by the Company and all of its material domestic subsidiaries and secured by substantially all of the assets of the Company. Availability under the SunTrust revolver is based on eligible accounts receivable and other factors. As of December 31, 2012, availability under the SunTrust revolver was \$8.1 million and we had no outstanding borrowings.

The SunTrust term loan requires quarterly principal payments of \$0.8 million beginning in March 2010, and a final principal payment of \$3.0 million due in January 2014. The loan agreement requires mandatory prepayments with the net cash proceeds from certain asset sales, equity offerings and insurance proceeds received by the Company. In connection with the equity offering (see Note 3, Earnings Per Common Share), we obtained a waiver of the requirement to prepay the loan from SunTrust that enabled us to retain the net proceeds from the offering. The loan agreement also requires an annual additional prepayment contingently payable in April of each year based on excess cash flow ( ECF ) in the prior year if our leverage ratio as defined in the agreement exceeds a certain threshold. Our leverage ratio has remained below the threshold and ECF payments have not been required in any year, and we do not anticipate one being required in 2013.

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Interest on both the revolver and term loan is payable monthly and accrues at an index rate using the one-month LIBOR rate, plus an applicable margin as determined by the loan agreement. The applicable interest rate margin varies from 2.25% per annum to 3.5% per annum, dependent on our consolidated leverage ratio, and is determined in accordance with a pricing grid under the SunTrust loan agreement. The applicable margin was 2.5% and the interest rate was approximately 2.71% at December 31, 2012. We also must pay a commitment fee of 0.5% per annum, payable quarterly, on the unused portion of the \$15.0 million SunTrust revolving credit facility. The weighted-average interest rate on term loan balances outstanding under the SunTrust credit facility during 2012, including fees, was 3.8%.

The SunTrust credit facility includes customary affirmative, negative, and financial covenants binding on the Company, including delivery of financial statements and other reports, maintenance of existence, and transactions with affiliates. The negative covenants limit the ability of the Company, among other things, to incur debt, incur liens, make investments, sell assets, repurchase shares of its capital stock or declare or pay dividends on its capital stock. The financial covenants included in the SunTrust credit facility, among other things, limit the amount of capital expenditures the Company can make, set forth maximum leverage and net funded debt ratios for the Company and a minimum fixed charge coverage ratio, and also require the Company to maintain minimum consolidated earnings before interest, taxes, depreciation and amortization. In addition, the SunTrust credit facility includes customary events of default. The Company was in compliance with the covenants in its SunTrust credit facility as of December 31, 2012.

We used substantially all the funds from the SunTrust term loan to repay in full the principal of \$14.1 million outstanding under a previous term loan. In conjunction with terminating the previous credit facility, we recorded a loss on extinguishment of debt totaling \$1.4 million consisting of the write-off of the unamortized deferred loan costs.

In September 2010 we entered into an amendment of the SunTrust credit facility that lowered the required minimum adjusted EBITDA and fixed charge coverage ratio through December 31, 2010. In October 2010 we entered into an interest rate swap agreement with SunTrust that limits our exposure to increases in the one-month LIBOR rate. In October 2011 we entered into an amendment of the SunTrust credit facility that increased our capital expenditure limits for 2011 and 2012.

***Future Minimum Payments***

Future minimum principal payments of long-term debt as of December 31, 2012 are as follows (in thousands):

<b>Year Ending December 31,</b>	
2013	\$ 3,000
2014	3,000
2015	
2016	
2017	
Thereafter	
	<b>\$ 6,000</b>

**(6) LEASE COMMITMENTS**

PRGX is committed under noncancelable lease arrangements for facilities and equipment. Rent expense, excluding costs associated with the termination of noncancelable lease arrangements, was \$6.2 million in 2012, \$6.7 million in 2011 and \$6.2 million in 2010.

We have subleased approximately 58,000 square feet of our principal executive office space to independent third parties. The sublease rental income we earn is less than the lease payments we make. We also accrue future rental obligations relating to leases for which we no longer are utilizing the office space. At December 31, 2012, our liabilities relating to these lease obligations were \$2.0 million, of which we have included



\$1.1 million in

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Accounts payable and accrued expenses and \$0.9 million in Other long-term liabilities in our Consolidated Balance Sheet. We adjust the fair value of the remaining lease payments, net of sublease income, based on payments we make and sublease income we receive. We include accretion of this liability related to discounting in rent expense.

We have entered into several operating lease agreements that contain provisions for future rent increases, free rent periods or periods in which rent payments are reduced (abated). We charge the total amount of rental payments due over the lease term to rent expense on the straight-line, undiscounted method over the lease terms.

Future minimum lease payments under noncancelable operating leases (both gross and net of any sublease income) are as follows (in thousands):

Year Ending December 31,	Gross	Sublease Income	Net
2013	\$ 8,127	\$ (847)	\$ 7,280
2014	7,375	(863)	6,512
2015	1,590		1,590
2016	971		971
2017	476		476
Thereafter			
<b>Total payments</b>	<b>\$ 18,539</b>	<b>\$ (1,710)</b>	<b>\$ 16,829</b>

**(7) INCOME TAXES**

Earnings (loss) before income taxes relate to the following jurisdictions (in thousands):

	Years Ended December 31,		
	2012	2011	2010
United States	\$ 3,158	\$ (3,182)	\$ (3,189)
Foreign	3,531	7,290	8,324
	<b>\$ 6,689</b>	<b>\$ 4,108</b>	<b>\$ 5,135</b>

The provision for income taxes consists of the following (in thousands):

	Years Ended December 31,		
	2012	2011	2010
Current:			
Federal	\$ 78	\$	\$
State	(30)	79	30
Foreign	2,048	3,364	3,206

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	2,096	3,443	3,236
Deferred:			
Federal		(1,603)	(514)
State		(133)	
Foreign	(799)	(415)	(840)
	(799)	(2,151)	(1,354)
Total	\$ 1,297	\$ 1,292	\$ 1,882

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The significant differences between the U.S. federal statutory tax rate of 34% and the Company's effective income tax expense for earnings (in thousands) are as follows:

	Years Ended December 31,		
	2012	2011	2010
Statutory federal income tax rate	\$ 2,274	\$ 1,397	\$ 1,746
State income taxes, net of federal effect	24	(130)	577
Change in deferred tax asset valuation allowance	(1,883)	(1,910)	(3,254)
Foreign taxes in excess of U.S. statutory rate	486	1,481	2,407
Compensation deduction limitation	265	360	448
Other, net	131	94	(42)
	\$ 1,297	\$ 1,292	\$ 1,882

The tax effects of temporary differences and carry-forwards that give rise to deferred tax assets and liabilities consist of the following (in thousands):

	December 31,	
	2012	2011
Deferred income tax assets:		
Accounts payable and accrued expenses	\$ 2,088	\$ 1,770
Accrued payroll and related expenses	3,902	2,998
Stock-based compensation expense	9,221	8,700
Depreciation of property and equipment	3,746	3,861
Non-compete agreements	27	50
Operating loss carry-forwards of foreign subsidiary	1,501	1,422
Federal operating loss carry-forwards	27,494	26,332
Intangible assets	6,195	11,935
State operating loss carry-forwards	2,648	2,625
Other	3,243	3,630
Gross deferred tax assets	60,065	63,323
Less valuation allowance	48,489	51,630
Gross deferred tax assets net of valuation allowance	11,576	11,693
Deferred income tax liabilities:		
Intangible assets	5,790	7,405
Unbilled receivables and refund liabilities	2,538	1,781
Capitalized software	969	974
Other	675	679
Gross deferred tax liabilities	9,972	10,839
Net deferred tax assets	\$ 1,604	\$ 854

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Our reported effective tax rates on earnings approximated 19.4% in 2012, 31.5% in 2011 and 36.7% in 2010. Reported income tax expense in each year primarily results from taxes on the income of foreign subsidiaries. The effective tax rates generally are less than the expected tax rate primarily due to reductions of the Company's deferred tax asset valuation allowance.

We reduce our deferred tax assets by a valuation allowance if it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences are deductible. In making this determination, we consider all available positive and negative evidence affecting specific deferred tax assets, including our past and anticipated future performance, the reversal of deferred tax liabilities, the length of carry-back and carry-forward periods and the implementation of tax planning strategies.

Objective positive evidence is necessary to support a conclusion that a valuation allowance is not needed for all or a portion of deferred tax assets when significant negative evidence exists. Cumulative tax losses in recent years are the most compelling form of negative evidence considered by management in this determination. As of

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December 31, 2012, management determined that based on all available evidence, a valuation allowance of \$48.5 million is appropriate, representing a decrease of \$3.1 million from the valuation allowance of \$51.6 million recorded as of December 31, 2011.

As of December 31, 2012, we had approximately \$78.6 million of U.S. federal loss carry-forwards available to reduce future U.S. federal taxable income. The U.S. federal loss carry-forwards expire through 2032. As of December 31, 2012, we had approximately \$91.3 million of state loss carry-forwards available to reduce future state taxable income. The state loss carry-forwards expire to varying degrees between 2017 and 2032 and are subject to certain limitations.

Generally, we have not provided deferred taxes on the undistributed earnings of international subsidiaries as we consider these earnings to be permanently reinvested. However, in 2011, we determined that the earnings of our Canadian subsidiary should no longer be considered to be permanently reinvested. This change resulted in earnings of \$4.8 million that we anticipated we would repatriate, and we provided additional deferred taxes of \$0.2 million in 2011 relating to this potential repatriation, representing the estimated withholding tax liability to be due when such amounts are repatriated. In 2012, our Canadian subsidiary generated \$4.3 million of earnings that we anticipated would be repatriated at some future date, and we provided additional deferred taxes of \$0.2 million in 2012 relating to this potential repatriation, which represents the estimated withholding tax liability due if such amounts are repatriated. We did not provide additional incremental U.S. income tax expense on these amounts as the Canadian subsidiary is classified as a branch for U.S. income tax purposes.

On March 17, 2006, the Company experienced an ownership change as defined under Section 382 of the Internal Revenue Code ( IRC ). This ownership change resulted in an annual IRC Section 382 limitation that limits the use of certain tax attribute carry-forwards. Of the \$78.6 million of U.S. federal loss carry-forwards available to the Company, \$17.8 million of the loss carry-forwards are subject to an annual usage limitation of \$1.4 million.

We currently are in the process of determining if we experienced an ownership change subsequent to March 17, 2006, but have not yet completed this analysis. Based on preliminary calculations we have made with the assistance of external advisors, we believe that any additional limitations on the usage of our loss carry-forwards that would be imposed if an additional ownership change has occurred would be minimal. We do not believe that an additional ownership change would have a material adverse impact on our financial position, results of operations or cash flows.

We apply a more-likely-than-not recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. We refer to GAAP for guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. Our policy for recording potential interest and penalties associated with uncertain tax positions is to record such items as a component of earnings before income taxes.

We recorded unrecognized tax benefits of \$2.2 million as of December 31, 2012, a decrease of \$0.4 million over the \$2.6 million recorded at December 31, 2011. We recorded accrued interest and penalties of \$1.4 million as of December 31, 2012, a decrease of \$0.8 million over the \$2.2 million recorded at December 31, 2011. We recognized a reduction of interest expense of \$0.8 million in 2012 and additions to interest expense of \$0.4 million in 2011 related to the liability for unrecognized tax benefits. The decreases in the unrecognized tax benefits and the related accrued interest and penalties in 2012 occurred for several reasons, including the expiration of the statute of limitations for certain of these taxes in several states and in two foreign jurisdictions, completion of an audit by a foreign jurisdiction that resulted in a lower tax assessment than we had estimated, and the imposition of limitations on our potential liability resulting from our beginning the voluntary disclosure agreement process with one state. Due to the complexity of the tax rules underlying these unrecognized tax benefits, and the unclear timing of tax audits, tax agency determinations, and other events, we cannot establish reasonably reliable estimates for the periods in which the cash settlement of these liabilities will occur.

We file U.S., state, and foreign income tax returns in jurisdictions with varying statutes of limitations. As of December 31, 2012, the 2009 through 2011 tax years generally remain subject to examination by federal and most state and foreign tax authorities. The use of net operating losses generated in tax years prior to 2009 may also subject returns for those years to examination.



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**(8) EMPLOYEE BENEFIT PLANS**

We maintain a defined contribution retirement plan in accordance with Section 401(k) of the Internal Revenue Code, which allows eligible participating employees to defer receipt of up to 50% of their annual compensation and contribute such amount to one or more investment funds. We match employee contributions in a discretionary amount to be determined by management and approved by the Board of Directors each plan year up to the lesser of 6% of an employee's annual compensation or \$3,000 per participant. We also may make additional discretionary contributions to the Plan as determined by management and approved by the Board of Directors each plan year. Company matching funds and discretionary contributions vest 100% after three years of service for participants who either had attained three or more years of service or were hired on or after January 1, 2012. For all other participants, company matching funds and discretionary contributions vest at the rate of 20% after two years of service and 100% after three years of service. We contributed approximately \$1.1 million in 2012 and \$1.0 million in 2010 to the Plan. We did not make a contribution in 2011 to the Plan.

**(9) SHAREHOLDER RIGHTS PLAN AND PARTICIPATING PREFERRED STOCK**

On August 1, 2000, the Board authorized a shareholder protection rights plan designed to protect Company shareholders from coercive or unfair takeover techniques through the use of a Shareholder Protection Rights Agreement approved by the Board (the "Rights Plan"). The terms of the Rights Plan, as amended, provide for a dividend of one right (collectively, the "Rights") to purchase a fraction of a share of participating preferred stock for each share owned. This dividend was declared for each share of common stock outstanding at the close of business on August 14, 2000. The Rights, which expire on August 9, 2013, may be exercised only if certain conditions are met, such as the acquisition (or the announcement of a tender offer, the consummation of which would result in the acquisition) of 15% or more of our common stock by a person or affiliated group in a transaction that is not approved by the Board. Issuance of the Rights does not affect our finances, interfere with our operations or business plans, or affect our earnings per share. The dividend was not taxable to the Company or its shareholders and did not change the way in which the Company's shares may be traded.

Effective July 31, 2000, in connection with the Rights Plan, the Board amended the Company's Articles of Incorporation to establish a new series of stock, which is designated as participating preferred stock. The Company's remaining, undesignated preferred stock may be issued at any time or from time to time in one or more series with such designations, powers, preferences, rights, qualifications, limitations and restrictions (including dividend, conversion and voting rights) as may be determined by the Board, without any further votes or action by the shareholders.

**(10) COMMITMENTS AND CONTINGENCIES**

***Legal Proceedings***

On December 16, 2011, an employee of our wholly owned subsidiary PRGX USA, Inc., filed a lawsuit in the U.S. District Court for the District of Minnesota (Civil Action No. 0:11-CV-03631-PJS-FLN) alleging that PRGX USA, Inc. failed to pay overtime wages to the Plaintiff and other similarly situated individuals as required by the Fair Labor Standards Act (FLSA). In this collective action, the Plaintiff sought an unspecified amount of monetary damages and costs, including attorneys' fees. We filed an Answer denying all of the asserted claims on January 31, 2012, and the parties then conducted limited discovery. In August 2012, the parties reached an agreement to settle the case for \$135,000, which includes the plaintiffs' attorney fees, and all of the plaintiffs have approved the settlement. The settlement received court approval on November 19, 2012 and the case has been dismissed.

We are party to a variety of legal proceedings arising in the normal course of business. While the results of these proceedings cannot be predicted with certainty, management believes that the final outcome of these proceedings will not have a material adverse effect on our financial position or results of operations.



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**(11) STOCK-BASED COMPENSATION**

The Company currently has three stock-based compensation plans under which awards have been granted: (1) the Stock Incentive Plan ( SIP ), (2) the 2006 Management Incentive Plan ( 2006 MIP ), and (3) the 2008 Equity Incentive Plan ( 2008 EIP ) (collectively, the Plans ). The Company generally issues authorized but previously unissued shares to satisfy stock option exercises, grants of restricted stock awards and vesting of restricted stock units and settlements of 2006 MIP Performance Units.

**SIP Awards**

The SIP, as amended, authorized the grant of options or other stock-based awards, with respect to up to 1,237,500 shares of the Company s common stock to key employees, directors, consultants and advisors. The majority of options granted pursuant to the SIP had five to seven year terms and vested and became fully exercisable on a ratable basis over one to five years of continued employment or service. The SIP expired in June 2008.

**2008 EIP Awards**

During the first quarter of 2008, the Board of Directors of the Company adopted the 2008 EIP, which was approved by the shareholders at the annual meeting of the shareholders on May 29, 2008. The 2008 EIP authorizes the grant of incentive and non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units and other incentive awards. Two million shares of the Company s common stock initially were reserved for issuance under the 2008 EIP pursuant to award grants to key employees, directors and service providers. The options granted pursuant to the 2008 EIP have seven year terms.

An amendment to the 2008 EIP was adopted by the Company s Board of Directors in April 2010 and approved at the Company s annual meeting of shareholders held on June 15, 2010. This amendment, among other things, increased the number of shares reserved for issuance under the 2008 EIP by 3,400,000 shares to a total of 5,400,000 shares and provides that restricted stock awards and other full value awards will count as 1.41 shares against the available pool of shares under the plan. Another amendment to the 2008 EIP was adopted by the Company s Board of Directors in April 2012 and approved at the Company s annual meeting of shareholders held on June 19, 2012. This amendment increased the number of shares reserved for issuance under the 2008 EIP by 2,200,000 shares to a total of 7,600,000 shares. As of December 31, 2012, there were 2,125,164 shares available for future grants under the 2008 EIP.

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Stock options granted under the 2008 EIP generally have a term of seven years and vest in equal annual increments over the vesting period, which typically is three years for employees and one year for directors. The following table summarizes stock option grants during the years ended December 31, 2012, 2011 and 2010:

Grantee Type	# of Options Granted	Vesting Period	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value
<b>2012</b>				
Director group	56,261	1 year or less	\$ 7.55	\$ 3.89
Director	8,546	3 years	7.72	4.25
Employee group	597,250	3 years	7.54	4.12
Employee inducement	45,000	3 years (1)	8.54	4.58
<b>2011</b>				
Director group	65,801	1 year or less	\$ 7.23	\$ 4.06
Director group	16,237	3 years	6.32	3.98
Employee group	140,000	2 years	6.09	3.72
Employee group	475,064	3 years	7.38	4.33
Employee inducement	200,000	3-4 years (2)	5.37	3.13
<b>2010</b>				
Director group	51,276	1 year or less	\$ 4.20	\$ 2.53
Director	8,546	3 years	5.39	4.00
Employee group	649,010	3 years	4.14	2.68

- (1) The Company granted non-qualified stock options outside its existing stock-based compensation plans in the third quarter of 2012 to one employee in connection with the employee joining the company.
- (2) The Company granted non-qualified stock options outside its existing stock-based compensation plans in the fourth quarter of 2011 to three employees in connection with their joining the company, which included 100,000 performance-based options. These options were forfeited in 2012.

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## PRGX GLOBAL, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Nonvested stock awards, including both restricted stock and restricted stock units, generally are nontransferable until vesting and the holders are entitled to receive dividends with respect to the nonvested shares. Prior to vesting, the grantees of restricted stock are entitled to vote the shares, but the grantees of restricted stock units are not entitled to vote the shares. Generally, nonvested stock awards vest in equal annual increments over the vesting period, which typically is three years for employees and one year for directors. The following table summarizes nonvested stock awards (restricted stock and restricted stock units) grants during the years ended December 31, 2012, 2011 and 2010:

Grantee Type	# of Shares Granted	Vesting Period	Weighted Average Grant Date Fair Value
<b>2012</b>			
Director group	56,261	1 year or less	\$ 7.55
Director	8,546	3 years	7.72
Employee group	426,286	3 years	7.55
Employee inducement	45,000	3 years (1)	8.54
<b>2011</b>			
Director group	65,801	1 year or less	\$ 7.23
Director group	17,237	3 years	6.34
Employee group	60,000	2 years	6.09
Employee group	455,064	3 years	7.41
Employee inducement	120,000	3-4 years (2)	5.66
<b>2010</b>			
Director group	51,276	1 year or less	\$ 4.20
Director	8,546	3 years	5.39
Employee group	600,010	3 years	4.02

(1) The Company granted nonvested stock awards (restricted stock) outside its existing stock-based compensation plans in the third quarter of 2012 to one employee in connection with the employee joining the company.

The Company granted performance-based nonvested stock awards (restricted stock) outside its existing stock-based compensation plans in the fourth quarter of 2011 to two employees in connection with their joining the company. These restricted stock awards were forfeited in 2012.

A summary of option activity as of December 31, 2012, and changes during the year then ended is presented below:

Options	Shares	Weighted-Average Exercise Price (Per Share)	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value (\$ 000 s)
Outstanding at January 1, 2012	2,860,890	\$ 6.61		
Granted	707,057	7.60		
Exercised	(141,849)	3.93		\$ 467
Forfeited	(411,938)	6.66		
Expired	(30,000)	31.60		

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Outstanding at December 31, 2012	2,984,160	\$ 6.70	3.33 years	\$ 3,147
Exercisable at December 31, 2012	1,691,200	\$ 6.78	1.53 years	\$ 2,347

The weighted-average grant date fair value of options granted was \$4.13 per share in 2012, \$3.94 per share in 2011 and \$2.69 per share in 2010. The total intrinsic value of options exercised was \$0.5 million in 2012, \$0.4 million in 2011 and less than \$0.1 million in 2010.

**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

A summary of nonvested stock awards (restricted stock and restricted stock units) activity as of December 31, 2012, and changes during the year then ended is presented below:

		<b>Weighted Average Grant Date Fair Value (Per Share)</b>
<b>Nonvested Stock</b>	<b>Shares</b>	
Nonvested at January 1, 2012	1,418,494	\$ 5.37
Granted	536,093	7.64
Vested	(685,740)	5.16
Forfeited	(200,839)	5.93
<b>Nonvested at December 31, 2012</b>	<b>1,068,008</b>	<b>\$ 6.54</b>

The weighted-average grant date fair value of nonvested stock awards (restricted stock and restricted stock units) granted was \$7.64 per share in 2012, \$6.96 per share in 2011 and \$4.05 per share in 2010. The total vest date fair value of stock awards vested during the year was \$4.9 million in 2012, \$3.6 million in 2011, and \$1.5 million in 2010.

**2006 MIP Performance Units**

At the annual meeting of shareholders held on August 11, 2006, the shareholders of the Company approved a proposal granting authorization to issue up to 2.1 million shares of the Company's common stock under the 2006 MIP. At Performance Unit settlement dates, participants were issued that number of shares of Company common stock equal to 60% of the number of Performance Units being settled, and were paid in cash an amount equal to 40% of the fair market value of that number of shares of common stock equal to the number of Performance Units being settled. Prior to 2012, Performance Units were only granted in 2006 and 2007, and the last of such units were settled in May 2011. No Performance Units were outstanding as of December 31, 2011.

On June 19, 2012, seven senior officers of the Company were granted 154,264 Performance Units under the 2006 MIP, comprising all remaining available awards under the plan. The awards had an aggregate grant date fair value of \$1.2 million and vest ratably over three years. On vesting, the Performance Units will be settled by the issuance of Company common stock equal to 60% of the number of Performance Units being settled and the payment of cash in an amount equal to 40% of the fair market value of that number of shares of common stock equal to the number of Performance Units being settled.

All Performance Units must be settled before April 30, 2016. We recognized compensation expense of \$0.2 million in 2012 and less than \$0.1 million in both 2011 and 2010 related to these 2006 MIP Performance Unit awards. We determined the amount of compensation expense recognized on the assumption that none of the Performance Unit awards would be forfeited.

There was no settlement of Performance Units during 2012. During 2011, one current executive officer settled 44,831 Performance Units, resulting in the issuance of 26,898 shares of common stock and a cash payment of \$0.1 million. During 2010, three current and former executive officers settled an aggregate of 224,158 Performance Units resulting in the issuance of 134,490 shares of common stock and cash payments totaling \$0.6 million.

Stock-based compensation charges aggregated \$6.3 million in 2012, \$5.1 million in 2011 and \$4.0 million in 2010. We include these charges in Selling, general and administrative expenses in the accompanying Consolidated Statements of Income. As of December 31, 2012, there was \$8.7 million of unrecognized stock-based compensation expense related to stock options and nonvested stock which we expect to be recognized over a weighted average period of 1.60 years.



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**PRGX GLOBAL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(12) BUSINESS ACQUISITIONS**

We completed several acquisitions since 2010 that we describe below. Generally, we acquire businesses that we believe will provide a strategic fit for our existing operations, cost savings and revenue synergies, or enable us to expand our capabilities in our New Services segment.

We allocate the total purchase price in a business acquisition to the fair value of identified assets acquired and liabilities assumed based on the fair values at the acquisition date, and record amounts exceeding the fair values as goodwill. If the fair value of the assets acquired exceeds the purchase price, we record this excess as a gain on bargain purchase. We determine the estimated fair values of intangible assets acquired using our estimates of future discounted cash flows to be generated by the acquired business over the estimated duration of those cash flows. We base the estimated cash flows on our projections of future revenue, cost of revenue, capital expenditures, working capital needs and tax rates. We estimate the duration of the cash flows based on the projected useful life of the assets and business acquired. We determine the discount rate based on specific business risk, cost of capital and other factors.

***Etesius Limited***

In February 2010, the Company's UK subsidiary acquired all the issued and outstanding capital stock of Etesius Limited ( Etesius ), a privately-held European provider of purchasing and payables technologies and spend analytics based in Chelmsford, United Kingdom. We have included the results of operations of Etesius in our New Services segment results of operations since the acquisition date. We intend for Etesius to expand our capabilities in our Profit Optimization services business.

The financial terms of the Etesius share purchase agreement ( SPA ) required an initial payment to the Etesius shareholders of \$2.8 million and a \$0.3 million payment for obligations on behalf of Etesius shareholders which resulted in a total estimated purchase price value of approximately \$3.1 million.

The SPA requires deferred payments of \$1.2 million over four years from the date of the SPA to certain selling shareholders who are now our employees. The SPA also provides for potential additional variable payments ( earn-out ) to these selling shareholders/employees over the same four-year period based on the financial performance of certain of the Company's services lines, up to a maximum of \$3.8 million. Because we will not be obligated to make the deferred and earn-out payments upon the termination of employment of these employees under certain circumstances, we have recognized these payments as compensation expense as earned. From the acquisition date to December 31, 2012, we paid \$0.2 million of the deferred payments. An additional \$1.0 million will be due through February 2014 unless there is a termination of employment of these employees under certain circumstances. We currently estimate that we will not pay any variable consideration relating to these provisions.

***TJG Holdings LLC***

In November 2010, we acquired the business and certain assets of TJG Holdings LLC ( TJG ), a privately-held provider of finance and procurement operations improvement services based in Chicago, Illinois. We have included the results of operations of TJG in our New Services segment results of operations since the acquisition date. We intend for the TJG acquisition to allow us to expand our Profit Optimization services business. We recorded goodwill in connection with this acquisition, representing the value of the assembled workforce, including a management team with deep industry knowledge. This goodwill is deductible for tax purposes.

The financial terms of the TJG Asset Purchase Agreement required an initial payment to the TJG owners of \$2.3 million. Additional variable consideration ( earn-out ) may also be due based on the operating results generated by the acquired business over the next two years subject to a maximum of \$1.9 million. We recorded an additional \$1.4 million payable based on management's estimate of the fair value of the earn-out liability. We calculated the earn-out liability based on estimated future discounted cash flows to be generated by the acquired business over a two year period. We determined the discount rate based on specific business risk, cost of capital and other factors. The total estimated purchase price was valued at approximately \$3.7 million. From the acquisition date to December 31, 2012, we paid \$1.8 million of the earn-out and recorded accretion and other adjustments of the liability of \$0.5 million, resulting in an earn-out payable of less than \$0.1 million as of December 31, 2012.





**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****Associate Migrations**

During 2012, we acquired the assets of several third-party audit firms to which we had subcontracted a portion of our audit services in our Recovery Audit Services Europe/Asia-Pacific segment. We refer to the subcontractors as associates, and to the acquisitions as associate migrations. We generally transfer all of the employees of the associate entity to PRGX, and continue to service the related clients with the same personnel after the associate migration as were providing services prior to the associate migration. We intend for the associate migrations to provide more standardization and centralization of our audit procedures, thereby increasing client service while also decreasing costs. Generally, revenue remains unchanged as a result of an associate migration, and expenses change from a fixed percentage of revenue to a variable amount based on employee and related costs. These associate migrations included CRC Management Consultants LLP ( CRC ) in January 2012 for a purchase price valued at \$1.0 million; QFS Ltd ( QFS ) in June 2012 for a purchase price valued at \$0.4 million; and Nordic Profit Provider AB ( NPP ) in November 2012 for a purchase price valued at \$0.1 million. The allocation of the aggregate fair values of the assets acquired and purchase price for these associate migrations is summarized as follows (in thousands):

Fair values of net assets acquired:	
Equipment	\$ 10
Intangible assets, primarily non-compete agreements	171
Working capital, including work in progress	666
Goodwill	695
Fair value of net assets acquired	\$ 1,542
Fair value of purchase price	\$ 1,542

**Business Strategy, Inc.**

In December 2011, we acquired Business Strategy, Inc. and substantially all of the assets of an affiliated company (collectively BSI ), based in Grand Rapids, Michigan, for a purchase price valued at \$11.9 million. BSI was a provider of recovery audit and related procure-to-pay process improvement services for commercial clients, and a provider of customized software solutions and outsourcing solutions to improve back office payment processes. We have included the results of operations of Business Strategy, Inc. in our Recovery Audit Services Americas segment and the results of operations of the affiliated company in our New Services segment results of operations since the acquisition date. These amounts aggregated \$0.8 million of revenue and \$0.1 million of net earnings in 2011 and \$10.9 million of revenue and \$1.5 million of net earnings in 2012. We intend for the BSI acquisition to allow us to expand our commercial recovery audit capabilities and to expand the services we offer to our clients.

The purchase price included an initial cash payment of \$2.8 million and 640,614 shares of our common stock having a value of \$3.7 million. An additional payment of approximately \$0.8 million was due and paid in the first half of 2012 for working capital received in excess of a specified minimum level. Additional variable consideration of up to \$5.5 million, payable via a combination of cash and shares of our common stock, may be due based on the performance of the acquired businesses over a two-year period from the date of acquisition. We may also be required to pay additional consideration of up to \$8.0 million, payable in cash over a period of two years, based on certain net cash fee receipts from a particular recovery audit claim at a specific client. We recorded an additional \$4.9 million payable based on management's estimate of the fair value of the variable consideration payable. We adjusted the \$12.2 million initial estimates of the fair value of the assets and liabilities in 2012, resulting in reductions to goodwill of \$0.2 million, and the fair value of the purchase price of \$0.2 million, and recorded this change retroactively to 2011.

**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The final allocation of the fair values of the assets acquired and purchase price is summarized as follows (in thousands):

	<b>Final Allocation</b>
Fair values of net assets acquired:	
Equipment	\$ 70
Intangible assets, primarily customer relationships	4,041
Working capital, including work in progress	1,967
Deferred tax liabilities	(1,736)
Goodwill	7,577
<b>Fair value of net assets acquired</b>	<b>\$ 11,919</b>
Fair value of purchase price	\$ 11,919

From the acquisition date to December 31, 2012, we paid \$0.7 million of deferred consideration, \$0.4 million of the earn-out liability and recorded accretion and other adjustments of the earn-out liability of \$0.8 million, resulting in an earn-out payable of \$4.9 million as of December 31, 2012.

The following unaudited pro forma condensed financial information presents the combined results of operations of the Company, BSI, CRC, QFS, and NPP as if the acquisitions had occurred as of January 1, 2011. The unaudited pro forma financial information is not indicative of, nor does it purport to project, the future financial position or operating results of the Company. Pro forma adjustments included in these amounts consist primarily of amortization expense associated with the intangible assets recorded in the allocation of the purchase price. The unaudited pro forma financial information excludes acquisition and integration costs and does not give effect to any estimated and potential cost savings or other operating efficiencies that could result from the acquisition.

	<b>Year Ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
Revenue	\$ 208,503	\$ 210,073
Net earnings	\$ 5,913	\$ 4,341

**Table of Contents****PRGX GLOBAL, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****(13) QUARTERLY RESULTS****(13) QUARTERLY RESULTS (UNAUDITED)**

The following tables set forth certain unaudited condensed quarterly financial data for each of the last eight quarters during our fiscal years ended December 31, 2012 and 2011. We have derived the information from unaudited Condensed Consolidated Financial Statements that, in the opinion of management, reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of such quarterly information. The operating results for any quarter are not necessarily indicative of the results to be expected for any future period.

	Mar. 31	2012 Quarter Ended			Mar. 31	2011 Quarter Ended		
		June 30	Sept. 30	Dec. 31		June 30	Sept. 30	Dec. 31
	(In thousands, except per share data)							
Revenue	\$ 51,649	\$ 51,658	\$ 52,087	\$ 53,109	\$ 50,718	\$ 50,704	\$ 51,751	\$ 49,944
Operating expenses:								
Cost of revenue	34,218	33,312	32,461	34,399	34,594	34,523	34,125	34,240
Selling, general and administrative expenses	12,637	12,696	13,242	13,952	12,430	12,297	12,417	11,958
Depreciation of property and equipment	1,513	1,579	1,716	2,276	1,181	1,214	1,464	1,542
Amortization of intangible assets	2,327	1,459	1,431	2,007	1,121	1,129	1,277	1,464
Total operating expenses	50,695	49,046	48,850	52,634	49,326	49,163	49,283	49,204
Operating income	954	2,612	3,237	475	1,392	1,541	2,468	740
Foreign currency transaction (gains) losses on short-term intercompany balances	(339)	497	(348)	(187)	(448)	(431)	1,055	241
Interest expense (income), net	504	529	515	(582)	347	478	398	393
Earnings before income taxes	789	1,586	3,070	1,244	1,493	1,494	1,015	106
Income tax expense (benefit)	497	584	505	(289)	1,121	784	593	(1,206)
Net earnings	\$ 292	\$ 1,002	\$ 2,565	\$ 1,533	\$ 372	\$ 710	\$ 422	\$ 1,312
Basic earnings per common share (1)	\$ 0.01	\$ 0.04	\$ 0.10	\$ 0.06	\$ 0.02	\$ 0.03	\$ 0.02	\$ 0.05
Diluted earnings per common share (1)	\$ 0.01	\$ 0.04	\$ 0.10	\$ 0.06	\$ 0.02	\$ 0.03	\$ 0.02	\$ 0.05

(1) We calculate each quarter as a discrete period; the sum of the four quarters may not equal the calculated full-year amount. In the fourth quarter of 2012, we reduced our tax expense by \$0.4 million and our interest expense by \$0.8 million to reflect adjustments to our estimates for uncertain tax positions. We adjusted our estimates for several reasons, including the expiration of the statute of limitations for certain of these taxes in several states and in two foreign jurisdictions, completion of an audit by a foreign jurisdiction that resulted in a lower tax

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assessment than we had estimated, and the imposition of limitations on our potential liability resulting from our beginning the voluntary disclosure agreement process with one state.

In the fourth quarter of 2011, management determined that a valuation allowance was no longer required against the deferred tax assets for one of the Company's foreign subsidiaries given its return to profitability and future projected profitability. This adjustment resulted in a \$0.5 million income tax benefit in the fourth quarter of 2011. Also in the fourth quarter of 2011, management recorded the initial purchase accounting entries for the December 2011 acquisition of Business Strategy, Inc. As a part of this process, we recorded a \$1.7 million reduction in the deferred tax asset valuation allowance that resulted from the deferred tax liabilities that we recorded relating to the acquisition. This reduction was accounted for as an income tax benefit in the fourth quarter of 2011.

As part of an ongoing Canadian tax audit, we continue to defend our tax position related to the valuation of an intercompany transaction. We recognized \$0.6 million of additional tax expense in the fourth quarter of 2011 to reflect our estimate of the potential tax due based on our continuing discussions with the Canadian tax authorities.

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**PRGX GLOBAL, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(14) SUBSEQUENT EVENTS**

In connection with the common stock offering we completed on December 11, 2012, the underwriters elected to exercise an overallotment option for an additional 687,385 shares, and completed the additional sale on January 8, 2013. The net proceeds to us from the overallotment, after deducting underwriting discounts and commission and offering expenses were \$4.1 million.

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**ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None

**ITEM 9A. Controls and Procedures**

Evaluation of Disclosure Controls and Procedures

The Company carried out an evaluation, under the supervision and with the participation of its management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in the Exchange Act Rule 13a-15(e)) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective as of December 31, 2012.

Management's Annual Report on Internal Control Over Financial Reporting

The Company's management is responsible for establishing and maintaining an adequate system of internal control over financial reporting, as defined in the Exchange Act Rule 13a-15(f). Our internal control system is designed to provide reasonable assurance regarding the preparation and fair presentation of financial statements for external purposes in accordance with generally accepted accounting principles. All internal control systems, no matter how well designed, have inherent limitations and can provide only reasonable assurance that the objectives of the internal control system are met. Under the supervision and with the participation of the Company's management, including the Company's President and Chief Executive Officer along with the Company's Chief Financial Officer and Treasurer, the Company conducted an assessment of the effectiveness of internal control over financial reporting based on the framework in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on the assessment, management concluded that, as of December 31, 2012, the Company's internal control over financial reporting is effective. The Company's internal control over financial reporting as of December 31, 2012 has been audited by BDO USA, LLP, an independent registered public accounting firm, as stated in their report which is included herein, which expresses an unqualified opinion on the effectiveness of the Company's internal control over financial reporting as of December 31, 2012.

There was no change in the Company's internal control over financial reporting that occurred during the Company's most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. Management's report shall not be deemed filed for purposes of Section 18 of the Exchange Act.

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders

PRGX Global, Inc.

Atlanta, Georgia

We have audited PRGX Global, Inc. and subsidiaries (the Company) internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The Company's management is responsible 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 Item 9A, "Management's Annual Report on Internal Control Over Financial Reporting". Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit 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 audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.



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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 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 or procedures may deteriorate.

In our opinion, PRGX Global, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2012 and our report dated March 13, 2013 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Atlanta, Georgia

March 13, 2013

**ITEM 9B. Other Information.**

None.



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**PART III**

**ITEM 10. Directors, Executive Officers and Corporate Governance**

Except as set forth below, the information required by Item 10 of this Form 10-K is incorporated herein by reference to the information contained in the sections captioned Proposal I: Election of Directors , Information about the Board of Directors and Committees of the Board of Directors , Executive Officers and Section 16(a) Beneficial Ownership Reporting Compliance of our definitive proxy statement (the Proxy Statement ) for the 2013 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission pursuant to Regulation 14A under the Securities and Exchange Act of 1934, as amended (the Exchange Act ).

We have undertaken to provide to any person without charge, upon request, a copy of our code of ethics applicable to our chief executive officer and senior financial officers. You may obtain a copy of this code of ethics free of charge from our website, [www.prgx.com](http://www.prgx.com).

**ITEM 11. Executive Compensation**

The information required by Item 11 of this Form 10-K is incorporated by reference to the information contained in the sections captioned Executive Compensation , Information about the Board of Directors and Committees of the Board of Directors , and Report of the Compensation Committee of the Proxy Statement.

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**ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

Except as set forth below, the information required by Item 12 of this Form 10-K is incorporated by reference to the information contained in the section captioned "Ownership of Directors, Principal Shareholders and Certain Executive Officers" of the Proxy Statement.

**Securities Authorized for Issuance Under Equity Compensation Plans**

The Company currently has three stock-based compensation plans under which awards have been granted: (1) the Stock Incentive Plan ( "SIP" ), (2) the 2006 Management Incentive Plan ( "2006 MIP" ), and (3) the 2008 Equity Incentive Plan ( "2008 EIP" ). The SIP, as amended, authorized the grant of options or other stock-based awards, with respect to up to 1,237,500 shares of the Company's common stock to key employees, directors, consultants and advisors. The SIP expired in June 2008.

At the annual meeting of shareholders held on August 11, 2006, the shareholders of the Company approved a proposal granting authorization to issue up to 2.1 million shares of the Company's common stock under the 2006 MIP. At Performance Unit settlement dates (which varied), participants were paid in common stock and in cash. Participants received a number of shares of Company common stock equal to 60% of the number of Performance Units being paid out, plus a cash payment equal to 40% of the fair market value of that number of shares of common stock equal to the number of Performance Units being paid out. The awards were 50% vested at the award date and the remainder of the awards vested ratably over approximately the following eighteen months. The awards contain certain anti-dilution and change of control provisions. Also, the number of Performance Units awarded were automatically adjusted on a pro-rata basis upon the conversion into common stock of any of the Company's senior convertible notes or Series A convertible preferred stock.

During the first quarter of 2008, the Board of Directors of the Company adopted the 2008 EIP, which was approved by the shareholders at the annual meeting of the shareholders on May 29, 2008. The 2008 EIP authorizes the grant of incentive and non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units and other incentive awards. Two million shares of the Company's common stock initially were reserved for issuance under the 2008 EIP pursuant to award grants to key employees, directors and service providers.

An amendment to the 2008 EIP was adopted by the Company's Board of Directors in April 2010 and approved at the Company's annual meeting of shareholders held on June 15, 2010. The amendment, among other things, increased the number of shares reserved for issuance under the 2008 EIP by 3,400,000 shares to a total of 5,400,000 shares and provided that restricted stock awards and other full value awards would count as 1.41 shares against the available pool of shares under the plan.

An amendment to the 2008 EIP was adopted by the Company's Board of Directors in April 2012 and approved at the Company's annual meeting of shareholders held on June 19, 2012. This amendment increased the number of shares reserved for issuance under the 2008 EIP by 2,200,000 shares to a total of 7,600,000 shares.

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The following table presents certain information with respect to compensation plans under which equity securities of the registrant were authorized for issuance as of December 31, 2012:

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders:			
Stock Incentive Plan	452,955	\$ 11.24	
2008 Equity Incentive Plan	2,217,686	6.12	2,125,164
Share awards (1)	92,558		
Equity compensation plans not approved by security holders (2), (3)	313,519	4.28	
Total	3,076,718	\$ 6.70	2,125,164

- (1) Amounts presented represent 60% of Performance Unit awards under the Company's 2006 Management Incentive Plan. Performance Unit awards are required to be settled 60% in common stock and 40% in cash.
- (2) Inducement Option Grant during the first quarter of 2009, in connection with his joining the Company as its President and Chief Executive Officer, the Company made inducement grants outside its existing stock-based compensation plans to Mr. Romil Bahl. Mr. Bahl received an option to purchase 296,296 shares of the common stock of the Company and had exercised options to purchase 27,777 shares through December 31, 2012.
- (3) Inducement Option Grant during the third quarter of 2012, in connection with an employee joining the Company in a senior leadership position, the Company made an inducement grant outside its existing stock-based compensation plans to the executive. The executive received an option to purchase 45,000 shares of the common stock of the Company.

**ITEM 13. Certain Relationships and Related Transactions, and Director Independence**

The information required by Item 13 of this Form 10-K is incorporated by reference to the information contained in the sections captioned Information about the Board of Directors and Committees of the Board of Directors, Executive Compensation, Employment Agreements and Certain Transactions of the Proxy Statement.

**ITEM 14. Principal Accountants Fees and Services**

The information required by Item 14 of this Form 10-K is incorporated by reference to the information contained in the sections captioned Principal Accountants Fees and Services of the Proxy Statement.

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**PART IV**

**ITEM 15. Exhibits, Financial Statement Schedules**

(a) Documents filed as part of the report

(1) Consolidated Financial Statements:

For the following consolidated financial information included herein, see Index on Page 39.

<u>Report of Independent Registered Public Accounting Firm</u>	<b>Page</b>
<u>Consolidated Statements of Income for the Years ended December 31, 2012, 2011, and 2010</u>	40
<u>Consolidated Statements of Comprehensive Income for the Years ended December 31, 2012, 2011, and 2010</u>	41
<u>Consolidated Balance Sheets as of December 31, 2012 and 2011</u>	41
<u>Consolidated Statements of Shareholders' Equity for the Years ended December 31, 2012, 2011, and 2010</u>	42
<u>Consolidated Statements of Cash Flows for the Years ended December 31, 2012, 2011, and 2010</u>	43
<u>Notes to Consolidated Financial Statements</u>	44
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(2) Financial Statement Schedule:

<u>Schedule II Valuation and Qualifying Accounts</u>	S-1
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(3) Exhibits

Exhibit

Number

Description

2.1	Share Purchase Agreement dated February 28, 2010 by and between PRGX U.K. Limited and Sajid Ghani and Others (incorporated by reference to Exhibit 2.1 to the Registrant's Form 10-K filed on March 29, 2010).
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- 2.2 Acquisition Agreement dated December 1, 2011, among PRGX Global, Inc., PRGX Commercial LLC, Business Strategy, Inc., Strategic Document Solutions, LLC, DD&C Investments, L.L.C., Charles Fayon, Daniel Geelhoed and Dennis VanDyke. (incorporated by reference to Exhibit 2.1 to the Registrant's Form 8-K filed on December 2, 2011).
- 3.1 Restated Articles of Incorporation of the Registrant, as amended and corrected through August 11, 2006 (restated solely for the purpose of filing with the Commission) (incorporated by reference to Exhibit 3.1 to the Registrant's Form 8-K filed on August 17, 2006).
  - 3.1.1 Articles of Amendment of the Registrant effective January 20, 2010 (incorporated by reference to Exhibit 3.1 to the Registrant's Form 8-K filed on January 25, 2010).
- 3.2 Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Form 8-K filed on December 11, 2007).
- 4.1 Specimen Common Stock Certificate (incorporated by reference to Exhibit 4.1 to the Registrant's Form 10-K for the year ended December 31, 2001).
- 4.2 See Restated Articles of Incorporation and Bylaws of the Registrant, filed as Exhibits 3.1 and 3.2, respectively.
- 4.3 Shareholder Protection Rights Agreement, dated as of August 9, 2000, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.1 to the Registrant's Form 8-K filed on August 9, 2000).
- 4.3.1 First Amendment to Shareholder Protection Rights Agreement, dated as of March 12, 2002, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.3 to the Registrant's Form 10-Q for the quarterly period ended June 30, 2002).

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4.3.2	Second Amendment to Shareholder Protection Rights Agreement, effective as of August 16, 2002, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.3 to the Registrant's Form 10-Q for the quarterly period ended September 30, 2002).
4.3.3	Third Amendment to Shareholder Protection Rights Agreement, effective as of November 7, 2005, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.1 to the Registrant's Form 8-K filed on November 14, 2005).
4.3.4	Fourth Amendment to Shareholder Protection Rights Agreement, effective as of November 14, 2005, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.1 to the Registrant's Form 8-K filed on November 30, 2005).
4.3.5	Fifth Amendment to Shareholder Protection Rights Agreement, effective as of March 15, 2006, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.9 to the Registrant's Form 10-K for the year ended December 31, 2005).
4.3.6	Sixth Amendment to Shareholder Protection Rights Agreement, effective as of September 17, 2007, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.1 to the Registrant's Form 8-K filed on September 21, 2007).
4.3.7	Seventh Amendment to Shareholder Protection Rights Agreement, effective as of August 9, 2010, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.1 to the Registrant's Form 8-K filed on August 9, 2010).
4.3.8	Eighth Amendment to Shareholder Protection Rights Agreement, effective as of August 4, 2011, between the Registrant and Rights Agent (incorporated by reference to Exhibit 10.1 to the Registrant's Form 10-Q for the quarterly period ended June 30, 2011).
4.3.9	Ninth Amendment to Shareholder Protection Rights Agreement, effective as of August 2, 2012, between the Registrant and Rights Agent (incorporated by reference to Exhibit 4.3.9 to the Registrant's Form 10-Q for the quarterly period ended June 30, 2012).
+10.1	1996 Stock Option Plan, dated as of January 25, 1996, together with Forms of Non-qualified Stock Option Agreement (incorporated by reference to Exhibit 10.2 to the Registrant's March 26, 1996 Registration Statement No. 333-1086 on Form S-1).
+10.2	Form of Indemnification Agreement between the Registrant and Directors and certain officers, including named executive officers, of the Registrant (incorporated by reference to Exhibit 10.4 to the Registrant's Form 10-K for the year ended December 31, 2003).
+10.3	Form of the Registrant's Non-Qualified Stock Option Agreement (incorporated by reference to Exhibit 10.2 to the Registrant's Form 10-Q for the quarterly period ended June 30, 2001).
10.4	Noncompetition, Nonsolicitation and Confidentiality Agreement among The Profit Recovery Group International, Inc., Howard Schultz & Associates International, Inc., Howard Schultz, Andrew Schultz and certain trusts, dated January 24, 2002 (incorporated by reference to Exhibit 10.34 to the Registrant's Form 10-K for the year ended December 31, 2001).
10.5	Office Lease Agreement between Galleria 600, LLC and PRG-Schultz International, Inc. (incorporated by reference to Exhibit 10.43 to the Registrant's Form 10-K for the year ended December 31, 2001).
10.5.1	First Amendment to Office Lease Agreement between Galleria 600, LLC and PRG-Schultz International, Inc. (incorporated by reference to Exhibit 10.65 to the Registrant's Form 10-K for the year ended December 31, 2002).
+10.6	Amended Stock Incentive Plan (incorporated by reference to Exhibit 10.3 to the Registrant's Form 10-Q for the quarterly period ended June 30, 2002).
+10.7	Amended HSA-Texas Stock Option Plan (incorporated by reference to Exhibit 10.4 to the Registrant's Form 10-Q for the quarterly period ended June 30, 2002).
+10.9	Form of Non-employee Director Option Agreement (incorporated by reference to Exhibit 99.1 to the Registrant's Report on Form 8-K filed on February 11, 2005).
+10.22	Amended and Restated 2006 Management Incentive Plan (incorporated by reference to Exhibit 10.1 to the Registrant's Form 10-Q for the quarter ended September 30, 2006).
+10.22.1	Form of Performance Unit Agreement under 2006 Amended and Restated Management Incentive Plan (incorporated by reference to Exhibit 10.2 to the Registrant's Form 8-K filed on June 22, 2012).
+10.24	Form of Non-Employee Director Stock Option Agreement (incorporated by reference to Exhibit 10.1 to the Registrant's Form 8-K filed on September 18, 2007).



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+10.26.1	PRGX Global, Inc. 2008 Equity Incentive Plan, as Amended and Restated Effective April 23, 2012 (incorporated by reference to Exhibit 10.1 to the Registrant's Form 8-K filed on June 22, 2012).
+10.26.2	Form of Restricted Stock Agreement for Non-Employee Directors (incorporated by reference to Exhibit 10.2 to the Registrant's Form 8-K filed on June 4, 2008).
+10.26.3	Form of Non-Qualified Stock Option Agreement for Non-Employee Directors (incorporated by reference to Exhibit 10.3 to the Registrant's Form 8-K filed on June 4, 2008).
+10.27	Employment Agreement dated January 8, 2009, by and between Mr. Romil Bahl and the Registrant (incorporated by reference to Exhibit 10.1 to the Registrant's Form 8-K filed on January 14, 2009).
+10.27.1	Form of Nonqualified Stock Option Agreement (incorporated by reference to Exhibit 10.2 to the Registrant's Form 8-K filed on January 14, 2009).
+10.27.2	Form of Restricted Stock Agreement (incorporated by reference to Exhibit 10.3 to the Registrant's Form 8-K filed on January 14, 2009).
+10.28	Employment Agreement dated May 26, 2009 by and between the Registrant and Robert B. Lee (incorporated by reference to Exhibit 10.1 to the Registrant's Form 8-K filed on June 1, 2009).
10.29	Revolving Credit and Term Loan Agreement dated as of January 19, 2010, by and among PRGX Global, Inc. (formerly PRG-Schultz International, Inc), and PRGX USA, Inc. (formerly PRG-Schultz USA, Inc.), as co-borrowers, the lenders from time to time party thereto, SunTrust Bank, as issuing bank, and SunTrust Bank, as administrative agent (incorporated by reference to Exhibit 10.2 to the Registrant's Form 10-Q filed on November 7, 2011).
10.29.1	Subsidiary Guaranty Agreement dated as of January 19, 2010 by and among PRGX Global, Inc. (formerly PRG-Schultz International, Inc), and PRGX USA, Inc. (formerly PRG-Schultz USA, Inc.), as borrowers, each of the subsidiaries of PRGX Global, Inc. listed on Schedule I thereto, as guarantors, and SunTrust Bank, as administrative agent (incorporated by reference to Exhibit 10.2 to the Registrant's Form 8-K filed on January 25, 2010).
10.29.2	Security Agreement dated January 19, 2010 among PRGX Global, Inc. (formerly PRG-Schultz International, Inc), PRGX USA, Inc. (formerly PRG-Schultz USA, Inc.), and the other direct and indirect subsidiaries of PRGX Global, Inc. signatory thereto, as grantors, in favor of SunTrust Bank, as administrative agent (incorporated by reference to Exhibit 10.3 to the Registrant's Form 8-K filed on January 25, 2010).
10.29.3	Equity Pledge Agreement dated as of January 19, 2010, made by PRGX Global, Inc. (formerly PRG-Schultz International, Inc), PRGX USA, Inc. (formerly PRG-Schultz USA, Inc.), and the other direct and indirect subsidiaries of PRGX Global, Inc. signatory thereto, as grantors, in favor of SunTrust Bank, as administrative agent (incorporated by reference to Exhibit 10.4 to the Registrant's Form 8-K filed on January 25, 2010).
10.29.4	Loan Documents Modification Agreement dated June 21, 2010, by and among the Borrowers, the Guarantors and the Lender (incorporated by reference to Exhibit 10.29.4 to the Registrant's Form 10-K filed on March 15, 2012).
10.29.5	Second Loan Documents Modification Agreement dated September 30, 2010, by and among the Borrowers and the Lender (incorporated by reference to Exhibit 10.1 to the Registrant's Form 8-K filed on October 1, 2010).
10.29.6	Third Loan Documents Modification Agreement dated October 17, 2011, by and among the Borrowers and the Lender (incorporated by reference to Exhibit 10.29.6 to the Registrant's Form 10-K filed on March 15, 2012).
+10.30	Employment Agreement between the Registrant and Victor A. Allums dated November 28, 2008 (incorporated by reference to Exhibit 10.31 to the Registrant's Form 10-K filed on March 29, 2010).
+10.32	Employment Agreement between the Registrant and James Shand dated March 12, 2009 (incorporated by reference to Exhibit 10.33 to the Registrant's Form 10-K filed on March 29, 2010).



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+10.33	Employment Agreement between the Registrant and Michael Noel dated September 30, 2009. (incorporated by reference to Exhibit 10.33 to the Registrant's Form 10-K filed on March 16, 2011).
+10.34	Employment Agreement between the Registrant and Catherine Lafiandra dated February 1, 2010 (incorporated by reference to Exhibit 10.34 to the Registrant's Form 10-K filed on March 15, 2012).
+10.35	Employment Agreement between the Registrant and Puneet Pamnani dated February 8, 2012 (incorporated by reference to Exhibit 10.35 to the Registrant's Form 10-K filed on March 15, 2012).
14.1	Code of Ethics for Senior Financial Officers (incorporated by reference to Exhibit 14.1 to the Registrant's Form 10-K for the year ended December 31, 2003).
21.1	Subsidiaries of the Registrant.
23.1	Consent of BDO USA, LLP
31.1	Certification of the Chief Executive Officer, pursuant to Rule 13a-14(a) or 15d-14(a), for the year ended December 31, 2012.
31.2	Certification of the Chief Financial Officer, pursuant to Rule 13a-14(a) or 15d-14(a), for the year ended December 31, 2012.
32.1	Certification of the Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, for the year ended December 31, 2012.
101	The following financial information from the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2012, formatted in Extensible Business Reporting Language (XBRL): (i) Consolidated Statements of Income, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Balance Sheets, (iv) Consolidated Statements of Cash Flows and (v) Notes to Consolidated Financial Statements.*

+ Designates management contract or compensatory plan or arrangement.

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

**Table of Contents****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.

**PRGX GLOBAL, INC.**

By: /s/ ROMIL BAHL  
Romil Bahl  
*President, Chief Executive Officer, Director*  
*(Principal Executive Officer)*

Date: March 13, 2013

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 and on the dates indicated.

Signature	Title	Date
/s/ ROMIL BAHL Romil Bahl	President, Chief Executive Officer and Director (Principal Executive Officer)	March 13, 2013
/s/ ROBERT B. LEE Robert B. Lee	Chief Financial Officer and Treasurer (Principal Financial Officer)	March 13, 2013
/s/ BRIAN D. LANE Brian D. Lane	Controller (Principal Accounting Officer)	March 13, 2013
/s/ DAVID A. COLE David A. Cole	Director	March 13, 2013
/s/ PATRICK G. DILLS Patrick G. Dills	Chairman of the Board	March 13, 2013
/s/ ARCHELLE GEORGIU FELDSHON Archelle Georgiou Feldshon	Director	March 13, 2013
/s/ MYLLE H. MANGUM Mylle H. Mangum	Director	March 13, 2013
/s/ PHILIP J. MAZZILLI, JR. Philip J. Mazzilli, Jr.	Director	March 13, 2013
/s/ STEVEN P. ROSENBERG Steven P. Rosenberg	Director	March 13, 2013
/s/ RONALD E. STEWART Ronald E. Stewart	Director	March 13, 2013
/s/ JOSEPH E. WHITTERS Joseph E. Whitters	Director	March 13, 2013



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## SCHEDULE VALUATION AND QUALIFYING ACCOUNTS

## SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS

## FOR THE YEARS ENDED DECEMBER 31, 2012, 2011 AND 2010

(In thousands)

Description	Balance at Beginning of Year	Additions Charge (Credit) to Costs and Expenses	Deductions Credit to the respective receivable (1)	Balance at End of Year
<b>2012</b>				
Allowance for doubtful accounts receivable	\$ 811	882		\$ 1,693
Allowance for doubtful employee advances and miscellaneous receivables	\$ 272	584	(318)	\$ 538
Deferred tax valuation allowance	\$ 51,630	(3,141)		\$ 48,489
<b>2011</b>				
Allowance for doubtful accounts receivable	\$ 591	221	(1)	\$ 811
Allowance for doubtful employee advances and miscellaneous receivables	\$ 669	366	(763)	\$ 272
Deferred tax valuation allowance	\$ 54,801	(3,171)		\$ 51,630
<b>2010</b>				
Allowance for doubtful accounts receivable	\$ 1,032	(360)	(81)	\$ 591
Allowance for doubtful employee advances and miscellaneous receivables	\$ 351	559	(241)	\$ 669
Deferred tax valuation allowance	\$ 58,304	(3,503)		\$ 54,801

(1) Write-offs, net of recoveries

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