

TRINET GROUP INC
Form 10-Q
August 06, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2014

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

Commission File Number: 001-36373

TriNet Group, Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware 95-3359658
(State or other jurisdiction of (I.R.S. Employer

incorporation or organization) Identification No.)

1100 San Leandro Blvd., Suite 400

San Leandro, CA 94577

(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code: (510) 352-5000

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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 the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (do not check if a smaller reporting company) Smaller reporting company

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

As of July 31, 2014, the registrant had 69,114,655 shares of common stock outstanding.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

TriNet Group, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

	June 30, 2014	December 31, 2013
Assets	(unaudited)	
Current assets:		
Cash and cash equivalents	\$ 100,288	\$ 94,356
Restricted cash	15,050	15,267
Prepaid income taxes	12,821	3,331
Deferred income taxes	68	68
Prepaid expenses	9,094	7,849
Deferred loan costs and other current assets	4,418	5,238
Worksite employee related assets	664,279	772,437
Total current assets	806,018	898,546
Workers compensation receivable	40,826	25,381
Restricted cash and investments	43,454	36,968
Property and equipment, net	30,389	25,690
Goodwill	288,857	288,857
Other intangible assets, net	107,204	134,020
Deferred income taxes	1,000	1,000
Deferred loan costs and other assets	15,300	24,276
Total assets	\$ 1,333,048	\$ 1,434,738
Liabilities and stockholders' deficit		
Current liabilities:		
Accounts payable	\$ 13,145	\$ 7,315
Accrued corporate wages	23,095	26,264
Deferred income taxes	25,406	16,535
Current portion of notes payable and borrowings under capital leases	6,061	6,669
Other current liabilities	9,943	9,078
Worksite employee related liabilities	658,040	767,624
Total current liabilities	735,690	833,485
Notes payable and borrowings under capital leases, less current portion	569,650	812,208
Workers compensation liabilities	56,253	45,309
Deferred income taxes	2,292	8,888
Other liabilities	5,822	5,210
Total liabilities	1,369,707	1,705,100
Commitments and contingencies (Note 10)		
Series G convertible preferred stock, \$.0001 per share stated value	—	59,059

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(aggregate liquidation preference of \$59,306); no shares authorized, issued and outstanding

at June 30, 2014; 5,391,441 shares authorized, issued and outstanding at December 31, 2013

Series H convertible preferred stock, \$.0001 per share stated value

(aggregate liquidation preference of \$60,000); no shares authorized, issued and outstanding

at June 30, 2014; 4,124,986 shares authorized, issued and outstanding at December 31, 2013

— 63,819

Stockholders' deficit:

Preferred stock, \$.000025 per share stated value; 20,000,000 shares authorized;

no shares issued and outstanding at June 30, 2014 and December 31, 2013

— —

Common stock, \$.000025 per share stated value; 750,000,000 shares authorized;

69,103,537 and 15,259,540 shares issued and outstanding at June 30, 2014

and December 31, 2013

424,222 74,160

Accumulated deficit

(460,711) (467,209)

Accumulated other comprehensive loss

(170) (191)

Total stockholders' deficit

(36,659) (393,240)

Total liabilities and stockholders' deficit

\$1,333,048 \$1,434,738

See accompanying notes.

TriNet Group, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except share and per share data)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Professional service revenues	\$82,260	\$61,080	\$165,135	\$120,311
Insurance service revenues	442,746	302,352	868,783	594,191
Total revenues	525,006	363,432	1,033,918	714,502
Costs and operating expenses:				
Insurance costs	400,195	269,217	781,352	523,129
Cost of providing services (exclusive of depreciation and amortization of intangible assets)	34,034	23,671	67,677	46,486
Sales and marketing	34,992	25,389	66,829	48,020
General and administrative	12,682	12,741	27,019	25,228
Systems development and programming costs	6,565	5,578	12,459	10,088
Amortization of intangible assets	13,267	10,178	26,816	20,484
Depreciation	3,242	2,726	6,460	5,552
Total costs and operating expenses	504,977	349,500	988,612	678,987
Operating income	20,029	13,932	45,306	35,515
Other income (expense):				
Interest expense and bank fees	(8,860)	(7,037)	(30,712)	(12,189)
Other, net	(25)	161	78	234
Income before provision for income taxes	11,144	7,056	14,672	23,560
Provision for income taxes	4,923	2,713	6,911	8,680
Net income	\$6,221	\$4,343	\$7,761	\$14,880
Net income per share:				
Basic	\$0.09	\$0.09	\$0.13	\$0.30
Diluted	\$0.09	\$0.08	\$0.12	\$0.28
Weighted average shares:				
Basic	69,053,403	10,898,957	42,914,458	10,834,724
Diluted	72,658,822	15,303,439	46,028,300	14,874,720

See accompanying notes.

TriNet Group, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	Three Months		Six Months	
	Ended June 30,		Ended June 30,	
	2014	2013	2014	2013
Net income	\$6,221	\$4,343	\$7,761	\$14,880
Other comprehensive income (loss), net of tax				
Unrealized gains (losses) on investments	3	(59)	20	(54)
Unrealized gains on interest rate cap	–	34	–	21
Foreign currency translation adjustments	43	(28)	1	(39)
Total other comprehensive income (loss), net of tax	46	(53)	21	(72)
Comprehensive income	\$6,267	\$4,290	\$7,782	\$14,808

See accompanying notes.

TriNet Group, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Six Months Ended June 30,	
	2014	2013
Operating activities		
Net income	\$7,761	\$14,880
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	39,070	26,143
Deferred income taxes	2,276	5,933
Stock-based compensation	5,070	2,865
Excess tax benefit from equity incentive plan activity	(3,029)	(1,876)
Accretion of workers compensation and leases fair value adjustment	(695)	(768)
Changes in operating assets and liabilities:		
Restricted cash	10,520	(979)
Prepaid expenses and other current assets	(3,960)	(1,571)
Workers compensation receivables	(14,737)	(414)
Other assets	4,871	1,874
Accounts payable	3,405	(157)
Income tax payable/receivable	(6,461)	3,062
Other current liabilities	(753)	2,792
Other liabilities	11,745	1,659
Worksite employee related assets	108,158	(37,161)
Worksite employee related liabilities	(109,584)	44,272
Net cash provided by operating activities	53,657	60,554
Investing activities		
Proceeds from sale and maturity of debt securities	–	500
Purchase of debt securities	(16,789)	(6,752)
Purchase of property and equipment	(8,709)	(4,653)
Net cash used in investing activities	(25,498)	(10,905)
Financing activities		
Proceeds from issuance of common stock, net of issuance costs	218,613	–
Proceeds from issuance of common stock on exercised options	631	1,296
Excess tax benefit from equity incentive plan activity	3,029	1,876
Borrowings under notes payable	–	150,000
Repayment of notes payable	(243,025)	(4,854)
Payment of debt issuance costs	–	(2,639)
Payments of special dividend	–	(52)
Repayments under capital leases	(188)	(458)
Repurchase of common stock	(1,288)	(6,063)
Net cash provided by (used in) financing activities	(22,228)	139,106
Effect of exchange rate changes on cash and cash equivalents	1	(39)
Net increase in cash and cash equivalents	5,932	188,716

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Cash and cash equivalents at beginning of period	94,356	63,749
Cash and cash equivalents at end of period	\$ 100,288	\$ 252,465
Supplemental disclosures of cash flow information		
Cash paid for interest	\$ 23,407	\$ 6,804
Cash paid for income taxes, net of refunds	11,067	(721)
Supplemental schedule of noncash investing and financing activities		
Payable for purchase of property and equipment	3,970	62

See accompanying notes.

TriNet Group, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

NOTE 1. DESCRIPTION OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

Description of Business

TriNet Group, Inc. (the Company or TriNet), a Delaware corporation incorporated in January 2000, provides a comprehensive human resources solution for small to medium-sized businesses. The Company's solution includes payroll processing, human capital consulting, employment law compliance and employee benefits, including health insurance, retirement plans and workers compensation insurance.

The Company provides its services through co-employment relationships with its customers, under which the Company and its customers each take responsibility for certain portions of the employer-employee relationship for worksite employees (WSEs). The Company is the employer of record for most administrative and regulatory purposes, including the following: (i) compensation through wages and salaries; (ii) employer payroll-related taxes payment; (iii) employee payroll-related taxes withholding and payment; (iv) employee benefit programs including health and life insurance, and others; and (v) workers compensation coverage.

Initial Public Offering

In March 2014, the Company completed its initial public offering (IPO) in which the Company issued and sold 15,000,000 shares of common stock at a public offering price of \$16.00 per share. In addition, another 2,250,000 shares were sold by certain selling stockholders pursuant to the underwriters' option to purchase additional shares. The Company received net proceeds of approximately \$217.6 million, after deducting underwriting discounts and commissions of \$16.8 million and offering expenses of \$5.6 million. The Company did not receive any proceeds from the sale by the selling stockholders. Upon the closing of the IPO, all shares of the Company's then-outstanding preferred stock were converted into an aggregate of 38,065,708 shares of common stock.

Segment Information

The Company operates in one reportable segment in accordance with ASC 280. All of the Company's service revenues are generated from external customers. Less than 1% of revenues are generated outside of the United States of America (U.S.). Substantially all of the Company's long-lived assets are located in the U.S.

Basis of Presentation

The accompanying unaudited consolidated financial statements and footnotes thereto of the Company and its wholly owned subsidiaries have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company's prospectus filed with the SEC pursuant to Rule 424(b) under the Securities Act of 1933 with the SEC on March 27, 2014. There have been no changes to the Company's significant accounting policies described in the prospectus that have had a material impact on our consolidated financial statements and related notes.

All intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited consolidated balance sheets present the current assets and current liabilities directly related to the processing of human resources transactions as WSE-related assets and WSE-related liabilities, respectively. WSE-related assets are comprised of cash and investments restricted for current workers compensation claim payments, payroll funds collected, accounts receivable, unbilled service revenues, and refundable or prepaid amounts related to the Company-sponsored workers compensation and health plan programs. WSE-related liabilities are comprised of customer prepayments, wages and payroll taxes accrued and payable, and liabilities related to the Company-sponsored workers compensation and health plan programs resulting from workers compensation case reserves, premium amounts due to providers for enrolled employees, and workers compensation and health reserves that are expected to be disbursed within the next 12 months.

The unaudited interim financial statements have been prepared on the same basis as the annual financial statements and, in the opinion of management, reflect all adjustments, consisting only of normal recurring adjustments, necessary for fair presentation. The results of the six months ended June 30, 2014 are not necessarily indicative of the results to be expected for the year ending December 31, 2014.

Seasonality

Historically, the Company has experienced its highest monthly addition of WSEs, as well as its highest monthly levels of client attrition, in the month of January, primarily because clients that change their payroll service providers tend to do so at the beginning of a calendar year. In addition, the Company experiences higher levels of client attrition in connection with renewals of the health insurance it provides for its WSEs, in the event that such renewals result in increased premiums that it passes on to its clients. The Company has also historically experienced higher insurance claim volumes in the second and third quarters of a fiscal year than in the first and fourth quarters of a fiscal year, as WSEs typically access their health care providers more often in the second and third quarters of a fiscal year, which has negatively impacted the Company's insurance costs in these quarters. These historical trends may change, and other seasonal trends may develop that make it more difficult for the Company to manage its business.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. These estimates include, but are not limited to, allowances for accounts receivable, workers compensation related assets and liabilities, health plan assets and liabilities, recoverability of goodwill and other intangible assets, income taxes, stock-based compensation and other contingent liabilities. Such estimates are based on historical experience and on various other assumptions that Company management believes to be reasonable under the circumstances. Actual results could differ from those estimates.

Recent Accounting Pronouncements

In June 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-12—Compensation-Stock Compensation, which requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. ASU 2014-12 is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2015. Early adoption is permitted. The amendments may be applied prospectively to all awards granted or modified after the effective date or retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented. The Company does not expect this guidance to have a material effect on its consolidated financial statements. The Company expects to adopt this guidance in 2016.

In May 2014, the FASB issued ASU 2014-09—Revenue from Contracts with Customers, which will replace most existing revenue recognition guidance under GAAP. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard provides a five-step analysis of transactions to determine when and how revenue is recognized. ASU 2014-09 is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2016. Early adoption is not permitted. The amendments may be applied retrospectively or as a cumulative-effect adjustment as of the date of adoption. The Company expects to adopt this guidance in 2017. The Company has not yet selected a method of adoption and is currently evaluating the effect that the amendments will have on the consolidated financial statements.

In July 2013, the FASB issued ASU 2013-11—Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists, which requires that an unrecognized tax benefit, or portion of an unrecognized tax benefit, be presented as a reduction of a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. If an applicable deferred tax asset is not available or a company does not expect to use the applicable deferred tax asset, the unrecognized tax benefit should be presented as a liability in the financial statements and should not be combined with an unrelated deferred tax asset. ASU 2013-11 is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2013. The amendments should be applied prospectively to all unrecognized tax benefits that exist at the

effective date, however retrospective application is permitted. The Company adopted this guidance in 2014. The adoption of ASU 2013-11 did not have a material impact on the Company's consolidated financial statements.

NOTE 2. WORKSITE EMPLOYEE-RELATED ASSETS AND LIABILITIES

The following schedule presents the components of the Company's WSE-related assets and WSE-related liabilities (in thousands):

	June 30, 2014	December 31, 2013
Worksite employee-related assets:		
Restricted cash	\$65,297	\$ 19,154
Restricted investment	12,276	2,317
Payroll funds collected	291,715	490,058
Unbilled revenue, net of advance collection of \$34,685 and \$54,159 at June 30, 2014 and December 31, 2013, respectively	255,974	200,641
Accounts receivable, net of allowance for doubtful accounts of \$231 and \$865 at June 30, 2014 and December 31, 2013, respectively	9,817	10,450
Prepaid health plan expenses	5,594	7,584
Refundable health plan premiums	265	17,601
Refundable workers compensation premiums	16,565	20,834
Prepaid workers compensation expenses	2,720	1,414
Other payroll assets	4,056	2,384
Total worksite employee-related assets	\$664,279	\$ 772,437
Worksite employee-related liabilities:		
Unbilled wages accrual	\$283,005	\$ 243,640
Payroll taxes payable	199,760	358,285
Health benefits payable	81,798	67,132
Customer prepayments	36,282	51,902
Workers compensation payable	34,979	23,453
Other payroll deductions	22,216	23,212
Total worksite employee-related liabilities	\$658,040	\$ 767,624

NOTE 3. WORKERS COMPENSATION

The Company has agreements with various insurance carriers to provide workers compensation insurance coverage for worksite employees. Insurance carriers are responsible for administrating and paying claims. The Company is responsible for reimbursing each carrier up to a deductible limit per occurrence.

The following summarizes the activities in liability for unpaid claims and claims adjustment expenses (in thousands):

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	For the six months ended June 30, 2014	For the year ended December 31, 2013
Liability for unpaid claims and claims adjustment at beginning of period	\$58,610	\$ 53,900
Plans acquired through business combinations	–	481
Incurred related to:		
Current year	25,798	26,401
Prior years	(685)	(3,319)
Total incurred	25,113	23,082
Paid related to:		
Current year	(3,289)	(8,055)
Prior years	(4,774)	(10,798)
Total paid	(8,063)	(18,853)
Liability for unpaid claims and claims adjustment at end of period	75,660	58,610
Other premiums and collateral liabilities	15,572	10,152
Total workers compensation liabilities at end of period	\$91,232	\$ 68,762
Current portion included in worksite employer-related liability	34,979	23,453
Long term portion	\$56,253	\$ 45,309

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Under the terms of its agreements with its workers compensation insurance carriers, the Company collects and holds premiums in restricted accounts pending claims payments by the claims administrator. As of June 30, 2014 and December 31, 2013, such restricted amounts of \$50.3 million and \$21.5 million, respectively, are presented as restricted cash and restricted investment within WSE-related assets in the accompanying consolidated balance sheets. In addition, the Company invests premium collateral in excess of short term claim obligations in certain longer term securities. While it is the intention of the Company to reinvest maturing securities, periodically certain securities will be classified as short term to the extent the Company does not intend to reinvest the proceeds upon maturity. At June 30, 2014 and December 31, 2013, \$43.5 million and \$37.0 million, respectively, are presented as restricted long-term investments.

NOTE 4. MARKETABLE SECURITIES AND FAIR VALUE MEASUREMENTS

The Company's noncurrent restricted cash and investments include \$43.1 million of available-for-sale marketable securities and \$0.4 million of cash collateral at June 30, 2014. The Company's restricted investments within WSE-related assets include \$10.0 million of available-for-sale marketable securities and \$2.3 million of certificates of deposit as of June 30, 2014. The available-for-sale marketable securities as of June 30, 2014 and December 31, 2013 consist of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
June 30, 2014				
U.S. treasuries	\$ 52,566	\$ 62	\$ (12)	\$ 52,616
Mutual funds	500	9	–	509
Total investments	\$ 53,066	\$ 71	\$ (12)	\$ 53,125
December 31, 2013:				
U.S. treasuries	\$ 35,900	\$ 38	\$ (20)	\$ 35,918
Mutual funds	500	8	–	508
Total investments	\$ 36,400	\$ 46	\$ (20)	\$ 36,426

There were no realized gains or losses for the three and six months ended June 30, 2014 and 2013. As of June 30, 2014 and December 31, 2013, the contractual maturities of the U.S. treasuries were two to three years.

As of June 30, 2014, certain of the Company's U.S. treasuries were in unrealized loss position principally due to changes in interest rates and credit spreads. No U.S. treasuries were in an unrealized loss position for more than 12 months as of either June 30, 2014 or December 31, 2013. In analyzing an issuer's financial condition, the Company considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts' reports. The fair value of these securities in an unrealized loss position represented 39% of the total fair value of all securities available for sale and their unrealized loss was \$0.01 million as of June 30, 2014. As the Company has the ability to hold debt securities until maturity, or for the foreseeable future as classified as available for sale, no decline was deemed to be other-than-temporary.

Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability.

As a basis for considering such assumptions, the Company uses a three-tier value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

- Level I—observable inputs such as quoted prices in active markets
- Level II—inputs other than the quoted prices in active markets that are observable either directly or indirectly
- Level III—unobservable inputs in which there is little or no market data, which requires the Company to develop its own assumptions

This hierarchy requires the Company to use observable market data when available and to minimize the use of unobservable inputs when determining fair value. On a recurring basis, the Company measures its financial assets at fair value.

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The following table summarizes the Company's financial assets measured at fair value on a recurring basis (in thousands):

	Total			
	Fair Value	Level I	Level II	Level III
June 30, 2014				
Certificate of deposit	\$2,317	\$2,317	\$ –	\$ –
U.S. treasuries	52,616	52,616	–	–
Mutual funds	509	509	–	–
Interest rate cap	5	–	5	–
Total	\$55,447	\$55,442	\$ 5	\$ –
December 31, 2013:				
Certificates of deposit	\$2,858	\$2,858	\$ –	\$ –
U.S. treasuries	35,918	35,918	–	–
Mutual funds	508	508	–	–
Interest rate cap	47	–	47	–
Total	\$39,331	\$39,284	\$ 47	\$ –

There were no transfers between Level I and Level II assets for the three months ended June 30, 2014 or the year ended December 31, 2013.

As of June 30, 2014 and December 31, 2013, certificate of deposit consisted of certificates of deposit held by domestic financial institutions, which are presented as restricted investments within WSE-related assets in the accompanying consolidated balance sheets.

The book value of the Company's financial instruments not measured at fair value, including cash, restricted cash, WSE-related assets and liabilities, line of credit and accrued corporate wages, approximates fair value due to the relatively short maturity, cash repayments or market interest rates of such instruments. The fair value of such financial instruments, other than cash and restricted cash, is determined using the income approach based on the present value of estimated future cash flows. The fair value of all of these instruments would be categorized as Level II of the fair value hierarchy, with the exception of cash and cash equivalents, which would be categorized as Level I.

At June 30, 2014 and December 31, 2013, the carrying value of our notes payable of \$575.4 million and \$818.4 million, respectively, approximated fair value. The estimate fair values of our notes payable are considered a Level II valuation in the hierarchy for fair value measurement and are based on a cash flow model discounted at market interest rates that considers the underlying risks of unsecured debt.

NOTE 5. NOTES PAYABLE AND BORROWINGS UNDER CAPITAL LEASES

The following schedule summarizes the components of the Company's notes payable and borrowings under capital leases balances (in thousands):

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	June 30, 2014	December 31, 2013
Notes payable under credit facility	\$ 575,400	\$ 818,425
Capital leases	311	452
Less current portion	(6,061)	(6,669)
	\$ 569,650	\$ 812,208

In August 2013, the Company, as guarantor, its subsidiary TriNet HR Corporation, as borrower, and certain of its other subsidiaries as subsidiary guarantors entered into two senior secured credit facilities:

- a \$705.0 million first lien credit facility with JPMorgan Chase Bank, N.A., as administrative agent; and
 - a \$190.0 million second lien credit facility with Wilmington Trust, National Association, as administrative agent.
- The credit facilities are secured by substantially all of the Company's assets and the assets of the borrower and of the subsidiary guarantors, other than specifically excluded assets.

The first lien credit facility provides for a five-year revolving credit facility of \$75.0 million, three-year first lien tranche B-1 term loan of \$175.0 million and seven-year first lien tranche B-2 term loan of \$455.0 million. A second lien credit facility provides for seven-year-and-six-month term loan of \$190.0 million. All first lien and second lien term loans were fully drawn in August 2013. The

\$75.0 million revolving credit facility includes capacity for a \$30.0 million letter of credit facility and a \$10.0 million swingline facility. The total unused portion of the revolving credit facility was \$59.5 million as of June 30, 2014. The proceeds of the first and second lien credit facilities were used to repay approximately \$448.3 million of indebtedness outstanding under the Company's previous credit facility, declare a special dividend, provide cash collateral to guarantee a letter of credit and pay transaction costs. In connection with the credit facilities, the Company incurred \$23.1 million of debt issuance costs, which were deferred and are being amortized over the term of the credit facilities.

In March 2014, the proceeds from the IPO were used to fully repay the \$190.0 million second lien credit facility, which resulted in a prepayment premium of \$3.8 million, and to repay \$25.0 million of the first lien tranche B-1 term loan. Additionally, the remaining balance of the loan fees associated with the second lien credit facility and a portion of the loan fees associated with the first lien credit facility were fully amortized in March 2014 for a charge of \$5.0 million. In May 2014, the Company repaid \$25.0 million of the first lien tranche B-1 term loan. As a result, a portion of the loan fees associated with the first lien credit facility were fully amortized in May 2014 for a charge of \$0.5 million.

The credit facilities contain customary representations and warranties and customary affirmative and negative covenants applicable to us and our subsidiaries, including, among other things, restrictions on indebtedness, liens, investments, mergers, dispositions, prepayment of other indebtedness, and dividends and other distributions. Under the revolving credit facility, so long as there are any outstanding revolving loans and/or outstanding letters of credit in excess of \$15.0 million other than letters of credit that have been cash collateralized, we are required to comply with a financial covenant that requires us and our subsidiaries to maintain a maximum first lien leverage ratio at 5.25 to 1.00 on a consolidated basis as of June 30, 2014. The Company was in compliance with the restrictive covenants under the credit facilities at June 30, 2014. The company amended and restated the credit facility in July 2014 as discussed in Note 11.

NOTE 6. CONVERTIBLE PREFERRED STOCK

On June 7, 2005, the Company issued 5,391,441 shares of Series G convertible preferred stock (Series G) at \$11.00 per share for an aggregate cash purchase price of \$59.3 million. The Company recorded the issuance of Series G at \$59.1 million, net of issuance costs of \$0.2 million. On June 1, 2009, the Company issued 4,124,986 shares of Series H convertible preferred stock (Series H) at \$16.69 per share for an aggregate cash purchase price of \$68.8 million. The Company recorded the issuance of Series H at \$63.8 million, net of issuance costs of \$5.0 million. Upon the issuance of Series H, certain terms related to Series G were amended. In March 2014, upon completion of the Company's IPO, all of the outstanding shares of Series H and Series G were converted into 38,065,708 shares of common stock.

NOTE 7: STOCKHOLDERS' EQUITY

Equity-Based Incentive Plans

In 2000, the Company established the 2000 Equity Incentive Plan (the 2000 Plan), which provided for granting incentive stock options, nonstatutory stock options, bonus awards and restricted stock awards to eligible employees, directors, and consultants of the Company. In December 2009, the Board of Directors approved the 2009 Equity Incentive Plan (the 2009 Plan) as the successor to and continuation of the 2000 Plan. As of the 2009 Plan effective date, remaining shares available for issuance under the 2000 Plan were cancelled and became available for issuance under the 2009 Plan. No additional stock awards will be granted under the 2000 Plan. The 2009 Plan provides for the grant of the following awards to eligible employees, directors, and consultants: incentive stock options, nonstatutory stock options, stock appreciation rights, restricted stock awards, restricted stock unit awards, performance stock

awards, performance cash awards, and other stock awards. Incentive stock options may only be granted to employees. Nonemployee directors are eligible to receive nonstatutory stock options automatically at designated intervals over their period of continuous service on the Board. In February 2014, the Board approved an amendment to the 2009 Plan authorizing an additional 3,000,000 shares available for grant. The amended 2009 Plan also provides that the number of shares reserved for issuance under the 2009 Plan will increase on January 1 of each year for a period of up to five years by 4.5% of the total number of shares of capital stock outstanding on December 31 of the preceding calendar year, which will begin on January 1, 2015 and continue through January 1, 2019.

The exercise price per share of all incentive stock options granted under the 2000 Plan and the 2009 Plan must be at least equal to the fair market value of the shares at the date of grant as determined by the Board of Directors. Options issued to recipients other than nonemployee directors generally vest over four years with a one year cliff and monthly thereafter, and have a maximum contractual term of 10 years. Options issued to members of the Board of Directors are issued with varying vesting schedules. Incentive stock options granted at 110% of the fair market value to stockholders who have greater than 10% ownership have a maximum term of five years.

The Company also has granted restricted stock units to members of the Board of Directors and certain executives. These restricted stock units represent rights to receive shares of the Company's common stock on satisfaction of applicable vesting conditions. The fair value of restricted stock units is equal to the fair value of the Company's common stock on the date of grant. The

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restricted stock units vest at a rate of 25% at the end of the first year and then pro rata monthly thereafter over the remaining vesting term of three or two years, as applicable.

Activity under the 2000 Plan and the 2009 Plan for the six months ended June 30, 2014 is summarized as follows:

	Shares Available for Grant
Balance at December 31, 2013	2,004,464
Authorized	3,000,000
Granted	(2,508,500)
Forfeited	292,676
Expired	6,580
Balance at June 30, 2014	2,795,220

The following table summarizes stock option activity under the Company's equity-based plans for the six months ended June 30, 2014:

	Number of Shares	Weighted Average Exercise Price	Weighted- Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (in thousands)
Balance at December 31, 2013	6,281,148	\$ 1.74	8.55	\$ 53,373
Granted	2,508,500	11.48		
Exercised	(762,010)	0.83		
Forfeited	(264,676)	4.69		
Expired	(6,580)	0.50		
Balance at June 30, 2014	7,756,382	\$ 4.88	8.60	\$ 148,864
Exercisable at June 30, 2014	1,735,542	\$ 0.86	7.52	\$ 40,285
Vested and expected to vest at June 30, 2014	7,145,265	\$ 4.71	8.56	\$ 138,319

The weighted-average grant-date fair value of stock options granted in each of the three months ended June 30, 2014 and June 30, 2013 was \$12.46 and \$3.60 per share, respectively. The weighted-average grant-date fair value of stock options granted in each of the six months ended June 30, 2014 and June 30, 2013 was \$6.33 and \$3.50 per share,

respectively. The total fair value of options vested for the three months ended June 30, 2014 and June 30, 2013 was \$1.3 million and \$0.8 million, respectively. The total fair value of options vested for the six months ended June 30, 2014 and June 30, 2013 was \$4.6 million and \$2.5 million, respectively.

The total intrinsic value of options exercised for the three months ended June 30, 2014 and June 30, 2013 was \$3.8 million and \$6.5 million, respectively. The total intrinsic value of options exercised for the six months ended June 30, 2014 and June 30, 2013 was \$10.0 million and \$7.2 million, respectively. Cash received from options exercised during the three months ended June 30, 2014 and June 30, 2013 was \$0.1 million and \$1.0 million, respectively. Cash received from options exercised during the six months ended June 30, 2014 and June 30, 2013 was \$0.6 million and \$1.3 million, respectively. The exercise price of all options granted was equal to the fair value of the common stock on the date of grant.

As of June 30, 2014, unrecognized compensation expense, net of forfeitures, associated with nonvested options outstanding was \$24.6 million and is expected to be recognized over a weighted-average period of 3.02 years.

For the three and six months ended June 30, 2014, there were no grants or vesting of restricted stock units. For the three and six months ended June 30, 2014, 28,000 restricted stock units were forfeited. The total grant date fair value of restricted stock units vested in the six months ended June 30, 2014 and 2013 was \$0.0 million and \$0.1 million, respectively. As of June 30, 2014, unrecognized compensation expense, net of forfeitures, associated with the nonvested restricted stock units outstanding was \$0.1 million, and is expected to be recognized over a weighted-average period of 3.01 years.

Stock Split

On March 7, 2014, the Company's board of directors and stockholders approved and effected an amendment to the amended and restated certificate of incorporation providing for a 2-for-1 stock split of the outstanding common stock. All of the share numbers,

share prices, and exercise prices have been adjusted within these financial statements, on a retroactive basis, to reflect this 2-for-1 stock split.

Employee Stock Purchase Plan

The Company adopted the 2014 Employee Stock Purchase Plan (ESPP) in February 2014, which became effective on March 26, 2014. The ESPP was approved with a reserve of 1.1 million shares of common stock for future issuance under various terms provided for in the ESPP, which will automatically increase on January 1 of each year from 2015 through 2024 by the lesser of 1% of the total number of shares outstanding on December 31 of the preceding calendar year or 1,800,000 shares. We commenced our first purchase period under the ESPP on March 26, 2014 with the purchase price at the lesser of 85% of the fair market value of the common stock on the offering date and 85% of the fair market value of the common stock on the applicable purchase date. Offering periods will be six months in duration and will end on or about May 15 and November 15 of each year, with the exception of the initial offering period which commenced on March 26, 2014 and that ends on November 14, 2014. Employees may contribute a minimum of 1% and a maximum of 15% of their earnings.

Stock-Based Compensation

Stock-based compensation expense of \$5.1 million and \$2.9 million was recognized for the six months ended June 30, 2014 and 2013, respectively. An income tax benefit of \$1.4 million and \$0.8 million was recognized relating to tax deductible stock-based compensation expense for the six months ended June 30, 2014 and 2013, respectively. The actual tax benefit realized from stock options exercised was \$3.8 million and \$2.7 million for the six months ended June 30, 2014 and 2013, respectively.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions:

	Three Months Ended June 30, 2014		Six Months Ended June 30, 2013	
Expected term (in years)	5.85	6.08	6.04	6.04
Expected volatility	58.3%	45.1%	58.3%	45.3%
Risk-free interest rate	1.81%	1.02%	1.80%	1.12%
Expected dividend yield	0%	0%	0%	0%

NOTE 8: EARNINGS PER SHARE

Basic net income per share attributable to common stockholders is computed by dividing the net income attributable to common stockholders by the weighted average number of shares of common stock outstanding during the period and participating convertible preferred stock that were outstanding prior to the IPO. Diluted net income per share is computed by giving effect to all potential shares of common stock, including shares issuable upon the conversion of our convertible preferred stock that were outstanding prior to the IPO, shares issuable upon the exercise of outstanding stock options, and stock related to unvested restricted stock unit awards to the extent dilutive.

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The following table sets forth the computation of the Company's basic and diluted net income per share attributable to common stock (in thousands, except per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Numerator (basic)				
Net income	\$6,221	\$4,343	\$7,761	\$14,880
Less net income allocated to participating securities	–	(3,377)	(2,366)	(11,583)
Net income attributable to common stock	\$6,221	\$966	\$5,395	\$3,297
Denominator (basic)				
Weighted average shares of common stock outstanding	69,053	10,899	42,914	10,835
Basic EPS	\$0.09	\$0.09	\$0.13	\$0.30
Numerator (diluted)				
Net income	\$6,221	\$4,343	\$7,761	\$14,880
Less net income allocated to participating securities	–	(3,098)	(2,253)	(10,699)
Net income attributable to common stock	\$6,221	\$1,245	\$5,508	\$4,181
Denominator (diluted)				
Weighted average shares of common stock	69,053	10,899	42,914	10,835
Dilutive effect of stock options and restricted stock units	3,605	4,404	3,114	4,040
Weighted average shares of common stock outstanding	72,659	15,303	46,028	14,875
Diluted EPS	\$0.09	\$0.08	\$0.12	\$0.28
Common stock equivalents excluded from income per diluted share				
because of their anti-dilutive effect	143	653	827	1,655

NOTE 9. INCOME TAXES

The Company is subject to taxation in the United States and Canada. However, business is conducted primarily in the United States. The effective tax rate differs from the statutory rate primarily due to state taxes, tax credits and changes in uncertain tax positions. The Company makes estimates and judgments about its future taxable income that are based on assumptions that are consistent with the Company's plans and estimates. Should the actual amounts differ from these estimates, the amount of the valuation allowance could be materially affected.

Income taxes are computed using the asset and liability method, under which deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. Changes in valuation allowances are reflected as a component of provision for income taxes.

The Company's effective tax rate (ETR) was 44.2% and 38.4% for the three months ended June 30, 2014 and 2013, respectively. The Company's ETR was 47.1% and 36.8% for the six months ended June 30, 2014 and 2013, respectively. The increase is primarily due to non-deductible stock-based compensation and for the revaluation of deferred taxes, based on a regulatory state tax change enacted during the three months ended March 31, 2014. The remainder of the increase is primarily due to the expiration of the federal research and development tax credit in 2014, as well as a release of uncertain tax positions recognized for the three months ended March 31, 2013

The Company has not been subject to U.S. federal, state and local income tax examinations by tax authorities in material jurisdictions for tax years beginning prior to January 1, 2009. However, there are outstanding Notices of Proposed Assessment disallowing employment tax credits totaling \$10.5 million in connection with the Internal Revenue Service (IRS) examination of Gevity HR, Inc. and Subsidiaries, which was acquired by TriNet on June 1, 2009. While Appeals has denied the credits, and the Company plans to exhaust all administrative efforts to resolve this issue, it is likely that the matter will ultimately be resolved through litigation. With regard to these employment tax credits, the Company believes it is more likely than not that the Company will prevail. Therefore, no reserve has been recognized related to this matter.

NOTE 10. COMMITMENTS AND CONTINGENCIES

Lease Commitments

The Company leases office facilities, including its headquarters and other facilities, and equipment under non-cancelable operating leases. The Company also leases certain software and furniture, fixtures, and equipment under capital leases. The lease agreements generally provide for rental payments on a graduated basis and for options to renew, which could increase future minimum lease payments if exercised. The Company recognizes rent expense on a straight-line basis over the lease period and accrues for rent expense incurred but not paid. Rent expense for the three months ended June 30, 2014 and 2013 was \$2.9 million and \$2.2 million, respectively. Rent expense for the six months ended June 30, 2014 and 2013 was \$5.7 million and \$4.4 million, respectively.

Operating Covenants

To meet various states' licensing requirements and maintain accreditation by Employer Services Assurance Corporation, the Company is subject to various minimum working capital and net worth requirements. As of June 30, 2014, the Company believes it has fully complied in all material respects with all applicable state regulations regarding minimum net worth, working capital and all other financial and legal requirements. Further, the Company has maintained positive working capital throughout the period covered by the financial statements.

Contingencies

The Company may from time to time become involved in various litigation matters arising in the ordinary course of business, including suits by its clients. The unfavorable resolution of any such matter could have a material effect on the Company's consolidated financial position and results of operations.

Due to the nature of the Company's relationship with its WSEs, the Company could be subject to liability for federal and state law violations even if the Company does not participate in such violations. While the Company's agreements with its clients contain indemnification provisions related to the conduct of its clients, the Company historically has not encountered situations requiring enforcement of these indemnification provisions.

The Company has been named as a defendant in various class action lawsuits arising from the nature of the Company's relationship with its WSEs. At this stage of the lawsuits, management believes an unfavorable outcome to the Company is not probable. There are significant uncertainties involved in any class action litigation. Management is unable to estimate a possible loss or range of loss for these class action lawsuits.

NOTE 11. SUBSEQUENT EVENTS

2014 Credit Facility

On July 9, 2014, the Company amended and restated its first lien credit facility pursuant to an amended and restated first lien credit agreement (the Amended and Restated Credit Agreement). The Amended and Restated Credit Agreement provides for: (i) \$375 million principal amount of "tranche A term loans," (ii) \$200 million principal amount of "tranche B term loans," and (iii) a revolving credit facility of \$75 million. The proceeds of the tranche A term loans were used to refinance in part the tranche B-2 term loans outstanding under the original first lien credit facility. The proceeds of the tranche B term loans were used to (i) refinance the remaining tranche B-2 term loans outstanding under the original first lien credit facility, (ii) refinance other amounts outstanding under the original first lien credit facility and (iii) pay fees and expenses related thereto. The revolving credit facility replaced the revolving credit facility under the original first lien credit facility.

The tranche A term loans and the revolving credit facility will mature on July 9, 2019. The tranche B term loans will mature on July 9, 2017. Loans under the revolving credit facility are expected to be used for working capital and other general corporate purposes.

The Amended and Restated Credit Agreement contains customary representations and warranties and customary affirmative and negative covenants applicable to the Company and its subsidiaries, including, among other things, restrictions on indebtedness, liens, investments, mergers, dispositions, prepayment of other indebtedness, and dividends and other distributions. The Amended and Restated Credit Agreement also contains financial covenants that require the Company to maintain a minimum consolidated interest coverage ratio of at least 3.50 to 1.00, beginning with the fiscal quarter ending September 30, 2014, and a maximum total leverage ratio, currently at 5.00 to 1.00.

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

You should read the following discussion of our financial condition and results of operations in conjunction with our consolidated financial statements and the related notes included elsewhere in this Quarterly Report on Form 10-Q and our Prospectus filed pursuant to Rule 424(b) under the Securities Act of 1933, as amended, with the Securities and Exchange Commission on March 27, 2014.

Special Note Regarding Forward-Looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Forward-looking statements are often identified by the use of words such as, but not limited to, "anticipate," "believe," "can," "continue," "could," "estimate," "expect," "intend," "may," "plan," "project," "seek," "should," "strategy," "target," "will," "would" and similar expressions or variations thereof to identify forward-looking statements. These statements are not guarantees of future performance, but are based on management's expectations as of the date of this report and assumptions that are inherently subject to uncertainties, risks and changes in circumstances that are difficult to predict. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be materially different from any future results, performance or achievements. Important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements include, but are not limited to, those identified below and those discussed in the section titled "Risk Factors" included under Part II, Item 1A below. All information provided in this report is as of the date of this report and the company undertakes no duty to update this information except as required by law.

Overview

TriNet is a leading provider of a comprehensive human resources solution for small to medium-sized businesses, or SMBs. We enhance business productivity by enabling our clients to outsource their HR function to one strategic partner and allowing them to focus on operating and growing their core businesses. Our HR solution includes services such as payroll processing, human capital consulting, employment law compliance and employee benefits, including health insurance, retirement plans and workers compensation insurance. Our services are delivered by our expert team of HR professionals and enabled by our proprietary, cloud-based technology platform, which allows our clients and their employees to efficiently conduct their HR transactions anytime and anywhere. We believe we are a leader in the industry due to our size, our presence in the United States and Canada and the number of clients and employees that we serve.

We utilize a co-employment model pursuant to which both we and our clients become employers of our clients' employees, which we refer to as worksite employees, or WSEs. This model affords us a close and embedded relationship with our clients and their employees. Under the co-employment model, employment-related liabilities are contractually allocated between us and our clients. We assume responsibility for, and manage the risks associated with, each clients' employee payroll obligations, including the liability for payment of salaries and wages to each client employee, the payment of payroll taxes and, at the client's option, responsibility for providing group health, welfare, workers compensation and retirement benefits to such individuals. Unlike a payroll service provider, we issue each WSE a payroll check drawn on our bank accounts and contract with insurance carriers to provide health and workers compensation insurance to WSEs under TriNet's name.

We serve thousands of clients in specific industry vertical markets, including technology, life sciences, property management, professional services, banking and financial services, retail, manufacturing and hospitality services, as well as non-profit entities. As of June 30, 2014, we served over 9,000 clients in all 50 states, the District of Columbia and Canada and co-employed approximately 259,000 WSEs.

Our total revenues consist of professional service revenues and insurance service revenues. For the three and six months ended June 30, 2014 and 2013, 16% and 17% of our total revenues, respectively, consisted of professional service revenues, and 84% and 83% of our total revenues, respectively, consisted of insurance service revenues. We earn professional service revenues by processing HR transactions, such as payroll and employment tax withholding, and providing labor and benefit law compliance services, on behalf of our clients. We earn insurance service revenues by providing risk-based, third-party plans to our clients, primarily employee health benefit plans and workers compensation insurance.

For professional service revenues, we recognize as revenues the fees we earn for processing HR transactions, which fees do not include the payroll that is paid to us by the client and paid out to WSEs or remitted as taxes. We recognize as insurance service revenues all insurance-related billings and administrative fees collected from clients and withheld from WSEs for risk-based insurance plans provided through third-party insurance carriers, primarily employee health insurance and workers compensation insurance. We in turn pay premiums to third-party insurance carriers for these insurance benefits, as well as reimburse them for claim payments within our insurance deductible layer. These premiums and reimbursements are classified as insurance costs on our statements of operations. To augment our financial information prepared in accordance with U.S. generally accepted accounting principles, or GAAP, we use internally a non-GAAP financial measure, Net Insurance Service Revenues, which consists of insurance service revenues less insurance costs. We also use a measure of total non-GAAP revenue, or Net Service Revenues, which is the sum of

professional service revenues and Net Insurance Service Revenues. For the three months ended June 30, 2014 and 2013, 66% and 65% of our Net Service Revenues, respectively, consisted of professional service revenues and 34% and 35% of our Net Service Revenues, respectively, consisted of Net Insurance Service Revenues. For the six months ended June 30, 2014 and 2013, 65% and 63% of our Net Service Revenues, respectively, consisted of professional service revenues and 35% and 37% of our Net Service Revenues, respectively, consisted of Net Insurance Service Revenues.

We sell our services primarily through our direct sales force, which consists of sales representatives who focus on serving clients in specific industry vertical markets. For the three months ended June 30, 2014 and 2013, our sales and marketing expenses were \$35.0 million and \$25.4 million, respectively, or 7% and 7% of our total revenues and 28% and 27% of our Net Service Revenues, respectively. For the six months ended June 30, 2014 and 2013, our sales and marketing expenses were \$66.9 million and \$48.0 million, respectively, or 6% and 7% of our total revenues and 26% and 25% of our Net Service Revenues, respectively.

We have made significant investments in our proprietary, cloud-based technology platform, including implementing client information and management software to provide our clients with enhanced features and functionality with which to conduct their HR transactions, manage their employees and analyze employee benefits data. For the three months ended June 30, 2014 and 2013, our systems development and programming costs were \$6.6 million and \$5.6 million, respectively, or 1% and 2% of our total revenues and 5% and 6% of our Net Service Revenues, respectively. For the six months ended June 30, 2014 and 2013, our systems development and programming costs were \$12.5 million and \$10.1 million, respectively, or 1% and 1% of our total revenues and 5% and 5% of our Net Service Revenues, respectively.

Strategic Acquisitions

We operate in a highly fragmented industry and have completed numerous strategic acquisitions over the course of the past decade. We intend to continue to pursue strategic acquisitions that will enable us to add new clients and employees to our existing business and offer our clients and their employees more comprehensive and attractive services. Our operations could be adversely impacted if our strategic acquisitions are not integrated effectively. Because many of the companies we have acquired to date were focused on specific industries, our acquisitions have allowed us to expand our vertical service offerings into areas such as financial services, property management and food services, hospitality and manufacturing in which we did not previously have a significant presence. In addition, we have acquired sales representatives with experience in these vertical markets. Our acquisitions have provided us with additional clients and WSEs to allow us to continue to leverage our operations over a larger client base. These acquisitions have resulted in increased revenues and costs, as described below in our results of operations. We expect to continue to pursue strategic acquisitions.

Key Operating Metrics

We regularly review certain key operating metrics to evaluate growth trends, measure our performance and make strategic decisions. Our key operating metrics as of and for the three and six month periods ended June 30, 2014 and 2013 were as follows:

	Three Months Ended		Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
	2014	2013	2014	2013
Net Insurance Service Revenues (in thousands)	\$42,551	\$33,135	\$87,431	\$71,062
Net Service Revenues (in thousands)	\$124,811	\$94,215	\$252,566	\$191,373

Total WSEs	258,985	197,458
Total Sales Representatives	388	298

Total WSEs

We define Total WSEs at the end of a given fiscal period as the total number of WSEs paid in the last calendar month of the fiscal period. We believe that comparing our Total WSEs at the end of a fiscal period to that of prior periods is an indicator of our success in growing our business, both organically and through the integration of acquired businesses, and retaining clients, and that our Total WSEs paid in the last calendar month of the fiscal period is a leading indicator of our anticipated revenues for future fiscal periods.

Total Sales Representatives

Our direct sales force consists of sales representatives who focus on serving clients in specific industry vertical markets. We define Total Sales Representatives at the end of a given fiscal period as the total number of our direct sales force employees at that date. We believe that comparing our Total Sales Representatives at the end of a fiscal period to our Total Sales Representatives at the end of a prior fiscal period is an indicator of our success in growing our business, and that our Total Sales Representatives at the end of recent fiscal periods is a key indicator of our ability to increase our revenues in the following fiscal periods.

Net Insurance Service Revenues and Net Service Revenues

We define Net Insurance Service Revenues as insurance service revenues less insurance costs. We define Net Service Revenues as the sum of professional service revenues and Net Insurance Service Revenues. Our total revenues on a GAAP basis represent the total amount invoiced by us to our clients, net of direct pass-through costs such as payroll and payroll tax payments, for the services we provide to our clients. Our insurance costs include the premiums we pay to insurance carriers for the health and workers compensation insurance coverage provided to our clients and WSEs and the reimbursements we pay to the insurance carriers for claim payments within our insurance deductible layer. We act principally as the service provider to add value in the execution and procurement of these services to our clients. Net Insurance Service Revenues is the primary indicator of our ability to source, add value and offer benefit services to WSEs through third-party insurance carriers, and is considered by management to be a key performance measure. We believe that Net Service Revenues is also a key performance measure as it provides a useful measure of total revenues for the two main components of our revenues calculated on a consistent basis. In addition, management believes measuring operating costs as a function of Net Service Revenues provides a useful metric, as we believe it enables better evaluation of the performance of our business.

Non-GAAP Financial Results

We use Net Insurance Service Revenues, Net Service Revenues, Adjusted EBITDA and Adjusted Net Income to provide an additional view of our operational performance. Net Insurance Service Revenues, Net Service Revenues, Adjusted EBITDA and Adjusted Net Income are financial measures that are not prepared in accordance with GAAP. We define Net Insurance Service Revenues as insurance service revenues less insurance costs, which include the premiums we pay to insurance carriers for the health and workers compensation insurance coverage provided to our clients and WSEs and the reimbursements we pay to the insurance carriers for claim payments within our insurance deductible layer. We define Net Service Revenues as the sum of professional service revenues and Net Insurance Service Revenues. We define Adjusted EBITDA as net income, excluding the effects of our income tax provision, interest expense, depreciation, amortization of intangible assets and stock-based compensation expense. We define Adjusted Net Income as net income, excluding the effects of stock-based compensation, amortization of intangible assets, non-cash interest expense and the income tax effect of these pre-tax adjustments at our effective tax rate. For the six months ended June 30, 2014, the effective tax rate is adjusted to 39.5% to exclude income tax on non-deductible stock-based compensation and discrete items including the cumulative effect of state law changes. Non-cash interest expense represents amortization and write-off of our debt issuance costs and, for the six months ended June 30, 2014, a debt prepayment premium.

We believe that the use of Net Insurance Service Revenues provides useful information as it presents a measure of revenues from our provision of insurance services to our clients that eliminates the cost of insurance. We believe that Net Service Revenues provides a useful measure of total revenues for the two main components of our revenues calculated on a consistent basis. We believe that the use of Adjusted EBITDA and Adjusted Net Income provides additional period-to-period comparisons and analysis of trends in our business, as they exclude certain one-time and non-cash expenses. We believe that Net Insurance Service Revenues, Net Service Revenues, Adjusted EBITDA and Adjusted Net Income are useful for our stockholders and board of directors by helping them to identify trends in our business and understand how our management evaluates our business. We use Net Insurance Service Revenues, Net Service Revenues and Adjusted EBITDA to monitor and evaluate our operating results and trends on an ongoing basis and internally for operating, budgeting and financial planning purposes, in addition to allocating our resources to enhance the financial performance of our business and evaluating the effectiveness of our business strategies. We also use Net Service Revenues and Adjusted EBITDA in determining the incentive compensation for management.

Net Insurance Service Revenues, Net Service Revenues, Adjusted EBITDA and Adjusted Net Income are not prepared in accordance with, and should not be considered in isolation of, or as an alternative to, measurements required by GAAP. In addition, these non-GAAP measures are not based on any comprehensive set of accounting rules or principles. As non-GAAP measures, Net Insurance Service Revenues, Net Service Revenues, Adjusted

EBITDA and Adjusted Net Income have limitations in that they do not reflect all of the amounts associated with our results of operations as determined in accordance with GAAP. In particular:

- Net Insurance Service Revenues and Net Service Revenues are reduced by the insurance costs that we pay to the insurance carriers;
- Adjusted EBITDA does not reflect interest expense, or the cash requirements necessary to service interest or principal payments on our debt;
- Adjusted EBITDA does not reflect the amounts we paid in taxes or other components of our tax provision;
- Adjusted EBITDA does not reflect our cash expenditures or future requirements for capital expenditures or contractual commitments;
- Adjusted EBITDA and Adjusted Net Income do not reflect changes in, or cash requirements for, our working capital needs;
- Adjusted EBITDA and Adjusted Net Income do not reflect the non-cash component of employee compensation;

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- Although depreciation and amortization of intangible assets are non-cash charges, the assets being depreciated and amortized often will have to be replaced in the future, and Adjusted EBITDA does not reflect any cash requirements for such replacements; and
- Other companies in our industry may calculate –these measures or similar measures differently than we do, limiting their usefulness as a comparative measure.

Because of these limitations, you should consider Net Insurance Service Revenues, Net Service Revenues, Adjusted EBITDA and Adjusted Net Income alongside other financial performance measures, including total revenues, net income and our financial results presented in accordance with GAAP.

The table below sets forth a reconciliation of GAAP insurance service revenues to Net Insurance Service Revenues:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in thousands)			
Insurance service revenues	\$442,746	\$302,352	\$868,783	\$594,191
Less: Insurance costs	400,195	269,217	781,352	523,129
Net Insurance Service Revenues	\$42,551	\$33,135	\$87,431	\$71,062

The table below sets forth a reconciliation of GAAP total revenues to Net Service Revenues:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in thousands)			
Total revenues	\$525,006	\$363,432	\$1,033,918	\$714,502
Less: Insurance costs	400,195	269,217	781,352	523,129
Net Services Revenues	\$124,811	\$94,215	\$252,566	\$191,373

The table below sets forth a reconciliation of GAAP net income to Adjusted EBITDA:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in thousands)			
Net income	\$6,221	\$4,343	\$7,761	\$14,880
Provision for income taxes	4,923	2,713	6,911	8,680
Stock-based compensation	2,923	1,505	5,070	2,865
Interest expense and bank fees	8,860	7,037	30,712	12,189
Depreciation	3,242	2,726	6,460	5,552
Amortization of intangible assets	13,267	10,178	26,816	20,484
Adjusted EBITDA	\$39,436	\$28,502	\$83,730	\$64,650

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The table below sets forth a reconciliation of GAAP net income to Adjusted Net Income:

	Three Months		Six Months Ended	
	Ended June 30, 2014	2013	June 30, 2014	2013
	(in thousands)			
Net income	\$6,221	\$4,343	\$7,761	\$14,880
Effective income tax rate adjustment	521	-	1,116	-
Stock-based compensation	2,923	1,505	5,070	2,865
Amortization of intangible assets	13,267	10,178	26,816	20,484
Non-cash interest expense	1,380	684	7,486	1,297
Debt prepayment premium	-	-	3,800	-
Income tax impact of pre-tax adjustments at 39.5%	(6,940)	(4,658)	(17,053)	(9,282)
Adjusted Net Income	\$17,372	\$12,052	\$34,996	\$30,244

Impact of Health Care Reform

The Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010, which we refer to collectively as the Act, entail sweeping health care reforms with staggered effective dates from 2010 through 2018, and many provisions of the Act require the issuance of additional guidance from the U.S. Departments of Labor and Health and Human Services, the IRS and U.S. states. Beginning in 2014, a number of key provisions of the Act take effect, including the establishment of state insurance exchanges, insurance market reforms, “pay or play” penalties on applicable large employers and the imposition and assessment of excise taxes on the health insurance industry and reinsurance taxes on insurers and third-party administrators. Collectively, these items have the potential to significantly change the insurance marketplace for employers and how employers offer or provide insurance to employees.

We are not yet able to determine the impacts to our business, and to our clients, resulting from the Act. In future periods, the Act may result in increased costs to us and our clients and could affect our ability to attract and retain clients. Additionally, we may be limited or delayed in our ability to increase service fees to offset any associated potential increased costs resulting from compliance with the Act. Furthermore, the uncertainty surrounding the terms and application of the Act may delay or inhibit the decisions of potential clients to outsource their HR needs. As a result, these changes could have a negative impact on our operating results.

Seasonality

Historically, we have experienced our highest monthly addition of WSEs, as well as our highest monthly levels of client attrition, in the month of January, primarily because clients that change their payroll service providers tend to do so at the beginning of a calendar year. In addition, we experience higher levels of client attrition in connection with renewals of the health insurance we provide for our WSEs, in the event that such renewals result in increased premiums that we pass on to our clients. We have also historically experienced higher insurance claim volumes in the second and third quarters of a fiscal year than in the first and fourth quarters of a fiscal year, as WSEs typically access their health care providers more often in the second and third quarters of a fiscal year, which has negatively impacted our insurance costs in these quarters. These historical trends may change, and other seasonal trends may develop that make it more difficult for us to manage our business.

Basis of Presentation and Key Components of Our Results of Operations

Total Revenues

Our total revenues consist of professional service revenues and insurance service revenues.

We earn professional service revenues by processing HR transactions, such as payroll and employment tax withholding, payment to WSEs, and labor and benefit law compliance, on behalf of our clients. Our clients pay us these fees based on either a fixed fee per WSE per month or per transaction, or a percentage of the WSE's payroll cost, pursuant to written professional services agreements that are generally cancelable by us or our clients upon 30 days' prior written notice. We also earn professional service revenues by providing strategic HR services to our clients, such as talent acquisition, performance management and time and expense reporting services. Our clients pay us professional service fees for these services based on separate written agreements.

We earn insurance service revenues by providing risk-based, third-party plans to our clients, primarily employee health benefit plans and workers compensation insurance. Insurance service revenues consist of insurance-related billings and administrative fees. We recognize as insurance service revenues insurance-related billings and administrative fees collected from clients and withheld from WSEs for risk-based insurance plans provided through third-party insurance carriers, primarily employee health insurance and

workers compensation insurance. We in turn pay premiums to third-party insurance carriers for these insurance benefits, as well as reimburse them for claim payments within our insurance deductible layer. These premiums and reimbursements are classified as insurance costs on our statements of operations.

Our clients pay us administrative fees, typically based on a percentage of insurance-related amounts, collected from clients and withheld from WSEs, primarily in exchange for our administration of employee health benefit plans.

Insurance Costs

Insurance costs include the premiums we pay to the insurance carriers for the health and workers compensation insurance coverage provided to the clients and WSEs and the reimbursements we pay to the insurance carriers for claim payments made to the WSEs within the insurance deductible layer.

Our insurance costs are, in part, a function of the type and terms of agreements that we enter into with the insurance carriers that provide fully-insured coverage for our WSEs. Our future premiums under these, or ensuing, policies will be influenced by the WSE claims activity in prior periods. The remainder of the health insurance policies and all of the workers compensation insurance policies that we provide to our clients are policies with respect to which we agree to reimburse our carriers for any claims that they pay within our deductible layer. Under these policies, WSEs file claims with the carriers, which are responsible for paying the claims up to the maximum coverage under the policies. The carriers then seek reimbursement from us up to our deductible per incident for workers compensation claims, or up to a cap for health insurance claims in accordance with the terms of the underlying health insurance policies. In no event are we liable to pay the claims directly to WSEs. As we evaluate the claims experience for each fiscal period, we adjust, as we deem necessary, our workers compensation and health benefits reserves, and this in turn has a corresponding impact on our insurance costs. As a result, our insurance costs fluctuate from period to period depending on the number and severity of the claims incurred by our WSEs. We expect our insurance costs to continue to increase in absolute dollars on an annual basis for the foreseeable future due to expected growth in WSEs.

Cost of Providing Services

Cost of providing services consists primarily of costs incurred by us associated with direct customer support, such as payroll and benefits processing, professional HR consultants, employee liability insurance and costs associated with defending clients in employment-related legal claims, benefits and risk management, postage and shipping expenses and consulting expenses. We expect our cost of providing services to continue to increase in absolute dollars on an annual basis for the foreseeable future due to expected growth in WSEs, partially offset by improved efficiencies, although these expenses may fluctuate as a percentage of our total revenues from period to period depending on the timing of those expenses.

Sales and Marketing Expenses

Sales and marketing expenses consist primarily of salaries, commissions and related variable compensation expenses, commission payments to partners and the cost of marketing programs. Marketing programs consist of advertising, lead generation, marketing events, corporate communications, brand building and product marketing activities, as well as various incentivized partnership and referral programs. We expect our sales and marketing expenses to continue to increase, both in absolute dollars and as a percentage of our total revenues on an annual basis, for the foreseeable future as we expand our sales force and our other sales and marketing efforts to build our brand, although these expenses may fluctuate as a percentage of our total revenues from period to period depending on the timing of those expenses.

General and Administrative Expenses

General and administrative expenses consist primarily of compensation-related expenses, legal and other professional services fees and other general corporate expenses. We expect our general and administrative expenses to continue to increase in absolute dollars for the foreseeable future due to increases in our legal and financial compliance costs in connection with being a newly public company, although these expenses may fluctuate as a percentage of our total revenues from period to period depending on the timing of those expenses.

Systems Development and Programming Costs

Systems development and programming costs consist primarily of compensation-related expenses for our employees and contractors dedicated to systems development and programming, as well as fees that we pay to third-party consulting firms. We expect our systems development and programming costs to continue to increase modestly in absolute dollars for the foreseeable future as we continue to invest in and improve our technology platform. However, over time, we expect our systems development and programming costs to remain relatively consistent as a percentage of our total revenues on an annual basis, although these costs may fluctuate as a percentage of our total revenues from period to period depending on when we incur those costs.

Amortization of Intangible Assets

Amortization of intangible assets represents costs associated with an acquired company's developed technologies, client lists, trade names and contractual agreements. We amortize these intangibles over their respective estimated useful lives using either the straight-line method or the accelerated method.

Depreciation

Depreciation consists primarily of amortization of the cost of software and furniture, fixtures and equipment.

Other Income (Expense)

Other income (expense) consists primarily of interest expense under our credit facility and capital leases, debt issuance cost amortization, and a prepayment premium.

Provision for Income Taxes

We are subject to taxation in the United States and Canada. We conduct our business primarily in the United States, and all of our clients are U.S. employers. However, we provide services to certain clients with employees in Canada. The percentage of our total revenues attributable to WSEs in Canada was less than 1% in 2013 and for the three and six months ended June 30, 2014. Our effective tax rate differs from the statutory rate primarily due to state taxes, tax credits, non-deductible charges and changes in uncertain tax positions. We make estimates and judgments about our future taxable income based on assumptions that are consistent with our plans and estimates. Should the actual amounts differ from our estimates, the amount of our valuation allowance could be materially affected.

Income taxes are computed using the asset and liability method, under which deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. Changes in valuation allowances are reflected as a component of provision for income taxes.

Critical Accounting Policies, Estimates and Judgments

Our consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles, or GAAP. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. These estimates include, but are not limited to, allowances for accounts receivable, workers compensation related assets and liabilities, health plan assets and liabilities, recoverability of goodwill and other intangible assets, income taxes, stock-based compensation and other contingent liabilities. Such estimates are based on historical experience and on various other assumptions that Company management believes to be reasonable under the circumstances. Actual results could differ significantly from our estimates. To the extent that there are material differences between these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected.

This Quarterly Report on Form 10-Q should be read in conjunction with the consolidated financial statements and accompanying notes included in the Company's prospectus filed with the SEC pursuant to Rule 424(b) under the Securities Act of 1933 with the SEC on March 27, 2014. There have been no material changes to our critical accounting policies described in the prospectus for the year ended December 31, 2013.

Recent Accounting Pronouncements

In June 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-12—Compensation-Stock Compensation, which requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. ASU 2014-12 is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2015. Early adoption is permitted. The amendments may be applied prospectively to all awards granted or modified after the effective date or retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented. We do not expect this guidance to have a material effect on our consolidated financial statements. We expect to adopt this guidance in 2016.

In May 2014, the FASB issued ASU 2014-09—Revenue from Contracts with Customers, which will replace most existing revenue recognition guidance under GAAP. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard provides a five-step analysis of transactions to determine when and how revenue is recognized. ASU 2014-09 is effective for annual reporting periods, and interim periods within those years, beginning after

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December 15, 2016. Early adoption is not permitted. The amendments may be applied retrospectively or as a cumulative-effect adjustment as of the date of adoption. We expect to adopt this guidance in 2017. We have not yet selected a method of adoption and are currently evaluating the effect that the amendments will have on our consolidated financial statements.

In July 2013, the FASB issued ASU 2013-11—Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists, which requires that an unrecognized tax benefit, or portion of an unrecognized tax benefit, be presented as a reduction of a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. If an applicable deferred tax asset is not available or a company does not expect to use the applicable deferred tax asset, the unrecognized tax benefit should be presented as a liability in the financial statements and should not be combined with an unrelated deferred tax asset. ASU 2013-11 is effective for annual reporting periods, and interim periods within those years, beginning after December 15, 2013. The amendments should be applied prospectively to all unrecognized tax benefits that exist at the effective date, however retrospective application is permitted. We adopted this guidance in 2014. The adoption of ASU 2013-11 did not have a material impact on our consolidated financial statements.

Results of Operations

The following tables set forth our results of operations for the periods presented and as a percentage of our total revenues and Net Service Revenues for those periods. Period-to-period comparisons of our financial results are not necessarily indicative of financial results to be achieved in future periods.

	Three Months Ended		Six Months Ended	
	June 30,	2013	June 30,	2013
	2014		2014	
Consolidated Statement of Operations:				
(in thousands)				
Professional service revenues	\$82,260	\$61,080	\$165,135	\$120,311
Insurance service revenues	442,746	302,352	868,783	594,191
Total revenues	525,006	363,432	1,033,918	714,502
Costs and operating expenses:				
Insurance costs	400,195	269,217	781,352	523,129
Cost of providing services (exclusive of depreciation and amortization of intangible assets) ⁽¹⁾	34,034	23,671	67,677	46,486
Sales and marketing ⁽¹⁾	34,992	25,389	66,829	48,020
General and administrative ⁽¹⁾	12,682	12,741	27,019	25,228
Systems development and programming costs ⁽¹⁾	6,565	5,578	12,459	10,088
Amortization of intangible assets	13,267	10,178	26,816	20,484
Depreciation	3,242	2,726	6,460	5,552
Total costs and operating expenses	504,977	349,500	988,612	678,987
Operating income	20,029	13,932	45,306	35,515
Other income (expense):				
Interest expense and bank fees	(8,860)	(7,037)	(30,712)	(12,189)
Other, net	(25)	161	78	234
Income before provision for income taxes	11,144	7,056	14,672	23,560
Provision for income taxes	4,923	2,713	6,911	8,680
Net income	\$6,221	\$4,343	\$7,761	\$14,880

(1) Includes stock-based compensation expense as follows:

	Three Months Ended June 30, 2014		Six Months Ended June 30, 2014	
	2013	2013	2013	2013
	(in thousands)			
Cost of providing services (exclusive of depreciation and amortization of intangible assets)	\$801	\$269	\$1,255	\$516
Sales and marketing	774	359	1,291	632
General and administrative	1,045	767	2,053	1,520
Systems development and programming costs	303	110	471	197
Total stock-based compensation expense	\$2,923	\$1,505	\$5,070	\$2,865

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	Three Months		Six Months	
	Ended June 30,		Ended June 30,	
	2014	2013	2014	2013
Percentage of total revenues:				
Professional service revenues	16 %	17 %	16 %	17 %
Insurance service revenues	84 %	83 %	84 %	83 %
Total revenues	100 %	100 %	100 %	100 %
Costs and operating expenses:				
Insurance costs	76 %	74 %	76 %	73 %
Cost of providing services (exclusive of depreciation and				
amortization of intangible assets)	6 %	7 %	7 %	7 %
Sales and marketing	7 %	7 %	6 %	7 %
General and administrative	2 %	4 %	3 %	4 %
Systems development and programming costs	1 %	2 %	1 %	1 %
Amortization of intangible assets	3 %	3 %	3 %	3 %
Depreciation	1 %	1 %	1 %	1 %
Total costs and operating expenses	96 %	96 %	96 %	95 %
Operating income	4 %	4 %	4 %	5 %
Other income (expense):				
Interest expense and bank fees	(2 %)	(2 %)	(3 %)	(2 %)
Other, net	(0 %)	0 %	0 %	0 %
Income before provision for income taxes	2 %	2 %	1 %	3 %
Provision for income taxes	1 %	1 %	1 %	1 %
Net income	1 %	1 %	1 %	2 %

	Three Months		Six Months	
	Ended June 30,		Ended June 30,	
	2014	2013	2014	2013
Percentage of Net Service Revenues:				
Professional service revenues	66 %	65 %	65 %	63 %
Net Insurance Service Revenues	34 %	35 %	35 %	37 %
Net Service Revenues	100 %	100 %	100 %	100 %
Other operating expenses:				
Cost of providing services (exclusive of depreciation and				
amortization of intangible assets)	27 %	25 %	27 %	24 %
Sales and marketing	28 %	27 %	26 %	25 %
General and administrative	10 %	14 %	11 %	13 %
Systems development and programming costs	5 %	6 %	5 %	5 %
Amortization of intangible assets	11 %	11 %	11 %	11 %
Depreciation	3 %	3 %	3 %	3 %
Total other operating expenses	84 %	85 %	82 %	81 %
Operating income	16 %	15 %	18 %	19 %
Other income (expense):				
Interest expense and bank fees	(7 %)	(7 %)	(12 %)	(6 %)
Other, net	(0 %)	0 %	0 %	0 %
Income before provision for income taxes	9 %	7 %	6 %	12 %
Provision for income taxes	4 %	3 %	3 %	5 %

Net income	5	%	5	%	3	%	8	%
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Three and Six Months Ended June 30, 2014 and 2013

Total Revenues

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	\$	%	June 30, 2014	2013	\$	%
	(in thousands, except percentages)							
Professional service revenues	\$82,260	\$61,080	\$21,180	35%	\$165,135	\$120,311	\$44,824	37%
Insurance service revenues	442,746	302,352	140,394	46%	868,783	594,191	274,592	46%
Total revenues	\$525,006	\$363,432	\$161,574	44%	\$1,033,918	\$714,502	\$319,416	45%

Key operating metrics:

Total WSEs	258,985	197,458	61,527	31%
Total Sales Representatives	388	298	90	30%

Total revenues increased by \$161.6 million, or 44%, and \$319.4 million, or 45%, for the three and six months ended June 30, 2014, respectively, compared to the same period of prior year. Professional service revenues and insurance service revenues represented 16% and 84%, respectively, of total revenues for the three and six months ended June 30, 2014, compared to 17% and 83%, respectively, of total revenues in the same period of the prior year. The increase in total revenues was attributable to the significant growth of our Total WSEs and revenues from our acquisition of Ambrose Employer Group, LLC, or Ambrose, in the third quarter of 2013, as further described below.

Professional service revenues for the three months ended June 30, 2014 increased by \$21.2 million, or 35%, compared to the same period of the prior year. The increase was mainly attributable to our increase in Total WSEs and our acquisition of Ambrose in third quarter of 2013, which accounted for \$8.5 million of professional service revenues during the three months ended June 30, 2014.

Professional service revenues for the six months ended June 30, 2014 increased by \$44.8 million, or 37%, compared to the same period of the prior year. The increase was mainly attributable to our increase in Total WSEs and our acquisition of Ambrose in third quarter of 2013, which accounted for \$15.4 million of professional service revenues during the six months ended June 30, 2014. In addition, we received a \$2.3 million refund related to prior year payroll taxes in the six months ended June 30, 2014.

Insurance service revenues increased by \$140.4 million, or 46%, and by \$274.6 million, or 46%, for the three and six months ended June 30, 2014, respectively, compared to the same period of the prior year. The increase was primarily due to our increase in Total WSEs, and our acquisition of Ambrose, which accounted for \$63.9 million and \$130.4 million of insurance service revenues during the three and six months ended June 30, 2014, respectively.

Total WSEs at June 30, 2014 increased by 61,527, or 31%, compared to Total WSEs at June 30, 2013, with approximately 13,000 of such increase due to the Ambrose acquisition. Our Total Sales Representatives increased from 298 at June 30, 2013 to 388 at June 30, 2014, 12 of which we acquired from Ambrose.

Insurance Costs

	Three months ended	Change	Six months ended	Change
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June 30,		2014 vs. 2013		June 30,		2014 vs. 2013	
2014	2013	\$	%	2014	2013	\$	%

(in thousands, except percentages)

Insurance costs	\$400,195	\$269,217	\$130,978	49%	\$781,352	\$523,129	\$258,223	49%
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Insurance costs increased \$131.0 million, or 49%, for the three months ended June 30, 2014 compared to the same period of the prior year, \$59.0 million of which is due to our acquisition of Ambrose. The remaining increase resulted from an increase in Total WSEs other than those acquired from Ambrose and a 2% increase in average insurance costs per WSE other than those acquired from Ambrose.

Insurance costs increased \$258.2 million, or 49%, for the six months ended June 30, 2014 compared to the same period of the prior year, \$118.6 million of which is due to our acquisition of Ambrose. The remaining increase resulted from an increase in Total WSEs other than those acquired from Ambrose and a 2% increase in average insurance costs per WSE other than those acquired from Ambrose.

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Net Insurance Service Revenues and Net Service Revenues

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	2014 vs. 2013	%	June 30, 2014	2013	2014 vs. 2013	%
	(in thousands, except percentages)							
Insurance service revenues	\$442,746	\$302,352	\$140,394	46%	\$868,783	\$594,191	\$274,592	46%
Less: Insurance costs	400,195	269,217	130,978	49%	781,352	523,129	258,223	49%
Net Insurance Service Revenues	\$42,551	\$33,135	\$9,416	28%	\$87,431	\$71,062	\$16,369	23%

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	2014 vs. 2013	%	June 30, 2014	2013	2014 vs. 2013	%
	(in thousands, except percentages)							
Total revenues	\$525,006	\$363,432	\$161,574	44%	\$1,033,918	\$714,502	\$319,416	45%
Less: Insurance costs	400,195	269,217	130,978	49%	781,352	523,129	258,223	49%
Net Service Revenues	\$124,811	\$94,215	\$30,596	32%	\$252,566	\$191,373	\$61,193	32%

For the reasons set forth above with respect to the increases in our insurance service revenues and total revenues, our Net Insurance Service Revenues increased by \$9.4 million, or 28%, and by \$16.4 million, or 23% for the three and six months ended June 30, 2014, respectively, as compared to the same period of the prior year. Similarly, our Net Service Revenues increased by \$30.6 million, or 32%, and by \$61.2 million, or 32%, for the three and six months ended June 30, 2014, respectively, as compared to the same period of the prior year.

Other Operating Expenses

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	2014 vs. 2013	%	June 30, 2014	2013	2014 vs. 2013	%
	(in thousands, except percentages)							
Cost of providing services	\$34,034	\$23,671	\$10,363	44%	\$67,677	\$46,486	\$21,191	46%
Sales and marketing	34,992	25,389	9,603	38%	66,829	48,020	18,809	39%
General and administrative	12,682	12,741	(59)	(0%)	27,019	25,228	1,791	7%
System development and programming costs	6,565	5,578	987	18%	12,459	10,088	2,371	24%
Amortization of intangible assets	13,267	10,178	3,089	30%	26,816	20,484	6,332	31%
Depreciation	3,242	2,726	516	19%	6,460	5,552	908	16%
Total operating expenses	\$104,782	\$80,283	\$24,499	31%	\$207,260	\$155,858	\$51,402	33%

Cost of Providing Services

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	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	\$	%	June 30, 2014	2013	\$	%
	(in thousands, except percentages)							
Compensation-related costs	\$24,924	\$16,474	\$8,450	51%	\$49,019	\$32,873	\$16,146	49%
Facilities	1,770	1,173	597	51%	3,381	2,384	997	42%
Information technology and communication	2,022	1,943	79	4%	4,517	3,559	958	27%
Other expenses	5,318	4,081	1,237	30%	10,760	7,670	3,090	40%
Total cost of providing services	\$34,034	\$23,671	\$10,363	44%	\$67,677	\$46,486	\$21,191	46%

Cost of providing services for the three months ended June 30, 2014 increased by \$10.4 million, or 44%, compared to the same period of the prior year, due in part to our acquisition of Ambrose, which accounted for \$2.9 million of the increase. Compensation-related costs increased by \$8.5 million due to increased headcount, including \$2.1 million from our acquisition of Ambrose. Facilities-related costs increased by \$0.6 million due to our acquisition of Ambrose. The remainder of the increase was due to an increase in WSEs other than those that we acquired from Ambrose. Cost of providing services has decreased to 6% of total revenues in the three

months ended June 30, 2014, from 7% of total revenues in the same period of the prior year. Cost of providing services increased to 27% of Net Service Revenues in the three months ended June 30, 2014 from 25% of Net Service Revenues, in the same period of the prior year. The increase was due to costs associated with the integration of our recently acquired subsidiaries.

Cost of providing services for the six months ended June 30, 2014 increased by \$21.2 million, or 46%, compared to the same period of the prior year, due in part to our acquisition of Ambrose, which accounted for \$4.9 million of the increase. Compensation-related costs increased by \$16.1 million due to increased headcount, including \$4.0 million from our acquisition of Ambrose. Facilities-related costs increased by \$1.0 million due to our acquisition of Ambrose. The remainder of the increase was due to an increase in WSEs other than those that we acquired from Ambrose. Cost of providing services remained at 7% of total revenues for the six months ended June 30, 2014 compared to the same period of the prior year. Cost of providing services has increased to 27% of Net Service Revenues in the six months ended June 30, 2014, from 24% of Net Service Revenues in the same period of the prior year. The increase was due to costs associated with the integration of our recently acquired subsidiaries.

Sales and Marketing

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	\$	%	June 30, 2014	2013	\$	%
	(in thousands, except percentages)							
Compensation-related costs	\$24,426	\$17,261	\$7,165	42%	\$47,720	\$33,154	\$14,566	44%
Marketing and advertising	4,678	3,729	949	25%	8,581	7,126	1,455	20%
Facilities	939	836	103	12%	1,713	1,669	44	3%
Other expenses	4,949	3,563	1,386	39%	8,815	6,071	2,744	45%
Total sales and marketing	\$34,992	\$25,389	\$9,603	38%	\$66,829	\$48,020	\$18,809	39%

Sales and marketing expenses for the three months ended June 30, 2014 increased by \$9.6 million, or 38%, compared to the same period of the prior year. Of this increase, \$7.2 million was due to compensation-related costs, including \$1.3 million from our acquisition of Ambrose and \$5.9 million from our growth in direct sales channels, primarily the addition of new sales representatives. Marketing and advertising expenses increased \$0.9 million, or 25%, primarily due to our acquisition of Ambrose. Other expenses increased \$1.4 million, or 39%, primarily due to increased sales travel, meeting and conference activities, as well as other expenses associated with recruiting efforts and information technology. Sales and marketing expenses as a percentage of total revenues remained unchanged at 7% in the three months ended June 30, 2014 and 2013. As a percentage of Net Service Revenues, sales and marketing expenses increased to 28% in the three months ended June 30, 2014, from 27% in the same period of the prior year, mainly due to investment in growing our sales organization, which resulted in our sales and marketing expenses outpacing the growth in Net Service Revenues.

Sales and marketing expenses for the six months ended June 30, 2014 increased by \$18.8 million, or 39%, compared to the same period of the prior year. Of this increase, \$14.6 million was due to compensation-related costs, including \$2.9 million from our acquisition of Ambrose and \$11.7 million from our growth in direct sales channels, primarily the addition of new sales representatives. Marketing and advertising expenses increased \$1.5 million, or 20%, primarily due to our acquisition of Ambrose. Other expenses increased \$2.7 million, or 45%, primarily due to increased sales travel, meeting and conference activities, as well as other expenses associated with recruiting efforts and information technology. Sales and marketing expenses as a percentage of total revenues decreased to 6% in the

six months ended June 30, 2014, from 7% in the same period of prior year. As a percentage of Net Service Revenues, sales and marketing expenses increased to 26% in the six months ended June 30, 2014, from 25% in the same period of the prior year, mainly due to investment in growing our sales organization, which resulted in our sales and marketing expenses outpacing the growth in Net Service Revenues.

General and Administrative

	Three months ended		Change 2014 vs. 2013		Six months ended		Change 2014 vs. 2013	
	June 30, 2014	2013	\$	%	June 30, 2014	2013	\$	%
	(in thousands, except percentages)							
Compensation-related costs	\$8,212	\$8,232	\$(20)	(0 %)	\$16,707	\$16,103	\$604	4 %
Legal and professional fees	1,133	1,632	(499)	(31 %)	3,066	3,590	(524)	(15 %)
Other expenses	3,337	2,877	460	16 %	7,246	5,535	1,711	31 %
Total general and administrative	\$12,682	\$12,741	\$(59)	(0 %)	\$27,019	\$25,228	\$1,791	7 %

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General and administrative expenses for the three months ended June 30, 2014 increased by \$0.1 million, or 0%, compared to the same period of the prior year. Compensation-related costs were flat compared to the same period of the prior year. Legal and professional fees decreased by \$0.5, or 31%, as a result of lower costs incurred in relation to employment and corporate matters. Other expenses increased \$0.5 million, or 16%, primarily due to costs associated with the integration of our recently acquired subsidiaries. General and administrative expenses decreased to 2% of total revenues, or 10% of Net Service Revenues, in the three months ended June 30, 2014, from 4% of total revenues, or 14% of Net Service Revenues, in the same period of the prior year as a result of efficiencies realized subsequent to our acquisitions.

General and administrative expenses for the six months ended June 30, 2014 increased by \$1.8 million, or 7%, compared to the same period of the prior year. Compensation-related costs increased by \$0.6 million, or 4%, compared to the same period of the prior year, which was attributable to an increase in headcount primarily related to our acquisition of Ambrose. Legal and professional fees decreased by \$0.5 million, or 15%, as a result of as a result of lower costs incurred in relation to employment and corporate matters. Other expenses increased \$1.7 million, or 31%, primarily due to costs associated with the integration of our recently acquired subsidiaries. General and administrative expenses decreased to 3% of total revenues, or 11% of Net Service Revenues, in the six months ended June 30, 2014, from 4% of total revenues, or 13% of Net Service Revenues, in the same period of the prior year as a result of an increase in revenues as well as efficiencies realized subsequent to our acquisitions.

Systems Development and Programming

	Three months ended				Six months ended			
	June 30, 2014		June 30, 2013		June 30, 2014		June 30, 2013	
			Change 2014 vs. 2013				Change 2014 vs. 2013	
	\$	\$	\$	%	\$	\$	\$	%
(in thousands, except percentages)								
Compensation-related costs	\$5,450	\$4,238	\$1,212	29 %	\$10,310	\$7,552	\$2,758	37 %
Other expenses	1,115	1,340	(225)	(17 %)	2,149	2,536	(387)	(15 %)
Total systems development and programming costs	\$6,565	\$5,578	\$987	18 %	\$12,459	\$10,088	\$2,371	24 %

Our systems development and programming costs for the three months ended June 30, 2014 increased by \$1.0 million, or 18%, compared to the same period of the prior year. The increase was due to a \$1.2 million increase in compensation-related costs resulting from the increase in headcount including those we acquired from Ambrose, to support and enhance our technology product delivery. Despite these increases, systems development and programming costs decreased to 1% of total revenues, or 5% of Net Service Revenues, in the three months ended June 30, 2014, from 2% of total revenues, or 6% of Net Service Revenues, in the same period of the prior year as a result of an increase in revenues.

Our systems development and programming costs for the six months ended June 30, 2014 increased by \$2.4 million, or 24%, compared to the same period of the prior year. Of this increase, \$0.5 million was attributable to increased headcount from our acquisition of Ambrose. The remaining increase was due to a \$2.3 million increase in compensation-related costs resulting from the increase in headcount, other than those we acquired from Ambrose, to support and enhance our technology product delivery. Systems development and programming costs remained unchanged at 1% of total revenues, or 5% of Net Service Revenues, in the six months ended June 30, 2014.

Amortization of Intangible Assets and Depreciation

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	2014 vs. 2013	%	June 30, 2014	2013	2014 vs. 2013	%
	(in thousands, except percentages)							
Amortization of intangible assets	\$13,267	\$10,178	\$3,089	30%	\$26,816	\$20,484	\$6,332	31%
Depreciation	\$3,242	\$2,726	\$516	19%	\$6,460	\$5,552	\$908	16%

Our amortization of intangible assets increased by \$3.1 million, or 30%, and by \$6.3 million, or 31%, for the three and six months ended June 30, 2014, respectively, compared to the same period of the prior year. The increase was primarily attributable to our acquisition of Ambrose. Depreciation expense increased by \$0.5 million, or 19%, and by \$0.9 million, or 16%, for the three and six months ended June 30, 2014, respectively, compared to the same period of the prior year, primarily attributable to depreciation from our acquisition of Ambrose.

Other Income (Expense)

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	2014 vs. 2013	%	June 30, 2014	2013	2014 vs. 2013	%
	(in thousands, except percentages)							
Interest expense and bank fees	\$ (8,860)	\$ (7,037)	\$ (1,823)	26%	\$ (30,712)	\$ (12,189)	\$ (18,523)	152%

Other income (expense) was primarily the result of interest expense under our credit facilities. In October 2012, we amended and restated our secured credit facility to provide for total borrowings of \$350.0 million, which was amended again in April 2013 to provide for total borrowings of \$500.0 million. In August 2013, we entered into two new senior secured credit facilities for total borrowings of \$820.0 million to pay off our previous credit facilities and pay a special dividend. In March 2014, the Company repaid \$216.6 million of these facilities from its IPO proceeds. Interest expense increased in the three and six months ended June 30, 2014 due to a \$5.0 million charge related to the acceleration of loan fee amortization due to our refinancing activities, a \$3.8 million prepayment premium related to our partial repayment of the credit facilities during the period, and an increase in interest expense resulting from the higher debt level.

Provision for Income Taxes

	Three months ended		Change		Six months ended		Change	
	June 30, 2014	2013	2014 vs. 2013	%	June 30, 2014	2013	2014 vs. 2013	%
	(in thousands, except percentages)							
Provision for income taxes	\$ 4,923	\$ 2,713	\$ 2,210	81%	\$ 6,911	\$ 8,680	\$ (1,769)	(20%)
Effective tax rates	44.2 %	38.4 %			47.1 %	36.8 %		

Our provision for income taxes for the three months ended June 30, 2014 increased by \$2.2 million compared to the same period of the prior year, primarily due to the increase in our pre-tax income. Our effective tax rate (ETR) increased from 38.4% for the three months ended June 30, 2013 to 44.2% for the three months ended June 30, 2014, primarily due to non-deductible stock-based compensation related to February 2014 stock option grants, and to the implementation of an employee stock purchase plan which went into effect on March 26, 2014. The remainder of the increase is primarily due to the expiration of the federal research and development tax credit in 2014.

Our provision for income taxes for the six months ended June 30, 2014 decreased by \$1.8 million compared to the same period of the prior year, primarily due to a decrease in our pre-tax income. Our effective tax rate increased from 36.8% for the six months ended June 30, 2013 to 47.1% for the six months ended June 30, 2014, primarily due to non-deductible stock-based compensation related to February 2014 stock option grants, and to the implementation of an employee stock purchase plan which went into effect on March 26, 2014 and to a discrete tax charge of \$0.5 million, for the revaluation of deferred taxes, based on a regulatory state tax change enacted during the three months ended March 31, 2014. The remainder of the increase is primarily due to the expiration of the federal research and development tax credit in 2014, as well as a release of uncertain tax positions recognized for the three months ended

March 31, 2013.

Liquidity and Capital Resources

Our principal source of liquidity for operations is derived from cash provided by operating activities. We rely on cash provided by operating activities to meet our short-term liquidity requirements, which primarily relate to the payment of corporate payroll and other operating costs, and capital expenditures. Our credit facilities have been used to fund acquisitions and dividends, and we have not relied on these facilities to provide liquidity for our operations. Our cash flow related to WSE payroll and benefits is generally matched by advance collection from our clients. To minimize the credit risk associated with remitting the payroll and associated taxes and benefits costs, we require clients to prefund the payroll and related payroll taxes and benefits costs. To the extent this does not occur, our results of operations and cash flow may be negatively impacted.

WSE-related liabilities can fluctuate significantly due to various factors, including the day of the week on which a client payroll period ends, the existence of holidays at or immediately following a client payroll period-end and various federal and state compliance calendars. We report the advance collection from our clients as payroll funds collected within WSE-related assets on our balance sheet. Our cash and cash equivalents reported on our balance sheet represent our corporate cash available to meet corporate liquidity requirements, capital spending and expansion plans, potential acquisitions, debt service requirements and other corporate operating cash needs.

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Cash Flows

We generated positive cash flows from operating activities during the six months ended June 30, 2014 and 2013. We also have the ability to generate cash through our financing arrangements under our credit facility to meet short-term funding requirements related to WSE-related obligations. The following table shows our cash flows from operating activities, investing activities and financing activities for the stated periods:

	Six Months Ended June 30,	
	2014	2013
	(in thousands)	
Net cash provided by (used in):		
Operating activities	\$53,657	\$60,554
Investing activities	(25,498)	(10,905)
Financing activities	(22,228)	139,106
Effect of exchange rates on cash and cash equivalents	1	(39)
Net increase in cash and cash equivalents	\$5,932	\$188,716

Cash Flows from Operating Activities

Net cash provided by operating activities was \$53.7 million and \$60.6 million for the six months ended June 30, 2014 and 2013, respectively. Historically, cash provided by operating activities has been affected by our net income, adjusted for non-cash expense items (such as depreciation, amortization of intangible assets, deferred income taxes, expense associated with stock-based compensation) and changes in working capital accounts. The fluctuation in our working capital accounts was primarily driven by WSE-related assets and liabilities.

Cash Flows from Investing Activities

Net cash used in investing activities was \$25.5 million for the six months ended June 30, 2014, as compared to \$10.9 million in the same period of the prior year. In the six months ended June 30, 2014, we invested \$16.8 million in debt securities compared to \$6.8 million for the same period of 2013. Investments to purchase property and equipment were \$8.7 million for the six months ended June 30, 2014 compared to \$4.7 million for the same period of 2013.

Cash Flows from Financing Activities

Net cash used in financing activities was \$22.2 million for the six months ended June 30, 2014, compared to \$139.1 million in the same period of the prior year. Net cash provided by financing activities during the six months ended June 30, 2014 was attributable to \$219.2 million of net proceeds received from the issuance of common stock in our IPO and exercise of stock options, offset by \$243.0 million in loan repayments. Net cash provided by financing activities during the six months ended June 30, 2013 was attributable to the borrowing of \$150.0 million from our credit facility in connection with our acquisition of Ambrose, partially offset by \$6.1 million in common stock repurchases and \$4.9 million in loan repayments.

2014 Credit Facility

In August 2013, we, as guarantor, our subsidiary TriNet HR Corporation, as borrower, and certain of our other subsidiaries as subsidiary guarantors entered into two senior secured credit facilities: (i) a \$705.0 million first lien credit facility with JPMorgan Chase Bank, N.A., as administrative agent, and (ii) a \$190.0 million second lien credit

facility with Wilmington Trust, National Association, as administrative agent. Proceeds from our IPO were used to fully repay the \$190.0 million second lien credit facility, which resulted in a prepayment premium of \$3.8 million, and to repay \$25.0 million of the first lien credit tranche B-1 term loan. Additionally, the remaining balance of the loan fees associated with the second lien credit facility and a portion of the loan fees associated with the first lien credit facility were fully amortized in March 2014 for a charge of \$5.0 million. On July 9, 2014, we amended and restated our first lien credit facility pursuant to an amended and restated first lien credit agreement, or the Amended and Restated Credit Agreement.

The amended and restated credit agreement provides for: (i) \$375 million principal amount of “tranche A term loans,” (ii) \$200 million principal amount of “tranche B term loans,” and (iii) a revolving credit facility of \$75 million, which we refer to as the revolving credit facility. The proceeds of the tranche A term loans were used to refinance in part the tranche B-2 term loans outstanding under the original first lien credit facility. The proceeds of the tranche B term loans were used to (i) refinance the remaining tranche B-2 term loans outstanding under the original first lien credit facility, (ii) refinance other amounts outstanding under the original first lien credit facility and (iii) pay fees and expenses related thereto. The revolving credit facility replaced the revolving credit facility under the original first lien credit facility.

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The tranche A term loans and the revolving credit facility will mature on July 9, 2019. The tranche B term loans will mature on July 9, 2017. Loans under the revolving credit facility are expected to be used for working capital and other general corporate purposes.

The tranche A term loans and loans under the revolving credit facility bear interest, at our option, at a rate equal to either the LIBOR rate, plus an applicable margin equal to 2.75% per annum, or the prime lending rate, plus an applicable margin equal to 1.75% per annum. The applicable margins for the tranche A term loans and loans under the revolving credit facility are subject to reduction by 0.25% or 0.50%, or increase by 0.25% based upon our total leverage ratio. The tranche B term loans bear interest, at our option, at a rate equal to either the LIBOR rate, plus an applicable margin equal to 2.75% per annum or the prime lending rate, plus an applicable margin equal to 1.75% per annum. We are required to pay a commitment fee of 0.50%, subject to decrease to 0.375% based on our total leverage ratio, on the daily unused amount of the commitments under the revolving credit facility, as well as fronting fees and other customary fees for letters of credit issued under the revolving credit facility.

We are permitted to make voluntary prepayments at any time without payment of a premium, except that a 1% premium would apply to a repricing of the tranche B term loans effected on or prior to the six-month anniversary of the effective date for the amendment and restatement of our credit facility. We are required to make mandatory prepayments of term loans (without payment of a premium) with (i) net cash proceeds from issuances of debt (other than certain permitted debt), (ii) net cash proceeds from certain non-ordinary course asset sales and casualty and condemnation proceeds (subject to reinvestment rights and other exceptions), and (iii) beginning with the fiscal year ending December 31, 2015, 50% of our excess cash flow (subject to decrease to (x) 25% if our total leverage ratio as of the last day of such fiscal year is less than 3.75 to 1.0 and equal to or greater than 3.00 to 1.0, and (y) 0% if our total leverage ratio as of the last day of such fiscal year is less than 3.00 to 1.0), provided that we may defer prepayments based on excess cash flow to the extent such payments would result our GAAP working capital being less than \$10 million (after giving effect to such prepayments).

The tranche A term loans will be paid in equal quarterly installments in an aggregate annual amount equal to: (i) beginning on December 31, 2014 to December 31, 2016, 5% of the original principal amount thereof, (ii) beginning on December 31, 2016 to December 31, 2018, 7.5% of the original principal amount thereof, and (iii) beginning on December 31, 2018 to June 30, 2019, 10% of the original principal amount thereof with any remaining balance payable on the final maturity date of the tranche A term loans. The tranche B term loans will be paid in equal quarterly installments in an aggregate annual amount equal to 1% of the original principal amount thereof, with any remaining balance payable on the final maturity date of the tranche B term loans.

Our credit facility contains customary representations and warranties and customary affirmative and negative covenants applicable to us and our subsidiaries, including, among other things, restrictions on indebtedness, liens, investments, mergers, dispositions, prepayment of other indebtedness, and dividends and other distributions. Our credit facility also contains financial covenants that require us to maintain a minimum consolidated interest coverage ratio and a maximum total leverage ratio.

Contractual Obligations and Commitments

The following table summarizes our contractual obligations and commercial commitments as of June 30, 2014, and the effect they are expected to have on our liquidity and capital resources (in thousands):

	Payments Due by Period			
	Less than 1 year	1-3 years	3-5 years	More than 5 years
Total				

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Long-term debt obligations	\$575,000	5,187	43,844	254,094	271,875
Interest on debt obligations	96,989	8,295	42,181	38,095	8,418
Workers compensation liabilities	102,689	20,165	28,589	15,221	38,714
Capital lease obligations	333	194	119	20	-
Operating lease obligations	27,242	5,333	14,010	4,677	3,222
Purchase obligations	3,243	2,917	326	-	-
Uncertain tax positions	3,000	2,545	455	-	-
Total	\$808,496	\$44,636	\$129,524	\$312,107	\$322,229

Long-term debt obligations and interest on debt obligations reflect the terms of the amended and restated credit agreement discussed above. The projected interest payments incorporate the forward LIBOR curve as of June 30, 2014.

Workers compensation liabilities represented in the table above are considered contractual obligations because they represent the estimated costs of reimbursing the carriers for paying claims within the deductible layer in accordance with workers compensation insurance policies. Workers compensation liabilities include estimates for reported claims, plus estimates for claims incurred but not reported, and estimates of certain expenses associated with processing and settling the claims. These estimates are subject to

significant uncertainty. The actual amount to be paid is not finally determined until we reach a settlement with the insurance carrier. Final claim settlements may vary significantly from the present estimates, particularly because many claims will not be settled until well into the future. In estimating the timing of future payments by year, we have assumed that our historical payment patterns will continue. However, the actual timing of future payments could vary materially from these estimates due to, among other things, changes in claim reporting and payment patterns and large unanticipated settlements.

Our purchase obligations represented in the table above primarily consist of obligations for renewal premiums on workers compensation policies, software licenses and maintenance, sales and marketing events and professional and consulting fees. These are associated with agreements that we believe are enforceable and legally binding and that specify all significant terms, including fixed or minimum services to be used, fixed, minimum or variable price provisions, and the approximate timing of the transaction. Obligations under contracts that we can cancel without a significant penalty are not included in the table above. The table includes purchase obligations individually greater than \$100,000 and with a remaining term in excess of one year.

To support our growth and expansion, we may lease additional office space. Many of our operating lease agreements provide us with the option to renew. Our future operating lease obligations would change if we exercised these options and if we entered into additional operating lease agreements as we expand our operations.

In the normal course of business, we make representations and warranties that guarantee the performance of services under service arrangements with clients. Historically, there has been no material losses related to such guarantees. In addition, in connection with our initial public offering, we have entered into indemnification agreements with our officers and directors, which require us to defend and, if necessary, indemnify these individuals for certain pending or future legal claims as they relate to their services provided to us. Such indemnification obligations are not included in the table above.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to certain market risks in the ordinary course of our business. These risks primarily include interest rate sensitivities as follows.

We had cash and cash equivalents, restricted cash, restricted investments, payroll funds collected, and interest bearing receivable in connection with workers compensation premiums totaling \$568.9 million at June 30, 2014. Included in this amount were \$55.4 million in time deposits and U.S. Treasuries. Such interest-earning instruments carry a degree of interest rate risk. To date, fluctuations in interest income have not been significant. Fluctuations in the value of our investment securities caused by a change in interest rates (gains or losses on the carrying value) are recorded in other comprehensive income, and are realized only if we sell the underlying securities. Our investments are made for capital preservation purposes. An immediate increase or decrease in the interest rates in effect at either December 31, 2013 or June 30, 2014 of 100-basis points would not result in a material market value reduction or increase at such date.

The cash and cash equivalents, restricted cash, payroll funds collected and workers compensation receivable are held for working capital purposes. Our cash equivalents, payroll funds collected, workers compensation receivable and our investments are subject to market risk due to changes in interest rates. Fixed rate securities may have their market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectation due to changes in interest rates or we may suffer losses in principal if we are forced to sell securities that decline in market value due to changes in interest rates. However, because we classify our debt securities as “available for sale,” no gains or losses are recognized due to changes in interest rates unless such securities are sold prior to maturity or

declines in fair value are determined to be other-than-temporary. Our fixed-income portfolio is subject to interest rate risk.

We also had total outstanding indebtedness of \$575.4 million as of June 30, 2014, of which \$15.6 million is due within 12 months. Amounts outstanding under our credit facility carry estimated variable interest rates ranging from 3.0% to 6.0% over the term of the facility. As a result of our credit facility, we are exposed to changes in interest rates. With an increase in interest rates in effect at June 30, 2014 of 100 basis points, our interest expense for 2014 through 2019 would be \$119.6 million. On the other hand, with a decrease in interest rates in effect at June 30, 2014 of 100 basis points, our interest expense for 2014 through 2019 would be \$74.4 million.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2014. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), means controls and

other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure. Based on the evaluation of our disclosure controls and procedures as of June 30, 2014, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Remediation Efforts on Previously Identified Material Weakness

In preparing and reviewing our consolidated financial statements as of and for the nine months ended September 30, 2013, and in connection with our restatement of previously issued consolidated financial statements for the years ended December 31, 2010 and 2011, we and our independent registered public accounting firm identified a material weakness in our internal control over financial reporting. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our financial statements will not be prevented or detected on a timely basis. The material weakness identified related to our incorrectly recording a deferred tax asset in connection with our accounting for our acquisition of Ambrose that should have been reported as goodwill as of September 30, 2013, and to incorrectly recording a true-up to the income tax provision in 2011 related to the allocation of stock compensation between qualified and nonqualified stock options that should have been identified and recorded in 2010. As a result, there were adjustments required in connection with closing our books and records and preparing our consolidated financial statements for the nine months ended September 30, 2013 and a restatement was required for our consolidated financial statements for the years ended 2010 and 2011.

In response to this material weakness, we have hired a Director of Income Tax Accounting, who reports directly to the Chief Accounting Officer. We also will continue to engage external technical advisers to assist us with the evaluation of complex tax issues and improve the processes, procedures and documentation standards relating to the preparation of the income tax provision calculations. We will continue to assess and develop our tax professionals in order to ensure adequate technical and accounting expertise commensurate with our needs to properly consider and apply GAAP for income taxes.

Our remediation efforts are continuing and we expect to make additional changes to our controls over income tax reporting processes that we believe will strengthen our internal control. We have dedicated resources to the design, implementation, documentation, and testing of our internal controls. We will continue to evaluate the effectiveness of our internal control over accounting for income taxes and will continue to utilize external technical advisers to ensure that our financial statements continue to be fairly stated in all material respects. Neither we nor our independent registered public accounting firm has performed an evaluation of our internal control over financial reporting during any period in accordance with the provisions of the Sarbanes-Oxley Act. In light of the material weakness that was identified as a result of the limited procedures performed, we believe that it is possible that, had we and our independent registered public accounting firm performed an evaluation of our internal control over financial reporting in accordance with the provisions of the Sarbanes-Oxley Act, additional material weaknesses or significant control deficiencies may have been identified.

As we continue to evaluate and test improvements to our internal control over financial reporting, we may determine to take additional measures to address control deficiencies or decide to modify certain of the remediation measures described above. We expect that the material weakness will be remediated in 2014, although there can be no assurances that our efforts will be effective. Our Chief Executive Officer and Chief Financial Officer considered this material weakness in evaluating our disclosure controls and procedures as of June 30, 2014, and determined that the material weakness did not impact our disclosure controls and procedures for the period ended June 30, 2014.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the quarter ended June 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. As described above, we are implementing changes to our disclosure controls and procedures and internal control over financial reporting to remediate the material weakness identified above.

Limitations on Effectiveness of Controls and Procedures

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply judgment in evaluating the benefits of possible controls and procedures relative to their costs.

PART II—OTHER INFORMATION

Item 1. Legal Proceedings

We may from time to time become involved in various litigation matters arising in the ordinary course of business, including suits by our clients. The unfavorable resolution of any such matter could have a material effect on our consolidated financial position and results of operations.

Due to the nature of our relationship with our WSEs, we could be subject to liability for federal and state law violations even if we do not participate in such violations. While our agreements with our clients contain indemnification provisions related to the conduct of our clients, we historically have not encountered situations requiring enforcement of these indemnification provisions.

We have been named as a defendant in various class action lawsuits arising from the nature of our relationship with our WSEs. At this stage of the lawsuits, management believes an unfavorable outcome to the Company is not probable. There are significant uncertainties involved in any class action litigation. Management is currently unable to estimate a possible loss or range of loss for these class action lawsuits.

Item 1A. Risk Factors

RISK FACTORS

Investing in our common stock involves a high degree of risk. You should carefully consider the following risks and all of the other information contained in this report, including our consolidated financial statements and related notes. If any of the following risks materialize, our business, financial condition and results of operations could be materially and adversely affected. In that case, the trading price of our common stock could decline, and you may lose some or all of your investment.

Risks Related to Our Business and Industry

Our success depends on growth in market acceptance of the human resources outsourcing and related services we provide.

Our success depends on the willingness of SMBs to outsource their HR function to a third-party service provider. We estimate that fewer than 5% of U.S. employees of businesses with fewer than 500 employees are part of a co-employment arrangement, in which all or some portion of the employer's HR function was outsourced to a single third-party provider such as TriNet. We believe that our growth opportunity is primarily a function of our ability to penetrate the SMB market. Many companies have invested substantial personnel, infrastructure and financial resources in their own internal HR organizations and therefore may be reluctant to switch to our solution. Companies may not engage us for other reasons, including a desire to maintain control over all aspects of their HR activities, a belief that they manage their HR activities more effectively using their internal administrative organizations, perceptions about the expenses associated with our services, perceptions about whether our services comply with laws and regulations applicable to them or their businesses, or other considerations that may not always be evident. Additional concerns or considerations may also emerge in the future. We must address our potential clients' concerns and explain the benefits of our approach in order to convince them to change the way that they manage their HR activities, particularly in parts of the United States where our company and solution are less well-known. If we are not successful in addressing potential clients' concerns and convincing companies that our solution can fulfill their HR needs, then the market for our solution may not develop as we anticipate and our business may not grow.

If we are unable to rapidly grow our sales force, we will not be able to grow our business at the rate that we anticipate, which could harm our business, results of operations and financial condition.

In order to raise awareness of the benefits of our services and identify and acquire new clients, we must rapidly grow our direct sales force, which consists of regional sales representatives who focus on serving clients in specific industry vertical markets. Competition for skilled sales personnel is intense, and we cannot assure you that we will be successful in attracting, training and retaining qualified sales personnel, or that our newly hired sales personnel will function effectively, either individually or as a group. In addition, our newly hired sales personnel are typically not productive for up to a year following their hiring. This results in increased near-term costs to us relative to the sales contributions of these newly hired sales personnel. If we are unable to rapidly grow and effectively train our sales force, our revenues likely will not increase at the rate that we anticipate, which could harm our business, results of operations and financial condition.

We are subject to client attrition.

We regularly experience significant client attrition due to a variety of factors, including increases in administrative fees and insurance costs, disruption caused by the transition of WSEs we have gained through acquisition to our technology platform, client business failure, competition and clients determining to bring HR administration in-house. Our standard client service agreement can be cancelled by us or by the client without penalty with 30 days' prior written notice. Clients who intend to cease doing business with us often elect to do so effective as of the beginning of a calendar year. As a result, in the first quarter of each year we experience our largest concentration of client attrition. In addition, we experience higher levels of client attrition in connection with renewals of the health insurance we provide for WSEs in the event that such renewals result in increased premiums that we pass on to our clients. If we were to experience client attrition in excess of our projected annual attrition rate of approximately 20% of our installed WSE base, as we did in 2010 and 2011, it could harm our business, results of operations and financial condition.

Our acquisition strategy creates risks for our business.

We have completed numerous acquisitions of other businesses, and we expect that we will continue to grow through acquisitions of other businesses, assets or technologies. We may fail to identify attractive acquisition candidates or we may be unable to reach acceptable terms for future acquisitions. If we are unable to complete acquisitions in the future, our ability to grow our business will be impaired.

We may pay for acquisitions by issuing additional shares of our common stock, which would dilute our stockholders, or by issuing debt, which could include terms that restrict our ability to operate our business or pursue other opportunities and subject us to meaningful debt service obligations. We may also use significant amounts of cash to complete acquisitions. To the extent that we complete acquisitions in the future, we likely will incur future depreciation and amortization expenses associated with the acquired assets. We may also record significant amounts of intangible assets, including goodwill, which could become impaired in the future. Acquisitions involve numerous other risks, including:

- difficulties integrating the operations, technologies, services and personnel of the acquired companies, including the migration of WSEs from an acquired company's technology platform to ours;
- challenges maintaining our internal standards, controls, procedures and policies;
- diversion of management's attention from other business concerns;
- over-valuation by us of acquired companies;
- litigation resulting from activities of the acquired company, including claims from terminated employees, customers, former stockholders and other third parties;
- insufficient revenues to offset increased expenses associated with the acquisitions and unanticipated liabilities of the acquired companies;
- insufficient indemnification or security from the selling parties for legal liabilities that we may assume in connection with our acquisitions;
- entering markets in which we have no prior experience and may not succeed;
- risks associated with foreign acquisitions, such as communication and integration problems resulting from geographic dispersion and language and cultural differences, compliance with foreign laws and regulations and general economic or political conditions in other countries or regions;
- potential loss of key employees of the acquired companies; and
- impairment of relationships with clients and employees of the acquired companies or our clients and employees as a result of the integration of acquired operations and new management personnel.

If we fail to integrate newly acquired businesses effectively, we might not achieve the growth, service enhancement or operational efficiency objectives of the acquisitions, and our business, results of operations and financial condition could be harmed.

Unexpected changes in workers compensation and health insurance claims by worksite employees could harm our business.

Our insurance costs are impacted significantly by our WSEs' health and workers compensation insurance claims experience. We establish reserves to provide for the estimated costs of reimbursing our workers compensation and health insurance carriers for paying claims within the deductible layer in accordance with their insurance policies. Estimating these reserves involves our consideration of a number of factors and requires significant judgment. If there is an unexpected increase in the severity or frequency of claims, such as due to our WSEs generating additional claims activity, or if we subsequently receive updated information indicating insurance claims were higher than previously estimated and reported, our insurance costs could be higher in that period or subsequent

periods as we adjust our reserves accordingly. In addition, we may be unable to increase our pricing to offset increases in insurance costs on a timely basis. A number of factors affect claim activity levels, such as changes in general economic conditions, proposed and enacted regulatory changes and disease outbreaks.

Our quarterly results of operations may fluctuate as a result of numerous factors, many of which are outside of our control.

Our quarterly results of operations are likely to fluctuate, and our results in some quarters may be below the expectations of research analysts and our investors, which could cause the price of our common stock to decline. Some of our significant expenses, such as insurance costs for our WSEs, rent expense and debt expense, may require significant lead time to reduce. If we do not achieve our expected revenues targets, we may be unable to adjust our costs quickly enough to offset any revenues shortfall, which could harm our results of operations. Some of the important factors that may cause our revenues, results of operations and cash flows to fluctuate from quarter to quarter include:

- the number of our new clients initiating service and the number of WSEs employed by each new client;
- our loss of existing clients;
- reduction in the number of WSEs at existing clients;
- the number and severity of health and workers compensation insurance claims by WSEs and the timing of claims information provided by our insurance carriers;
- the timing of client payments and payment defaults by clients;
- the amount and timing of our operating expenses and capital expenditures;
- costs associated with our acquisitions of companies, assets and technologies;
- payments or drawdowns on our credit facilities, or any amendments to our obligations under our credit facilities;
- expenses we incur for geographic and service expansion;
- our regulatory compliance costs;
- changes to our credit ratings by rating agencies;
- changes in our effective tax rate;
- extraordinary expenses such as litigation or other dispute-related settlement payments; and
- the impact of new accounting pronouncements.

Many of the above factors are discussed in more detail elsewhere in this “Risk Factors” section and in the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations”. Many of these factors are outside our control, and the variability and unpredictability of these factors could cause us to fail to meet our expectations for revenues or results of operations for a given period. In addition, the occurrence of one or more of these factors might cause our results of operations to vary widely, which could lead to negative impacts on our margins, short-term liquidity or ability to retain or attract key personnel, and could cause other unanticipated issues. Accordingly, we believe that quarter-to-quarter comparisons of our revenues, results of operations and cash flows may not be meaningful and should not be relied upon as an indication of our future performance.

Our business is subject to numerous state and federal laws, and uncertainty as to the application of these laws, or adverse applications of these laws, as well as changes in applicable laws, could adversely affect our business.

Our operations are governed by numerous federal, state and local laws relating to labor, tax, benefits, insurance and employment matters. We are a professional employer organization, and by entering into a co-employer relationship with WSEs, we assume certain obligations, responsibilities and potential legal risks of an employer under these laws. However, many of these laws (such as the Employee Retirement Income Security Act, or ERISA, and federal and state employment tax laws) do not specifically address the obligations and responsibilities of a provider of outsourced HR in a co-employer relationship, and the definition of employer under these laws is not uniform. In addition, many states have not addressed the co-employer relationship for purposes of compliance with applicable state laws governing the relationship between employers and employees and state insurance laws. There is even greater uncertainty on the federal level, such as the application of immigration reform to a co-employer relationship, and tax

credits for small businesses that utilize a co-employer relationship.

We are not able to predict whether broader federal or state regulation governing the co-employer relationship will be implemented, or if it is, how it will affect us. Any adverse application or interpretation (in courts, agencies or otherwise) of new or existing federal or state laws to the co-employer relationship with our WSEs and clients could harm our business. If federal, state or local jurisdictions were to change their regulatory framework related to outsourced HR, or introduce new laws governing our industry

that were materially different from existing laws, those changes could reduce or eliminate the need for some of our services, or could require that we make significant changes in our methods of doing business, which could increase our cost of doing business. Changes in regulations could also affect the extent and type of benefits employers can or must provide employees, the amount and type of taxes employers and employees are required to pay or the time within which employers must remit taxes to the applicable authority. These changes could substantially decrease our revenues and substantially increase our cost of doing business. If we fail to educate and assist our clients regarding new or revised legislation that impacts them, our reputation could be harmed.

Although some states do not explicitly regulate professional employer organizations, 42 states have passed laws that have licensing, certification or registration requirements applicable to professional employer organizations or recognize the professional employer organization model, and other states may implement such requirements in the future. Laws regulating professional employer organizations vary from state to state, but generally provide for oversight of the fiscal responsibility of professional employer organizations, and in some cases codify and clarify the co-employment relationship for processing unemployment claims, workers compensation and other purposes under state law. We may be required to spend significant time and resources to satisfy licensing requirements or other applicable regulations in some states, and we may not be able to satisfy these requirements or regulations in all states, which could prohibit us from doing business in such states. In addition, we cannot assure you that we will be able to renew our licenses in all states.

If we are not recognized as an employer of worksite employees under federal and state regulations, we and our clients could be adversely impacted.

In order for WSEs to receive the full benefit of our benefits offerings, it is important that we act and qualify as an employer of the WSEs under the Internal Revenue Code of 1986, or the Code, and ERISA. In addition, our status as an employer is important for purposes of ERISA preemption of state laws. The definition of employer under various laws is not uniform, and under both the Code and ERISA the term is defined in part by complex multi-factor tests under common law. We believe that we qualify as an employer of our WSEs in the United States under both the Code and ERISA, and we implement processes to protect and preserve this status. However, the U.S