

ERESEARCHTECHNOLOGY INC /DE/

Form 10-Q

August 05, 2011

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 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, 2011**

or

**Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transitional period from _____ to _____**

Commission file number: 0-29100

eResearchTechnology, Inc.

(Exact name of registrant as specified in its charter)

Delaware

22-3264604

(State or other jurisdiction of incorporation
or organization)

(I.R.S. Employer Identification No.)

1818 Market Street
Philadelphia, PA

19103

(Address of principal executive offices)

(Zip code)

215-972-0420

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See 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

Smaller reporting
company

(Do not check if a 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

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

The number of shares of Common Stock, \$.01 par value, outstanding as of July 22, 2011, was 49,231,172.

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eResearchTechnology, Inc. and Subsidiaries
 Consolidated Balance Sheets
 (In thousands, except share and per share amounts)
 (unaudited)

| | December 31, 2010 | June 30, 2011 |
|---|----------------------|---------------|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 30,343 | \$ 31,601 |
| Short-term investments | 50 | 50 |
| Investment in marketable securities | 648 | 972 |
| Accounts receivable, less allowance for doubtful accounts of \$515 and \$555, respectively | 37,236 | 34,525 |
| Inventory | 4,698 | 10,893 |
| Prepaid income taxes | 1,988 | 3,216 |
| Prepaid expenses and other | 4,393 | 5,886 |
| Deferred income taxes | 3,431 | 3,431 |
| | | |
| Total current assets | 82,787 | 90,574 |
| Property and equipment, net | 42,615 | 47,767 |
| Goodwill | 71,637 | 77,357 |
| Intangible assets | 17,187 | 15,702 |
| Other assets | 609 | 680 |
| | | |
| Total assets | \$ 214,835 | \$ 232,080 |
| | | |
| Liabilities and Stockholders Equity | | |
| Current Liabilities: | | |
| Accounts payable | \$ 7,136 | \$ 5,569 |
| Accrued expenses | 16,162 | 13,731 |
| Deferred revenues | 11,670 | 13,588 |
| | | |
| Total current liabilities | 34,968 | 32,888 |
| | | |
| Deferred rent | 2,368 | 2,397 |
| Deferred income taxes | 3,703 | 4,098 |
| Long-term debt | 21,000 | 21,000 |
| Other liabilities | 2,141 | 2,146 |
| | | |
| Total liabilities | 64,180 | 62,529 |

Commitments and contingencies

Stockholders' Equity:

| | | | |
|--|----|----------|------------|
| Preferred stock \$10.00 par value, 500,000 shares authorized, none issued and outstanding | | | |
| Common stock \$.01 par value, 175,000,000 shares authorized, 60,460,782 and 60,807,913 shares issued, respectively | | 605 | 608 |
| Additional paid-in capital | | 100,441 | 102,548 |
| Accumulated other comprehensive (loss) income | | (1,545) | 10,413 |
| Retained earnings | | 131,037 | 135,911 |
| Treasury stock, 11,589,603 and 11,596,966 shares at cost, respectively | | (79,883) | (79,929) |
| | | | |
| Total stockholders' equity | | 150,655 | 169,551 |
| | | | |
| Total liabilities and stockholders' equity | \$ | 214,835 | \$ 232,080 |

The accompanying notes are an integral part of these statements.

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eResearchTechnology, Inc. and Subsidiaries
Consolidated Statements of Operations
(In thousands, except per share amounts)
(unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|-----------------------------|-----------|---------------------------|-----------|
| | 2010 | 2011 | 2010 | 2011 |
| Net revenues: | | | | |
| Services | \$ 18,697 | \$ 22,416 | \$ 33,532 | \$ 46,393 |
| Site support | 10,399 | 20,433 | 17,432 | 38,155 |
| Total net revenues | 29,096 | 42,849 | 50,964 | 84,548 |
| Costs of revenues: | | | | |
| Cost of services | 8,325 | 13,615 | 15,636 | 26,771 |
| Cost of site support | 4,957 | 13,189 | 7,756 | 23,312 |
| Total costs of revenues | 13,282 | 26,804 | 23,392 | 50,083 |
| Gross margin | 15,814 | 16,045 | 27,572 | 34,465 |
| Operating expenses: | | | | |
| Selling and marketing | 3,941 | 4,426 | 7,349 | 8,601 |
| General and administrative | 9,753 | 7,247 | 14,498 | 14,755 |
| Research and development | 1,069 | 1,802 | 1,927 | 3,185 |
| Total operating expenses | 14,763 | 13,475 | 23,774 | 26,541 |
| Operating income | 1,051 | 2,570 | 3,798 | 7,924 |
| Foreign exchange gains (losses) | 399 | (266) | 479 | (1,275) |
| Other (expense) income, net | (3) | (168) | 17 | (269) |
| Income before income taxes | 1,447 | 2,136 | 4,294 | 6,380 |
| Income tax provision | 621 | 355 | 1,716 | 1,506 |
| Net income | \$ 826 | \$ 1,781 | \$ 2,578 | \$ 4,874 |
| Net income per share: | | | | |
| Basic | \$ 0.02 | \$ 0.04 | \$ 0.05 | \$ 0.10 |
| Diluted | \$ 0.02 | \$ 0.04 | \$ 0.05 | \$ 0.10 |
| Shares used in computing net income per share: | | | | |
| Basic | 48,831 | 49,146 | 48,753 | 49,021 |
| Diluted | 49,383 | 49,330 | 49,114 | 49,291 |

The accompanying notes are an integral part of these statements.

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eResearchTechnology, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
(In thousands)
(unaudited)

| | Six Months Ended June 30, | |
|---|----------------------------------|-------------|
| | 2010 | 2011 |
| Operating activities: | | |
| Net income | \$ 2,578 | \$ 4,874 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 6,307 | 12,460 |
| Cost of sales of equipment | 4 | 8 |
| Share-based compensation | 1,425 | 1,421 |
| Deferred income taxes | 216 | 413 |
| Loss on disposal of equipment | | 780 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (1,722) | 3,648 |
| Inventory | (436) | (4,973) |
| Prepaid expenses and other | (925) | (1,761) |
| Accounts payable | 1,227 | (1,002) |
| Accrued expenses | 4,925 | (2,624) |
| Income taxes | (1,120) | (1,288) |
| Deferred revenues | 102 | 1,738 |
| Deferred rent | (204) | 23 |
| Net cash provided by operating activities | 12,377 | 13,717 |
| Investing activities: | | |
| Purchases of property and equipment | (8,773) | (14,754) |
| Purchases of investments | (999) | |
| Proceeds from sales of investments | 10,731 | |
| Payments for acquisition | (80,475) | (117) |
| Net cash used in investing activities | (79,516) | (14,871) |
| Financing activities: | | |
| Proceeds from long-term debt | 23,000 | |
| Proceeds from exercise of stock options | 205 | 629 |
| Stock option income tax benefit | 12 | 12 |
| Repurchase of common stock for treasury | | (46) |
| Net cash provided by financing activities | 23,217 | 595 |
| Effect of exchange rate changes on cash | (2,553) | 1,817 |
| Net (decrease) increase in cash and cash equivalents | (46,475) | 1,258 |
| Cash and cash equivalents, beginning of period | 68,979 | 30,343 |
| Cash and cash equivalents, end of period | \$ 22,504 | \$ 31,601 |

The accompanying notes are an integral part of these statements.

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**eResearchTechnology, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
(unaudited)**

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements, which include the accounts of eResearchTechnology, Inc. (the Company, ERT or we) and its wholly-owned subsidiaries, have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the interim periods ended June 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. Further information on potential factors that could affect our financial results can be found in our Report on Form 10-K for the year ended December 31, 2010 as filed with the Securities and Exchange Commission (SEC). Subsequent events have been evaluated for disclosure and recognition.

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Note 2. Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of ERT and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated. We consider our business to consist of one segment which is providing services and customizable medical devices to biopharmaceutical organizations and, to a lesser extent, healthcare organizations.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition

Our services revenues consist primarily of revenue derived from our cardiac safety (Cardiac Safety), respiratory efficacy (Respiratory) and, to a lesser extent, our electronic patient-reported outcomes (ePRO) solutions that we provide on a fee for services basis. Our services revenues are recognized as the services are performed. We also provide consulting services on a time and materials basis and recognize revenues as we perform the services. Our site support revenue, consisting of equipment rentals and sales along with related supplies and logistics management, are recognized at the time of sale or over the rental period.

At the time of each transaction, management assesses whether the fee associated with the transaction is fixed or determinable and whether or not collection is reasonably assured. If a significant portion of a fee is due after our normal payment terms or upon implementation or customer acceptance, the fee is accounted for as not being fixed or determinable and revenue is recognized as the fees become due or after implementation or customer acceptance has occurred.

Collectability is assessed based on a number of factors, including past transaction history with the customer and the creditworthiness of the customer. If it is determined that collection of a fee is not reasonably assured, the fee is deferred and revenue is recognized at the time collection becomes reasonably assured, which is generally upon receipt of cash. Under a typical contract for Cardiac Safety services, customers pay us a portion of our fee for these services upon contract execution as an upfront deposit, some of which is typically nonrefundable upon contract termination. Revenues are then recognized under Cardiac Safety service contracts as the services are performed.

For arrangements with multiple deliverables entered into prior to 2011, where the fair value of each element is known, the revenue is allocated to each component based on the relative fair value of each element. For arrangements with multiple deliverables where the fair value of one or more delivered elements is not known, revenue is allocated to each component of the arrangement using the residual method provided that the fair value of all undelivered elements is known. Fair values for undelivered elements are based primarily upon stated renewal rates for future products or

services.

For arrangements with multiple deliverables entered into from and after January 1, 2011, the revenue is allocated to each element (both delivered and undelivered items) based on their relative selling prices or management's best estimate of their selling prices.

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We have recorded reimbursements received for out-of-pocket expenses incurred as revenue in the accompanying consolidated statements of operations.

Unbilled revenue is revenue that is recognized but is not currently billable to the customer pursuant to contractual terms. In general, such amounts become billable in accordance with predetermined payment schedules, but recognized as revenue as services are performed. Amounts included in unbilled revenue are expected to be collected within one year and are included within current assets.

Business Combinations

On May 28, 2010, we acquired Research Services Germany 234 GmbH (Research Services or RS), which provides respiratory diagnostics services and is a manufacturer of equipment and also offers cardiac safety and ePRO services. We paid \$82.7 million for RS. The acquisition and related transaction costs were financed from our existing cash and the \$23.0 million drawn from our \$40.0 million revolving credit facility through Citizens Bank of Pennsylvania. The credit facility was established on May 27, 2010. See Note 4 for additional disclosure on the RS acquisition and Note 7 for additional disclosure regarding the revolving credit facility.

We allocated the purchase price to the tangible and intangible assets we acquired and liabilities we assumed based on their estimated fair values. This valuation requires management to make significant estimates and assumptions, especially with respect to long-lived and intangible assets.

Critical estimates in valuing certain of the intangible assets include but are not limited to: future expected cash flows from customer contracts, customer relationships, proprietary technology and discount rates. Our estimates of fair value are based upon assumptions we believe to be reasonable, but which are inherently uncertain and unpredictable. Assumptions may be incomplete or inaccurate, and unanticipated events and circumstances may occur.

Concentration of Credit Risk and Significant Customers

Our business depends entirely on the clinical trials that biopharmaceutical and healthcare organizations conduct. Our revenues and profitability will decline if there is less competition in the biopharmaceutical and healthcare industries, which could result in fewer products under development and decreased pressure to accelerate a product approval. Our revenues and profitability will also decline if the FDA or similar agencies in foreign countries modify their requirements in a manner that decreases the need for our solutions.

Financial instruments that potentially subject us to concentration of credit risk consist primarily of trade accounts receivable from companies operating in the biopharmaceutical and healthcare industries. For the six months ended June 30, 2010, one customer accounted for approximately 20% of net revenues. For the six months ended June 30, 2011, three customers accounted for approximately 21%, 15% and 14% of net revenues, respectively. The loss of these customers could have a material adverse effect on our operations. We maintain reserves for potential credit losses. Such losses, in the aggregate, have not historically exceeded management's estimates.

Cash and Cash Equivalents

We consider cash on deposit and in overnight investments and investments in money market funds with financial institutions to be cash equivalents. At the balance sheet dates, cash equivalents consisted primarily of investments in money market funds. At December 31, 2010 and June 30, 2011, approximately \$6.9 million and \$10.0 million, respectively, was held by our UK subsidiary. At December 31, 2010 and June 30, 2011, approximately \$13.1 million and \$10.2 million, respectively, was held by our German subsidiary.

Short-term Investments and Investments in Marketable Securities

At June 30, 2011, short-term investments consisted of an auction rate security issued by a municipality while marketable securities consisted of publicly-traded shares of common stock received from the buyer of certain assets of our electronic data capture (EDC) operations. Available-for-sale securities are carried at fair value, based on quoted market prices, with unrealized gains and losses reported as a separate component of stockholders' equity. We classified our short-term investments and investment in marketable securities at December 31, 2010 and June 30, 2011 as available-for-sale. At December 31, 2010 and June 30, 2011, unrealized gains and losses were immaterial. Realized gains and losses during the six months ended June 30, 2010 and 2011 were immaterial. For purposes of determining realized gains and losses, the cost of the securities sold is based upon specific identification.

Inventory

We compute inventory cost on a first-in, first-out basis (FIFO). We reduce the carrying value of inventories to a lower of cost or market basis for those items that are potentially excess, obsolete or slow-moving. We record charges for inventory obsolescence based upon sales trends and age of on-hand inventory. Work-in-process and finished goods inventories include raw materials, direct labor and manufacturing overhead. Finished goods inventories include equipment that may be sold directly to customers or transferred to rental equipment in property and equipment. We also may, on occasion, sell rental equipment, as described below in Property and Equipment.

Table of Contents**Property and Equipment**

Property and equipment are stated at cost. Depreciation is provided using the straight-line method over the estimated useful lives of three years for computer and other equipment, two to four years for rental equipment, five years for furniture and fixtures and three to five years for system development costs. Leasehold improvements are amortized using the straight-line method over the shorter of the estimated useful life of the asset or the remaining lease term. Repair and maintenance costs are expensed as incurred. Improvements and betterments are capitalized. Depreciation expense was \$1.9 million and \$3.3 million for the three months ended June 30, 2010 and 2011, respectively, and \$3.6 million and \$6.6 million for the six months ended June 30, 2010 and 2011, respectively. The depreciation expense for the six months ended June 30, 2011 includes \$0.2 million related to the three months ended March 31, 2011 that has been reclassified to conform to the current period's presentation for consistent presentation.

We capitalize costs associated with internally developed and/or purchased software systems for new products and enhancements to existing products that have reached the application development stage and meet recoverability tests. These costs are included in property and equipment. Capitalized costs include external direct costs of materials and services utilized in developing or obtaining internal-use software, and payroll and payroll-related expenses for employees who are directly associated with and devote time to the internal-use software project.

Amortization of capitalized software development costs is charged to costs of revenues. Amortization of capitalized software development costs was \$0.9 million and \$1.0 million for the three months ended June 30, 2010 and 2011, respectively, and \$1.8 million and \$2.0 million for the six months ended June 30, 2010 and 2011, respectively. For the six month periods ended June 30, 2010 and 2011, we capitalized \$2.5 million and \$6.5 million, respectively, of software development costs. As of June 30, 2011, \$11.9 million of capitalized costs had not yet been placed in service and were therefore not being amortized.

The largest component of property and equipment is rental equipment which we manufacture internally and also purchase from third parties. Our customers use the rental equipment to perform Cardiac Safety, Respiratory and ePRO tests and collect and send the related data to us. We provide this equipment to customers primarily through rentals via cancellable agreements although, in some cases, we sell equipment outright to customers on a non-recourse basis. The equipment rentals and sales are included in our services agreements with our customers and the decision to rent or buy equipment is made by our customers prior to the start of the study. The decision to buy rather than rent is usually predicated upon the economics to the customer based upon the length of the study and the number of diagnostic tests to be performed each month. The longer the study and the fewer the number of tests performed, the more likely it is that the customer may request to purchase equipment rather than rent. Regardless of whether the customer rents or buys the equipment, we consider the resulting cash flow to be part of our operations and reflect it as such in our consolidated statements of cash flows.

Our services agreements contain multiple elements. As a result, significant contract interpretation is sometimes required to determine the appropriate accounting. In doing so, we consider factors such as whether the deliverables specified in a multiple element arrangement should be treated as separate units of accounting for revenue recognition purposes and, if so, how the contract value should be allocated among the deliverable elements and when to recognize revenue for each element.

The gross cost for rental equipment was \$56.2 million and \$65.4 million at December 31, 2010 and June 30, 2011, respectively. The accumulated depreciation for rental equipment was \$35.9 million and \$44.5 million at December 31, 2010 and June 30, 2011, respectively. See note 14 for further details on the correction of accumulated depreciation of rental equipment recorded in the three month period ending June 30, 2011.

Goodwill

The carrying value of goodwill was \$71.6 million and \$77.4 million as of December 31, 2010 and June 30, 2011, respectively. The change in goodwill was due to foreign currency translation. See Note 4 for additional disclosure regarding the RS and Covance Cardiac Safety Services (CCSS) acquisitions. Goodwill is not amortized but is subject to an impairment test at least annually. We perform the impairment test annually as of December 31 or more frequently if events or circumstances indicate that the value of goodwill might be impaired. No provisions for goodwill impairment were recorded during 2010 or during the six months ended June 30, 2011.

When it is determined that the carrying value of goodwill may not be recoverable, measurement of any impairment will be based on a projected discounted cash flow method using a discount rate commensurate with the risk inherent in the current business model.

Long-lived Assets

When events or circumstances so indicate, we assess the potential impairment of our long-lived assets based on anticipated undiscounted cash flows from the assets. Such events and circumstances include a sale of all or a significant part of the operations associated with the long-lived asset, or a significant decline in the operating performance of the asset. If an impairment is indicated, the amount of the impairment charge would be calculated by comparing the anticipated discounted future cash flows to the carrying value of the long-lived asset. No impairment was indicated during either of the six-month periods ended June 30, 2010 or 2011.

Table of Contents**Software Development Costs**

Research and development expenditures related to software development are charged to operations as incurred. We capitalize certain software development costs subsequent to the establishment of technological feasibility. Because software development costs have not been significant after the establishment of technological feasibility, all such costs have been charged to expense as incurred.

Share-Based Compensation*Accounting for Share-Based Compensation*

Share-based compensation expense is measured at the grant date based on the fair value of the award and is recognized as expense over the vesting period. The aggregate share-based compensation expense recorded in the consolidated statements of operations was \$0.6 million and \$0.8 million for the three months ended June 30, 2010 and 2011, respectively and \$1.4 million for each of the six-month periods ended June 30, 2010 and 2011.

Valuation Assumptions for Options Granted

The fair value of each stock option granted during the six months ended June 30, 2010 and 2011 was estimated at the date of grant using Black-Scholes, assuming no dividends and using the weighted-average valuation assumptions noted in the following table.

| | 2010 | 2011 |
|-------------------------|-----------|-----------|
| Risk-free interest rate | 2.44% | 2.19% |
| Expected dividend yield | 0.00% | 0.00% |
| Expected life | 3.8 years | 4.2 years |
| Expected volatility | 61.73% | 59.25% |

The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant. The expected life (estimated period of time outstanding) of the stock options granted was estimated using the historical exercise behavior of employees. Expected volatility was based on historical volatility for a period equal to the stock options' expected life, calculated on a daily basis. Fluctuations in the market that affect these estimates could have an impact on the resulting compensation cost. The above assumptions were used to determine the weighted-average per share fair value of \$3.24 and \$3.07 for stock options granted during the first six months of 2010 and 2011, respectively.

Equity Incentive Plans

In 1996, we adopted a stock option plan (the 1996 Plan) that authorized the grant of both incentive and non-qualified options to acquire up to 9,450,000 shares of the Company's common stock, as subsequently amended. Our Board of Directors determined the exercise price of the options under the 1996 Plan. The exercise price of incentive stock options was not below the market value of the common stock on the grant date. Incentive stock options under the 1996 Plan expire ten years from the grant date and are exercisable in accordance with vesting provisions set by the Board, which generally are over three to five years. No additional options have been granted under this plan, as amended, since December 31, 2003 and no additional options may be granted thereunder in accordance with the terms of the 1996 Plan.

In May 2003, the stockholders approved a new stock option plan (the 2003 Plan) that authorized the grant of both incentive and non-qualified options to acquire shares of our common stock and provided for an annual option grant of 10,000 shares to each outside director. The Compensation Committee of our Board of Directors determines or makes recommendations to our Board of Directors regarding the recipients of option grants, the exercise price and other terms of the options under the 2003 Plan. The exercise price of incentive stock options may not be set below the market value of the common stock on the grant date. Incentive stock options under the 2003 Plan expire ten years from the grant date, or at the end of such shorter period as may be designated by the Compensation Committee, and are exercisable in accordance with vesting provisions set by the Compensation Committee, which generally are over four years.

On April 26, 2007, the stockholders approved the adoption of the Company's Amended and Restated 2003 Equity Incentive Plan (the Amended 2003 Plan) which included prohibition on repricing of any stock options granted under the Plan unless the stockholders approve such repricing and permitted awards of stock appreciation rights, restricted stock, long term performance awards and performance shares in addition to grants of stock options. On April 29, 2009

the Board of Directors approved a revised amendment to the Amended 2003 Plan that provides for the inclusion of restricted stock units in addition to the other equity-based awards authorized thereunder and eliminated the fixed option grants to outside directors. Restricted stock was granted for the first time in 2010 and is being recorded as compensation expense over the one-year vesting period or the four-year vesting period for grants to the Company's directors and management, respectively. On April 28, 2011, our stockholders approved an amendment to the Amended 2003 Plan that increased the number of shares reserved for issuance thereunder by 3.5 million shares. In accordance with the terms of the Amended 2003 Plan, there are a total of 10,818,625 shares reserved for issuance under the Amended 2003 Plan and there were 4,377,503 shares available for grant as of June 30, 2011.

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Information regarding the stock option and equity incentive plans for the six months ended June 30, 2011 is as follows:

| Share Options | Shares | Weighted Average Exercise Price | Remaining Contractual Term (in years) | Intrinsic Value (in thousands) |
|---|---------------|--|--|---|
| Outstanding as of January 1, 2011 | 4,727,943 | \$ 9.36 | | |
| Granted | 998,974 | 6.42 | | |
| Exercised | (210,618) | 2.99 | | |
| Cancelled/forfeited | (330,431) | 8.50 | | |
| Outstanding as of June 30, 2011 | 5,185,868 | \$ 9.11 | 4.2 | \$ 1,955 |
| Options exercisable or expected to vest at June 30, 2011 | 4,886,934 | \$ 9.27 | 4.1 | \$ 1,830 |
| Options exercisable at June 30, 2011 | 3,192,973 | \$ 10.71 | 3.1 | \$ 1,127 |
| Restricted Stock | | | Shares | Weighted Average Grant Date Fair Value |
| Outstanding as of January 1, 2011 | | | 153,785 | \$ 6.28 |
| Granted | | | 196,254 | 6.41 |
| Vested | | | (52,550) | 6.60 |
| Cancelled/forfeited | | | (4,410) | 7.37 |
| Outstanding as of June 30, 2011 | | | 293,079 | \$ 6.29 |

The aggregate intrinsic value in the share options table above represents the total pre-tax intrinsic value (the difference between the closing price of our common stock on the last trading day of the second quarter of 2011 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on June 30, 2011. This amount changes based on the fair market value of the Company's common stock. The total intrinsic value of options exercised for the six months ended June 30, 2010 and 2011 was approximately \$0.2 million and \$0.7 million, respectively.

As of June 30, 2011, there was \$6.6 million of total unrecognized compensation cost related to non-vested share-based compensation arrangements (including stock options and restricted stock awards) granted under the plans. That cost is expected to be recognized over a weighted-average period of 2.5 years.

Tax Effect Related to Share-based Compensation Expense

Income tax effects of share-based payments are recognized in the consolidated financial statements for those awards that will normally result in tax deductions under existing tax law. Under current U.S. federal tax law, we receive a

compensation expense deduction related to non-qualified stock options only when those options are exercised. Accordingly, the consolidated financial statement recognition of compensation cost for non-qualified stock options creates a deductible temporary difference which results in a deferred tax asset and a corresponding deferred tax benefit in the consolidated statements of operations. We do not recognize a tax benefit for compensation expense related to incentive stock options (ISOs) unless the underlying shares are disposed of in a disqualifying disposition. Accordingly, compensation expense related to ISOs is treated as a permanent difference for income tax purposes. The tax benefit recognized in our consolidated statements of operations for the six months ended June 30, 2010 and 2011 related to stock-based compensation expense was approximately \$0.3 million and \$0.2 million, respectively.

Note 3. Fair Value of Financial Instruments

A fair value measurement assumes that the transaction to sell an asset or transfer a liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. Fair value is based upon an exit price model.

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We measure certain financial assets and liabilities at fair value on a recurring basis, including available-for-sale securities. Available-for-sale securities as of June 30, 2011 consisted of an auction rate security, or ARS, issued by a municipality and publicly-traded shares of common stock. Available-for-sale securities are included in short-term investments in our consolidated balance sheets with the exception of the common stock which is included in investment in marketable securities. The marketable securities are included in investments in marketable securities in our consolidated balance sheets. The three levels of the fair value hierarchy are described below:

Level 1 Unadjusted quoted prices in active markets for identical assets or liabilities

Level 2 Unadjusted quoted prices in active markets for similar assets or liabilities, or Unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or Inputs other than quoted prices that are observable for the asset or liability

Level 3 Unobservable inputs for the asset or liability

The following tables represent our fair value hierarchy for financial assets (cash equivalents and investments) measured at fair value on a recurring basis as of December 31, 2010 and June 30, 2011 (in thousands):

Fair Value Measurements at December 31, 2010

| | Total | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|---------------------------|------------------|---|--|--|
| Cash and cash equivalents | \$ 30,343 | \$ 30,343 | \$ | \$ |
| Municipal securities | 50 | | | 50 |
| Marketable securities | 648 | | 648 | |
| Total | \$ 31,041 | \$ 30,343 | \$ 648 | \$ 50 |

Fair Value Measurements at June 30, 2011

| | Total | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|---------------------------|------------------|---|--|--|
| Cash and cash equivalents | \$ 31,601 | \$ 31,601 | \$ | \$ |
| Municipal securities | 50 | | | 50 |
| Marketable securities | 972 | | 972 | |
| Total | \$ 32,623 | \$ 31,601 | \$ 972 | \$ 50 |

Cash and cash equivalents consist primarily of checking accounts and highly rated money market funds with original maturities of three months or less. The original cost of these assets approximates fair value due to their short term maturity. Bank debt consists of loans drawn under our bank credit facility. Based on our assessment of the current

financial market and corresponding risks associated with the debt, we believe that the carrying amount of bank debt at June 30, 2011 approximates fair value based on the level 2 valuation hierarchy of the fair value measurements standard.

Note 4. Business Combinations

Research Services (RS)

On May 28, 2010, we acquired RS. See Note 2 for a summary of the terms of this acquisition. We have included RS's operating results in our consolidated statements of operations from the date of the acquisition. We paid \$82.7 million for RS and additionally incurred transaction costs of \$4.1 million. The tax bases of the assets acquired and liabilities assumed in the RS transaction were stepped-up to fair value at the date of the RS acquisition.

Pro Forma Results

The unaudited financial information in the table below summarizes the combined results of operations for us and RS on a pro forma basis as though the companies had been combined as of the beginning of each of the periods presented after giving effect to certain adjustments. The unaudited pro forma financial information for the three and six months ended June 30, 2010 combines our historical results for these periods with the historical results for the comparable reporting periods for RS. Our historical results of operations for the three and six months ended June 30, 2011 include the results of RS. The unaudited pro forma financial information below is for informational purposes only and is not indicative of the results of operations or financial condition that would have been achieved if the acquisition would have taken place at the beginning of each of the periods presented and should not be taken as indicative of our future consolidated results of operations or financial condition. Acquisition-related transaction costs of \$3.3 million and \$4.0 million were excluded from the pro forma results for the three and six months ended June 30, 2010, respectively. Pro forma adjustments are tax-effected at our effective tax rate.

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| | Three Months Ended June 30, 2010 (Unaudited, in thousands except per share amounts) | Six Months Ended June 30, 2010 (Unaudited, in thousands except per share amounts) |
|------------------------------|---|---|
| Revenue | \$ 41,037 | \$ 79,304 |
| Operating income | 6,306 | 8,534 |
| Net income | 3,777 | 5,861 |
| Basic net income per share | \$ 0.08 | \$ 0.12 |
| Diluted net income per share | \$ 0.08 | \$ 0.12 |

Covance Cardiac Safety Services, Inc. (CCSS)

On November 28, 2007, we completed the acquisition of CCSS from Covance Inc. (Covance). The following table sets forth the activity and balance of our accrued liability relating to lease costs associated with the closing of CCSS operations, which is included in Accrued expenses and Other liabilities on our Consolidated Balance Sheets (in thousands):

| | Lease Liability |
|------------------------------|--------------------|
| Balance at December 31, 2010 | \$ 1,901 |
| Cash payments | \$ (283) |
| Balance at June 30, 2011 | \$ 1,618 |

Goodwill

The following tables reflect changes in the carrying value of goodwill:

| | |
|----------------------------------|-----------|
| Balance at December 31, 2010 | 71,637 |
| Currency translation adjustments | 5,720 |
| Balance at June 30, 2011 | \$ 77,357 |

Goodwill increased \$2,579 and intangible assets increased \$1,124 as of June 30, 2011 for foreign currency translation adjustments related to fiscal 2010.

Note 5. Inventory

Inventory consisted of the following:

| | December 31, 2010 | June 30, 2011 |
|-----------------|----------------------|---------------|
| Raw materials | \$ 2,196 | \$ 7,022 |
| Work in process | 843 | 986 |
| Finished goods | 1,659 | 2,885 |
| | \$ 4,698 | \$ 10,893 |

Table of Contents**Note 6. Intangible Assets**

Amortization of intangible assets represents the amortization of the intangible assets from the RS and CCSS acquisitions. The gross and net carrying amounts of the acquired intangible assets as of December 31, 2010 and June 30, 2011 were as follows (in thousands):

| Description | December 31, 2010 | | | Estimated Useful Life (in years) |
|--------------------------|-------------------|--------------------------|----------------|-------------------------------------|
| | Gross Value | Accumulated Amortization | Net Book Value | |
| CCSS: | | | | |
| Backlog | \$ 1,900 | \$ 1,900 | \$ * | 3 |
| Customer Relationships | 1,700 | 524 | \$ 1,176 | 10 |
| Technology | 400 | 400 | \$ | 1 |
| Total | \$ 4,000 | \$ 2,824 | \$ 1,176 | |
| RS: | | | | |
| Backlog | \$ 12,782 | \$ 4,687 | \$ 8,095* | 4 |
| Technology | 8,248 | 602 | 7,646 | 8 |
| Covenants not-to-compete | 319 | 49 | 270 | 4 |
| Total | \$ 21,349 | \$ 5,338 | \$ 16,011 | |
| | | | | |
| Description | June 30, 2011 | | | Estimated Useful Life (in years) |
| | Gross Value | Accumulated Amortization | Net Book Value | |
| CCSS: | | | | |
| Backlog | \$ 1,900 | \$ 1,900 | \$ * | 3 |
| Customer Relationships | 1,700 | 609 | \$ 1,091 | 10 |
| Technology | 400 | 400 | \$ | 1 |
| Total | \$ 4,000 | \$ 2,909 | \$ 1,091 | |
| RS: | | | | |
| Backlog | \$ 14,005 | \$ 7,901 | \$ 6,104* | 4 |
| Technology | 9,432 | 1,191 | 8,241 | 8 |
| Covenants not-to-compete | 360 | 94 | 266 | 4 |
| Total | \$ 23,797 | \$ 9,186 | \$ 14,611 | |

*

CCSS backlog was amortized over three years on an accelerated basis and RS backlog is being amortized over four years on an accelerated basis.

The related amortization expense reflected in our consolidated statements of operations for each of the three and six months ended June 30, 2010 was \$0.7 million. The related amortization expense reflected in our consolidated statements of operations for the three and six months ended June 30, 2011 was \$2.0 million and \$3.9 million, respectively.

Estimated amortization expense for the remaining estimated useful life of the acquired intangible assets is as follows for the years ending December 31 (in thousands):

| Years ending December 31, | Amortization of Intangible Assets | | |
|---------------------------|-----------------------------------|-----------|-----------|
| | CCSS | RS | Total |
| 2011 | \$ 85 | \$ 3,892 | \$ 3,977 |
| 2012 | \$ 170 | 3,742 | 3,912 |
| 2013 | \$ 170 | 1,677 | 1,847 |
| 2014 | \$ 170 | 1,230 | 1,400 |
| 2015 | \$ 170 | 1,191 | 1,361 |
| Thereafter | \$ 326 | 2,879 | 3,205 |
| Total | \$ 1,091 | \$ 14,611 | \$ 15,702 |

Table of Contents**Note 7. Credit Agreement**

We have a credit agreement (Credit Agreement) with Citizens Bank of Pennsylvania (Lender) which provides for a \$40 million revolving credit facility. The balance under the Credit Agreement was \$21.0 million at June 30, 2011. At our option, borrowings under the Credit Agreement bear interest either at the Lender's prime rate or at a rate equal to LIBOR plus a margin ranging from 1.00% to 1.75% based on our senior leverage ratio as calculated under the Credit Agreement. In addition, we pay a quarterly unused commitment fee ranging from 0.10% to 0.20% of the unused commitment based on our senior leverage ratio. For the six months ended June 30, 2011, the annual interest rate ranged from 1.44% to 1.51% and the unused commitment fee was 0.15% resulting in expenses of \$0.2 million. Borrowings under the Credit Agreement may be prepaid at any time in whole or in part without premium or penalty, other than customary breakage costs, if any. The Credit Agreement terminates, and any outstanding borrowings mature, on May 27, 2013.

The Credit Agreement requires us to maintain a maximum senior leverage ratio of 2.0 to 1.0 and a minimum debt service coverage ratio of 1.5 to 1.0, in each case as calculated under the Credit Agreement. The Credit Agreement contains other customary affirmative and negative covenants and customary events of default.

At June 30, 2011, we were in compliance with all debt covenants. Borrowings under the line of credit are secured by 65% of the capital stock of certain of our foreign subsidiaries.

Note 8. Net Income per Common Share

Basic net income per common share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted net income per common share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the period, adjusted for the dilutive effect of common stock equivalents, which consist of stock options. The dilutive effect of stock options is calculated using the treasury stock method.

The tables below set forth the reconciliation of the numerators and denominators of the basic and diluted net income per common share computations (in thousands, except per share amounts):

| Three Months Ended June 30, 2010 | Net Income | Shares | Per Share Amount |
|--|---------------|--------|---------------------|
| Basic net income | \$ 826 | 48,831 | \$ 0.02 |
| Effect of dilutive shares | | 552 | |
| Diluted net income | \$ 826 | 49,383 | \$ 0.02 |
| 2011 | | | |
| Basic net income | \$ 1,781 | 49,146 | \$ 0.04 |
| Effect of dilutive shares | | 184 | |
| Diluted net income | \$ 1,781 | 49,330 | \$ 0.04 |
| Six Months Ended June 30, 2010 | Net Income | Shares | Per Share Amount |

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| | | | | | |
|---------------------------|----|-------|--------|----|------|
| Basic net income | \$ | 2,578 | 48,753 | \$ | 0.05 |
| Effect of dilutive shares | | | 361 | | |

| | | | | | |
|--------------------|----|-------|--------|----|------|
| Diluted net income | \$ | 2,578 | 49,114 | \$ | 0.05 |
|--------------------|----|-------|--------|----|------|

2011

| | | | | | |
|---------------------------|----|-------|--------|----|------|
| Basic net income | \$ | 4,874 | 49,021 | \$ | 0.10 |
| Effect of dilutive shares | | | 270 | | |

| | | | | | |
|--------------------|----|-------|--------|----|------|
| Diluted net income | \$ | 4,874 | 49,291 | \$ | 0.10 |
|--------------------|----|-------|--------|----|------|

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In computing diluted net income per common share, options to purchase 2,615,000 and 3,680,000 shares of common stock were excluded from the computations for the three months ended June 30, 2010 and 2011, respectively, and options to purchase 2,792,000 and 2,940,000 shares of common stock were excluded from the computations for the six months ended June 30, 2010 and 2011, respectively. These options were excluded from the computations because the exercise prices of such options were greater than the average market price of our common stock during the respective period.

Note 9. Comprehensive Income (Loss)

We are required to classify items of other comprehensive income (loss) by their nature in the financial statements and display the accumulated balance of other comprehensive income (loss) separately from retained earnings and additional paid-in-capital in the stockholders' equity section of the balance sheet. Our comprehensive income (loss) includes net income and unrealized gains and losses from marketable securities and foreign currency translation as follows (in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|-----------------------------|----------|---------------------------|-----------|
| | 2010 | 2011 | 2010 | 2011 |
| Net income | \$ 826 | \$ 1,781 | \$ 2,578 | \$ 4,874 |
| Other comprehensive income (loss): | | | | |
| Change in unrealized losses on marketable securities | (224) | (81) | (35) | 324 |
| Currency translation adjustment | (1,407) | 1,572 | (2,384) | 11,634 |
| Comprehensive income (loss), net of tax | \$ (805) | \$ 3,272 | \$ 159 | \$ 16,832 |

Comprehensive income increased \$3,703 for the six months ended June 30, 2011 for foreign currency translation adjustments related to fiscal 2010 for our goodwill and intangible assets.

Note 10. Recent Accounting Pronouncements

In September 2009, the FASB issued a new accounting standard regarding revenue arrangements with multiple deliverables. As codified in ASC 605-25 (formerly Emerging Issues Task Force Issue No. 08-1, Revenue Arrangements with Multiple Deliverables), this accounting standard sets forth requirements that must be met for an entity to recognize revenue from the sale of a delivered item that is part of a multiple-element arrangement when other items have not yet been delivered. One of those current requirements is that there be objective and reliable evidence of the standalone selling price of the undelivered items, which must be supported by either vendor-specific objective evidence (VSOE) or third-party evidence (TPE).

This consensus eliminates the requirement that all undelivered elements have VSOE or TPE before an entity can recognize the portion of an overall arrangement fee that is attributable to items that already have been delivered. In the absence of VSOE or TPE of the standalone selling price for one or more delivered or undelivered elements in a multiple-element arrangement, entities will be required to estimate the selling prices of those elements. The overall arrangement fee will be allocated to each element (both delivered and undelivered items) based on their relative selling prices, regardless of whether those selling prices are evidenced by VSOE or TPE or are based on the entity's estimated selling price. Application of the residual method of allocating an overall arrangement fee between delivered and undelivered elements will no longer be permitted. The accounting standard is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The adoption of this consensus did not have a material impact on our consolidated financial statements.

In January 2010, the FASB issued Accounting Standard Update (ASU) 2010-06 which requires reporting entities to make new disclosures about recurring or nonrecurring fair-value measurements including significant transfers into and out of Level 1 and Level 2 fair-value measurements and information on purchases, sales, issuances, and settlements on

a gross basis in the reconciliation of Level 3 fair-value measurements. The FASB also clarified existing fair-value measurement disclosure guidance about the level of disaggregation, inputs, and valuation techniques. Except for the detailed Level 3 roll forward disclosures, we adopted this standard effective January 1, 2010. The adoption of this aspect of the accounting standard did not have any impact on our consolidated financial statements. The new disclosures about purchases, sales, issuances, and settlements in the roll forward activity for Level 3 fair-value measurements are effective for interim and annual reporting periods beginning after December 15, 2010. The adoption of these requirements did not have a material impact on our consolidated financial statements.

In May 2011, the FASB issued ASU No. 2011-04 which represents the converged guidance of the FASB and the IASB (the Boards) on fair value measurements. The collective efforts of the Boards and their staffs, reflected in ASU 2011-04, have resulted in common requirements for measuring fair value and for disclosing information about fair value measurements, including a consistent meaning of the term fair value. The Boards have concluded the common requirements will result in greater comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with GAAP and IFRSs. The amendments in this ASU are required to be applied prospectively, and are effective for interim and annual periods beginning after December 15, 2011. We do not expect that the adoption of ASU 2011-04 will have a significant impact on our consolidated financial statements.

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In June 2011, the FASB issued ASU 2011-05, which amends current comprehensive income guidance. This accounting update eliminates the option to present the components of other comprehensive income as part of the statement of shareholders' equity. Instead, we must report comprehensive income in either a single continuous statement of comprehensive income which contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. ASU 2011-05 will be effective for public companies during the interim and annual periods beginning after Dec. 15, 2011 with early adoption permitted. The adoption of ASU 2011-05 will not have an impact on our consolidated financial statements as it only requires a change in the format of the current presentation.

Note 11. Income Taxes

At December 31, 2010 and June 30, 2011, we had \$0.5 million and \$0.3 million, respectively, of unrecognized tax benefits, all of which would affect our effective tax rate if recognized. We recognize interest and penalties related to unrecognized tax benefits in income tax expense. The tax years 2007 through 2009 remain open to examination by the major taxing jurisdictions to which we are subject.

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various states and foreign jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2007. The examination of our 2006 and 2007 UK income tax returns by HM Revenue and Customs concluded in 2011 with no net adjustment. As a result, we reversed the \$0.2 million reserve for unrecognized tax benefits during the three months ended June 30, 2011, in connection with this examination that we initially recorded in the fourth quarter of 2010.

Our effective income tax rate was 42.9% and 16.6% for the three months ended June 30, 2010 and 2011, respectively, and 40.0% and 23.6% for the six months ended June 30, 2010 and 2011, respectively. Our effective income tax rate for the three and six months ended June 30, 2011 benefited from the lower tax rates applicable to the RS operations in Germany, the organizational restructuring activities undertaken during the latter half of 2010 and the \$0.2 million reversal of the provision for unrecognized tax benefits noted above.

Note 12. Related Party Transactions

Our Executive Vice President and Chief Scientific Officer, Dr. Morganroth, is a cardiologist who, through his wholly-owned professional corporation, provides medical professional services on behalf of the Company. Under this arrangement, Dr. Morganroth's professional corporation receives a percentage fee of 80% of the net amounts we bill for Dr. Morganroth's services to our customers (Percentage Fees). Our President and Chief Executive Officer is responsible for assigning the consulting work to internal and external resources, including Dr. Morganroth, based upon the requirements of the engagement. We recorded revenues in connection with services billed to customers under the consulting arrangement of approximately \$0.3 million in each of the three month periods ended June 30, 2010 and 2011 and \$0.6 million and \$0.8 million in the six month periods ended June 30, 2010 and 2011, respectively. We incurred Percentage Fees of approximately \$0.2 million in each of the three month periods ended June 30, 2010 and 2011, respectively, and \$0.5 million and \$0.7 million in the six-month periods ended June 30, 2010 and 2011, respectively. At December 31, 2010 and June 30, 2011, we owed \$0.2 million and less than \$0.1 million, respectively, to the professional corporation for Percentage Fees. These amounts are included in accounts payable.

Note 13. Commitments and Contingencies

We have a long-term strategic relationship with Healthcare Technology Systems, Inc. (HTS), a leading authority in the research, development and validation of computer administered clinical rating instruments. The strategic relationship includes the exclusive licensing (subject to one pre-existing license agreement) of 57 Interactive Voice Response (IVR) clinical assessments offered by HTS along with HTS's IVR system. As of June 30, 2011, we had paid HTS \$1.5 million for the license and \$1.0 million in advance payments against future royalties. As of June 30, 2011, HTS had earned royalties of \$0.3 million, which were offset against the advance royalty payments. Future royalty payments will be made to HTS based on the level of ePRO revenues received from the assessments and the IVR system, and such royalties will be applied against the advance royalty payments.

On November 28, 2007, we completed the acquisition of CCSS. The acquisition included a marketing agreement under which Covance is obligated to use us as its provider of centralized cardiac safety solutions, and to offer these solutions to Covance's customers, on an exclusive basis, for a 10-year period, subject to certain exceptions. We

expense payments to Covance based upon a portion of the revenues we receive during each calendar year of the 10-year term that are based primarily on referrals made by Covance under the agreement. The agreement does not restrict our continuing collaboration with our other key CRO, Phase I units, Academic Research Centers and other strategic partners.

We offer warranties on certain products for various periods of time. We accrue for the estimated cost of product warranties at the time revenue is recognized. Our product warranty liability reflects management's best estimate of probable liability based on current and historical product sales data and warranty costs incurred.

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Our costs in Germany are subject to foreign exchange fluctuations as the majority of these costs are paid in euros. We enter into foreign exchange contracts to mitigate such foreign exchange fluctuations. These contracts are not designated as hedging instruments and changes in fair value are immediately recognized into earnings in the line item foreign exchange gain (losses). The activity for the quarter ended June 30, 2011 was as follows:

| | Amount | Avg Rate |
|---|----------------|----------|
| Forward Contracts entered in Q2 2011 | \$21.9 million | \$ 1.44 |
| Forward Contracts settled in Q2 2011 | \$13.9 million | \$ 1.44 |
| Forward Contracts open at June 30, 2011 | \$ 8.0 million | \$ 1.44 |

For the six months ended June 30, 2011, we entered into \$25.7 million of foreign exchange forward contracts; \$17.7 million matured and \$8.0 million was outstanding at June 30, 2011. In July 2011, we entered into forward contracts to sell \$5.9 million U.S. dollars and purchase euros at an average of \$1.40 U.S. dollars to 1 euro. Such contracts have various maturities through September 30, 2011.

We are involved in legal proceedings from time to time in the ordinary course of our business. We accrue an estimated loss contingency in our consolidated financial statements if it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Because litigation is inherently unpredictable and unfavorable resolutions can occur, assessing contingencies is highly subjective and requires judgments about future events. We regularly review contingencies to determine whether our accruals are adequate. The amount of ultimate loss may differ from these estimates.

We recognize estimated loss contingencies for litigation in general and administrative operating expenses in our condensed consolidated statements of operations.

In December 2010, we terminated the employment relationship with one of our employees. The employee filed a lawsuit in December 2010 against such termination, applying for a ruling that the termination was not legally effective and that the employment relationship is not terminated. In the second quarter of 2011, we agreed to a settlement with the former employee which did not have a material effect on our consolidated financial statements.

Note 14. Operating Segments / Geographic Information

We consider our business to consist of one segment which is providing services and customizable medical devices to biopharmaceutical organizations and, to a lesser extent, healthcare organizations. We operate on a worldwide basis with two primary locations in the United States, categorized below as North America, and one primary location each in the United Kingdom and Germany. The majority of our revenues are allocated among our geographic segments based upon the profit split transfer pricing methodology, and revenues are generally allocated to the geographic segment in which the work is performed.

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Geographic information is as follows (in thousands of dollars):

Three Months Ended June 30, 2010

| | North America | UK | Germany | Eliminations | Total |
|-------------------------|--------------------------|-----------|----------------|---------------------|--------------|
| Service revenues | \$ 10,837 | \$ 5,285 | \$ 2,575 | \$ | \$ 18,697 |
| Site support revenues | 4,950 | 2,330 | 3,119 | | 10,399 |
| Total revenues | \$ 15,787 | \$ 7,615 | \$ 5,694 | \$ | \$ 29,096 |
| Operating income (loss) | \$ (2,444) | \$ 2,932 | \$ 563 | \$ | \$ 1,051 |
| Long-lived assets | \$ 22,130 | \$ 5,214 | \$ 10,917 | \$ | \$ 38,261 |
| Total assets | \$ 95,831 | \$ 13,002 | \$ 93,018 | \$ | \$ 201,851 |

Three Months Ended June 30, 2011

| | North America | UK | Germany (1) | Eliminations | Total |
|--------------------------------------|--------------------------|-----------|--------------------|---------------------|--------------|
| Service revenues | \$ 10,667 | \$ 4,613 | \$ 7,136 | \$ | \$ 22,416 |
| Site support revenues | 4,507 | 2,756 | 13,170 | | 20,433 |
| Net revenues from external customers | 15,174 | 7,369 | 20,306 | | 42,849 |
| Intersegment revenues | 6,726 | 30 | | (6,756) | |
| Total revenues | \$ 21,900 | \$ 7,399 | \$ 20,306 | \$ (6,756) | \$ 42,849 |
| Operating income (loss) | \$ 1,050 | \$ 1,897 | \$ (377) | \$ | \$ 2,570 |
| Long-lived assets | \$ 23,568 | \$ 7,239 | \$ 16,960 | \$ | \$ 47,767 |
| Total assets | \$ 100,252 | \$ 19,454 | \$ 112,374 | \$ | \$ 232,080 |

Six Months Ended June 30, 2010

| | North America | UK | Germany | Eliminations | Total |
|-------------------------|--------------------------|-----------|----------------|---------------------|--------------|
| Service revenues | \$ 20,781 | \$ 10,176 | \$ 2,575 | \$ | \$ 33,532 |
| Site support revenues | 9,723 | 4,590 | 3,119 | | 17,432 |
| Total revenues | \$ 30,504 | \$ 14,766 | \$ 5,694 | \$ | \$ 50,964 |
| Operating income (loss) | \$ (1,694) | \$ 4,929 | \$ 563 | \$ | \$ 3,798 |
| Long-lived assets | \$ 22,130 | \$ 5,214 | \$ 10,917 | \$ | \$ 38,261 |
| Total assets | \$ 95,831 | \$ 13,002 | \$ 93,018 | \$ | \$ 201,851 |

Six Months Ended June 30, 2011

| | North America | UK | Germany | Eliminations | Total |
|-----------------------|--------------------------|-----------|----------------|---------------------|--------------|
| Service revenues | \$ 20,996 | \$ 9,893 | \$ 15,504 | \$ | \$ 46,393 |
| Site support revenues | 9,179 | 5,230 | 23,746 | | 38,155 |
| | 30,175 | 15,123 | 39,250 | | 84,548 |

Net revenues from external
customers

| | | | | |
|-----------------------|------------|-----------|------------|-----------------------|
| Intersegment revenues | 12,941 | 59 | (13,000) | |
| Total revenues | \$ 43,116 | \$ 15,182 | \$ 39,250 | \$ (13,000) \$ 84,548 |
| Operating income | \$ 1,434 | \$ 4,114 | \$ 2,376 | \$ 7,924 |
| Long-lived assets | \$ 23,568 | \$ 7,239 | \$ 16,960 | \$ 47,767 |
| Total assets | \$ 100,252 | \$ 19,454 | \$ 112,374 | \$ 232,080 |

- (1) During the quarter ended June 30, 2011, we corrected accumulated depreciation related to the first quarter of 2011 for rental equipment of our RS subsidiary in the amount of \$0.5 million. We evaluated the materiality of the correction on our results of operations and concluded it was immaterial to our consolidated financial statements. Accordingly, we recorded this non-cash adjustment in the three months ended June 30, 2011 by increasing cost of sales - site support and increasing accumulated depreciation by \$0.5 million on a pre-tax basis which had the impact of reducing our net income by \$0.4 million. This minimal impact did not affect our reported diluted net income per share.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations
Cautionary Statement for Forward-Looking Information**

You should read the following discussion in conjunction with the financial statements and notes included elsewhere in this Quarterly Report on Form 10-Q. Except for historical matters, the matters discussed in this Form 10-Q are forward-looking statements that involve risks and uncertainties. Forward-looking statements include, but are not limited to, statements within the meaning of the Private Securities Litigation Reform Act of 1995 that reflect our current views as to future events and financial performance with respect to our operations. These statements can be identified by the fact that they do not relate strictly to historical or current facts. They use words such as aim, anticipate, are confident, estimate, expect, will be, will continue, will likely result, project, intend, to and other words and terms of similar meaning in conjunction with a discussion of future operating or financial performance. Our actual results could differ materially from the results contemplated by these forward-looking statements due to a number of factors, including those discussed in other sections of this Quarterly Report on Form 10-Q and in the 2010 Annual Report on Form 10-K.

Overview

eResearchTechnology, Inc. (ERT®), a Delaware corporation, was founded in 1977. ERT and its consolidated subsidiaries collectively are referred to as the Company or we. We are a global technology-driven provider of services and customizable medical devices to biopharmaceutical organizations and, to a lesser extent, healthcare organizations. We are the market leader for centralized cardiac safety (Cardiac Safety) and respiratory efficacy (Respiratory) services in drug development and also collect, analyze and distribute electronic patient reported outcomes (ePRO) information in multiple modalities across all phases of clinical research.

Clinical trials employ diagnostic tests to measure the effect of a drug or device on certain body organs and systems to determine the product's safety and efficacy. Our technology-based services are utilized by biopharmaceutical and healthcare organizations and CROs to improve the accuracy, timeliness and efficiency of trial set-up, data collection from sites worldwide, data interpretation, and new drug, biologic and device application submissions. Our Cardiac Safety solutions include the centralized collection, interpretation and distribution of electrocardiographic (ECG) data and images and are performed during clinical trials in all phases of the clinical research process. Customers use our centralized Respiratory solutions when they are developing new compounds for the treatment of asthma, emphysema, cystic fibrosis and Chronic Obstructive Pulmonary Disease (COPD) in order to assess the efficacy of a drug or to evaluate compounds that have an effect on pulmonary function. We also offer ePRO solutions along with proprietary clinical assessments to enable customers to efficiently and collect and analyze patient-reported feedback during a clinical trial. In addition, we offer site support, which includes the rental and sale of devices to support Cardiac Safety, Respiratory, and ePRO services along with related supplies and logistics management.

On May 28, 2010, we acquired Research Services Germany 234 GmbH (Research Services or RS). RS is comprised of the research services division of CareFusion Germany 234 GmbH and certain research operations of CareFusion Corporation. RS is the source of our Respiratory solutions business and also provides Cardiac Safety and ePRO services. In addition, RS is a manufacturer of diagnostic devices we rent or sell to customers in connection with our services. We paid \$82.7 million for RS. The acquisition and related transaction costs were financed from our existing cash and a portion of the \$23.0 million drawn from our \$40.0 million revolving credit facility through Citizens Bank of Pennsylvania.

Service Offerings

Our revenues by service solution as a percentage of total revenues were as follows:

| | Three Months Ended June | | Six Months Ended June | |
|---------------|-------------------------|-------|-----------------------|-------|
| | 30, | | 30, | |
| | 2010 | 2011 | 2010 | 2011 |
| Net revenues: | | | | |
| Services | 64.3% | 52.3% | 65.8% | 54.9% |
| Site support | 35.7 | 47.7 | 34.2 | 45.1 |

| | | | | |
|--------------------|-------|-------|-------|-------|
| Total net revenues | 100.0 | 100.0 | 100.0 | 100.0 |
|--------------------|-------|-------|-------|-------|

Our services revenues consist primarily of our services offered under our Cardiac Safety, Respiratory and, to a lesser extent, our ePRO solutions that we provide on a fee for services basis and are recognized as the services are performed. We also provide consulting services on a time and materials basis and recognize revenues as we perform the services. Our site support revenue for Cardiac Safety and Respiratory, consisting of equipment rentals and sales along with related supplies and logistics management, are recognized at the time of sale or over the rental period.

Table of Contents***Integrated Product Offering***

With the acquisition of RS, we now provide biopharmaceutical and healthcare organizations a one-stop-shop for clinical services in connection with respiratory trials, including Respiratory efficacy services and devices, centralized Cardiac Safety and related ePRO services and devices in a fully integrated solution, plus a single point of contact for all aspects of the electronic data collection process in clinical trials. Our technology platform also supports the integration of other devices to integrate additional key safety data to support cardiac, respiratory, and other trials.

The protocols of many of the respiratory trials in which we participate often also require ECGs and/or Holter monitoring and ePRO solutions. Our flagship investigator site device, MasterScope[®] CT, is a comprehensive solution for standardized and centralized spirometry, full PFT, ECG and ePRO in clinical trials. Using customized software, this innovative system combines protocol-driven workflows (with many diagnostic applications) into a single easy-to-use clinical trial workstation. These workflows can be specially tailored for multi-center studies. We believe our customers and their users consider the availability of a fully integrated platform for respiratory, cardiac safety and ePRO a major advantage that has enabled us to establish a preferred centralized respiratory vendor status with several of the top 20 pharmaceutical companies.

Results of Operations**Executive Overview**

Net revenues were \$42.9 million for the second quarter of 2011, an increase of \$13.8 million or 47.3% from \$29.1 million in the second quarter of 2010. The revenue changes were due primarily to the contributions by the RS business which we acquired on May 28, 2010. During the second quarter of 2011 we also experienced our second consecutive strong level of business development activities with bookings of \$70.9 million. Backlog was \$333.2 million at June 30, 2011.

Gross margin percentage was 37.4% in the second quarter of 2011 down sequentially from 44.2% in the first quarter of 2011 and down from 54.4% in the second quarter of 2010. The decrease in gross margin percentage sequentially was driven by increased costs in our RS business including incremental labor, consumables and freight charges to support the start of new respiratory studies, negative manufacturing variances and a \$0.5 million non-cash adjustment to the carrying value of returned rental equipment as of March 31, 2011 that was recorded in the June 2011 quarter (refer to Note 14 in our Notes to Consolidated Financial Statements). Further impacting gross profit margin compared to a year ago is the inclusion of a full quarter of RS activity in the second quarter of 2011 compared to only one month in the second quarter of 2010. We expect gross profit margins to improve in the coming quarter as a portion of the charges incurred in the second quarter of 2011 by the German operations are not expected to be recurring and projected increases in revenue should generate higher margins given the operating leverage in our cost structure.

Operating income for the second quarter of 2011 was \$2.6 million or 6.0% of total net revenues compared to \$1.1 million or 3.6% of total net revenues in the second quarter of 2010. Operating income for the second quarter of 2010 was negatively impacted by \$3.8 million of acquisition related costs and \$0.8 million of amortization of acquisition related costs. Operating income for 2011 was negatively impacted by \$2.0 million of amortization of acquisition related costs and the decrease in the gross profit margin. Our effective income tax rate for the second quarter of 2011 was 16.6% compared to 42.9% in the second quarter of 2010 as we have benefited from the lower tax rates applicable to the RS operations in Germany, the organizational restructuring activities undertaken during the latter half of 2010 and the \$0.2 million reversal of a reserve for unrecognized tax benefits in the second quarter of 2011.

Net income for the second quarter of 2011 was \$1.8 million, or \$0.04 per diluted share, compared to \$0.8 million, or \$0.02 per diluted share, in the second quarter of 2010.

We conduct our operations through offices in the United States (U.S.) and Europe (the United Kingdom and Germany). Our international net revenues represented approximately 40% and 64% of total net revenues for the six months ended June 30, 2010 and 2011, respectively. The majority of our revenues are allocated among our geographic segments based upon the profit split transfer pricing methodology which equalizes gross margins for each legal entity based upon its respective direct revenue or direct costs, as determined by the relevant revenue source.

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The following table presents certain financial data as a percentage of total net revenues:

| | Three Months Ended June | | Six Months Ended June | |
|---------------------------------|-------------------------|-------------|-----------------------|-------------|
| | 2010 | 30, 2011 | 2010 | 30, 2011 |
| Net revenues: | | | | |
| Services | 64.3% | 52.3% | 65.8% | 54.9% |
| Site support | 35.7 | 47.7 | 34.2 | 45.1 |
| Total net revenues | 100.0 | 100.0 | 100.0 | 100.0 |
| Costs of revenues: | | | | |
| Cost of services | 28.6 | 31.8 | 30.7 | 31.7 |
| Cost of site support | 17.0 | 30.8 | 15.2 | 27.5 |
| Total costs of revenues | 45.6 | 62.6 | 45.9 | 59.2 |
| Gross margin: | | | | |
| Gross margin services | 55.5 | 39.3 | 53.4 | 42.3 |
| Gross margin site support | 52.3 | 35.5 | 55.5 | 38.9 |
| Gross margin | 54.4 | 37.4 | 54.1 | 40.8 |
| Operating expenses: | | | | |
| Selling and marketing | 13.6 | 10.3 | 14.4 | 10.2 |
| General and administrative | 33.5 | 16.9 | 28.4 | 17.4 |
| Research and development | 3.7 | 4.2 | 3.8 | 3.8 |
| Total operating expenses | 50.8 | 31.4 | 46.6 | 31.4 |
| Operating income | 3.6 | 6.0 | 7.5 | 9.4 |
| Foreign exchange gains (losses) | 1.4 | (0.6) | 1.0 | (1.5) |
| Other income (expense), net | | (0.4) | | (0.3) |
| Income before income taxes | 5.0 | 5.0 | 8.5 | 7.6 |
| Income tax provision | 2.2 | 0.8 | 3.4 | 1.8 |
| Net income | 2.8% | 4.2% | 5.1% | 5.8% |

Table of Contents**Three Months Ended June 30, 2010 Compared to Three Months Ended June 30, 2011.**

The following table presents our consolidated statements of operations with product line detail (dollars in thousands):

| | Three Months Ended June | | | |
|---------------------------------|--------------------------------|-------------|----------------------------|---------|
| | 30, | | | |
| | 2010 | 2011 | Increase (Decrease) | |
| Services: | | | | |
| Net revenues | \$ 18,697 | \$ 22,416 | \$ 3,719 | 19.9% |
| Costs of revenues | 8,325 | 13,615 | 5,290 | 63.5% |
| Gross margin | \$ 10,372 | \$ 8,801 | \$ (1,571) | (15.1%) |
| Site support: | | | | |
| Net revenues | \$ 10,399 | \$ 20,433 | \$ 10,034 | 96.5% |
| Costs of revenues | 4,957 | 13,189 | 8,232 | 166.1% |
| Gross margin | \$ 5,442 | \$ 7,244 | \$ 1,802 | 33.1% |
| Total | | | | |
| Net revenues | \$ 29,096 | \$ 42,849 | \$ 13,753 | 47.3% |
| Costs of revenues | 13,282 | 26,804 | 13,522 | 101.8% |
| Gross margin | 15,814 | 16,045 | 231 | 1.5% |
| Operating expenses: | | | | |
| Selling and marketing | 3,941 | 4,426 | 485 | 12.3% |
| General and administrative | 9,753 | 7,247 | (2,506) | (25.7%) |
| Research and development | 1,069 | 1,802 | 733 | 68.6% |
| Total operating expenses | 14,763 | 13,475 | (1,288) | (8.7%) |
| Operating income | 1,051 | 2,570 | 1,519 | 144.5% |
| Foreign exchange gains (losses) | 399 | (266) | (665) | N.M. |
| Other income (expense), net | (3) | (168) | (165) | N.M. |
| Income before income taxes | 1,447 | 2,136 | 689 | 47.6% |
| Income tax provision | 621 | 355 | (266) | (42.8%) |
| Net income | \$ 826 | \$ 1,781 | \$ 955 | 115.6% |

N.M. Not meaningful

The following table presents costs of revenues as a percentage of related net revenues and operating expenses as a percentage of total net revenues:

| | Three Months Ended June | | |
|------------------|--------------------------------|-------------|----------------------------|
| | 30, | | |
| | 2010 | 2011 | Increase (Decrease) |
| Cost of services | 44.5% | 60.7% | 16.2% |

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| | | | |
|----------------------------|-------|-------|---------|
| Cost of site support | 47.7% | 64.5% | 16.8% |
| Total costs of revenues | 45.6% | 62.6% | 17.0% |
| Operating expenses: | | | |
| Selling and marketing | 13.6% | 10.3% | (3.3%) |
| General and administrative | 33.5% | 16.9% | (16.6%) |
| Research and development | 3.7% | 4.2% | 0.5% |

Table of Contents*Revenues*

Services revenues included \$7.1 million and \$2.6 million for the three months ended June 30, 2011 and 2010, respectively, from the operations of RS. Only one month of RS operations was included in our results for the three months ended June 30, 2010. Apart from the impact of RS, the \$0.8 million decrease in services revenues was primarily due to a reduction in ECG transaction revenue related to a lower volume of transactions performed in the three months ended June 30, 2011 as compared to the three months ended June 30, 2010.

Site support revenues included \$13.2 million and \$3.1 million for the three months ended June 30, 2011 and 2010, respectively, from the operations of RS. Apart from the impact of RS, site support revenues were relatively consistent in the three months ended June 30, 2011 as compared to the three months ended June 30, 2010.

Costs of Revenues

The cost of services revenues included \$6.4 million and \$1.2 million for the three months ended June 30, 2011 and 2010, respectively, from the operations of RS. During the June 2011 quarter, we expanded our RS staff which supports new study set up and customizations in response to increased demand for new studies with aggressive study timelines for key strategic customers in our respiratory and ePRO business lines. Apart from the impact of RS, the cost of services revenues, both in absolute terms and as a percentage of services revenues, increased for the three months ended June 30, 2011 as compared to the three months ended June 30, 2010 due to a \$0.2 million increase in labor costs associated with additional headcount and a \$0.1 million increase in costs billed to a customer as pass-through costs.

The cost of site support revenues included \$9.8 million and \$1.7 million for the three months ended June 30, 2011 and 2010, respectively, from the operations of RS. During the June 2011 quarter, we incurred additional labor, consumables, freight charges and negative manufacturing variances to support the start of new respiratory and ePRO studies. In addition, during the June 2011 quarter, we corrected accumulated depreciation related to the first quarter of 2011 for rental equipment of our RS subsidiary in the amount of \$0.5 million, by increasing cost of sales site support and increasing accumulated depreciation. Apart from the impact of RS, there was a \$0.2 million increase in the cost of site support revenues for the three months ended June 30, 2011 as compared to the three months ended June 30, 2010. The increase in the cost of site support revenues, both in absolute terms and as a percentage of site support revenues, was primarily due to an increase in depreciation resulting from purchases of rental equipment and the implementation of a new logistics management system.

Operating Expenses

Selling and marketing expenses included \$1.0 million and \$0.4 million for the three months ended June 30, 2011 and 2010, respectively, from the operations of RS. Apart from the impact of RS, selling and marketing expenses decreased \$0.1 million for the three months ended June 30, 2011 as compared to the three months ended June 30, 2010. The decrease in selling and marketing expenses was due to a number of small changes in expenses. Excluding the impact of RS, the small increase in selling and marketing expenses as a percentage of total net revenues reflects the fact that some of the costs do not necessarily change in direct relation with changes in revenue.

General and administrative expenses included \$2.4 million and \$1.2 million for the three months ended June 30, 2011 and 2010, respectively, from the operations of RS. Apart from the impact of RS, general and administrative expenses decreased \$3.7 million for the three months ended June 30, 2011 as compared to the three months ended June 30, 2010. The decrease in general and administrative expenses, both in absolute terms and as a percentage of total net revenues, was due primarily to \$3.3 million of professional fees incurred related to transaction costs in 2010 associated with our acquisition of RS. Additionally, in 2010, we added \$0.6 million to the reserve for losses on the lease of our Reno, Nevada facility. There were also smaller decreases in incentive compensation, consulting and stock option expense in the three months ended June 30, 2011. Partially offsetting these decreases was an increase in labor costs which included a reduction in the capitalized labor for IT staff who worked on development projects in 2010 but not in 2011, an increase in 401(k) company matches due to the increase in bonus payments in 2011 and the impact of salary merit increases.

Research and development expenses included \$1.0 million and \$0.3 million for the three months ended June 30, 2010 and 2011, respectively, from the operations of RS. Apart from the impact of RS, there was a small increase in research and development expenses, both in absolute terms and as a percentage of total net revenues, for the three months

ended June 30, 2011 as compared to the three months ended June 30, 2010.

Foreign exchange gains (losses) moved from a gain of \$0.4 million for the three months ended June 30, 2010 to a loss of \$0.3 million for the three months ended June 30, 2011 primarily due to the movement in the exchange rate between the euro and U.S. dollar that impacts our operations in Germany, particularly accounts receivable denominated in U.S. dollars. We entered into forward contracts to sell \$21.9 million U.S. dollars and purchase euros at an average price of \$1.44 U.S. dollars to 1 euro during the three months ended June 30, 2011. The related losses were insignificant.

Other income (expense), net, changed as we incurred interest expense on advances under our line of credit in the three months ended June 30, 2011 while the three months ended June 30, 2010 included a small amount of interest income on our cash balance, a substantial portion of which we used to purchase RS in May 2010.

Our effective tax rate for the three months ended June 30, 2011 was 16.6% compared to 42.9% for the three months ended June 30, 2010. Our effective income tax rate for the three months ended June 30, 2011 benefited from the lower tax rates applicable to the RS operations in Germany, organizational restructuring activities undertaken during the latter half of 2010 and a \$0.2 million reversal of the reserve for unrecognized tax benefits during the three months ended June 30, 2011 as a result of the conclusion of the examination of our 2006 and 2007 UK income tax returns.

Table of Contents**Six Months Ended June 30, 2010 Compared to Six Months Ended June 30, 2011.**

The following table presents our consolidated statements of operations with product line detail (dollars in thousands):

| | Six Months Ended June 30, | | Increase (Decrease) | |
|---------------------------------|----------------------------------|-------------|----------------------------|---------|
| | 2010 | 2011 | | |
| Services: | | | | |
| Net revenues | \$ 33,532 | \$ 46,393 | \$ 12,861 | 38.4% |
| Costs of revenues | 15,636 | 26,771 | 11,135 | 71.2% |
| Gross margin | \$ 17,896 | \$ 19,622 | \$ 1,726 | 9.6% |
| Site support: | | | | |
| Net revenues | \$ 17,432 | \$ 38,155 | \$ 20,723 | 118.9% |
| Costs of revenues | 7,756 | 23,312 | 15,556 | 200.6% |
| Gross margin | \$ 9,676 | \$ 14,843 | \$ 5,167 | 53.4% |
| Total | | | | |
| Net revenues | \$ 50,964 | \$ 84,548 | \$ 33,584 | 65.9% |
| Costs of revenues | 23,392 | 50,083 | 26,691 | 114.1% |
| Gross margin | 27,572 | 34,465 | 6,893 | 25.0% |
| Operating expenses: | | | | |
| Selling and marketing | 7,349 | 8,601 | 1,252 | 17.0% |
| General and administrative | 14,498 | 14,755 | 257 | 1.8% |
| Research and development | 1,927 | 3,185 | 1,258 | 65.3% |
| Total operating expenses | 23,774 | 26,541 | 2,767 | 11.6% |
| Operating income | 3,798 | 7,924 | 4,126 | 108.6% |
| Foreign exchange gains (losses) | 479 | (1,275) | (1,754) | N.M. |
| Other income (expense), net | 17 | (269) | (286) | N.M. |
| Income before income taxes | 4,294 | 6,380 | 2,086 | 48.6% |
| Income tax provision | 1,716 | 1,506 | (210) | (12.2%) |
| Net income | \$ 2,578 | \$ 4,874 | \$ 2,296 | 89.1% |

N.M. Not meaningful

The following table presents costs of revenues as a percentage of related net revenues and operating expenses as a percentage of total net revenues:

| | Six Months Ended June 30, | | Increase |
|-------------------------|----------------------------------|-------------|-------------------|
| | 2010 | 2011 | (Decrease) |
| Cost of services | 46.6% | 57.7% | 11.1% |
| Cost of site support | 44.5% | 61.1% | 16.6% |
| Total costs of revenues | 45.9% | 59.2% | 13.3% |

| | | | |
|----------------------------|-------|-------|---------|
| Operating expenses: | | | |
| Selling and marketing | 14.4% | 10.2% | (4.2%) |
| General and administrative | 28.4% | 17.4% | (11.0%) |
| Research and development | 3.8% | 3.8% | 0.0% |

Table of Contents*Revenues*

Services revenues included \$15.5 million and \$2.6 million for the six months ended June 30, 2011 and 2010, respectively, from the operations of RS. Only one month of RS operations was included in our results for the six months ended June 30, 2010. Apart from the impact of RS, services revenues were relatively consistent in the six months ended June 30, 2011 as compared to the six months ended June 30, 2010.

Site support revenues included \$23.7 million and \$3.1 million for the six months ended June 30, 2011 and 2010, respectively, from the operations of RS. Apart from the impact of RS, site support revenues increased approximately \$0.1 million in the six months ended June 30, 2011 as compared to the six months ended June 30, 2010.

Costs of Revenues

The cost of services revenues included \$12.1 million and \$1.2 million for the six months ended June 30, 2011 and 2010, respectively, from the operations of RS. During the June 2011 quarter, we expanded our RS staff which supports new study set up and customizations in response to increased demand for new studies with aggressive study timelines for key strategic customers in our respiratory and ePRO business lines. Apart from the impact of RS, the cost of services revenues increased \$0.4 million for the six months ended June 30, 2011 as compared to the six months ended June 30, 2010. The increase in the cost of services revenues, both in absolute terms and as a percentage of services revenues, was due to a \$0.5 million increase in labor costs associated with additional headcount and a \$0.2 million increase in costs billed to customers as pass-through costs, partially offset by decreases in several areas including incentive compensation, amortization and telephone and connectivity expenses.

The cost of site support revenues included \$16.4 million and \$1.7 million for the six months ended June 30, 2011 and 2010, respectively, from the operations of RS. During the June 2011 quarter, we incurred additional labor, consumables, freight charges and negative manufacturing variances to support the start of new respiratory and ePRO studies. Apart from the impact of RS, there was a \$0.9 million increase in the cost of site support for the six months ended June 30, 2011 as compared to the six months ended June 30, 2010. The increase in the cost of site support revenues, both in absolute terms and as a percentage of site support revenues, was primarily due to a \$0.5 million increase in labor that was largely a result of a change in the classification of the costs associated with the customer support center to report these as additional costs of site support in 2010 to better align costs with related revenue, an increase in depreciation resulting from purchases of rental equipment and the implementation of a new logistics management system.

Operating Expenses

Selling and marketing expenses included \$1.9 million and \$0.4 million for the six months ended June 30, 2011 and 2010, respectively, from the operations of RS. Apart from the impact of RS, selling and marketing expenses decreased \$0.2 million for the six months ended June 30, 2011 as compared to the six months ended June 30, 2010. The decrease in selling and marketing expenses, both in absolute terms and as a percentage of total revenues, was due to a number of small changes in expenses.

General and administrative expenses included \$4.8 million and \$1.2 million for the six months ended June 30, 2011 and 2010, respectively, from the operations of RS. Apart from the impact of RS, general and administrative expenses decreased \$3.3 million for the six months ended June 30, 2011 as compared to the six months ended June 30, 2010. The decrease, both in absolute terms and as a percentage of total revenues, was due primarily to \$3.3 million of professional fees incurred related to transaction costs in 2010 associated with our acquisition of RS. Additionally, in 2010, we added \$0.6 million to the reserve for losses on the lease of our Reno, Nevada facility. There were also decreases in consulting of \$0.5 million and stock option expense of \$0.2 million for the six months ended June 30, 2011. Partially offsetting these decreases was an increase in labor costs which included a reduction in the capitalized labor for IT staff who worked on development projects in 2010 but not in 2011, an increase in 401(k) company matches due to the increase in bonus payments in 2011, and the impact of salary merit increases.

Research and development expenses included \$1.6 million and \$0.3 million for the six months ended June 30, 2010 and 2011, respectively, from the operations of RS. Apart from the impact of RS, there was a small decrease in research and development expenses, both in absolute terms and as a percentage of total net revenues.

Foreign exchange gains (losses) moved from a gain of \$0.5 million for the six months ended June 30, 2010 to a loss of \$1.3 million for the six months ended June 30, 2011 primarily due to the movement in the exchange rate between the

euro and U.S. dollar that impacts our operations in Germany, particularly accounts receivable denominated in U.S. dollars, as well as movement in the exchange rate between the UK pound and U.S. dollar that impacts our operations in the UK, particularly accounts receivable denominated in U.S. dollars. We entered into forward contracts to sell \$25.7 million U.S. dollars and purchase euros at an average price of \$1.43 U.S. dollars to 1 euro during the six months ended June 30, 2011. The related losses were insignificant.

Other income (expense), net, changed as we incurred interest expense on advances under our line of credit in 2011 while 2010 included a small amount of interest income on our cash balance, a substantial portion of which we used to purchase RS in May 2010.

Our effective tax rate for the six months ended June 30, 2011 was 23.6% compared to 40.0% for the six months ended June 30, 2010. Our effective income tax rate for the six months ended June 30, 2011 benefited from the lower tax rates applicable to the RS operations in Germany, organizational restructuring activities undertaken during the latter half of 2010 and a \$0.2 million reversal of the reserve for unrecognized tax benefits during the six months ended June 30, 2011 as a result of the conclusion of the examination of our 2006 and 2007 UK income tax returns.

Table of Contents**Liquidity and Capital Resources**

At June 30, 2011, we had \$31.6 million of cash, cash equivalents and short-term investments, primarily invested in money market funds and commercial bank accounts. Of the \$31.6 million, \$10.0 million and \$10.2 million are held by our UK and German subsidiaries, respectively. Although a portion of our UK subsidiary's and all of our German subsidiary's current undistributed net earnings, as well as any future net earnings of our UK and German subsidiaries, will be permanently reinvested, we believe that this does not have a material impact on our overall liquidity.

For the six months ended June 30, 2011, our operations provided cash of \$13.7 million, an increase of \$1.3 million compared to \$12.4 million during the six months ended June 30, 2010. The increase was primarily the result of an \$8.4 million increase for the six months ended June 30, 2011 as compared to the six months ended June 30, 2010 in net income before depreciation and amortization as well as a \$3.6 million decrease in accounts receivable in the six months ended June 30, 2011 as compared to a \$1.7 million increase in the six months ended June 30, 2010. A number of items partially offset this increase, primarily inventory and accrued expenses. The decrease in the June 30, 2011 accrued expenses was largely due to the payment of the 2010 incentive compensation in the first quarter of 2011. The 2010 incentive compensation was significantly higher than the 2009 amount, which was paid in the first quarter of 2010.

For the six months ended June 30, 2011, our investing activities used cash of \$14.9 million as compared to \$79.5 million during the six months ended June 30, 2010, which included \$80.5 million used for the RS acquisition. Proceeds from sales of investments, net of purchases, were \$9.7 million during the six months ended June 30, 2010, with no activity during the six months ended June 30, 2011.

During the six months ended June 30, 2010 and 2011, we capitalized \$8.8 million and \$14.8 million, respectively, of property and equipment. Included in property and equipment acquisitions was \$2.5 million and \$6.5 million for the six months ended June 30, 2010 and 2011, respectively, of internal use software. The balance of the change was primarily due to an increase in purchases of rental equipment. The purchase of rental equipment included the activity of RS for only one month in the six months ended June 30, 2010.

For the six months ended June 30, 2011, our financing activities provided cash of \$0.6 million as compared to \$23.2 million for the six months ended June 30, 2010. The six months ended June 30, 2010 included proceeds from long-term debt of \$23.0 million associated with the RS acquisition.

We have a revolving line of credit arrangement with Citizens Bank of Pennsylvania in the aggregate amount of \$40.0 million, with an additional \$10.0 million increase option. As of June 30, 2011, we had outstanding \$21.0 million under our line of credit and \$29.0 million remained available for us to borrow including the increase option. The line has a three-year term which expires May 27, 2013 and annual interest rates based upon LIBOR plus a margin of 1.00% to 1.75% based upon a total leverage ratio and unused commitment fees of 0.10% to 0.20% based upon the same total leverage ratio. During the six-month period ended June 30, 2011, the annual interest rate ranged from 1.44% to 1.51% and the unused commitment fee was 0.15%. Financial covenants include maximum total senior funded debt to earnings before interest, income taxes, depreciation and amortization (EBITDA) of 2.0 and minimum debt service coverage ratio of 1.5. At June 30, 2011, the Company was in compliance with all debt covenants. Borrowings under the line of credit are secured by 65% of the capital stock in certain of our foreign subsidiaries.

In December 2010, we entered into a commitment to purchase \$5.1 million of equipment from a manufacturer over a 15-month period beginning in January 2011. We expect to purchase this cardiac safety equipment in the normal course of business and thus this commitment does not represent a significant commitment above our expected routine purchases of ECG equipment during this period. As of June 30, 2011, approximately \$2.1 million of equipment was purchased under the commitment; accordingly the balance of such commitment as of June 30, 2011 was \$3.0 million.

In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Act of 2010 became law. The provisions of the Acts have not had, and are not expected to have, a significant impact to our consolidated financial statements.

We expect that existing cash and cash equivalents, cash flows from operations and amounts available under the \$40 million credit facility as discussed above will be sufficient to meet our foreseeable cash needs for at least the next year. In addition, there may be acquisition and other growth opportunities that require additional external financing and we may from time to time seek to obtain additional funds from the public or private issuances of equity or debt

securities. There can be no assurance that any such acquisitions will occur or that such financing will be available or available on terms acceptable to us, particularly in view of current capital market uncertainty.

Our board of directors has authorized the repurchase of up to an aggregate of 12.5 million shares, of which 5.0 million shares remain available for purchase as of June 30, 2011. The stock buy-back authorization allows us, but does not require us, to purchase the authorized shares. The purchase of the remaining shares authorized could require us to use a significant portion of our cash, cash equivalents and investments and could also require us to seek additional external financing. No shares were purchased during the six months ended June 30, 2011 or 2010. The 7,363 additional shares added to treasury shares in the six months ended June 30, 2011 were the result of employee tax liabilities related to restricted stock awards that were funded by the employees surrendering their rights to the respective amount of vested shares.

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Inflation

We believe the effects of inflation and changing prices generally do not have a material effect on our consolidated results of operations or financial condition.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our primary financial market risks include fluctuations in interest rates and currency exchange rates.

Interest Rate Risk

Long-term debt

At June 30, 2011, our long-term debt was comprised of \$21.0 million drawn under our \$40.0 million credit facility with Citizens Bank of Pennsylvania. We do not manage the interest rate risk on our debt through the use of derivative instruments. Our credit facility's interest rates may be reset due to fluctuations in the London Interbank Offered Rate (LIBOR). A hypothetical 100-basis-point change in the interest rate of our credit facilities would change our annual pre-tax earnings by \$0.2 million based on our current borrowings under the credit facility.

Investments

We generally place our investments in highly-rated securities such as money market funds, municipal securities, bonds of government sponsored agencies, certificates of deposit with fixed rates with maturities of less than one year and A1P1 rated commercial bonds and paper. We actively manage our portfolio of cash equivalents and short-term investments, but in order to ensure liquidity, will only invest in instruments with high credit quality where a secondary market exists. We have not held and do not hold any derivatives related to our interest rate exposure. Due to the average maturity and conservative nature of our investment portfolio, a sudden change in interest rates would not have a material effect on the value of the portfolio. The impact on interest income of future changes in investment yields will depend largely on the gross amount of our cash, cash equivalents, short-term investments and long-term investments. See *Liquidity and Capital Resources* as part of *Management's Discussion and Analysis of Financial Condition and Results of Operations*.

Foreign Currency Risk

We operate on a global basis from locations in the United States (U.S.), the United Kingdom (UK) and Germany. All international net revenues and expenses are billed or incurred in either U.S. dollars, pounds sterling or euros. As such, we face exposure to adverse movements in the exchange rate of the pound sterling and euro. As the currency rate changes, translation of the statement of operations of our UK and German subsidiaries from the local currency to U.S. dollars affects year-to-year comparability of operating results. With the recent RS acquisition, there has been a significant increase in activity in countries outside the U.S. Our costs in Germany are subject to foreign exchange fluctuations as the majority of these costs are paid in euros. As a result, we entered into foreign exchange contracts during the six months ended June 30, 2011 to mitigate such foreign exchange fluctuations. Contracts totaling \$16.7 million settled during the six months ended June 30, 2011 at an average price of \$1.43 U.S. dollars to 1 euro. One contract remained open at June 30, 2011 to sell \$8.0 million U.S. dollars and purchase euros at a rate of \$1.44 U.S. dollars to 1 euro that we settled on July 29, 2011. In July 2011, we entered into forward contracts to sell \$5.9 million U.S. dollars and purchase euros at an average of \$1.40 U.S. dollars to 1 euro. Such contracts have various maturities through September 30, 2011.

Management estimates that a 10% change in the exchange rate of the pound sterling and euro would have impacted the reported operating income for the six months ended June 30, 2011 by approximately \$0.6 million. In addition, management estimates the effect of a 10% change in the exchange rates at June 30, 2011, primarily on U.S. dollar denominated accounts receivable held by our foreign subsidiaries, would have impacted the reported foreign exchange gains (losses) for the six months ended June 30, 2011 by approximately \$1.3 million before income taxes.

Item 4. Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures as of the end of the period covered by this report were designed and functioning effectively to provide reasonable assurance that information required to be disclosed by the Company (including our

consolidated subsidiaries) in the reports we file with or submit to the Securities and Exchange Commission is (i) recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms and (ii) accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. There were no changes in our internal control over financial reporting during the quarter ended June 30, 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II. Other Information

Item 6. Exhibits

- 10.31 Amended and Restated 2003 Equity Incentive Plan, as amended.*
- 10.44 Management Employment Agreement effective May 1, 2011 between Jeffrey S. Litwin and the Company.*
- 31.1 Certification of Chief Executive Officer.
- 31.2 Certification of Chief Financial Officer.
- 32.1 Statement of Chief Executive Officer Pursuant to Section 1350 of Title 18 of the United States Code.
- 32.2 Statement of Chief Financial Officer Pursuant to Section 1350 of Title 18 of the United States Code.

* Management contract or compensatory plan or arrangement

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Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

eResearchTechnology, Inc.
(Registrant)

Date: August 5, 2011

By: /s/ Jeffrey S. Litwin, MD, F.A.C.C

Jeffrey S. Litwin, MD, F.A.C.C.
President and Chief Executive Officer,
(Principal executive officer)

Date: August 5, 2011

By: /s/ Keith D. Schneck

Keith D. Schneck
Executive Vice President, Chief Financial
Officer, Treasurer and Secretary
(Principal financial and accounting officer)

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EXHIBIT INDEX

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