

Willdan Group, Inc.
Form 10-Q
August 11, 2011
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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

x

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

For the quarterly period ended July 1, 2011

OR

o

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

For the transition period from to

Commission file number 001-33076

WILLDAN GROUP, INC.

(Exact Name of Registrant as Specified in Its Charter)

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(State or other Jurisdiction of
Incorporation or Organization)

(IRS Employer Identification No.)

2401 East Katella Avenue, Suite 300
Anaheim, California
(Address of principal executive offices)

92806
(Zip code)

Registrant's Telephone Number, Including Area Code: **(800) 424-9144**

Not Applicable

(Former name, former address and former fiscal year, if changed since last report).

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

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

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

As of August 8, 2011, there were 7,270,368 shares of common stock, \$0.01 par value per share, of Willdan Group, Inc. issued and outstanding.

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**WILLDAN GROUP, INC.
FORM 10-Q QUARTERLY REPORT**

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	July 1, 2011 (unaudited)	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	\$ 7,174,000	\$ 6,642,000
Accounts receivable, net of allowance for doubtful accounts of \$741,000 and \$959,000 at July 1, 2011 and December 31, 2010, respectively	11,272,000	14,484,000
Costs and estimated earnings in excess of billings on uncompleted contracts	15,683,000	11,343,000
Other receivables	173,000	176,000
Prepaid expenses and other current assets	1,420,000	1,714,000
Total current assets	35,722,000	34,359,000
Equipment and leasehold improvements, net	1,362,000	1,496,000
Goodwill	15,208,000	12,475,000
Other intangible assets, net	68,000	95,000
Other assets	386,000	407,000
Deferred income taxes, net of current portion	622,000	622,000
Total assets	\$ 53,368,000	\$ 49,454,000
Liabilities and Stockholders Equity		
Current liabilities:		
Excess of outstanding checks over bank balance	\$ 1,512,000	\$ 1,223,000
Borrowings under line of credit		1,000,000
Accounts payable	3,986,000	5,380,000
Purchase price payable	2,733,000	
Accrued liabilities	8,490,000	5,985,000
Billings in excess of costs and estimated earnings on uncompleted contracts	1,313,000	1,041,000
Current portion of notes payable	88,000	90,000
Current portion of capital lease obligations	175,000	173,000
Current portion of deferred income taxes	1,407,000	1,407,000
Total current liabilities	19,704,000	16,299,000
Notes payable, less current portion	113,000	131,000
Capital lease obligations, less current portion	96,000	96,000
Deferred lease obligations	699,000	766,000
Total liabilities	20,612,000	17,292,000
Commitments and contingencies		
Stockholders equity:		

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Preferred stock, \$0.01 par value, 10,000,000 shares authorized, no shares issued and outstanding

Common stock, \$0.01 par value, 40,000,000 shares authorized: 7,257,000 and 7,246,000 shares issued and outstanding at July 1, 2011 and December 31, 2010, respectively	72,000	72,000
Additional paid-in capital	33,915,000	33,765,000
Accumulated deficit	(1,231,000)	(1,675,000)
Total stockholders' equity	32,756,000	32,162,000
Total liabilities and stockholders' equity	\$ 53,368,000	\$ 49,454,000

See accompanying notes to condensed consolidated financial statements.

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WILLDAN GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended		Six Months Ended	
	July 1, 2011	July 2, 2010	July 1, 2011	July 2, 2010
Contract revenue	\$ 25,812,000	\$ 20,367,000	\$ 48,554,000	\$ 37,318,000
Direct costs of contract revenue:				
Salaries and wages	6,628,000	5,612,000	12,999,000	10,626,000
Subconsultant services	6,567,000	3,542,000	13,793,000	5,479,000
Other direct costs	2,321,000	1,644,000	2,287,000	2,986,000
Total direct costs of contract revenue	15,516,000	10,798,000	29,079,000	19,091,000
Gross profit	10,296,000	9,569,000	19,475,000	18,227,000
General and administrative expenses:				
Salaries and wages, payroll taxes and employee benefits	5,303,000	4,484,000	10,864,000	8,926,000
Facilities and facilities related	1,319,000	1,035,000	2,397,000	2,129,000
Stock-based compensation	54,000	48,000	108,000	128,000
Depreciation and amortization	229,000	239,000	486,000	510,000
Other	2,437,000	2,498,000	4,946,000	4,884,000
Total general and administrative expenses	9,342,000	8,304,000	18,801,000	16,577,000
Income from operations	954,000	1,265,000	674,000	1,650,000
Other income (expense), net:				
Interest income	2,000	1,000	4,000	6,000
Interest expense	(14,000)	(18,000)	(32,000)	(26,000)
Other, net	(8,000)	10,000	(3,000)	20,000
Total other expense, net	(20,000)	(7,000)	(31,000)	(1,000)
Income before income taxes	934,000	1,258,000	643,000	1,650,000
Income tax expense	199,000		199,000	
Net income	\$ 735,000	\$ 1,258,000	\$ 444,000	\$ 1,650,000
Earnings per share:				
Basic and diluted	\$ 0.10	\$ 0.17	\$ 0.06	\$ 0.23
Weighted-average shares outstanding:				
Basic	7,257,000	7,229,000	7,254,000	7,226,000
Diluted	7,471,000	7,252,000	7,476,000	7,240,000

See accompanying notes to condensed consolidated financial statements.

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WILLDAN GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended	
	July 1, 2011	July 2, 2010
Cash flows from operating activities:		
Net income	\$ 444,000	\$ 1,650,000
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	519,000	518,000
Lease abandonment expense, net	9,000	13,000
Loss (gain) on sale of equipment	7,000	(19,000)
Provision for doubtful accounts	64,000	210,000
Stock-based compensation	108,000	128,000
Changes in operating assets and liabilities:		
Accounts receivable	3,148,000	(1,646,000)
Costs and estimated earnings in excess of billings on uncompleted contracts	(4,340,000)	(4,571,000)
Other receivables	3,000	41,000
Prepaid expenses and other current assets	294,000	(4,000)
Other assets	21,000	(38,000)
Accounts payable	(1,394,000)	(71,000)
Accrued liabilities	2,505,000	1,836,000
Billings in excess of costs and estimated earnings on uncompleted contracts	272,000	350,000
Deferred lease obligations	(76,000)	(134,000)
Net cash provided by (used in) operating activities	1,584,000	(1,737,000)
Cash flows from investing activities:		
Purchase of equipment and leasehold improvements	(263,000)	(241,000)
Proceeds from sale of equipment	1,000	30,000
Net cash used in investing activities	(262,000)	(211,000)
Cash flows from financing activities:		
Changes in excess of outstanding checks over bank balance	289,000	310,000
Payments on notes payable	(43,000)	(20,000)
Proceeds from notes payable	23,000	
Borrowings under line of credit	13,667,000	5,470,000
Repayments on line of credit	(14,667,000)	(5,470,000)
Principal payments on capital lease obligations	(101,000)	(81,000)
Proceeds from sales of common stock under employee stock purchase plan	42,000	47,000
Net cash (used in) provided by financing activities	(790,000)	256,000
Net increase (decrease) in cash and cash equivalents	532,000	(1,692,000)
Cash and cash equivalents at beginning of the period	6,642,000	8,445,000
Cash and cash equivalents at end of the period	\$ 7,174,000	\$ 6,753,000
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	\$ 37,000	\$ 28,000
Income taxes	18,000	2,000
Supplemental disclosures of noncash investing and financing activities:		
Equipment acquired under capital lease obligations	\$ 103,000	\$ 51,000
Purchase price payable	2,733,000	2,000,000

See accompanying notes to condensed consolidated financial statements.

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WILLDAN GROUP, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

**July 1, 2011
(Unaudited)**

1. BASIS OF PRESENTATION, ORGANIZATION AND OPERATIONS OF THE COMPANY

Basis of Presentation

The accompanying unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) and pursuant to the rules and regulations of the Securities and Exchange Commission and reflect all adjustments, which consist of only normal recurring adjustments, which are, in the opinion of management, necessary for a fair presentation of the consolidated results for the interim periods presented. Results for the interim periods are not necessarily indicative of results for the full year. Certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. The consolidated financial statements should be read in conjunction with Willdan Group, Inc. s 2010 Annual Report on Form 10-K filed on March 29, 2011.

Nature of Business

Willdan Group, Inc. and subsidiaries (Willdan Group or the Company) is a provider of professional technical and consulting services to small and mid-sized public agencies, large public utilities and, to a lesser extent, private industry in California, New York, Arizona and to a lesser extent, other states throughout the United States. The Company enables these public agencies to provide a wide range of specialized services without having to incur and maintain the overhead necessary to develop staffing in-house. The Company provides a broad range of services including civil engineering and planning, energy efficiency and sustainability, economic and financial consulting, homeland security and communications and technology. Clients primarily consist of cities, counties, public utilities, redevelopment agencies, water districts, school districts and universities, state agencies, federal agencies, a variety of other special districts and agencies, private industry and tribal governments.

Principles of Consolidation

The consolidated financial statements include the accounts of Willdan Group, Inc. and its wholly owned subsidiaries, Willdan Engineering, Willdan Energy Solutions, Public Agency Resources, Willdan Financial Services and Willdan Homeland Solutions. All significant intercompany balances and transactions have been eliminated in consolidation.

Accounting for Contracts

The Company enters into contracts with its clients that contain three principal types of pricing provisions: fixed price, time and materials, and unit based. Revenue on fixed price contracts is recognized on the percentage of completion method based generally on the ratio of direct costs (primarily exclusive of depreciation and amortization costs) incurred to date to estimated total direct costs at completion. Revenue on time and materials and unit based contracts is recognized as the work is performed in accordance with the specific terms of the contract. Contracts that provide for multiple services or deliverables are evaluated as multiple-element arrangements to determine the appropriate unit of accounting, allocation of contract value, and method of revenue recognition for each element. Revenue for amounts that have been billed but not earned is deferred and such deferred revenue is referred to as billings in excess of costs and estimated earnings on uncompleted contracts in the accompanying consolidated balance sheets.

Adjustments to contract cost estimates are made in the periods in which the facts requiring such revisions become known. When the revised estimate indicates a loss, such loss is provided for currently in its entirety. Claims revenue is recognized only upon resolution of the claim. Change orders in dispute are evaluated as claims. Costs related to un-priced change orders are expensed when incurred and recognition of the related contract revenue is based on an evaluation of the probability of recovery of the costs. Estimated profit is recognized for un-priced change orders if realization of the expected price of the change order is probable.

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Applying the percentage-of-completion method of recognizing revenue requires the Company to estimate the outcome of its long-term contracts. The Company forecasts such outcomes to the best of its knowledge and belief of current and expected conditions and its expected course of action. Differences between the Company's estimates and actual results often occur resulting in changes to reported revenue and earnings. Such changes could have a material effect on future consolidated financial statements.

Direct costs of contract revenue consist primarily of that portion of technical and nontechnical salaries and wages that has been incurred in connection with revenue producing projects. Direct costs of contract revenue also include production expenses, subconsultant services and other expenses that are incurred in connection with revenue producing projects.

Direct costs of contract revenue exclude that portion of technical and nontechnical salaries and wages related to marketing efforts, vacations, holidays and other time not spent directly generating revenue under existing contracts. Such costs are included in general and administrative expenses. Additionally, payroll taxes, bonuses and employee benefit costs for all Company personnel are included in general and administrative expenses in the accompanying consolidated statements of operations since no allocation of these costs is made to direct costs of contract revenue. No allocation of facilities costs is made to direct costs of contract revenue. Other companies may classify as direct costs of contract revenue some of the costs that the Company classifies as general and administrative costs. The Company expenses direct costs of contract revenue when incurred.

Accounts receivable are carried at original invoice amount less an estimate made for doubtful accounts based upon a review of all outstanding amounts on a quarterly basis. Management determines the allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Credit risk is generally minimal with governmental entities, but disputes may arise related to these receivable amounts. Accounts receivables are written off when deemed uncollectible. Recoveries of accounts receivables previously written off are recorded when received.

The value of retainage is included in accounts receivable in the accompanying consolidated financial statements. Retainage represents the billed amount that is retained by the customer, in accordance with the terms of the contract, generally until performance is substantially complete. At July 1, 2011 and December 31, 2010, the Company had retained accounts receivable of approximately \$532,000 and \$547,000, respectively.

Fair Value of Financial Instruments

The Company's cash, cash equivalents, accounts receivable, costs and estimated earnings in excess of billings on uncompleted contracts, income tax receivable, other receivables, prepaid expenses and other current assets, excess of outstanding checks over bank balance, accounts payable, purchase price payable, accrued liabilities and billings in excess of costs and estimated earnings on uncompleted contracts approximate their fair values because of the relatively short period of time between the origination of these instruments and their expected realization or payment. The carrying amounts of debt obligations approximate their fair values since the terms are comparable to terms currently offered by local lending institutions for loans of similar terms to companies with comparable credit risk.

Use of Estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

2. BUSINESS COMBINATION

On June 9, 2008, the Company acquired all of the outstanding stock of Willdan Energy Solutions, formerly known as Intergy Corporation, a California based consulting company that assists companies, institutions and agencies with planning and implementing their energy efficiency, water conservation and renewable energy

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strategies. The acquisition cost recorded by the Company as of July 1, 2011 was \$17.9 million, consisting of \$9.9 million in cash paid at closing, a \$0.2 million net asset value adjustment, a guaranteed payment of \$1.0 million in cash paid in June 2009, an earn-out payment of \$1.3 million paid in August 2009, an earn-out payment of \$2.1 million paid in September 2010, an earn-out payment of \$2.7 million to be paid in August 2011 and \$0.7 million in transaction costs. The final earn-out payment was required because Willdan Energy Solutions achieved certain financial targets over the twelve month period ending July 1, 2011. The Company has recorded \$15.2 million of goodwill associated with the acquisition through July 1, 2011.

3. GOODWILL AND OTHER INTANGIBLE ASSETS

As of July 1, 2011 and December 31, 2010, the Company had \$15.2 million and \$12.5 million of goodwill, respectively, all of which relates to the Energy Solutions reporting unit, which is a component of the Engineering Services reporting segment.

The gross amounts and accumulated amortization of the Company's acquired identifiable intangible assets with finite useful lives as of July 1, 2011 and December 31, 2010, included in intangible assets, net in the accompanying consolidated balance sheets, were as follows:

	July 1, 2011		December 31, 2010		Amortization Period (yrs)
	Gross Amount	Accumulated Amortization	Gross Amount	Accumulated Amortization	
Backlog	\$ 920,000	\$ 920,000	\$ 920,000	\$ 920,000	1
Training materials/courses	282,000	214,000	282,000	187,000	5
Non-compete agreements	30,000	30,000	30,000	30,000	3
	\$ 1,232,000	\$ 1,164,000	\$ 1,232,000	\$ 1,137,000	

The Company's amortization expense for acquired identifiable intangible assets with finite useful lives was \$13,000 and \$27,000 for the fiscal three and six months ended July 1, 2011, respectively, as compared to \$4,000 and \$16,000 for the fiscal three and six months ended July 2, 2010. Estimated amortization expense for acquired identifiable intangible assets for the remainder of fiscal 2011 and the succeeding years is as follows:

Fiscal year:	
2011	\$ 19,000
2012	37,000
2013	12,000
	\$ 68,000

4. EARNINGS PER SHARE (EPS)

Basic EPS is computed by dividing net income available to common stockholders by the weighted-average number of common shares outstanding. Diluted EPS is computed by dividing net income by the weighted-average number of common shares outstanding and dilutive potential common shares for the period. Potential common shares include the weighted-average dilutive effects of outstanding stock options using the treasury stock method.

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The following table sets forth the number of weighted-average shares used to compute basic and diluted EPS:

	Three Months Ended		Six Months Ended	
	July 1, 2011	July 2, 2010	July 1, 2011	July 2, 2010
Net income	\$ 735,000	\$ 1,258,000	\$ 444,000	\$ 1,650,000
Weighted-average common shares outstanding	7,257,000	7,229,000	7,254,000	7,226,000
Effect of dilutive stock options	214,000	23,000	222,000	14,000
Weighted-average common stock outstanding-diluted	7,471,000	7,252,000	7,476,000	7,240,000
Earnings per share:				
Basic	\$ 0.10	\$ 0.17	\$ 0.06	\$ 0.23
Diluted	\$ 0.10	\$ 0.17	\$ 0.06	\$ 0.23

For the three and six months ended July 1, 2011, 302,000 options were excluded from the calculation of dilutive potential common shares, compared to 306,000 and 326,000 options for the same periods last year. These options were not included in the computation of dilutive potential common shares because the assumed proceeds per share exceeded the average market price per share for the periods. Accordingly, the inclusion of these options would have been anti-dilutive.

5. EQUIPMENT AND LEASEHOLD IMPROVEMENTS

Equipment and leasehold improvements consist of the following:

	July 1, 2011	December 31, 2010
Furniture and fixtures	\$ 4,451,000	\$ 4,371,000
Computer hardware and software	5,310,000	5,227,000
Leasehold improvements	795,000	803,000
Equipment under capital leases	830,000	881,000
Automobiles, trucks, and field equipment	553,000	529,000
	11,939,000	11,811,000
Accumulated depreciation and amortization	(10,577,000)	(10,315,000)
Equipment and leasehold improvements, net	\$ 1,362,000	\$ 1,496,000

6. ACCRUED LIABILITIES

Accrued liabilities consist of the following:

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	July 1, 2011	December 31, 2010
Accrued bonuses	\$ 286,000	\$ 107,000
Paid leave bank	1,509,000	1,318,000
Compensation and payroll taxes	817,000	684,000
Accrued legal	71,000	46,000
Accrued workers compensation insurance	35,000	49,000
Accrued rent	357,000	420,000
Employee withholdings	223,000	179,000
Client deposits	762,000	157,000
Other	4,430,000	3,025,000
Total accrued liabilities	\$ 8,490,000	\$ 5,985,000

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7. LINE OF CREDIT

Under the terms of the Company's credit agreement with Wells Fargo Bank, National Association (Wells Fargo), the Company can borrow up to \$5.0 million from time to time (as may be limited by the covenants in the credit agreement as discussed below) up to and until January 1, 2012. Loans made under the revolving line of credit will accrue interest at either (i) the floating rate equal to the prime rate in effect from time to time or (ii) the fixed rate of 1.75% above LIBOR, at the Company's election. For prime rate loans, the interest rate will be adjusted when each prime rate change by the bank is announced and becomes effective. There were no outstanding borrowings under this agreement as of July 1, 2011.

Borrowings under the credit agreement are secured by all of the Company's accounts receivable and other rights to payment, general intangibles, inventory and equipment, including those of the Company's subsidiaries. In addition, borrowings under the credit agreement are secured by investments held in a securities account at Wells Fargo that must at all times have a collateral value of at least \$5.0 million. Each of the Company's subsidiaries (except Public Agency Resources) has signed an unconditional guaranty of the Company's obligations under the credit agreement.

The credit agreement contains customary representations and affirmative covenants, including a covenant to maintain a tangible net worth of at least \$18.0 million at all times. Tangible net worth is defined in the credit agreement as stockholders' equity less intangible assets and loans or advances to, or investments in, any related entities or individuals. The impact of any non-cash property lease termination expense of up to \$1.0 million in the aggregate recorded during the period from October 1, 2009 through December 31, 2010 was excluded from the calculation of tangible net worth under the credit agreement. As of July 1, 2011, the Company's tangible net worth as defined under the Company's credit agreement was met.

The credit agreement also includes customary negative covenants, including a covenant that prohibits the incurrence of additional indebtedness by the Company or the Company's subsidiaries other than purchase money indebtedness not to exceed \$2.0 million and indebtedness existing on the date of the credit agreement, and a covenant that prohibits payment of dividends on the Company's stock and redemptions, repurchases or other acquisitions of the Company's stock, except that the Company can repurchase stock with an aggregate fair market value up to \$5.0 million in any calendar year. In addition, the credit agreement includes customary events of default for a credit facility. Upon a default, the interest rate will be increased by a default rate margin of 4.0%. Upon the occurrence of an event of default under the credit agreement, including a breach of any of the covenants discussed above, Wells Fargo has the option to make any loans then outstanding under the credit agreement immediately due and payable and is no longer obligated to extend further credit to the Company under the credit agreement.

8. COMMITMENTS

Leases

The Company is obligated under capital leases for certain furniture and office equipment that expire at various dates through the year 2014.

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The Company also leases certain office facilities under noncancellable operating leases that expire at various dates through the year 2015 and is committed under noncancellable operating leases for the lease of computer equipment and automobiles through the year 2012.

Employee Benefit Plans

The Company has a qualified profit sharing plan (the Plan) pursuant to Code Section 401(a) and qualified cash or deferred arrangement pursuant to Code Section 401(k) covering substantially all employees. Employees may elect to contribute up to 50% of compensation limited to the amount allowed by tax laws. Company contributions are made solely at the discretion of the Company s board of directors.

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The Company has a discretionary bonus plan for regional managers, division managers and others as determined by the Company president. Bonuses are awarded if certain financial goals are achieved. The financial goals are not stated in the plan; rather they are judgmentally determined each year. In addition, the board of directors may declare discretionary bonuses to key employees and all employees are eligible for what the Company refers to as the "hot hand" bonus program, which pays awards for outstanding performance. The Company's compensation committee of the board of directors determines the compensation of the president.

Post Employment Health Benefits

In May 2006, the Company's board of directors approved providing lifetime health insurance coverage for Win Westfall, the Company's former chief executive officer and current chairman of the board of directors, and his spouse, and for Linda Heil, the widow of the Company's former chief executive officer, Dan Heil. Mrs. Heil is also a member of the Company's board of directors. Additionally, the board approved health insurance coverage for Mrs. Heil's two dependents until they reach the maximum age for dependent coverage under the Company's health insurance policy. These benefits relate to past services provided to the Company. Accordingly, there is no unamortized compensation cost for the benefits.

Additional Purchase Price Payable related to the Willdan Energy Solutions Acquisition

As discussed in Note 2, certain financial targets were achieved by Willdan Energy Solutions over the twelve month period ending on the last day of the Company's second fiscal quarter in 2011, which resulted in an earn-out payment being due. The remaining payment of \$2.7 million is expected to be paid in August 2011.

9. INCOME TAXES

Income taxes are accounted for under the asset and liability method and are determined using an estimated annual effective tax rate. Deferred tax assets and liabilities are recognized for the future tax consequences of temporary differences between the financial reporting basis and tax basis of the Company's assets and liabilities, subject to a judgmental assessment of recoverability of deferred tax assets. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recorded when it is more likely than not that some of the deferred tax assets may not be realized.

The Company recognizes the tax benefit from uncertain tax positions if it is more likely than not that the tax positions will be sustained on examination by the tax authorities, based on the technical merits of the position. The tax benefit is measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The Company recognizes interest and penalties related to unrecognized tax benefits in income tax expense.

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The Company recorded an income tax expense of \$0.2 million for the three and six months ended July 1, 2011, as compared to no income tax expense or benefit for the three and six months ended July 2, 2010.

10. SEGMENT INFORMATION

The Company has three reporting segments: Engineering Services, Public Finance Services and Homeland Security Services. The Engineering Services segment includes Willdan Engineering, Public Agency Resources and Willdan Energy Solutions. The Engineering Services segment performs services for a broad range of public agency clients and, to a lesser extent, private industry, and offers a full complement of civil engineering and municipal planning, energy efficiency and sustainability services to clients throughout the western United States. The Public Finance Services segment, which consists of Willdan Financial Services, provides expertise and support for the various financing techniques employed by public agencies to finance their operations and infrastructure along with the mandated reporting and other requirements associated with these financings. The Homeland Security Services segment, which consists of Willdan Homeland Solutions, provides homeland security and communications and technology consulting services to cities, counties and related municipal service agencies.

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The accounting policies applied to determine the segment information are the same as those described in the summary of significant accounting policies included in the Company's 2010 Annual Report on Form 10-K filed on March 29, 2011. There were no intersegment sales during the fiscal three and six months ended July 1, 2011. Management evaluates the performance of each segment based upon income or loss from operations before income taxes. Certain segment asset information including expenditures for long-lived assets has not been presented as it is not reported to or reviewed by the chief operating decision maker. In addition, enterprise-wide service line contract revenue is not included as it is impracticable to report this information for each group of similar services.

Financial information with respect to the reportable segments as of and for the fiscal three and six months ended July 1, 2011 and for the fiscal three and six months ended July 2, 2010 is as follows:

	Engineering Services	Public Finance Services	Homeland Security Services	Unallocated Corporate	Intersegment	Consolidated Total
Fiscal Three Months Ended						
July 1, 2011						
Contract revenue	\$ 21,614,000	\$ 2,549,000	\$ 1,649,000	\$	\$	\$ 25,812,000
Segment profit (loss) before income taxes	797,000	230,000	(93,000)			934,000
Net income (loss)	607,000	187,000	(59,000)			735,000
Segment assets	175,393,000	23,177,000	6,718,000	146,368,000	(298,288,000)	53,368,000
Segment net assets(1)	32,390,000	9,838,000	(1,037,000)	14,694,000	(23,129,000)	32,756,000
Fiscal Three Months Ended						
July 2, 2010						
Contract revenue	\$ 16,133,000	\$ 2,804,000	\$ 1,430,000	\$	\$	\$ 20,367,000
Segment profit (loss) before income taxes	990,000	312,000	234,000	(278,000)		1,258,000
Net income (loss)	990,000	312,000	234,000	(278,000)		1,258,000
Segment assets	151,577,000	23,448,000	6,855,000	144,874,000	(280,349,000)	46,405,000
Segment net assets(1)	28,387,000	9,608,000	(963,000)	14,202,000	(20,292,000)	30,942,000
Fiscal Six Months Ended						
July 1, 2011						
Contract revenue	\$ 40,568,000	\$ 4,880,000	\$ 3,106,000	\$	\$	\$ 48,554,000
Segment profit (loss) before income taxes	714,000	149,000	(220,000)			643,000
Net income (loss)	525,000	106,000	(187,000)			444,000
Segment assets	175,393,000	23,177,000	6,718,000	146,368,000	(298,288,000)	53,368,000
Segment net assets(1)	32,390,000	9,838,000	(1,037,000)	14,694,000	(23,129,000)	32,756,000
Fiscal Six Months Ended						
July 2, 2010						
Contract revenue	\$ 29,268,000	\$ 5,430,000	\$ 2,620,000	\$	\$	\$ 37,318,000
Segment profit (loss) before income taxes	1,242,000	443,000	270,000	(305,000)		1,650,000
Net income (loss)	1,242,000	443,000	270,000	(305,000)		1,650,000
Segment assets	151,577,000	23,448,000	6,855,000	144,874,000	(280,349,000)	46,405,000
Segment net assets(1)	28,387,000	9,608,000	(963,000)	14,202,000	(20,292,000)	30,942,000

(1) Segment net assets represent segment assets net of segment liabilities, which includes the effect of intersegment assets and liabilities which are eliminated in consolidation.

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11. CONTINGENCIES

Claims and Lawsuits

The Company is subject to claims and lawsuits from time to time, including those alleging professional errors or omissions that arise in the ordinary course of business against firms that operate in the engineering and consulting professions. The Company carries professional liability insurance, subject to certain deductibles and policy limits, for such claims as they arise and may from time to time establish reserves for litigation that is considered probable of a loss.

County of San Diego v. Willdan, Superior Court of California, Riverside County

A complaint was filed against the Company on February 28, 2008 relating to a project for the reconstruction of a portion of Valley Center Road located in an unincorporated area of San Diego County. The design was completed by the Company and a contract was awarded to a construction contractor for construction of the improvements. The construction was originally scheduled for completion in December 2008; however, completion was delayed until fall 2009. The lawsuit alleges that the delays in construction were caused by errors and omissions in the Company's preparation of reports and design and engineering of the project, resulting in additional design and construction costs. The Company entered into a settlement agreement with San Diego County wherein the Company agreed to pay the County a sum which is within the limits of the Company's insurance policy in exchange for a full release by the County and a dismissal of the County's lawsuit in its entirety, with prejudice.

French v. Willdan Engineering, Superior Court of California, Riverside County

In January 1991, the Company was originally retained by the City of Calimesa, California to review and process development plans. The Company has provided plan review continuously since that date under various contracts with the city. As the city receives applications from developers for project approvals, the city forwards the project plans to the Company for processing. The Company processes the plans and the city pays the Company for its services. In August 2008, a suit was filed by a city employee alleging that the city processed development applications without first collecting fees from developers to cover the costs of processing. The suit further alleges that even though the Company performed the work requested by the city, the city should not have paid the Company for work in advance of collecting the developers' fees. The complaint was amended by the plaintiff in May 2010 to provide additional details and the Company has filed an answer to the complaint. The plaintiff seeks to recover for the city amounts paid to the Company for processing project plans for which the developer fees have not been paid. The City of Calimesa has not requested any refunds from the Company or joined in the litigation, and the city continues to retain the Company's services. The Company does not believe that this suit has any merit and will vigorously defend this claim.

Vega v. City of Coachella, Superior Court of California, Riverside County

On February 2, 2011, the Company was served with a lawsuit concerning a fatal traffic accident on Dillon Road at Harrison Place in the City of Coachella on October 7, 2008. At the time of the accident, Dillon Road was in the midst of a street widening project. The Company had been under contract with the City of Coachella to provide construction management services. The accident occurred when an individual driving

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southbound on Dillon Road ran the stop sign at the intersection of Harrison Place, colliding with a vehicle making a left turn from northbound Dillon Road onto Harrison Place. The driver of the northbound vehicle was injured in the accident and a passenger seated in the front passenger seat was killed. At the time of the accident, there were STOP signs posted in both directions on Dillon Road, the construction zone was posted with 25 mph speed limit signs and construction zone signs, and there were STOP AHEAD signs posted in both directions on Dillon Road in advance of the intersection. The plaintiff, the driver of the northbound vehicle, seeks to recover unspecified damages from the Company. The Company does not believe that this suit has any merit. The City's general contractor and its general liability insurer have agreed to indemnify the Company from this claim and have assumed the defense on behalf of the Company.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the financial statements included elsewhere in this Quarterly Report and the audited financial statements for the year ended December 31, 2010, included in our Annual Report on Form 10-K (File No. 001-33076). This Quarterly Report contains, in addition to unaudited historical information, forward-looking statements, which involve risk and uncertainties. The words believe, expect, estimate, may, will, could, plan, or continue and similar expressions are intended to identify forward-looking statements. Our actual results could differ significantly from the results discussed in such forward-looking statements. Factors that could cause or contribute to such differences in results and outcomes include, without limitation, those discussed under the headings Item 1A. Risk Factors in our 2010 Annual Report on Form 10-K, and in other filings made from time to time with the United States Securities and Exchange Commission (SEC) after the date of this Quarterly Report on Form 10-Q. Readers are urged not to place undue reliance on these forward-looking statements, which speak only as of the date of this Quarterly Report on Form 10-Q. We undertake no obligation to (and we expressly disclaim any obligation to) revise or update any forward-looking statement, whether as a result of new information, subsequent events, or otherwise (except as may be required by law), in order to reflect any event or circumstance which may arise after the date of this Quarterly Report on Form 10-Q.

Overview

We are a provider of professional technical and consulting services to small and mid-sized public agencies, large public utilities and, to a lesser extent, private industry primarily in California, New York, and Arizona. We enable the public agencies to provide a wide range of specialized services, without having to incur and maintain the overhead necessary to develop staffing in-house, by providing a broad range of services, including:

- Civil Engineering and Planning;
- Energy Efficiency and Sustainability Consulting;
- Economic and Financial Consulting; and
- Homeland Security and Communications and Technology Consulting

We operate our business through a network of offices located primarily in California and New York. We also have operations in Arizona and, to a lesser extent, other states throughout the United States. As of July 1, 2011, we had a staff of 549 which includes licensed engineers and other professionals. Our traditional clients have been public agencies in communities with populations ranging from 10,000 to 300,000 people. We believe communities of this size are underserved by large outsourcing companies that tend to focus on securing large federal and state projects, as well as projects for the private sector. We also provide services to large public utilities which service major metropolitan communities. We seek to establish close working relationships with our public agency clients and, over time, to expand the breadth and depth of the services we

provide to them.

While we currently serve communities throughout the country, our business with public agencies is concentrated in California and neighboring states. We provide services to approximately 58% of the 482 cities and over 60% of the 58 counties in California. We also serve special districts, school districts, a range of public agencies, and to a lesser extent, private industry. Our business with large public utilities is concentrated in California and New York.

We were founded over 45 years ago, and today consist of a family of wholly-owned companies that operate within the following segments for financial reporting purposes:

Engineering Services. Our Engineering Services segment includes the operations of our subsidiaries, Willdan Engineering, Willdan Energy Solutions and Public Agency Resources (PARs). These businesses collectively provide civil engineering-related and city planning, energy efficiency and sustainability consulting services to public agencies and utilities and, to a lesser extent, private industry. Additionally, PARs primarily provides staffing to Willdan Engineering. Our core business is engineering and energy efficiency services. Contract revenue for the Engineering Services segment grew 38.6%, to \$40.6 million for the six months ended July 1, 2011 as compared to \$29.3 million of our consolidated contract revenue for the six months ended July 2, 2010.

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Public Finance Services. Our Public Finance Services segment consists of the business of our subsidiary, Willdan Financial Services, which offers financial and economic consulting services to public agencies. Contract revenue for the Public Finance Services segment represented approximately 10.1% and 14.5% of our consolidated contract revenue for the six months ended July 1, 2011 and July 2, 2010, respectively.

Homeland Security Services. Our Homeland Security Services segment consists of the operations of our subsidiary, Willdan Homeland Solutions, which offers homeland security and communications and technology consulting services. Contract revenue for our Homeland Security Services segment represented approximately 6.3% and 7.0% of our consolidated contract revenue for the six months ended July 1, 2011 and July 2, 2010, respectively.

Components of Income and Expense

Contract Revenue

We provide our services under contracts, purchase orders or retainer letters. The contracts we enter into with our clients contain three principal types of pricing provisions: time and materials, unit based, and fixed price. Revenue on our time and materials and unit based contracts are recognized as the work is performed in accordance with specific terms of the contract. Approximately 44.7% of our contracts are based on contractual rates per hour plus costs incurred. Some of these contracts include maximum contract prices, but the majority of these contracts are not expected to exceed the maximum. Contract revenue on our fixed price contracts is determined on the percentage of completion method based generally on the ratio of direct costs incurred to date to estimated total direct costs at completion. Many of our fixed price contracts are relatively short in duration, thereby lowering the risks of not properly estimating the percent complete.

Adjustments to contract cost estimates are made in the periods in which the facts requiring such revisions become known. When the revised estimate indicates a loss, such loss is recognized currently in its entirety. Claims revenue is recognized only upon resolution of the claim. Change orders in dispute are evaluated as claims. Costs related to un-priced change orders are expensed when incurred and recognition of the related contract revenue is based on an evaluation of the probability of recovery of the costs. Estimated profit is recognized for un-priced change orders if realization of the expected price of the change order is probable.

Our contracts come up for renewal periodically and at the time of renewal may be subject to renegotiation, which could impact the profitability on that contract. In addition, during the term of a contract, public agencies may request additional or revised services which may impact the economics of the transaction. Most of our contracts permit our clients, with prior notice, to terminate the contracts at any time without cause. While we have a large volume of transactions, the renewal, termination or modification of a contract, in particular our contract with Consolidated Edison of New York, may have a material adverse effect on our consolidated operations.

Direct Costs of Contract Revenue

Direct costs of contract revenue consist primarily of subconsultant services and that portion of technical and nontechnical salaries and wages that has been incurred in connection with revenue producing projects. Direct costs of contract revenue also include production expenses and other

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expenses that are incurred in connection with revenue producing projects. Direct costs of contract revenue generally exclude depreciation and amortization, that portion of technical and nontechnical salaries and wages related to marketing efforts, vacations, holidays and other time not spent directly generating revenue under existing contracts. Such costs are included in general and administrative expenses. Additionally, payroll taxes, bonuses and employee benefit costs for all of our personnel are included in general and administrative expenses since no allocation of these costs is made to direct costs of contract revenue. No allocation of facilities costs is made to direct costs of contract revenue nor is depreciation and amortization allocated to direct costs. We expense direct costs of contract revenue when incurred.

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As a firm that provides multiple and diverse services, we do not believe gross margin is a consistent or appropriate indicator of our performance and therefore we do not use this measure as construction contractors and other types of consulting firms may. Other companies may classify as direct costs of contract revenue some of the costs that we classify as general and administrative expenses. As a result, our direct costs of contract revenue may not be comparable to direct costs for other companies, either as a line item expense or as a percentage of contract revenue.

General and Administrative Expenses

General and administrative expenses include the costs of the marketing and support staffs, other marketing expenses, management and administrative personnel costs, payroll taxes, bonuses and employee benefits for all of our employees and the portion of salaries and wages not allocated to direct costs of contract revenue for those employees who provide our services. General and administrative expenses also include facility costs, depreciation and amortization, professional services, legal and accounting fees and administrative operating costs. Within general and administrative expenses, Other includes expenses such as professional services, legal and accounting, computer costs, travel and entertainment and marketing costs. We expense general and administrative costs when incurred.

Critical Accounting Policies

This discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles in the U.S., or GAAP. To prepare these financial statements in conformity with GAAP, we must make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amount of revenue and expenses in the reporting period. Our actual results may differ from these estimates. We have provided a summary of our significant accounting policies in Note 2 to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2010. We describe below those accounting policies that require material subjective or complex judgments and that have the most significant impact on our financial condition and results of operations. Our management evaluates these estimates on an ongoing basis, based upon information currently available and on various assumptions management believes are reasonable as of the date of this report.

Contract Accounting

Applying the percentage-of-completion method of recognizing revenue requires us to estimate the outcome of our long-term contracts. We forecast such outcomes to the best of our knowledge and belief of current and expected conditions and our expected course of action. Differences between our estimates and actual results often occur resulting in changes to reported revenue and earnings. Such changes could have a material effect on our future consolidated financial statements.

Accounts receivable are carried at original invoice amount less an estimate made for doubtful accounts based upon our review of all outstanding amounts on a monthly basis. We determine the allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Our credit risk is minimal with governmental entities. Account receivables are written off when deemed uncollectible. Recoveries of accounts receivable previously written off are recorded when received.

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For further information on the types of contracts under which we perform our services, see Management's Discussion and Analysis of Financial Condition and Results of Operations Components of Income and Expense Contract Revenue elsewhere in this report.

Goodwill

We test goodwill, at least annually, for possible impairment. Accordingly, we complete our annual testing of goodwill as of the last day of the first month of our fourth fiscal quarter each year to determine whether there is impairment. In addition to our annual test, we regularly evaluate whether events and circumstances have occurred that may indicate a potential impairment of goodwill. We did not recognize any goodwill impairment charges for the fiscal three or six months ended July 1, 2011.

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We test our goodwill for impairment at the level of our reporting units, which are components of our operating segments. The only reporting unit that has goodwill is Willdan Energy Solutions, which is part of our engineering services segment. The process of testing goodwill for impairment involves the determination of the fair value of the applicable reporting units. To estimate the fair value of our reporting units, we use both an income approach based on management's estimates of future cash flows and other market data and a market approach based upon multiples of EBITDA earned by similar public companies. For our fiscal year 2010 annual impairment testing, we weighted the income approach and the market approach at 80% and 20%, respectively. The income approach was given a higher weight because it has a more direct correlation to the specific economics of the reporting units than the market approach, which is based on multiples of public companies that, although comparable, may not provide the same mix of services as our reporting units.

Once the fair value is determined, we then compare the fair value of the reporting unit to its carrying value, including goodwill. If the fair value of the reporting unit is determined to be less than the carrying value, we perform an additional assessment to determine the extent of the impairment based on the implied fair value of goodwill compared with the carrying amount of the goodwill. In the event that the current implied fair value of the goodwill is less than the carrying value, an impairment charge is recognized.

Inherent in such fair value determinations are significant judgments and estimates, including but not limited to assumptions about our future revenue, profitability and cash flows, our operational plans and our interpretation of current economic indicators and market valuations. To the extent these assumptions are incorrect or economic conditions that would impact the future operations of our reporting units change, our goodwill may be deemed to be impaired, and an impairment charge could result in a material adverse effect on our financial position or results of operation. During our 2010 annual impairment testing, the estimated fair value of our Willdan Energy Solutions reporting unit exceeded the carrying value. A reduction in estimated fair value of our Willdan Energy Solutions reporting unit could result in an impairment charge in future periods.

Accounting for Claims Against the Company

We record liabilities to claimants for probable and estimable claims, if any, on our consolidated balance sheet, which we include in accrued liabilities, and record a corresponding receivable from our insurance company for the portion of the claim that is probable of being covered by insurance, which is included in other receivables. The estimated claim amount net of the amount estimated to be recoverable from the insurance company is included in our general and administrative expenses. Determining probability and estimating claim amounts is highly judgmental. Initial accruals and any subsequent changes in our estimates could have a material effect on our consolidated financial statements.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences of temporary differences between the financial reporting basis and tax basis of our assets and liabilities, subject to a judgmental assessment of recoverability of deferred tax assets. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recorded when it is more likely than not that some of the deferred tax assets may not be realized.

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We recognize the tax benefit from uncertain tax positions if it is more likely than not that the tax positions will be sustained on examination by the tax authorities, based on the technical merits of the position. The tax benefit is measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. We recognize interest and penalties related to unrecognized tax benefits in income tax expense.

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The following table sets forth, for the periods indicated, certain information derived from our consolidated statements of operations expressed as a percentage of contract revenue.

Statement of Operations Data	Fiscal Three Months Ended		Fiscal Six Months Ended	
	July 1, 2011	July 2, 2010	July 1, 2011	July 2, 2010
Contract revenue	100.0%	100.0%	100.0%	100.0%
Direct costs of contract revenue:				
Salaries and wages	25.7	27.6	26.8	28.5
Subconsultant services	25.4	17.4	28.4	14.7
Other direct costs, net	9.0	8.0	4.7	8.0
Total direct costs of contract revenue	60.1	53.0	59.9	51.2
General and administrative expenses:				
Salaries and wages, payroll taxes, employee benefits	20.5	22.0	22.4	23.9
Facilities and facilities related	5.1	5.1	4.9	5.7
Stock-based compensation	0.3	0.2	0.2	0.3
Depreciation and amortization	0.9	1.2	1.0	1.4
Other	9.4	12.3	10.2	13.1
Total general and administrative expenses	36.2	40.8	38.7	44.4
Income from operations	3.7	6.2	1.4	4.4
Other income (expense):				
Interest income				
Interest expense	(0.1)		(0.1)	
Other, net				
Total other income, net	(0.1)		(0.1)	
Income before income tax expense	3.6	6.2	1.3	4.4
Income tax expense	0.8		0.4	
Net income	2.8%	6.2%	0.9%	4.4%

Three Months Ended July 1, 2011 Compared to Three Months Ended July 2, 2010

Contract revenue. Our contract revenue was \$25.8 million for the three months ended July 1, 2011, with \$21.6 million attributable to the Engineering Services segment, \$2.6 million attributable to the Public Finance Services segment and \$1.6 million attributable to the Homeland Security Services segment. Consolidated contract revenue increased \$5.4 million, or 26.7%, to \$25.8 million for the three months ended July 1, 2011, from \$20.4 million for the three months ended July 2, 2010. This was due to increases of \$5.5 million, or 34.0%, in contract revenue for the Engineering Services segment, primarily as a result of the increase in demand for the energy efficiency, sustainability and renewable energy services of Willdan Energy Solutions, and \$0.2 million, or 15.3%, in contract revenue for the Homeland Security Services segment, partially offset by a decrease in contract revenue for the Public Finance Services segment of \$0.3 million, or 9.1%.

Contract revenue for Willdan Energy Solutions increased primarily because of increased demand for energy efficiency services in the states of California and New York. Contract revenue for other areas of the Engineering Services segment continues to be impacted by the decline in the California residential housing market and state and local government budget cuts. A source of revenue in our Engineering Services segment is fees assessed for building permits. Since the second half of fiscal 2007, we have experienced reductions in revenue from these fees because of

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the slowdown in residential construction in the western United States. We have also experienced a decline in our other building and safety projects which is both directly and indirectly affected by the housing market. Revenue in the Public Finance Services segment decreased primarily due to lower levels of activity

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in the financial consulting business as a result of the general downturn in macro-economic conditions. Revenue in the Homeland Security Services segment has increased due to an increase in demand for our traditional and expanded homeland security, management consulting and public safety consulting services. Our Homeland Security Services segment has expanded its service offerings beyond its traditional planning, training and exercise services to include public safety and interoperability communications and management consulting.

Direct costs of contract revenue. Direct costs of contract revenue were \$15.5 million for the three months ended July 1, 2011, with \$13.8 million attributable to the Engineering Services segment, \$0.9 million attributable to the Public Finance Services segment, and \$0.8 million attributable to the Homeland Security Services segment. Overall, direct costs increased by \$4.7 million, or 43.7%, to \$15.5 million for the three months ended July 1, 2011, from \$10.8 million for the three months ended July 2, 2010. This increase is primarily attributable to an increase in direct costs for our Engineering Services segment of \$4.5 million. Direct costs of contract revenue increased by \$0.2 million for our Homeland Security Services segment and remained flat for our Public Finance Services segment.

Direct costs increased as a result of increases in salaries and wages, subconsultant services and other direct costs of \$1.0 million, \$3.0 million and \$0.7 million, respectively. Within direct costs of contract revenue, salaries and wages decreased to 25.7% of contract revenue for the three months ended July 1, 2011 from 27.6% for the three months ended July 2, 2010 and subconsultant services increased to 25.4% of contract revenue for the three months ended July 1, 2011 from 17.4% of contract revenue for the three months ended July 2, 2010. Other direct costs increased to 9.0% of contract revenue for the three months ended July 1, 2011 from 8.1% for the three months ended July 2, 2010. Subconsultant services increased primarily because of increased demand for the energy efficiency, sustainability and renewable energy services of our subsidiary Willdan Energy Solutions, which generally utilizes a higher percentage of subconsultants than our other subsidiaries. Increased chargeability of labor also shifted more employee related costs to direct costs of contract revenue because we only allocate the portion of salaries and wages related to time spent directly generating revenues to direct costs of contract revenue.

General and administrative expenses. General and administrative expenses increased by \$1.0 million, or 12.5%, to \$9.3 million for the three months ended July 1, 2011 from \$8.3 million for the three months ended July 2, 2010. This was due to increases of \$1.1 million and \$0.4 million in general and administrative expenses of the Engineering Services segment and our Homeland Security Services segment, respectively, partially offset by decreases of \$0.2 million in general and administrative expenses of our Public Finance Services segment and \$0.3 million for unallocated corporate expenses. General and administrative expenses as a percentage of contract revenue decreased to 36.2% for the three months ended July 1, 2011 from 40.8% for the three months ended July 2, 2010.

Of the \$1.0 million increase in general and administrative expenses, approximately \$0.7 million relates to increases in salaries and wages, payroll taxes and employee benefits. The increase in employee related costs primarily resulted from increased headcount. As discussed above under Components of Income and Expense Direct Costs of Contract Revenue, we do not allocate that portion of salaries and wages not related to time spent directly generating revenue to direct costs of contract revenue, and the greater headcount resulted in more unallocated time. The remaining increase primarily relates to an increase in facilities and facilities related charges due to expanded facilities in Washington, D.C. and other areas.

Income from operations. As a result of the above factors, our operating income was \$1.0 million for the three months ended July 1, 2011 as compared to operating income of \$1.3 million for the three months ended July 2, 2010. Income from operations as a percentage of contract revenue was 3.7% for the three months ended July 1, 2011, as compared to 6.2% in the prior year period.

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Other income (expense). Other income (expense), net essentially remained flat in the three months ended July 1, 2011, as compared to the three months ended July 2, 2010.

Income tax expense. We recorded an income tax expense of \$0.2 million for the three months ended July 1, 2011, as compared to no income tax expense or benefit for the three months ended July 2, 2010.

Net income. As a result of the above factors, our net income was \$0.7 million for the three months ended July 1, 2011, as compared to net income of \$1.3 million for the three months ended July 2, 2010.

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Six Months Ended July 1, 2011 Compared to Six Months Ended July 2, 2010

Contract revenue. Our contract revenue was \$48.6 million for the six months ended July 1, 2011, with \$40.6 million attributable to the Engineering Services segment, \$4.9 million attributable to the Public Finance Services segment and \$3.1 million attributable to our Homeland Security Services during this period. Consolidated contract revenue increased \$11.2 million, or 30.1%, to \$48.6 million for the six months ended July 1, 2011, from \$37.3 million for the six months ended July 2, 2010. This increased primarily from an increase of \$11.3 million, or 38.6%, in contract revenue for the Engineering Services segment primarily as a result of the increase in demand for the services of our subsidiary, Willdan Energy Solutions. Contract revenue for our Public Finance Services segment decreased \$0.6 million, or 10.1%, to \$4.9 million for the six months ended July 1, 2011 as compared to \$5.4 million for the six months ended July 2, 2010. Contract revenue for our Homeland Security Services segment increased \$0.5 million, or 18.5%, to \$3.1 million for the six months ended July 1, 2011 as compared to \$2.6 million for the six months ended July 1, 2010.

Contract revenue for Willdan Energy Solutions increased primarily because of increased demand for energy efficiency services in the states of California and New York. Contract revenue for other areas of the Engineering Services segment continues to be impacted by the decline in the California residential housing market and state and local government budget cuts. A source of revenue in our Engineering Services segment is fees assessed for building permits. Since the second half of fiscal 2007, we have experienced reductions in revenue from these fees because of the slowdown in residential construction in the western United States. We have also experienced a decline in our other building and safety projects which is both directly and indirectly affected by the housing market. Revenue in the Public Finance Services segment decreased primarily due to lower levels of activity in the financial consulting business as a result of the general downturn in macro-economic conditions. Revenue in the Homeland Security Services segment has increased due to an increase in demand for our traditional and expanded homeland security, management consulting and public safety consulting services. Our Homeland Security Services segment has expanded its service offerings beyond its traditional planning, training and exercise services to include public safety and interoperability communications and management consulting.

Direct costs of contract revenue. Direct costs of contract revenue were \$29.1 million for the six months ended July 1, 2011, with \$26.0 million attributable to the Engineering Services segment, \$1.6 million attributable to the Public Finance Services segment and \$1.5 million attributable to the Homeland Security Services segment. Overall, direct costs increased by \$10.0 million, or 52.3%, to \$29.1 million for the six months ended July 1, 2011, from \$19.1 million for the six months ended July 2, 2010. This increase is attributable to increases in direct costs within our Engineering Services and Homeland Security Services segments of \$9.7 million and \$0.3 million, respectively. Direct costs within the Public Finance Services segment remained flat.

Direct costs increased as a result of increases in salaries and wages and subconsultant services of \$2.4 million and \$8.3 million, respectively, partially offset by a decrease in other direct costs of \$0.7 million. Within direct costs of contract revenue, salaries and wages decreased to 26.8% of contract revenue for the six months ended July 1, 2011 from 28.5% for the six months ended July 2, 2010, subconsultant services increased to 28.4% of contract revenue for the six months ended July 1, 2011 from 14.7% for the six months ended July 2, 2010, and other direct costs decreased to 4.7% of contract revenue for the six months ended July 1, 2011 from 8.0% for the six months ended July 2, 2010.

General and administrative expenses. General and administrative expenses increased by \$2.2 million, or 13.4%, to \$18.8 million for the six months ended July 1, 2011 from \$16.6 million for the six months ended July 2, 2010. This was due to increases in general and administrative expenses of \$2.2 million for the Engineering Services segment and \$0.7 million for the Homeland Security Services segment, partially offset by decreases of \$0.3 million for the Public Finance Services segment and \$0.4 million for unallocated corporate expenses. General and administrative expenses as a percentage of contract revenue decreased to 38.7% for the six months ended July 1, 2011 from 44.4% for the six months ended July 2, 2010.

Of the \$2.2 million increase in general and administrative expenses, approximately \$1.9 million relates to increases in salaries and wages, payroll taxes and employee benefits. The increase in employee related costs primarily resulted from increased headcount. As discussed above under Components of Income and Expense Direct Costs of Contract Revenue, we do not allocate that portion of salaries and wages not related to time spent directly generating revenue to direct costs of contract revenue. The increase in facilities and facilities related expenses of \$0.3 million primarily resulted from expanded facilities in Washington, D.C. and other areas. These increases were partially offset by a decrease of \$0.1 million in other general and administrative expenses.

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Income from operations. As a result of the above factors, our operating income was \$0.7 million for the six months ended July 1, 2011, as compared to operating income of \$1.7 million for the six months ended July 2, 2010. Income from operations as a percentage of contract revenue was 1.4% for the six months ended July 1, 2011, as compared to 4.4% in the prior year period.