

Information Services Group Inc.  
Form 10-Q  
November 09, 2015

**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 September 30, 2015**

**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 001-33287**

**INFORMATION SERVICES GROUP, INC.**

(Exact name of Registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of

**20-5261587**  
(I.R.S. Employer

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incorporation or organization)

Identification No.)

**Two Stamford Plaza  
281 Tresser Boulevard  
Stamford, CT 06901**

(Address of principal executive offices and zip code)

Registrant's telephone number, including area code: **(203) 517-3100**

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 or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act). (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

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

Class	Outstanding at October 30, 2015
Common Stock, \$0.001 par value	37,182,112 shares

**FORWARD-LOOKING STATEMENTS**

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We have based these forward-looking statements on our current expectations and projections about future events. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about us that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as may, should, could, would, expect, plan, anticipate, believe, estimate, the negative of such terms or other similar expressions. The actual results of ISG may vary materially from those expected or anticipated in these forward-looking statements. The realization of such forward-looking statements may be impacted by certain important unanticipated factors. Because of these and other factors that may affect ISG's operating results, past performance should not be considered as an indicator of future performance, and investors should not use historical results to anticipate results or trends in future periods. We undertake no obligation to publicly release the results of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Readers should carefully review the risk factors described in this and other documents that ISG files from time to time with the Securities and Exchange Commission, including subsequent Current Reports on Form 8-K, Quarterly Reports on Form 10-Q and Annual Reports on Form 10-K.

**PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)****INFORMATION SERVICES GROUP, INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)****(In thousands, except par value)**

	September 30, 2015	December 31, 2014
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 14,281	\$ 27,662
Accounts receivable, net of allowance of \$389 and \$234, respectively	43,965	41,148
Deferred tax asset	1,093	1,138
Prepaid expense and other current assets	2,543	2,130
Total current assets	61,882	72,078
Restricted cash	391	364
Furniture, fixtures and equipment, net	3,159	3,478
Goodwill	37,260	36,400
Intangible assets, net	15,157	18,335
Other assets	5,711	3,514
Total assets	\$ 123,560	\$ 134,169
<b>LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND STOCKHOLDERS EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 5,987	\$ 7,312
Current maturities of long-term debt	2,250	3,938
Deferred revenue	3,440	4,898
Accrued expenses	12,406	21,116
Total current liabilities	24,083	37,264
Long-term debt, net of current maturities	49,093	49,434
Other liabilities	5,153	6,007
Total liabilities	78,329	92,705
Commitments and contingencies (Note 7)		
Redeemable noncontrolling interest	954	747
<b>Stockholders equity</b>		
Preferred stock, \$0.001 par value; 10,000 shares authorized; none issued	38	38

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Common stock, \$0.001 par value, 100,000 shares authorized; 37,977 shares issued and 37,093 shares outstanding at September 30, 2015 and 37,943 shares issued and 36,762 outstanding at December 31, 2014

Additional paid-in-capital	204,699	204,525
Treasury stock (884 and 1,181 common shares, respectively, at cost)	(3,639)	(5,244)
Accumulated other comprehensive loss	(6,366)	(4,582)
Accumulated deficit	(150,455)	(154,020)
Total stockholders' equity	44,277	40,717
Total liabilities, redeemable noncontrolling interest and stockholders' equity	\$ 123,560	\$ 134,169

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

## INFORMATION SERVICES GROUP, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(In thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
<b>Revenues</b>	\$ 51,404	\$ 53,258	\$ 155,354	\$ 156,387
<b>Operating expenses</b>				
Direct costs and expenses for advisors	30,093	31,487	93,089	92,796
Selling, general and administrative	16,405	16,136	49,826	48,758
Depreciation and amortization	1,752	1,863	5,308	5,501
Operating income	3,154	3,772	7,131	9,332
Interest income	2	3	11	12
Interest expense	(419)	(502)	(1,357)	(1,524)
Bargain purchase gain				146
Foreign currency transaction gain (loss)	24	(75)	424	(112)
Income before taxes	2,761	3,198	6,209	7,854
Income tax provision	975	808	2,497	2,277
Net income	1,786	2,390	3,712	5,577
Net income attributable to noncontrolling interest	8	37	147	56
Net income attributable to ISG	\$ 1,778	\$ 2,353	\$ 3,565	\$ 5,521
<b>Weighted average shares outstanding:</b>				
Basic	37,315	37,039	37,182	37,214
Diluted	39,296	38,740	38,919	38,813
<b>Earnings per share attributable to ISG:</b>				
Basic	\$ 0.05	\$ 0.06	\$ 0.10	\$ 0.15
Diluted	\$ 0.05	\$ 0.06	\$ 0.09	\$ 0.14
<b>Comprehensive income:</b>				
Net income	\$ 1,786	\$ 2,390	\$ 3,712	\$ 5,577
Foreign currency translation, net of tax benefit of \$366, \$795, \$996 and \$669, respectively	(542)	(1,297)	(1,784)	(1,092)
Comprehensive income	1,244	1,093	1,928	4,485
Comprehensive income attributable to noncontrolling interest	8	37	147	56
Comprehensive income attributable to ISG	\$ 1,236	\$ 1,056	\$ 1,781	\$ 4,429

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

## INFORMATION SERVICES GROUP, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

	Nine Months Ended September 30,	
	2015	2014
<b>Cash flows from operating activities</b>		
Net income	\$ 3,712	\$ 5,577
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation expense	1,322	1,340
Amortization of intangibles	3,985	4,161
Amortization of deferred financing costs	107	114
Bargain purchase gain		(146)
Tax benefit from stock issuances	(203)	(423)
Compensation costs related to stock-based awards	3,640	2,069
Change in fair value of contingent consideration	220	403
Changes in accounts receivable allowance	166	(41)
Deferred tax benefit	(1,148)	(950)
Loss on disposal of furniture, fixtures and equipment	2	14
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable	(1,808)	(5,988)
Prepaid expense and other current assets	(2,712)	(667)
Accounts payable	(1,325)	989
Deferred revenue	(2,004)	(50)
Accrued liabilities	(2,475)	(8,557)
<b>Net cash provided by (used in) operating activities</b>	<b>1,479</b>	<b>(2,155)</b>
<b>Cash flows from investing activities</b>		
Acquisitions, net of cash acquired	(537)	(890)
Restricted cash	(28)	(135)
Purchase of furniture, fixtures and equipment	(1,057)	(1,702)
<b>Net cash used in investing activities</b>	<b>(1,622)</b>	<b>(2,727)</b>
<b>Cash flows from financing activities</b>		
Principal payments on borrowings	(2,028)	(2,531)
Payment of contingent consideration	(2,322)	(1,633)
Equity securities repurchased	(2,534)	(4,301)
Installment payment for acquisition of CCI	(661)	
Dividend paid	(5,189)	
Tax benefit from stock issuances	203	423
Proceeds from issuance of ESPP shares	440	410
<b>Net cash used in financing activities</b>	<b>(12,091)</b>	<b>(7,632)</b>
<b>Effect of exchange rate changes on cash</b>	<b>(1,147)</b>	<b>(938)</b>
<b>Net decrease in cash and cash equivalents</b>	<b>(13,381)</b>	<b>(13,452)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>27,662</b>	<b>35,085</b>

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Cash and cash equivalents, end of period	\$	14,281	\$	21,633
<b>Supplemental disclosures of cash flow information:</b>				
Noncash financing activities:				
Issuance of treasury stock for vested restricted stock units awards	\$	3,625	\$	1,605
Liability to CCI Sellers	\$		\$	747
Noncash investing activity:				
Accretion of noncontrolling interest	\$	59	\$	23

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



**INFORMATION SERVICES GROUP, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(tabular amounts in thousands, except per share data)**

**(unaudited)**

**NOTE 1 DESCRIPTION OF ORGANIZATION AND BUSINESS OPERATIONS**

Information Services Group, Inc. (the Company) was founded in 2006 with the strategic vision to become a high-growth, leading provider of information-based advisory services. In 2007, we consummated our initial public offering and completed the acquisition of TPI Advisory Services Americas, Inc. (TPI). The Company is a leading technology insights, market intelligence and advisory services company serving more than 500 clients around the world to help them achieve operational excellence. Based in Stamford, Connecticut, the Company has more than 900 employees and operates in 21 countries.

**NOTE 2 BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements as of September 30, 2015 and for the three and nine months ended September 30, 2015 and 2014, have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial statements and pursuant to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal recurring accruals) have been made that are considered necessary for a fair statement of the financial position of the Company as of September 30, 2015, the results of operations for the three and nine months ended September 30, 2015 and 2014 and the cash flows for the nine months ended September 30, 2015 and 2014. The condensed consolidated balance sheet as of December 31, 2014 has been derived from the Company's audited consolidated financial statements. Operating results for the three and nine months ended September 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015.

Certain information and disclosures normally included in the notes to annual financial statements prepared in accordance with GAAP have been omitted from these interim financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). Accordingly, these unaudited condensed consolidated financial statements should be read in conjunction with the financial statements for the fiscal year ended December 31, 2014, which are included in the Company's 2014 Form 10-K filed with the SEC.

**NOTE 3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets

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and liabilities at the date of the financial statements and revenues and expenses during the periods reported. Actual results may differ from those estimates. The complexity of the estimation process and issues related to the assumptions, risks and uncertainties inherent in the application of the proportional performance method of accounting affect the amounts of revenues, expenses, unbilled receivables and deferred revenue. Numerous internal and external factors can affect estimates. Estimates are also used for but not limited to: allowance for doubtful accounts, useful lives of furniture, fixtures and equipment, depreciation expense, contingent consideration, fair value assumptions in analyzing goodwill and intangible asset impairments, income taxes and deferred tax asset valuation, and the valuation of stock based compensation.

### **Fair Value**

The carrying value of the Company's cash and cash equivalents, restricted cash, receivables, accounts payable, other current liabilities, and accrued interest approximated their fair values at September 30, 2015 and December 31, 2014 due to the short-term nature of these instruments.

Fair value is the price that would be received upon a sale of an asset or paid upon a transfer of a liability in an orderly transaction between market participants at the measurement date (exit price). Market participants can use market data or assumptions in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market-corroborated, or generally unobservable. The use of unobservable inputs is intended to allow for fair value determinations in situations where there is little, if any, market activity for the asset or liability at the measurement date. Under the fair-value hierarchy:

- Level 1 measurements include unadjusted quoted market prices for identical assets or liabilities in an active market;

## INFORMATION SERVICES GROUP, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-(continued)

(tabular amounts in thousands, except per share data)

(unaudited)

- Level 2 measurements include quoted market prices for identical assets or liabilities in an active market that have been adjusted for items such as effects of restrictions for transferability and those that are not quoted but are observable through corroboration with observable market data, including quoted market prices for similar assets; and
- Level 3 measurements include those that are unobservable and of a highly subjective measure.

The following tables summarize assets and liabilities measured at fair value on a recurring basis at the dates indicated:

	Basis of Fair Value Measurements			Total
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
Cash equivalents	\$ 20	\$	\$	\$ 20
Total	\$ 20	\$	\$	\$ 20
<b>Liabilities:</b>				
Contingent consideration (1)	\$	\$	\$ 3,648	\$ 3,648
Long-term debt , including current portion			51,410	51,410
	\$	\$	\$ 55,058	\$ 55,058

	Basis of Fair Value Measurements			Total
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
Cash equivalents	\$ 20	\$	\$	\$ 20
Total	\$ 20	\$	\$	\$ 20
<b>Liabilities:</b>				
Contingent consideration (1)	\$	\$	\$ 4,825	\$ 4,825
Long-term debt , including current portion			53,412	53,412
	\$	\$	\$ 58,237	\$ 58,237

(1) The short-term portion is included in Accrued expenses. The long-term portion is included in Other liabilities.

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The Company's contingent consideration liability was \$3.6 million and \$4.8 million at September 30, 2015 and December 31, 2014, respectively. The Company paid \$2.3 million related to the contingent consideration during the second quarter of 2015. On August 7, 2015, the Company also recorded a liability of \$1.0 million representing the fair value of the contingent consideration related to the acquisition of Saugatuck Technology. The fair value measurement of this contingent consideration is classified within Level 3 of the fair value hierarchy and reflects the Company's own assumptions in measuring fair values using the income approach. In developing these estimates, the Company considered certain performance projections, historical results, and industry trends. This amount was estimated through a valuation model that incorporated probability-weighted assumptions related to the achievement of these milestones and the likelihood of the Company making payments. These cash outflow projections have then been discounted using a rate ranging from 2.3% to 14.5%.

The fair value of debt is classified within Level 3 of the fair value hierarchy. The fair values of debt have been estimated using a discounted cash flow analysis based on the Company's incremental borrowing rate for similar borrowing arrangements. The incremental borrowing rate used to discount future cash flows ranged from 2.31% to 2.45%. The Company also considered recent transactions of peer group companies for similar instruments with comparable terms and maturities as well as an analysis of current market conditions.

## INFORMATION SERVICES GROUP, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-(continued)

(tabular amounts in thousands, except per share data)

(unaudited)

The following table represents the change in the contingent consideration liability during the nine months ended September 30, 2015 and 2014:

	Nine months Ended September 30,	
	2015	2014
Beginning Balance	\$ 4,825	\$ 4,085
Payment of contingent consideration	(2,322)	(1,633)
Acquisitions	986	1,989
Change in fair value of contingent consideration	220	368
Accretion of contingent consideration	172	35
Impact of currency translation	(233)	(130)
Ending Balance	\$ 3,648	\$ 4,714

**Recently Issued Accounting Pronouncements**

In May 2014, the Financial Accounting Standards Board ( FASB ) issued new accounting guidance that outlines a single comprehensive model for entities to use in accounting for revenue. Under the guidance, revenue is recognized when a company transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The standard is effective for public entities with annual and interim reporting periods beginning after December 15, 2016. On July 9, 2015, the FASB approved the deferral of the effective date of the new revenue guidance by one year to annual reporting periods beginning after December 15, 2017, with early adoption being permitted for annual periods beginning after December 15, 2016. Entities have the option of using either a full retrospective or a modified retrospective approach to adopt the guidance. We are currently assessing the effects this guidance may have on our consolidated financial statements, as well as the method of transition that we will use in adopting the new standard.

In April 2015, the FASB issued guidance require the presentation of debt issuance costs in financial statements as a direct reduction of related debt liabilities with amortization of debt issuance costs reported as interest expense. Under current U.S. GAAP standards, debt issuance costs are reported as deferred charges (i.e., as an asset). In August 2015, the FASB clarified the guidance that debt issuance costs related to line-of-credit arrangements could continue to be presented as an asset and be subsequently amortized over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the arrangement. This guidance is effective for annual periods, and interim periods within those fiscal years, beginning after December 15, 2015 and is to be applied retrospectively upon adoption. Early adoption is permitted, including adoption in an interim period for financial statements that have not been previously issued. We are planning to adopt this guidance in the fourth quarter of 2015. At September 30, 2015, the Company had debt issuance costs of \$0.6 million.

In September 2015, the FASB issued updated guidance, which eliminates the requirement for an acquirer in a business combination to account for measurement-period adjustments retrospectively. Acquirers must recognize measurement-period adjustments during the period of resolution, including the effect on earnings of any amounts they would have recorded in previous periods if the accounting had been completed at the acquisition date. The updated guidance is effective for fiscal years beginning after December 15, 2015. Earlier adoption is permitted for any

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interim and annual financial statements that have not yet been issued. We do not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

### **NOTE 4 ACQUISITION**

#### *Saugatuck Technology Acquisition*

On August 7, 2015 (the Saugatuck Acquisition Date ), the Company executed an Asset Purchase Agreement (the Saugatuck Agreement ) by and among Saugatuck Technology Inc. ( Saugatuck ), ISG Information Services Group Americas, Inc. a wholly-owned subsidiary of ISG ( Buyer ), and the other parties thereto and consummated the acquisition of substantially all of the assets, and assumption of certain current liabilities, excluding debt and employee loans of Saugatuck.

## INFORMATION SERVICES GROUP, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-(continued)

(tabular amounts in thousands, except per share data)

(unaudited)

Saugatuck is a subscription-based research and analyst firm that provides C-level executives and technology business leaders with objective insights on the key market trends and emerging technologies that are driving business transformation and growth. This acquisition gives us a solid platform on which to build a strong analyst capability. Saugatuck's deep intellectual capital, respected analytical and forecasting capabilities, and influential market insights and opinions are the perfect complement to our growing Cloud, Digital and Automation consulting practices.

Under the terms of the Saugatuck Agreement, we acquired the specified assets for aggregate cash and stock consideration of \$0.7 million (net of cash received) consisting of \$0.5 million in cash and \$0.2 million in stock at closing. In addition, Saugatuck is eligible to receive a minimum of \$0 and a maximum of up to \$1.3 million of earn-out payments for fiscal years 2015-2018 if certain revenue targets are met, payable in a combination of cash and stock.

The following table summarizes the consideration transferred to acquire Saugatuck and the amounts of identified assets acquired and liabilities assumed as of the Saugatuck Acquisition Date:

The preliminary allocable purchase price consists of the following:

Cash	\$	600
Restricted stock*		150
Contingent consideration		986
<b>Total allocable purchase price</b>	<b>\$</b>	<b>1,736</b>

\* 33,784 shares at \$4.44 at close of market on August 7, 2015.

Recognized amounts of identifiable assets acquired and liabilities assumed as of the Saugatuck Acquisition Date:

Cash	\$	63
Accounts receivable		137
Other assets		4
Intangible assets		989
Accrued expenses and other		(564)

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Net assets acquired	\$	629
Goodwill(1)	\$	1,107

(1) Goodwill of approximately \$1.1 million acquired in the acquisition is deductible for tax purposes.

Costs associated with this acquisition are included in the selling, general and administrative expenses in the condensed consolidated statement of comprehensive income and totaled \$0.1 million during the nine months ended September 30, 2015. This business combination was accounted for under the acquisition method of accounting, and as such, the aggregate purchase price was allocated on a preliminary basis to the assets acquired and liabilities assumed based on estimated fair values as of the closing dates. The purchase price allocations will be finalized after the completion of the valuation of certain intangible assets and any adjustments to the preliminary purchase price allocations are not expected to have a material impact on the Company's results of operations. Based on the valuation and other factors as described above, the purchase price assigned to intangible assets and the amortization period were as follows:

	<b>Purchase Price Allocation</b>	<b>Asset Life</b>
Amortizable intangible assets:		
Customer relationships	\$ 984	15 years
Non-compete	5	3 years
Total intangible assets	\$ 989	

The Condensed Consolidated Financial Statements include the results of Saugatuck acquisition subsequent to the closing. Had the acquisition occurred as of January 1, 2014, the impact on the Company's results of operations would not have been material.



## INFORMATION SERVICES GROUP, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-(continued)

(tabular amounts in thousands, except per share data)

(unaudited)

## NOTE 5 NET INCOME PER COMMON SHARE

Basic earnings per share is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding for the period. The 250,000 contingently issuable shares related to the acquisition of STA Consulting as well as 50,000 contingently issuable shares related to the acquisition of CCI were excluded from basic and diluted earnings per share since the contingency has not been met as of the reporting period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that would share in the net income of the Company. For the three and nine months ended September 30, 2015 and September 30, 2014, the effect of 0.1 million stock appreciation rights have not been considered in the diluted earnings per share, since the market price of the stock was less than the exercise price during the period in the computation.

The following tables set forth the computation of basic and diluted earnings per share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
<b>Basic:</b>				
Net income attributable to ISG	\$ 1,778	\$ 2,353	\$ 3,565	\$ 5,521
Weighted average common shares	37,315	37,039	37,182	37,214
Earnings per share attributable to ISG	\$ 0.05	\$ 0.06	\$ 0.10	\$ 0.15
<b>Diluted:</b>				
Net income attributable to ISG	\$ 1,778	\$ 2,353	\$ 3,565	\$ 5,521
Interest expense of convertible debt, net of tax	21	25	60	71
Net income, attributable to ISG, as adjusted	\$ 1,799	\$ 2,378	\$ 3,625	\$ 5,592
Basic weighted average common shares	37,315	37,039	37,182	37,214
Potential common shares	1,981	1,701	1,737	1,599
Diluted weighted average common shares	39,296	38,740	38,919	38,813
Diluted earnings per share attributable to ISG	\$ 0.05	\$ 0.06	\$ 0.09	\$ 0.14

## NOTE 6 INCOME TAXES

The Company's effective tax rate for the three and nine months ended September 30, 2015 was 35.3% and 40.2% based on pretax income of \$2.8 million and \$6.2 million, respectively. Our effective tax rate for the quarter is higher than the statutory rate primarily due to state taxes, non-deductible expenses and net increase of valuation allowances against deferred tax assets. This compared to 25.3% and 29.0% for the three

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and nine months ended September 30, 2014, respectively. The difference for the three and nine months ended September 30, 2015 compared to the three and nine months ended September 30, 2014 is primarily due to changes in pre-tax income by jurisdiction, the impact of permanent items and state taxes on lower projections of pre-tax book income and certain discrete tax benefits in 2014 related to tax liabilities on unremitted foreign earnings and reversal of reserves for previously unrecognized tax positions.

As of September 30, 2015, the Company had total unrecognized tax benefits of approximately \$2.4 million all of which would impact the Company's effective tax rate if recognized. The Company recognizes interest and penalties related to unrecognized tax benefits within the income tax provision in its condensed consolidated statement of operations. As of September 30, 2015, the Company's accrual of interest and penalties amounted to \$0.6 million.

### **NOTE 7 COMMITMENTS AND CONTINGENCIES**

The Company is subject to contingencies which arise through the ordinary course of business. All material liabilities of which management is aware are properly reflected in the financial statements at September 30, 2015 and December 31, 2014.

**INFORMATION SERVICES GROUP, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-(continued)**

**(tabular amounts in thousands, except per share data)**

**(unaudited)**

**STA Consulting Contingent Consideration**

As of September 30, 2015, we have recorded a liability of \$1.6 million representing the estimated fair value of contingent consideration related to the acquisition of STA Consulting and is classified as current and included in accrued expenses on the consolidated balance sheet. During the nine months ended September 30, 2015, the Company paid \$1.7 million related to 2014 performance and the remaining contingent liability is expected to be paid in the first quarter of 2016. The Company also increased the contingent consideration liability by \$0.3 million for the nine months ended September 30, 2015 based on the latest estimates of future profit level due to completion of new projects.

**CCI Contingent Consideration**

As of September 30, 2015, we have recorded a liability of \$1.0 million representing the estimated fair value of contingent consideration related to the acquisition of CCI Consulting, of which \$0.5 million is classified as current and included in accrued expenses on the consolidated balance sheet. The Company paid \$0.6 million in April of 2015 related to 2014 performance and the remaining contingent liability is expected to be paid in the second quarter of 2016 and second quarter of 2017. The Company also increased the contingent consideration liability by \$0.1 million in the third quarter of 2015 based on the latest estimates of future profit level due to completion of new projects.

**Saugatuck Contingent Consideration**

As of September 30, 2015, we have recorded a liability of \$1.0 million representing the estimated fair value of contingent consideration related to the acquisition of Saugatuck, of which \$0.2 million is classified as current and included in accrued expenses on the consolidated balance sheet.

**NOTE 8 GOODWILL**

The changes in the carrying amount of goodwill for the period ended September 30, 2015 is as follows:

Balance as of December 31, 2014	\$	36,400
Acquisition		1,107

Foreign currency impact		(247)
Balance as of September 30, 2015	\$	37,260

**NOTE 9 REDEEMABLE NONCONTROLLING INTEREST**

The following provides a summary of activity in the noncontrolling interest account for the period ended September 30, 2015 relating to the CTP Acquisition:

Balance as of December 31, 2014	\$	747
Net income attributable to noncontrolling interest		147
Accretion attributable to noncontrolling interest		59
Impact of currency translation		1
Balance as of September 30, 2015	\$	954

**NOTE 10 SEGMENT AND GEOGRAPHICAL INFORMATION**

The Company operates as one reportable segment consisting primarily of fact-based sourcing advisory services. The Company operates principally in the Americas, Europe and Asia Pacific.

## INFORMATION SERVICES GROUP, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-(continued)

(tabular amounts in thousands, except per share data)

(unaudited)

Geographical revenue information for the segment is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
<b>Revenues</b>				
Americas	\$ 27,834	\$ 28,407	\$ 84,078	\$ 80,505
Europe	18,066	19,731	54,795	60,935
Asia Pacific	5,504	5,120	16,481	14,947
	\$ 51,404	\$ 53,258	\$ 155,354	\$ 156,387

The segregation of revenues by geographic region is based upon the location of the legal entity performing the services. The Company does not measure or monitor gross profit or operating income by geography for the purposes of making operating decisions or allocating resources.

**NOTE 11 FINANCING ARRANGEMENTS AND LONG-TERM DEBT**

On May 3, 2013 (the Closing), the Company entered into a five year senior secured credit facility (the 2013 Credit Agreement) comprised of a \$45.0 million term loan facility and a \$25.0 million revolving credit facility. On May 3, 2013, the Company borrowed \$55.0 million under the 2013 Credit Agreement to refinance our existing debt under the Company's prior credit facility and to pay transaction costs. The material terms of the senior secured credit facility under the 2013 Credit Agreement are as follows, subject to the amendments to the 2013 Credit Agreement described below:

- Each of the term loan facility and revolving credit facility has a maturity date of five years from the Closing.
- The credit facility is secured by all of the equity interests owned by the Company, and its direct and indirect domestic subsidiaries and, subject to agreed exceptions, the Company's direct and indirect first-tier foreign subsidiaries and a perfected first priority security interest in all of the Company's and its direct and indirect domestic subsidiaries tangible and intangible assets.
- The Company's direct and indirect existing and future wholly-owned domestic subsidiaries serve as

guarantors to the Company's obligations under the senior secured facility.

- At the Company's option, the credit facility bears interest at a rate per annum equal to either (i) the Base Rate (which is the highest of (a) the rate publicly announced from time to time by the administrative agent as its prime rate, (b) the Federal Funds Rate plus 0.5% per annum and (c) the Eurodollar Rate, plus 1.0%), plus the applicable margin (as defined below) or (ii) Eurodollar Rate (adjusted for maximum reserves) as determined by the Administrative Agent, plus the applicable margin. The applicable margin is adjusted quarterly based upon the Company's quarterly leverage ratio.
- The Term Loan is repayable in eight consecutive quarterly installments of \$843,750 each, commencing September 30, 2013, followed by eleven consecutive quarterly installments in the amount of \$1,125,000 each, commencing September 30, 2015, and a final payment of the outstanding principal amount of the Term Loan on the Maturity Date.
- Mandatory repayments of term loans shall be required from (subject to agreed exceptions) (i) 100% of the proceeds from asset sales by the Company and its subsidiaries, (ii) 100% of the net proceeds from issuances of debt and equity by the Company and its subsidiaries, and (iii) 100% of the net proceeds from insurance recovery and condemnation events of the Company and its subsidiaries.
- The senior secured credit facility contains a number of covenants that, among other things, place restrictions on matters customarily restricted in senior secured credit facilities, including restrictions on indebtedness (including guarantee obligations), liens, fundamental changes, sales or disposition of property or assets, investments (including loans, advances, guarantees and acquisitions), transaction with affiliates, dividends and other payments in respect of capital stock, optional payments and modifications of other material debt instruments, negative pledges and agreements restricting subsidiary distributions and changes in line of business. In addition, the Company is required to comply with a total leverage ratio and fixed charge coverage ratio. As of September 30, 2015, our maximum total leverage ratio was 3.00 to 1.00 and we were in compliance with all covenants contained in the 2013 Credit Agreement.

**INFORMATION SERVICES GROUP, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS-(continued)**

**(tabular amounts in thousands, except per share data)**

**(unaudited)**

- The senior secured credit facility contains customary events of default, including cross-default to other material agreements, judgment default and change of control.

The Company is required under the 2013 Credit Agreement to establish a fixed or maximum interest rate covering a notional amount of not less than 50% of the aggregate outstanding indebtedness for borrowed money (other than the total revolving outstanding) for a period of three years from the closing date of our 2013 Credit Agreement. Subsequent to May 3, 2013, the Company entered into an agreement to cap the interest rate at 5% on the LIBOR component of its borrowings under the term loan facility until May 3, 2016. This interest rate cap is not designated for hedging or speculative purposes. The expense related to this interest rate cap was not material.

On March 18, 2014, the Company's lenders agreed to amend the 2013 Credit Agreement to allow the Company to complete the acquisition of CCI. In addition, the Company's lenders agreed to allow the Company to exclude the acquisition from its \$5 million fiscal year permitted acquisition basket and from the calculation of its Consolidated Fixed Charge Coverage ratio. Lastly, the Company's lenders agreed to increase its permitted acquisition baskets during any fiscal year from \$5 million to \$10 million and during the term of our Credit Agreement from \$15 million to \$40 million. On April 15, 2014, the acquisition of CCI was completed.

On May 11, 2015, the Company amended the 2013 Credit Agreement to reduce annual mandatory principal payments, lower borrowing costs and extend the term of the 2013 Credit Agreement by two years, resulting in a maturity date of May 3, 2020. As a result of the amendment, the Term Loan is repayable in twenty consecutive quarterly installments of \$562,500 each, commencing June 30, 2015. In addition, the amendment also allows the Company to prepay up to \$3.5 million of the subordinated convertible notes issued in connection with the Company's acquisition of Compass in 2011.

As of September 30, 2015, the total principal outstanding under the term loan facility and revolving credit facility was \$38.0 million and \$10.0 million, respectively. Additional mandatory principal repayments totaling \$0.6 million and \$2.3 million will be due in 2015 and 2016, respectively.

**Compass Convertible Notes**

On January 4, 2011, as part of the consideration for the acquisition of Compass, the Company issued an aggregate of \$6.3 million in convertible notes to Compass (the Notes). The Notes mature on January 4, 2018 and interest is payable on the outstanding principal amount, computed daily, at the rate of 3.875% per annum on January 31 of each calendar year and on the seventh anniversary of the date of the Notes. The Notes

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were subject to transfer restrictions until January 31, 2013. If the price of the Company's common stock on the Nasdaq Global Market exceeds \$4 per share for 60 consecutive trading days (the Trigger Event), a holder of the Notes may convert all (but not less than all) of the outstanding principal amount of the Notes into shares of our common stock at the rate of 1 share for every \$4 in principal amount outstanding. After the Trigger Event, the Company may prepay all or any portion of the outstanding principal amount of the Notes by giving a holder 30 days written notice.

On April 26, 2013, the Company settled a portion of the Notes. The payee agreed to accept from the Company an amount equal to \$650,000 as satisfaction in full of all indebtedness of \$1.1 million owing by the Company to such payee. As a result of this transaction, the Company recognized a gain of \$0.5 million in the second quarter of 2013 representing the difference between the fair value of the consideration issued in the settlement transaction and the carrying value of the amounts due to the payee. This amount was recorded in *Gain on Extinguishment of Debt* in the accompanying consolidated statement of comprehensive income (loss).

On November 14, 2013, the Company's lenders agreed to amend the 2013 Credit Agreement to allow the Company to prepay the entire outstanding principal amount of the CPIV S.A. Convertible Note (CPIV Note) plus accrued interest and exclude the CPIV Note prepayment from the calculation of our consolidated fixed charge coverage ratio. On November 25, 2013, the Company settled a portion of the Notes and prepaid the CPIV Note and the payee agreed to accept from the Company an amount equal to the principal of \$1.7 million plus accrued interest as satisfaction in full of all indebtedness owing by the Company to such payee. Therefore, there was no gain or loss recorded as a result of this transaction.

On March 21, 2014, the Trigger Event occurred. As a result, a holder of the Notes may convert all (but not less than all) of the outstanding principal amount of the Notes into shares of our common stock at the rate of 1 share for every \$4 in principal amount outstanding. In addition, ISG may elect to prepay all or any portion of the outstanding principal amount of the Notes by giving a holder 30 days written notice; however, such holder shall be given the opportunity to convert the outstanding principal amount into shares as described above. No holder of the Notes has the option to require cash payment as a result of the Trigger Event, hence the Notes are classified as non-current.



**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

You should read the following discussion and analysis in conjunction with our financial statements and related notes included elsewhere in this report. Except for historical information, the discussion in this report contains certain forward-looking statements that involve risks and uncertainties. We have based these forward-looking statements on our current expectations and assumptions about future events. In some cases, you can identify forward-looking statements by terminology, such as may, should, could, predict, potential, continue, expect, anticipate, intend, plan, believe, estimate, forecast and similar expressions (or the negative of such expressions.) Forward-looking statements include statements concerning 2015 revenue growth rates and capital expenditures. Forward-looking statements are based on our beliefs as well as assumptions based on information currently available to us, including financial and operational information, the volatility of our stock price, and current competitive conditions. As a result, these statements are subject to various risks and uncertainties. For a discussion of material risks and uncertainties that the Company faces, see the discussion in our 2014 Form 10-K titled "Risk Factors."

**BUSINESS OVERVIEW**

Information Services Group, Inc. (ISG) (NASDAQ: III) is a leading technology insights, market intelligence and advisory services company serving more than 500 clients around the world to help them achieve operational excellence. We support private and public sector organizations to transform and optimize their operational environments through research, benchmarking, consulting and managed services with a focus on information technology, business process transformation, program management services and enterprise resource planning. Clients look to us for unique insights and innovative solutions for leveraging technology, our deep data source, and more than five decades of experience of global leadership in information and advisory services. Based in Stamford, Connecticut, we have more than 900 employees and operate in 21 countries.

Our strategy is to strengthen our existing market position and develop new services and products to support future growth plans. As a result, we are focused on growing our existing service model, expanding geographically, developing new industry sectors, productizing market data assets, expanding our managed services offering and growing via acquisitions. Although we do not expect any adverse conditions that will impact our ability to execute against our strategy over the next twelve months, the more significant factors that could limit our ability to grow in these areas include global macro-economic conditions and the impact on the overall sourcing market, competition, our ability to retain advisors and reductions in discretionary spending with our top strategic accounts or other significant client events. Other areas that could impact the business would also include natural disasters, legislative and regulatory changes and capital market disruptions.

We derive our revenues from fees and reimbursable expenses for professional services. Certain revenues are generated under hourly or daily rates billed on a time and expense basis. Clients are typically invoiced on a monthly basis, with revenue recognized as the services are provided. There are also client engagements in which we are paid a fixed amount for our services, often referred to as fixed fee billings. This may be one single amount covering the whole engagement or several amounts for various phases or functions. From time to time, we earn incremental revenues, in addition to hourly or fixed fee billings, which are contingent on the attainment of certain contractual milestones or objectives. Such revenues may cause unusual variations in quarterly revenues and operating results.

Our results are impacted principally by our full-time consultants' utilization rate, the number of business days in each quarter and the number of our revenue-generating professionals who are available to work. Our utilization rate can be negatively affected by increased hiring because there is generally a transition period for new professionals that result in a temporary drop in our utilization rate. Our utilization rate can also be affected by seasonal variations in the demand for our services from our clients. The number of business work days is also affected by the number of vacation days taken by our consultants and holidays in each quarter. We typically have fewer business work days available in the fourth

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quarter of the year, which can impact revenues during that period. Time-and-expense engagements do not provide us with a high degree of predictability as to performance in future periods. Unexpected changes in the demand for our services can result in significant variations in utilization and revenues and present a challenge to optimal hiring and staffing. The volume of work performed for any particular client can vary widely from period to period.

### **NON-GAAP FINANCIAL PRESENTATION**

This management's discussion and analysis presents supplemental measures of our performance that are derived from our consolidated financial information but are not presented in accordance with accounting principles generally accepted in the United States of America ( GAAP ). We refer to these financial measures, which are considered non-GAAP financial measures under SEC rules, as adjusted EBITDA, adjusted net income, and adjusted earnings per diluted share, each as defined below. See Non-GAAP Financial Measures below for information about our use of these non-GAAP financial

measures, including our reasons for including these measures and reconciliations of each non-GAAP financial measure to the most directly comparable GAAP financial measure.

## RESULTS OF OPERATIONS

### NON-GAAP FINANCIAL MEASURES

We use non-GAAP financial measures to supplement the financial information presented on a GAAP basis. We provide adjusted EBITDA (defined as net income before net income attributable to noncontrolling interest, interest, taxes, depreciation and amortization, foreign currency transaction gains/losses, non-cash stock compensation, impairment charges for goodwill and intangible assets, interest on contingent consideration, gain on extinguishment of debt and bargain purchase gain), adjusted net income (defined as net income plus amortization of intangible assets, non-cash stock compensation, foreign currency transaction gains/losses and non-cash impairment charges for goodwill and intangible assets, interest on contingent consideration, gain on extinguishment of debt and bargain purchase gain, on a tax-adjusted basis) and adjusted net income as earnings per diluted share, excluding the net of tax effect of the items set forth in the table below, which are non-GAAP measures that the Company believes provide useful information to both management and investors by excluding certain expenses and financial implications of foreign currency translations, which management believes are not indicative of ISG's core operations. These non-GAAP measures are used by the Company to evaluate the Company's business strategies and management's performance. These non-GAAP financial measures exclude non-cash and certain other special charges that many investors believe may obscure the user's overall understanding of the Company's current financial performance and the Company's prospects for the future. We believe that these non-GAAP measures provide useful information to investors because they improve the comparability of the financial results between periods and provide for greater transparency of key measures used to evaluate the Company's performance.

	<b>Three Months Ended September 30,</b>	
	<b>2015</b>	<b>2014</b>
	(in thousands)	
Net income attributable to ISG	\$ 1,778	\$ 2,353
Net income attributable to noncontrolling interest	8	37
Interest expense (net of interest income)	417	499
Income taxes	975	808
Depreciation and amortization	1,752	1,863
Interest on contingent consideration	36	
Foreign currency transaction	(24)	75
Non-cash stock compensation	1,415	857
Adjusted EBITDA	\$ 6,357	\$ 6,492

	<b>Three Months Ended September 30,</b>	
	<b>2015</b>	<b>2014</b>
	(in thousands)	
Net income attributable to ISG	\$ 1,778	\$ 2,353
Intangible amortization	1,332	1,403
Non-cash stock compensation	1,415	857
Interest on contingent consideration	36	
Foreign currency transaction	(24)	75
Tax effect (1)	(1,048)	(887)

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Adjusted net income	\$	3,489	\$	3,801
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	<b>Three Months Ended September 30,</b>			
		<b>2015</b>		<b>2014</b>
		(in thousands)		
Earnings per diluted share attributable to ISG	\$	0.05	\$	0.06
Intangible amortization		0.03		0.04
Non-cash stock compensation		0.04		0.02
Interest on contingent consideration		0.00		
Foreign currency transaction		0.00		0.00
Tax effect (1)		(0.03)		(0.02)
Non-GAAP earnings per diluted share	\$	0.09	\$	0.10

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	Nine Months Ended September 30,	
	2015	2014
	(in thousands)	
Net income attributable to ISG	\$ 3,565	\$ 5,521
Net income attributable to noncontrolling interest	147	56
Interest expense (net of interest income)	1,346	1,512
Income taxes	2,497	2,277
Depreciation and amortization	5,308	5,501
Bargain purchase gain		(146)
Interest on contingent consideration	36	
Foreign currency transaction	(424)	112
Non-cash stock compensation	3,640	2,069
Adjusted EBITDA	\$ 16,115	\$ 16,902

	Nine Months Ended September 30,	
	2015	2014
	(in thousands)	
Net income attributable to ISG	\$ 3,565	\$ 5,521
Intangible amortization	3,985	4,161
Non-cash stock compensation	3,640	2,069
Bargain purchase gain		(146)
Interest on contingent consideration	36	
Foreign currency transaction	(424)	112
Tax effect (1)	(2,750)	(2,354)
Adjusted net income	\$ 8,052	\$ 9,363

	Nine Months Ended September 30,	
	2015	2014
	(in thousands)	
Earnings per diluted share attributable to ISG	\$ 0.09	\$ 0.14
Intangible amortization	0.10	0.11
Non-cash stock compensation	0.10	0.05
Bargain purchase gain		0.00
Interest on contingent consideration	0.00	
Foreign currency transaction	(0.01)	0.00
Tax effect (1)	(0.07)	(0.06)
Non-GAAP earnings per diluted share	\$ 0.21	\$ 0.24

(1) Marginal tax rate of 38% applied.

**RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2015 AND SEPTEMBER 30, 2014**

**Revenues**

Revenues are generally derived from engagements priced on a time and materials basis as well as various fixed fee projects, and are recorded based on actual time worked and are recognized as the services are performed. Revenues related to materials (mainly out-of-pocket expenses such as airfare, lodging and meals) required during an engagement generally do not include a profit mark-up and can be charged and reimbursed discretely or as part of the overall fee structure. Invoices are issued to clients at least monthly.

We operate as one reportable segment, fact-based sourcing advisory services. We operate principally in the Americas, Europe, and Asia Pacific. Our foreign operations are subject to local government regulations and to the uncertainties of the economic and political conditions of those areas.

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Geographical revenue information for the segment is as follows:

Geographic Area	Three Months Ended September 30, (in thousands)				Percent Change
	2015	2014	Change		
Americas	\$ 27,834	\$ 28,407	\$ (573)		(2)%
Europe	18,066	19,731	(1,665)		(8)%
Asia Pacific	5,504	5,120	384		8%
Total revenues	\$ 51,404	\$ 53,258	\$ (1,854)		(4)%

Revenues decreased \$1.9 million or approximately 4% in 2015. Reported revenues in the Europe and Asia Pacific regions were negatively impacted by the strengthening of the U.S. dollar.

### *Operating Expenses*

The following table presents a breakdown of our operating expenses by category:

Operating Expenses	Three Months Ended September 30, (in thousands)				Percent Change
	2015	2014	Change		
Direct costs and expenses for advisors	\$ 30,093	\$ 31,487	\$ (1,394)		(4)%
Selling, general and administrative	16,405	16,136	269		2%
Depreciation and amortization	1,752	1,863	(111)		(6)%
Total operating expenses	\$ 48,250	\$ 49,486	\$ (1,236)		(3)%

Total operating expenses decreased \$1.2 million for the quarter with decreases in direct expenses and amortization expenses. The decreases were due primarily to lower compensation and benefits. These cost decreases were partially offset by increases in stock compensation expense and contract labor. The impact of foreign currency translation into US dollars also drove costs lower compared to the same prior 2014 period.

Compensation costs consist of a mix of fixed and variable salaries, annual bonuses, benefits and profit sharing plan contributions. A portion of compensation expenses for certain billable employees are allocated between direct costs and selling, general and administrative costs based on relative time spent between billable and non-billable activities. Bonus compensation is determined based on achievement against Company financial and individual targets, and is accrued monthly throughout the year based on management's estimates of target achievement. Statutory and elective profit sharing plans are offered to employees as appropriate. Direct costs also include employee taxes, health insurance, workers compensation and disability insurance.

Sales and marketing costs consist principally of compensation expense related to business development, proposal preparation and delivery and negotiation of new client contracts. Costs also include travel expenses relating to the pursuit of sales opportunities, expenses for hosting periodic client conferences, public relations activities, participation in industry conferences, industry relations, website maintenance and business intelligence activities. The Company maintains a dedicated global marketing function responsible for developing and managing sales campaigns,

brand promotion, the ISG Index and assembling proposals.

We maintain a comprehensive program for training and professional development. Related expenses include product training, updates on new service offerings or methodologies and development of project management skills. Also included in training and professional development are expenses associated with the development, enhancement and maintenance of our proprietary methodologies and tools and the systems that support them.

General and administrative expenses consist principally of executive management compensation, allocations of billable employee compensation related to general management activities, IT infrastructure, and costs for the finance, accounting, information technology and human resource functions. General and administrative costs also reflect continued investment associated with implementing and operating client and employee management systems. Because our billable personnel operate primarily on client premises, all occupancy expenses are recorded as general and administrative.

Depreciation and amortization expense in the third quarter of 2015 and 2014 was \$1.8 million and \$1.9 million, respectively. Our fixed assets consist of furniture, fixtures, equipment (mainly personal computers) and leasehold improvements. Depreciation expense is generally computed by applying the straight-line method over the estimated useful



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lives of assets. We also capitalize certain costs associated with the purchase and development of internal-use software, system conversions and website development costs. These costs are amortized over the estimated useful life of the software or system.

We amortize our intangible assets (e.g. client relationships and databases) over their estimated useful lives. Goodwill related to acquisitions is not amortized but is subject to annual impairment testing.

### *Other (Expense), Net*

The following table presents a breakdown of other (expense), net:

	<b>Three Months Ended September 30,</b>				<b>Change</b>	<b>Percent Change</b>
	<b>(in thousands)</b>					
	<b>2015</b>		<b>2014</b>			
Interest income	\$ 2		\$ 3		(1)	(33)%
Interest expense	(419)		(502)		83	17%
Foreign currency gain (loss)	24		(75)		99	132%
Total other expense, net	\$ (393)		\$ (574)		\$ 181	32%

The decrease of \$0.2 million was primarily the result of foreign currency gain as a result of the strengthening of the U.S dollar and lower interest expense due to a decrease in interest rates and lower debt balances.

### *Income Tax Expense*

Our quarterly effective tax rate varies from period to period based on the mix of earnings among the various state and foreign tax jurisdictions in which business is conducted and the level of non-deductible expenses projected to be incurred during the current fiscal year. Our effective tax rate for the three months ended September 30, 2015 was 35.3% compared to 25.3% for the three months ended September 30, 2014. The difference is primarily due to changes in pre-tax income by jurisdiction for the three months ended September 30, 2015 compared to the three months ended September 30, 2014, along with certain discrete tax benefits recorded in that period.

## **RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015 AND SEPTEMBER 30, 2014**

### *Revenues*

Geographical revenue information for the segment is as follows:

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Nine Months Ended September 30,  
(in thousands)

Geographic Area	2015	2014	Change	Percent Change
Americas	\$ 84,078	\$ 80,505	\$ 3,573	4%
Europe	54,795	60,935	(6,140)	(10)%
Asia Pacific	16,481	14,947	1,534	10%
Total revenues	\$ 155,354	\$ 156,387	\$ (1,033)	(1)%

Revenues decreased \$1.0 million or approximately 1% in 2015. Reported revenues in the Europe and Asia Pacific regions were negatively impacted by the strengthening of the U.S dollar.

**Operating Expenses**

The following table presents a breakdown of our operating expenses by category:

Operating Expenses	Nine Months Ended September 30, (in thousands)				Percent Change
	2015	2014	Change		
Direct costs and expenses for advisors	\$ 93,089	\$ 92,796	\$ 293		%
Selling, general and administrative	49,826	48,758	1,068		2%
Depreciation and amortization	5,308	5,501	(193)		(4)%
Total operating expenses	\$ 148,223	\$ 147,055	\$ 1,168		1%

Total operating expenses increased \$1.2 million for the first nine months of 2015 with increases in selling, general and administrative expenses and direct expenses. The increases were due primarily to higher contract labor and stock compensation expense and travel expenses. These cost increases were partially offset by decreases in compensation, professional and occupancy expense. The impact of foreign currency translation into US dollars also drove costs lower compared to the same prior 2014 period.

Depreciation and amortization expense in the first nine months of 2015 and 2014 was \$5.3 million and \$5.5 million, respectively. The decrease was primarily due to a decrease in amortization as a result of intangible assets that were fully amortized.

**Other (Expense), Net**

The following table presents a breakdown of other (expense), net:

	Nine Months Ended September 30, (in thousands)				Percent Change
	2015	2014	Change		
Interest income	\$ 11	\$ 12	\$ (1)		(8)%
Interest expense	(1,357)	(1,524)	167		11%
Foreign currency gain (loss)	424	(112)	536		479%
Total other expense, net	\$ (922)	\$ (1,624)	\$ 702		43%

The decrease of \$0.7 million was primarily the result of foreign currency gain as a result of the strengthening of the U.S dollar and lower interest expense due to a decrease in interest rates and lower debt balances.

**Income Tax Expense**

Our effective tax rate for the nine months ended September 30, 2015 was 40.2% compared to 29.0% for the nine months ended September 30, 2014. The difference is primarily due to changes in pre-tax income by jurisdiction for the nine month ended September 30, 2015 compared to the nine months ended September 30, 2014, along with certain discrete tax benefits recorded in that period.

## **LIQUIDITY AND CAPITAL RESOURCES**

### *Liquidity*

Our primary sources of liquidity are cash flows from operations, existing cash and cash equivalents and our revolving credit facility. Operating assets and liabilities consist primarily of receivables from billed and unbilled services, accounts payable, accrued expenses, and accrued payroll and related benefits. The volume of billings and timing of collections and payments affect these account balances.

As of September 30, 2015, our cash and cash equivalents were \$14.3 million, a net decrease of \$13.4 million from December 31, 2014, which was primarily attributable to the following:

- net cash provided by operating activities of \$1.5 million;
- payments of principal amounts due on the debt of \$2.0 million;
- payments of contingent consideration of \$2.3 million;

- installment payment for the acquisition of CCI of \$0.7 million;
- acquisitions, net of cash acquired of \$0.5 million;
- dividend payment of \$5.2 million;
- capital expenditures for furniture, fixtures and equipment of \$1.1 million; and
- equity repurchases of \$2.5 million.

*Capital Resources*

On May 3, 2013 (the Closing ), the Company entered into a five year senior secured credit facility (the 2013 Credit Agreement ) comprised of a \$45.0 million term loan facility and a \$25.0 million revolving credit facility. On May 3, 2013, the Company borrowed \$55.0 million under the 2013 Credit Agreement to refinance our existing debt under the Company s prior credit facility and to pay transaction costs. The material terms of the senior secured credit facility under the 2013 Credit Agreement are as follows, subject to the amendments to the 2013 Credit Agreement described below:

- Each of the term loan facility and revolving credit facility has a maturity date of five years from the Closing.
- The credit facility is secured by all of the equity interests owned by the Company, and its direct and indirect domestic subsidiaries and, subject to agreed exceptions, the Company s direct and indirect first-tier foreign subsidiaries and a perfected first priority security interest in all of the Company s and its direct and indirect domestic subsidiaries tangible and intangible assets.
- The Company s direct and indirect existing and future wholly-owned domestic subsidiaries serve as guarantors to the Company s obligations under the senior secured facility.
- At the Company s option, the credit facility bears interest at a rate per annum equal to either (i) the Base Rate (which is the highest of (a) the rate publicly announced from time to time by the administrative agent as its prime rate, (b) the Federal Funds Rate plus 0.5% per annum and (c) the Eurodollar Rate, plus 1.0%), plus the applicable margin

(as defined below) or (ii) Eurodollar Rate (adjusted for maximum reserves) as determined by the Administrative Agent, plus the applicable margin. The applicable margin is adjusted quarterly based upon the Company's quarterly leverage ratio.

- The Term Loan is repayable in eight consecutive quarterly installments of \$843,750 each, commencing September 30, 2013, followed by eleven consecutive quarterly installments in the amount of \$1,125,000 each, commencing September 30, 2015, and a final payment of the outstanding principal amount of the Term Loan on the Maturity Date.
- Mandatory repayments of term loans shall be required from (subject to agreed exceptions) (i) 100% of the proceeds from asset sales by the Company and its subsidiaries, (ii) 100% of the net proceeds from issuances of debt and equity by the Company and its subsidiaries, and (iii) 100% of the net proceeds from insurance recovery and condemnation events of the Company and its subsidiaries.
- The senior secured credit facility contains a number of covenants that, among other things, place restrictions on matters customarily restricted in senior secured credit facilities, including restrictions on indebtedness (including guarantee obligations), liens, fundamental changes, sales or disposition of property or assets, investments (including loans, advances, guarantees and acquisitions), transaction with affiliates, dividends and other payments in respect of capital stock, optional payments and modifications of other material debt instruments, negative pledges and agreements restricting subsidiary distributions and changes in line of business. In addition, the Company is required to comply with a total leverage ratio and fixed charge coverage ratio. As of September 30, 2015, our maximum total leverage ratio was 3.00 to 1.00 and we were in compliance with all covenants contained in the 2013 Credit Agreement.
- The senior secured credit facility contains customary events of default, including cross-default to other material agreements, judgment default and change of control.

The Company is required under the 2013 Credit Agreement to establish a fixed or maximum interest rate covering a notional amount of not less than 50% of the aggregate outstanding indebtedness for borrowed money (other than the total revolving outstanding) for a period of three years from the closing date of our 2013 Credit Agreement. Subsequent to May 3, 2013, the Company entered into an agreement to cap the interest rate at 5% on the LIBOR component of its borrowings under the term loan facility until May 3, 2016. This interest rate cap is not designated for hedging or speculative purposes. The expense related to this interest rate cap was not material.

On March 18, 2014, the Company's lenders agreed to amend the 2013 Credit Agreement to allow the Company to complete the acquisition of CCI. In addition, the Company's lenders agreed to allow the Company to exclude the acquisition from its \$5 million fiscal year permitted acquisition basket and from the calculation of its Consolidated Fixed Charge Coverage ratio. Lastly, the Company's lenders agreed to increase its permitted acquisition baskets during any fiscal year from \$5 million to \$10 million and during the term of our Credit Agreement from \$15 million to \$40 million. On April 15, 2014, the acquisition of CCI was completed.

On May 11, 2015, the Company amended the 2013 Credit Agreement to reduce annual mandatory principal payments, lower borrowing costs and extend the term of the 2013 Credit Agreement by two years, resulting in a maturity date of May 3, 2020. As a result of the amendment, the Term Loan is repayable in twenty consecutive quarterly installments of \$562,500 each, commencing June 30, 2015. In addition, the amendment also allows the Company to prepay up to \$3.5 million of the subordinated convertible notes issued in connection with the Company's acquisition of Compass in 2011.

As of September 30, 2015, the total principal outstanding under the term loan facility and revolving credit facility was \$38.0 million and \$10.0 million, respectively. Additional mandatory principal repayments totaling \$0.6 million and \$2.3 million will be due in 2015 and 2016, respectively.

#### **Compass Convertible Notes**

On January 4, 2011, as part of the consideration for the acquisition of Compass, the Company issued an aggregate of \$6.3 million in convertible notes to Compass (the Notes). The Notes mature on January 4, 2018 and interest is payable on the outstanding principal amount, computed daily, at the rate of 3.875% per annum on January 31 of each calendar year and on the seventh anniversary of the date of the Notes. The Notes were subject to transfer restrictions until January 31, 2013. If the price of the Company's common stock on the Nasdaq Global Market exceeds \$4 per share for 60 consecutive trading days (the Trigger Event), a holder of the Notes may convert all (but not less than all) of the outstanding principal amount of the Notes into shares of our common stock at the rate of 1 share for every \$4 in principal amount outstanding. After the Trigger Event, the Company may prepay all or any portion of the outstanding principal amount of the Notes by giving a holder 30 days written notice.

On April 26, 2013, the Company settled a portion of the Notes. The payee agreed to accept from the Company an amount equal to \$650,000 as satisfaction in full of all indebtedness of \$1.1 million owing by the Company to such payee. As a result of this transaction, the Company recognized a gain of \$0.5 million in the second quarter of 2013 representing the difference between the fair value of the consideration issued in the settlement transaction and the carrying value of the amounts due to the payee. This amount was recorded in *Gain on Extinguishment of Debt* in the accompanying consolidated statement of comprehensive income (loss).

On November 14, 2013, the Company's lenders agreed to amend the 2013 Credit Agreement to allow the Company to prepay the entire outstanding principal amount of the CPIV S.A. Convertible Note (CPIV Note) plus accrued interest and exclude the CPIV Note prepayment from the calculation of our consolidated fixed charge coverage ratio. On November 25, 2013, the Company settled a portion of the Notes and prepaid the CPIV Note and the payee agreed to accept from the Company an amount equal to the principal of \$1.7 million plus accrued interest as satisfaction in full of all indebtedness owing by the Company to such payee. Therefore, there was no gain or loss recorded as a result of this transaction.

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On March 21, 2014, the Trigger Event occurred. As a result, a holder of the Notes may convert all (but not less than all) of the outstanding principal amount of the Notes into shares of our common stock at the rate of 1 share for every \$4 in principal amount outstanding. In addition, ISG may elect to prepay all or any portion of the outstanding principal amount of the Notes by giving a holder 30 days written notice; however, such holder shall be given the opportunity to convert the outstanding principal amount into shares as described above. No holder of the Notes has the option to require cash payment as a result of the Trigger Event, hence the Notes are classified as non-current.

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

We do not have any off-balance sheet financing arrangements or liabilities, guarantee contracts, retained or contingent interests in transferred assets or any obligation arising out of a material variable interest in an unconsolidated entity.

### **Recently Issued Accounting Pronouncements**

See Note 3 to our condensed consolidated financial statements included elsewhere in this report.

### **Critical Accounting Policies and Accounting Estimates**

Our discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements. We prepare these financial statements in conformity with U.S. generally accepted accounting principles. As such, we are required to make certain estimates, judgments and assumptions that affect the reported amounts of assets and



liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. We base our estimates on historical experience, available information and various other assumptions we believe to be reasonable under the circumstances. On an on-going basis, we evaluate our estimates; however, actual results may differ from these estimates under different assumptions or conditions. There have been no material changes or developments in our evaluation of the accounting estimates and the underlying assumptions or methodologies that we believe to be Critical Accounting Policies and Estimates as disclosed in our Form 10-K, for the year ended December 31, 2014.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

We are exposed to financial market risks primarily related to changes in interest rates. A 100 basis point change in interest rates would result in an annual change in the results of operations of \$0.5 million pre-tax.

We operate in a number of international areas which exposes us to significant foreign currency exchange rate risk. We have significant international revenue, which is generally collected in local currency. As of September 30, 2015, we have no outstanding forward exchange contracts or other derivative instruments for hedging or speculative purposes. It is expected that our international revenues will continue to grow as European, Asian and other markets adopt sourcing solutions and as a result of our acquisition of Compass. We recorded a foreign exchange transaction gain of \$0.4 million for the nine months ended September 30, 2015. The translation of our revenues into U.S. dollars, as well as our costs of operating internationally, may adversely affect our business, results of operations and financial condition.

We have not invested in foreign operations in highly inflationary economies; however, we may do so in future periods.

Concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. All cash and cash equivalents are on deposit in fully liquid form in high quality financial institutions. We extend credit to our clients based on an evaluation of each client's financial condition.

Our 25 largest clients accounted for approximately 46% of revenue for the year ended December 31, 2014 and 51% for the year ended December 31, 2013. If one or more of our large clients terminate or significantly reduce their engagements or fail to remain a viable business, then our revenues could be materially and adversely affected. In addition, our large clients generally maintain sizable receivable balances at any given time and our ability to collect such receivables could be jeopardized if such client fails to remain a viable business.

### **ITEM 4. CONTROLS AND PROCEDURES**

#### **Disclosure Controls and Procedures**

Our disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934 as amended (the Exchange Act) is recorded, processed, summarized and reported within the time

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periods specified in the rules and forms of the Securities and Exchange Commission, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2015, as required by the Rule 13a-15(b) under the Exchange Act. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2015.

### **Internal Control Over Financial Reporting**

There have not been any changes in the our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **PART II - OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

None.

### **ITEM 1A. RISK FACTORS**

The risk factors included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014 have not materially changed.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS****Issuer Purchases of Equity Securities**

The following table details the repurchases that were made during the three months ended September 30, 2015.

Period	Total Number of Securities Purchased (In thousands)	Average Price per Securities	Total Numbers of Securities Purchased as Part of Publicly Announced Plan (In thousands)	Approximate Dollar Value of Securities That May Yet Be Purchased Under The Plan (In thousands)
July 1 July 31	31 shares	\$ 4.70	31	\$ 16,717
August 1 August 31	13 shares	\$ 4.40	13	\$ 16,660
September 1 September 30	273 shares	\$ 4.25	273	\$ 15,498

On May 6, 2014, the Company's Board of Directors approved a new share repurchase authorization of up to \$20 million. The repurchase program is expected to be executed over time. The shares may be repurchased from time to time in open market transactions at prevailing market prices, in privately negotiated transactions, pursuant to a Rule 10b5-1 repurchase plan or by other means in accordance with federal securities laws. The timing and the amount of any repurchases will be determined by the Company's management based on its evaluation of market conditions, capital allocation alternatives, and other factors. There is no guarantee as to the number of shares that will be repurchased, and the repurchase program may be extended, suspended or discontinued at any time without notice at the Company's discretion.

On August 7, 2015, in connection with the acquisition of substantially all of the assets, and assumption of certain current liabilities of Saugatuck Technology, Inc. (Saugatuck), the purchase price included 33,784 shares of the Company's common stock to Saugatuck. The issuance of these shares of our common stock was exempt from registration under Rule 4(a)(2) promulgated under the Securities Act. See Note 4 to our condensed consolidated financial statements included elsewhere in this report for further information regarding the Saugatuck acquisition.

**ITEM 6. EXHIBITS**

The following exhibits are filed as part of this report:

Exhibit Number	Description
31.1	* Certification of Chief Executive Officer Pursuant to SEC Rule 13a-14(a)/15d-14(a).
31.2	* Certification of Chief Financial Officer Pursuant to SEC Rule 13a-14(a)/15d-14(a).
32.1	* Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	* Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	* The following materials from ISG's Quarterly Report on Form 10-Q for the quarter ended September 30, 2015 formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheet, (ii) Consolidated Statements of

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Operations, (iii) Consolidated Statements of Cash Flows and (iv) the Notes to Consolidated Financial Statements.

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\* Filed herewith.

**SIGNATURES**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**INFORMATION SERVICES GROUP, INC.**

Date: November 9, 2015

/s/ Michael P. Connors  
Michael P. Connors, Chairman of the  
Board and Chief Executive Officer

Date: November 9, 2015

/s/ David E. Berger  
David E. Berger, Executive Vice  
President and Chief Financial Officer