INSIGHT ENTERPRISES INC
Form 10-Q
August 11, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended: June 30, 2008

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: 0-25092

INSIGHT ENTERPRISES, INC.

(Exact name of registrant as specified in its charter)

Delaware	**86-0766246**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

1305 West Auto Drive, Tempe, Arizona 85284

(Address of principal executive offices) (Zip Code)

(480) 902-1001

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No o

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. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No þ

The number of shares outstanding of the issuer s common stock as of August 6, 2008 was 45,556,370.

INSIGHT ENTERPRISES, INC.
QUARTERLY REPORT ON FORM 10-Q
Three Months Ended June 30, 2008
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INSIGHT ENTERPRISES, INC.
FORWARD-LOOKING INFORMATION

Certain statements in this Quarterly Report on Form 10-Q, including statements in Management s Discussion and Analysis of Financial Condition and Results of Operations in Part I, Item 2 of this report, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements may include: projections of matters that affect net sales, gross profit, operating expenses, earnings or losses from continuing operations, non-operating income and expenses, net earnings or losses or cash flows, the recoverability of deferred tax assets, the payment of accrued expenses and liabilities and costs or gains that may result from post-closing adjustments pertaining to business acquisitions or dispositions; effects of acquisitions or dispositions and our intentions about additional acquisitions; projections of capital expenditures; our effective tax rate and earnings or losses per share in 2008; hiring plans; plans for future operations; the availability of financing and our needs or plans relating thereto; plans relating to our products and services; the effect of new accounting principles or changes in accounting policies; the effect of guaranty and indemnification obligations and off balance sheet arrangements; the outcome of ongoing tax audits; statements related to accounting estimates, including estimated stock option and other equity award forfeitures, and deferred compensation cost amortization periods; statements of belief; and statements of assumptions underlying any of the foregoing. Forward-looking statements are identified by such words as believe, anticipate, expect, estimate, intend, plan, project, will, may and variations of similar expressions, and are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified. Future events and actual results could differ materially from those set forth in, contemplated by, or underlying the forward-looking statements. There can be no assurances that the events discussed in the forward-looking statements will occur, and actual results could differ materially from those suggested by the forward-looking statements. Some of the important factors that could cause our actual results to differ materially from those projected in any forward-looking statements include, but are not limited to, the following:

- changes in the information technology industry and/or the economic environment;
- our reliance on partners for product availability, marketing funds, purchasing incentives and competitive products to sell;
- disruptions in our information technology systems and voice and data networks, including our system upgrade and the migration of acquired businesses to our information technology systems and voice and data networks;
- the integration and operation of acquired businesses, including our ability to achieve expected benefits of the acquisitions;
- actions of our competitors, including manufacturers and publishers of products we sell;
- the informal inquiry from the Securities and Exchange Commission (SEC) and stockholder litigation related to our historical stock option granting practices and the related restatement of our consolidated financial statements;
- the risks associated with international operations;
- seasonal changes in demand for sales of software licenses;
- increased debt and interest expense and lower availability on our financing facilities and changes in the overall capital markets that could increase our borrowing costs or reduce future availability of financing;
- exposure to currency exchange risks and volatility in the U.S. dollar exchange rate;

our dependence on key personnel;

risk that purchased goodwill or intangible assets become impaired;

failure to comply with the terms and conditions of our public sector contracts;

rapid changes in product standards; and

intellectual property infringement claims and challenges to our registered trademarks and trade names.

Additionally, there may be other risks that are otherwise described from time to time in the reports that we file with the SEC. Any forward-looking statements in this report should be considered in light of various important factors, including the risks and uncertainties listed above, as well as others. We assume no obligation to update, and do not intend to update, any forward-looking statements. We do not endorse any projections regarding future performance that may be made by third parties.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

INSIGHT ENTERPRISES, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)
(unaudited)

	June 30, 2008	December 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 109,563	$ 56,718
Accounts receivable, net of allowances for doubtful accounts of $22,701 and $22,831, respectively	1,222,860	1,072,612
Inventories	98,924	98,863
Inventories not available for sale	31,379	21,450
Deferred income taxes	21,905	22,020
Other current assets	33,499	38,916
Total current assets	1,518,130	1,310,579
Property and equipment, net of accumulated depreciation of $121,944 and $107,577, respectively	166,864	158,467
Goodwill	91,640	306,742
Intangible assets, net of accumulated amortization of $19,013 and $12,262, respectively	104,750	80,922
Deferred income taxes	111,319	392
Other assets	19,344	10,076
	$ 2,012,047	$ 1,867,178
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 873,551	$ 685,578
Accrued expenses and other current liabilities	114,660	113,891
Current portion of long-term debt		15,000
Deferred revenue	54,376	42,885
Total current liabilities	1,042,587	857,354
Long-term debt	339,000	187,250
Deferred income taxes	28,455	27,305
Other liabilities	24,259	20,075
	1,434,301	1,091,984

Commitments and contingencies (Note 11)

Stockholders equity:		
Preferred stock, $0.01 par value, 3,000 shares authorized; no shares issued		
Common stock, $0.01 par value, 100,000 shares authorized; 45,554 shares at June 30, 2008 and 48,458 shares at December 31, 2007 issued and outstanding,	456	485
Additional paid-in capital	366,663	386,139
Retained earnings	154,788	340,641
Accumulated other comprehensive income foreign currency translation adjustments	55,839	47,929
Total stockholders equity	577,746	775,194
	$ 2,012,047	$ 1,867,178

See accompanying notes to consolidated financial statements.

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INSIGHT ENTERPRISES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three Months Ended June 30, 2008	Three Months Ended June 30, 2007	Six Months Ended June 30, 2008	Six Months Ended June 30, 2007
Net sales	$ 1,397,722	$ 1,283,449	$ 2,505,511	$ 2,407,424
Costs of goods sold	1,195,980	1,098,636	2,150,614	2,069,436
Gross profit	201,742	184,813	354,897	337,988
Selling and administrative expenses	151,909	138,323	284,863	268,081
Goodwill impairment	313,949		313,949	
Severance and restructuring expenses	3,508	2,841	5,408	2,841
(Loss) earnings from operations	(267,624)	43,649	(249,323)	67,066
Non-operating (income) expense:				
Interest income	(700)	(396)	(1,301)	(1,054)
Interest expense	3,948	2,981	6,664	7,286
Net foreign currency exchange loss (gain)	1,055	(3,002)	118	(3,656)
Other expense, net	171	496	490	713
(Loss) earnings from continuing operations before income taxes	(272,098)	43,570	(255,294)	63,777
Income tax (benefit) expense	(97,821)	16,761	(91,537)	24,672
Net (loss) earnings from continuing operations	(174,277)	26,809	(163,757)	39,105
Net earnings from a discontinued operation				4,972
Net (loss) earnings	$ (174,277)	$ 26,809	$ (163,757)	$ 44,077
Net (loss) earnings per share Basic:				
Net (loss) earnings from continuing operations	$ (3.74)	$ 0.55	$ (3.44)	$ 0.80
Net earnings from a discontinued operation				0.10
Net (loss) earnings per share	$ (3.74)	$ 0.55	$ (3.44)	$ 0.90
Net (loss) earnings per share Diluted:				
Net (loss) earnings from continuing operations	$ (3.74)	$ 0.54	$ (3.44)	$ 0.79
Net earnings from a discontinued operation				0.10
Net (loss) earnings per share	$ (3.74)	$ 0.54	$ (3.44)	$ 0.89
Shares used in per share calculations:				

Basic	46,594	49,099	47,567	49,054
Diluted	46,594	49,402	47,567	49,346

See accompanying notes to consolidated financial statements.

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INSIGHT ENTERPRISES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Six Months Ended June 30, 2008	2007
Cash flows from operating activities:		
Net (loss) earnings from continuing operations	$ (163,757)	$ 39,105
Plus: net earnings from a discontinued operation		4,972
Net (loss) earnings	(163,757)	44,077
Adjustments to reconcile net (loss) earnings to net cash provided by operating activities:		
Goodwill impairment	313,949	
Depreciation and amortization	19,408	17,641
Provision for losses on accounts receivable	1,529	1,459
Write-downs of inventories	4,275	2,841
Non-cash stock-based compensation	5,638	5,663
Gain on sale of a discontinued operation		(7,937)
Excess tax benefit from employee gains on stock-based compensation	(108)	(45)
Deferred income taxes	(110,270)	(2,753)
Changes in assets and liabilities:		
Increase in accounts receivable	(90,819)	(42,488)
(Increase) decrease in inventories	(14,217)	484
Decrease in other current assets	14,505	11,759
Decrease (increase) in other assets	2,406	(2,221)
Increase in accounts payable	141,297	105,175
Increase (decrease) in deferred revenue	8,289	(12,937)
Decrease in accrued expenses and other liabilities	(13,084)	(17,172)
Net cash provided by operating activities	119,041	103,546
Cash flows from investing activities:		
Acquisition of Calence, net of cash acquired	(124,671)	
Proceeds from sale of a discontinued operation, net of direct expenses	(900)	28,631
Purchases of property and equipment	(15,617)	(18,867)
Net cash (used in) provided by investing activities	(141,188)	9,764
Cash flows from financing activities:		
Borrowings on senior revolving credit facility	372,770	
Repayments on senior revolving credit facility	(176,770)	
Borrowings on long-term financing facility	181,500	262,000
Repayments on long-term financing facility	(184,500)	(398,000)
Repayments on term loan	(56,250)	(3,750)
Net borrowings on short-term line of credit		27,000
Repayments on assumed debt	(7,083)	
Deferred financing fees	(3,300)	

Proceeds from sales of common stock under employee stock plans	3,078	2,475
Excess tax benefit from employee gains on stock-based compensation	108	45
Payment of payroll taxes on stock-based compensation through shares withheld	(1,983)	
Repurchases of common stock	(50,000)	
Decrease in book overdrafts	(3,893)	(15,606)
Net cash provided by (used in) financing activities	73,677	(125,836)
Foreign currency exchange effect on cash flows	1,315	3,973
Increase (decrease) in cash and cash equivalents	52,845	(8,553)
Cash and cash equivalents at beginning of period	56,718	54,697
Cash and cash equivalents at end of period	$ 109,563	$ 46,144

See accompanying notes to consolidated financial statements.

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INSIGHT ENTERPRISES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of Presentation and Recently Issued Accounting Pronouncements

We are a leading provider of brand-name information technology (IT) hardware, software and services to large enterprises, small- to medium-sized businesses (SMB) and public sector institutions in North America, Europe, the Middle East, Africa and Asia-Pacific. The Company is organized in the following three operating segments, which are primarily defined by their related geographies:

Operating Segment	Geography
North America	United States and Canada
EMEA	Europe, Middle East and Africa
APAC	Asia-Pacific

Currently, our offerings in North America and the United Kingdom include brand-name IT hardware, software and services. Our offerings in the remainder of our EMEA segment and in APAC currently only include software and select software-related services.

On April 1, 2008, we completed the acquisition of Calence, LLC (Calence) for a cash purchase price of $125,000,000 plus a preliminary working capital adjustment of $4,032,000, offset by a final post-closing working capital adjustment of $383,000. Up to an additional $35,000,000 of purchase price consideration may be due if Calence achieves certain performance targets over the next four years. During the three months ended June 30, 2008, we accrued an additional $716,000 of purchase price consideration as a result of Calence achieving certain performance targets during the quarter. Such amount was recorded as additional goodwill (see Note 3). We also assumed Calence s existing debt totaling approximately $7,400,000, of which $7,100,000 was repaid by us at closing. In addition, on April 1, 2008, we entered into a new five-year $300,000,000 senior revolving credit facility, which replaced our existing $75,000,000 revolving credit facility and our term loan facility (see Note 4). The Calence acquisition was funded, in part, using borrowings under the new facility.

In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments necessary to present fairly our financial position as of June 30, 2008, our results of operations for the three and six months ended June 30, 2008 and 2007 and our cash flows for the six months ended June 30, 2008 and 2007. The consolidated balance sheet as of December 31, 2007 was derived from the audited consolidated balance sheet at such date. The accompanying unaudited consolidated financial statements and notes have been prepared in accordance with the rules and regulations promulgated by the Securities and Exchange Commission (SEC) and consequently do not include all of the disclosures normally required by United States generally accepted accounting principles (GAAP). The results of operations for such interim periods are not necessarily indicative of results for the full year, due in part to the seasonal nature of the business. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements, including the related notes thereto, in our Annual Report on Form 10-K for the year ended December 31, 2007.

The preparation of consolidated financial statements in conformity with GAAP 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. Additionally, these estimates and assumptions affect the reported amounts of net sales and expenses during the reported period. Actual results could differ from those estimates. On an on-going basis, we evaluate our estimates, including those related to allowances for doubtful accounts, write-downs of inventories, litigation-related obligations, valuation allowances for deferred tax assets and impairment of goodwill, intangible assets and other long-lived assets if indicators of potential impairment exist.

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INSIGHT ENTERPRISES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

The consolidated financial statements include the accounts of Insight Enterprises, Inc. and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation. References to the Company, we, us, our and other similar words refer to Insight Enterprises, Inc. and its consolidated subsidiar unless the context suggests otherwise.

Recently Issued Accounting Pronouncements

Other than the partial adoption of Statement of Financial Accounting Standard No. 157 *Fair Value Measurements* (SFAS No. 157) effective January 1, 2008, as discussed in Note 8, there have been no material changes or additions to the recently issued accounting pronouncements as previously reported in Note 1 to our Consolidated Financial Statements in Part II, Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2007 which affect or may affect our financial statements.

2. Net (Loss) Earnings from Continuing Operations Per Share (EPS)

Basic EPS is computed by dividing net (loss) earnings from continuing operations available to common stockholders by the weighted-average number of common shares outstanding during each quarter. Diluted EPS is computed on the basis of the weighted average number of shares of common stock plus the effect of dilutive potential common shares outstanding during the period using the treasury stock method. Dilutive potential common shares include outstanding stock options, restricted stock awards and restricted stock units. A reconciliation of the denominators of the basic and diluted EPS calculations follows (in thousands, except per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Numerator:				
Net (loss) earnings from continuing operations	$ (174,277)	$ 26,809	$ (163,757)	$ 39,105
Denominator:				
Weighted-average shares used to compute basic EPS	46,594	49,099	47,567	49,054
Dilutive potential common shares due to dilutive options and restricted stock, net of tax effect		303		292
Weighted-average shares used to compute diluted EPS	46,594	49,402	47,567	49,346
Net (loss) earnings from continuing operations per share:				
Basic	$ (3.74)	$ 0.55	$ (3.44)	$ 0.80
Diluted	$ (3.74)	$ 0.54	$ (3.44)	$ 0.79

No potential common shares were included in the diluted EPS computation for the three and six months ended June 30, 2008 because of the net loss from continuing operations in those periods, which would result in an antidilutive per share amount. During the three and six months ended June 30, 2007, 1,480,000 and 2,456,000 weighted-average outstanding stock options, respectively, were not included in the diluted EPS calculations because the exercise prices of these options were greater than the average market price of our common stock during the respective periods.

INSIGHT ENTERPRISES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

3. Impairment

Goodwill

SFAS No. 142, *Goodwill and Other Intangible Assets*, requires that goodwill be tested for impairment at the reporting unit level on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying value. Multiple valuation techniques can be used to assess the fair value of the reporting unit. All of these techniques include the use of estimates and assumptions that are inherently uncertain. Changes in these estimates and assumptions could materially affect the determination of fair value or goodwill impairment, or both. The Company has three reporting units which are the same as our operating segments. At December 31, 2007, our goodwill balance was $306,742,000 allocated among all three of our operating segments, which represented the purchase price in excess of the net amount assigned to assets acquired and liabilities assumed by Insight in connection with previous acquisitions, adjusted for changes in foreign currency exchange rates. We tested goodwill for impairment during the fourth quarter of 2007. At that time, we concluded that the fair value of each of our reporting units was in excess of the carrying value.

On April 1, 2008, we acquired Calence, which has been integrated into our North America business. Under the purchase method of accounting, the purchase price of $139,639,000 was allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values. The excess purchase price over fair value of net assets acquired of $93,709,000 was recorded as goodwill (see Note 13). The primary driver of the acquisition was to enhance our technical capabilities around networking, advanced communications and managed services and to help accelerate our transformation to a broad-based technology solutions advisor and provider. During the three months ended June 30, 2008, we accrued an additional $716,000 of purchase price consideration (the earnout) as a result of Calence achieving certain performance targets during the quarter. Such amount was recorded as additional goodwill. The Calence acquisition and resulting additional goodwill of $94,425,000 was recorded as part of the North America reporting unit.

In consideration of the current market conditions in which we operate and the decline in our overall market capitalization resulting from decreases in the market price of Insight s publicly traded common stock, we evaluated whether an event (a triggering event) had occurred during the second quarter that would require us to perform an interim period goodwill impairment test in accordance with SFAS No. 142. Subsequent to the first quarter of 2008, the Company experienced a relatively consistent decline in market capitalization due to deteriorating market conditions and a significant decline subsequent to our announcement of preliminary first quarter 2008 results on April 23, 2008. During the first quarter of 2008, the market price of Insight s publicly traded common stock ranged from a high of $19.00 to a low of $15.49, ending the quarter at $17.50 on March 31, 2008. During the second quarter of 2008, the market price of Insight s publicly traded common stock ranged from a high of $18.20 to a low of $11.00 on April 24, 2008, when the price dropped by 22.5% and did not return to levels above that single day drop through the end of the quarter. Based on the sustained significant decline in the market price of our common stock during the second quarter of 2008, we concluded that a triggering event had occurred subsequent to March 31, 2008, which would more likely than not reduce the fair value of one or more of our reporting units below its respective carrying value.

As a result, we performed the first step of the two-step goodwill impairment test in the second quarter of 2008 in accordance with SFAS No. 142 and compared the fair values of our reporting units to their carrying values. The fair values of our reporting units were determined using established valuation techniques, specifically the market and income approaches. We determined that the fair value of the North America reporting unit was less than the carrying value of the net assets of the reporting unit, and thus, we performed step two of the impairment test for the North America reporting unit. The results of the first step of the two-step goodwill impairment test indicated that the fair value of each of our EMEA and APAC reporting units was in excess of the carrying value, and thus, step two of the impairment test for EMEA and APAC was not performed.

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INSIGHT ENTERPRISES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(unaudited)

In step two of the impairment test, we determined the implied fair value of the goodwill in our North America reporting unit and compared it to the carrying value of the goodwill. We allocated the fair value of the North America reporting unit to all of its assets and liabilities as if the reporting unit had been acquired in a business combination and the fair value of the North America reporting unit was the price paid to acquire the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. Our step two analysis resulted in no implied fair value of goodwill for the North America reporting unit, and therefore, we recognized a non-cash goodwill impairment charge of $313,949,000, $201,167,000 net of taxes, which represented the entire goodwill balance recorded in our North America operating segment as of June 30, 2008, including the entire amount of the goodwill recorded in connection with the Calence acquisition, including the earnout. The charge is included in (loss) earnings from continuing operations for the three and six months ended June 30, 2008. This non-cash charge will not impact our debt covenant compliance, cash flows or ongoing results of operations.

The changes in the carrying amount of goodwill for the six months ended June 30, 2008 are as follows (in thousands):

	North America	EMEA	APAC	Consolidated
Balance at December 31, 2007	$ 219,909	$ 68,725	$ 18,108	$ 306,742
Goodwill recorded in connection with the acquisition of Calence	94,425			94,425
Impairment charge	(313,949)			(313,949)
Other adjustments	(385)	3,322	1,485	