

KORN FERRY INTERNATIONAL  
Form 10-Q  
December 10, 2007  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

\_\_\_\_\_  
**FORM 10-Q**  
\_\_\_\_\_

**x** **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended October 31, 2007

or

**..** **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 001-14505

\_\_\_\_\_  
**KORN/FERRY INTERNATIONAL**

(Exact name of registrant as specified in its charter)

\_\_\_\_\_

**Delaware**  
(State of other jurisdiction  
of incorporation or organization)

**1900 Avenue of the Stars, Suite 2600, Los Angeles, California 90067**

**95-2623879**  
(I.R.S. Employer  
Identification Number)

(Address of principal executive offices) (Zip code)

**(310) 552-1834**

(Registrant's telephone number, including area code)

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

Large accelerated filer  an accelerated filer  or a non-accelerated filer

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

The number of shares outstanding of our common stock as of December 3, 2007 was 46,645,339.

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**KORN/FERRY INTERNATIONAL AND SUBSIDIARIES**

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**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Condensed Financial Statements****KORN/FERRY INTERNATIONAL AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(in thousands, except per share amounts)**

	As of October 31,	As of April 30,
	2007 (unaudited)	2007
<b>ASSETS</b>		
Cash and cash equivalents	\$ 166,908	\$ 232,531
Marketable securities	75,089	91,736
Receivables due from clients, net of allowance for doubtful accounts of \$12,874 and \$9,822, respectively	144,803	107,751
Income tax and other receivables	7,393	6,357
Deferred income taxes	9,914	9,524
Prepaid expenses	18,219	16,861
Total current assets	422,326	464,760
Property and equipment, net	29,459	25,999
Cash surrender value of company owned life insurance policies, net of loans	80,480	76,478
Deferred income taxes	44,691	42,013
Goodwill	139,308	124,268
Intangible assets, net	15,794	18,040
Investments and other	11,763	9,933
Total assets	\$ 743,821	\$ 761,491
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Accounts payable	\$ 11,305	\$ 10,383
Income taxes payable	24,406	22,432
Compensation and benefits payable	109,264	158,145
Other accrued liabilities	35,237	38,529
Total current liabilities	180,212	229,489
Deferred compensation and other retirement plans	104,145	91,360
Other liabilities	5,680	7,687
Total liabilities	290,037	328,536
Stockholders' equity:		
Common stock: \$0.01 par value, 150,000 shares authorized, 54,466 and 45,453 shares issued and 46,615 and 47,174 shares outstanding, respectively	392,045	400,126
Retained earnings	63,012	32,344
Unearned restricted stock compensation	(38,251)	(19,567)
Accumulated other comprehensive income	37,527	20,605

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Stockholders' equity	454,333	433,508
Less: Notes receivable from stockholders	(549)	(553)
Total stockholders' equity	453,784	432,955
Total liabilities and stockholders' equity	\$ 743,821	\$ 761,491

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

**Table of Contents****KORN/FERRY INTERNATIONAL AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME**

(in thousands, except per share amounts)

(unaudited)

	Three Months Ended		Six Months Ended	
	October 31, 2007	October 31, 2006	October 31, 2007	October 31, 2006
Fee revenue	\$ 195,857	\$ 155,718	\$ 381,210	\$ 308,481
Reimbursed out-of-pocket engagement expenses	10,967	9,069	21,891	17,452
Total revenue	206,824	164,787	403,101	325,933
Compensation and benefits	130,404	102,072	253,390	206,509
General and administrative expenses	34,212	28,260	65,913	52,625
Out-of-pocket engagement expenses	14,287	10,939	28,414	20,646
Depreciation and amortization	2,539	2,368	4,889	4,657
Total operating expenses	181,442	143,639	352,606	284,437
Operating income	25,382	21,148	50,495	41,496
Interest and other income, net	2,014	1,731	4,744	4,163
Interest expense	1,215	2,603	2,447	5,116
Income before provision for income taxes and equity in earnings of unconsolidated subsidiaries	26,181	20,276	52,792	40,543
Provision for income taxes	9,966	7,484	20,400	15,084
Equity in earnings of unconsolidated subsidiaries, net	894	774	1,817	1,770
Net income	\$ 17,109	\$ 13,566	\$ 34,209	\$ 27,229
Basic earnings per common share	\$ 0.38	\$ 0.35	\$ 0.76	\$ 0.70
Basic weighted average common shares outstanding	44,529	39,018	44,785	39,019
Diluted earnings per common share	\$ 0.37	\$ 0.31	\$ 0.74	\$ 0.62
Diluted weighted average common shares outstanding	45,841	46,568	46,573	46,667

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

**Table of Contents****KORN/FERRY INTERNATIONAL AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****(in thousands)****(unaudited)**

	<b>Six Months Ended</b>	
	<b>October 31, 2007</b>	<b>2006</b>
<b>Cash from operating activities:</b>		
Net income	\$ 34,209	\$ 27,229
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>		
Depreciation and amortization	4,889	4,657
Stock compensation expense	1,470	3,292
Amortization of discount on convertible securities		491
Loss on disposition of property and equipment	125	
Provision for doubtful accounts	6,520	4,104
Gain on cash surrender value of life insurance policies	(3,945)	(2,152)
Realized gains on marketable securities	(827)	(395)
Deferred income taxes	(6,610)	(4,817)
Non-cash compensation arrangements	6,624	3,451
<b>Change in other assets and liabilities, net of effect of acquisitions:</b>		
Deferred compensation	12,785	10,286
Receivables	(44,608)	(29,269)
Prepaid expenses	(1,357)	(1,023)
Investment in unconsolidated subsidiaries	(2,256)	(1,896)
Income taxes payable	9,019	7,128
Accounts payable and accrued liabilities	(56,815)	(33,102)
Other	(2,593)	(1,665)
<b>Net cash used in operating activities</b>	<b>(43,370)</b>	<b>(13,681)</b>
<b>Cash from investing activities:</b>		
Purchase of property and equipment	(8,050)	(5,951)
Proceeds from sales of marketable securities, net	19,674	22,929
Cash paid for acquisitions, net of cash acquired	(3,755)	(21,239)
Premiums on life insurance policies	(484)	(463)
Dividends received from unconsolidated subsidiaries	1,027	636
<b>Net cash provided by (used) in investing activities</b>	<b>8,412</b>	<b>(4,088)</b>
<b>Cash from financing activities:</b>		
Borrowings under life insurance policies	427	277
Purchase of common stock	(54,532)	(25,924)
Proceeds from issuance of common stock upon exercise of employee stock options and in connection with an employee stock purchase plan	14,928	13,546
Tax benefit from exercise of stock options	3,276	3,668
Receipts on stockholders' notes	4	4
<b>Net cash used in financing activities</b>	<b>(35,897)</b>	<b>(8,429)</b>

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Effect of exchange rates on cash and cash equivalents	5,232	(507)
Net decrease in cash and cash equivalents during the period	(65,623)	(26,705)
Cash and cash equivalents at beginning of the period	232,531	211,768
Cash and cash equivalents at end of the period	\$ 166,908	\$ 185,063

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



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**KORN/FERRY INTERNATIONAL AND SUBSIDIARIES**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED STATEMENTS**

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

**1. Summary of Significant Accounting Policies**

*Basis of Presentation*

The condensed consolidated financial statements for the three and six months ended October 31, 2007 and 2006 include the accounts of Korn/Ferry International and all of its wholly and majority owned/controlled domestic and international subsidiaries (collectively, the Company). The condensed consolidated financial statements are unaudited, but include all adjustments, consisting of normal recurring accruals and any other adjustments that management considers necessary for a fair presentation of the results for these periods. These financial statements have been prepared consistently with the accounting policies described in the Company's Annual Report on Form 10-K for the fiscal year ended April 30, 2007 (the Annual Report) and should be read together with the Annual Report.

*Critical Accounting Policies and Use of Estimates*

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (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 financial statements and the reported amounts of revenue and expenses during the reporting period. As a result, actual results could differ from these estimates. The most significant areas that require management judgment are revenue recognition, deferred compensation and the carrying values of goodwill, other intangible assets and deferred income taxes.

*Cash and Cash Equivalents*

The Company considers cash equivalents to be only those investments which are highly liquid, readily convertible and mature within three months from the date of purchase.

*Available-for-Sale Securities*

The Company considers its marketable securities as available-for-sale as defined in SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. These investments are recorded at fair value and are classified as marketable securities in the accompanying consolidated balance sheets as of October 31, 2007 and April 30, 2007. The changes in fair values, net of applicable taxes, are recorded as unrealized gains (losses) as a component of accumulated other comprehensive income in stockholders' equity. Investments are made based on the Company's investment policy which restricts the types of investments that can be made.

As of October 31, 2007 and April 30, 2007, the Company's marketable securities included \$52.5 million and \$35.2 million, respectively, held in trust for settlement of the Company's obligations under its Executive Capital Accumulation Plan (ECAP). See additional discussion in Footnote 4, Deferred Compensation, Retirement Plans and Executive Capital Accumulation Plan.

A portion of our marketable securities consist of auction rate securities. These investments, which have original maturities beyond one year, are classified as current in the accompanying balance sheets based on their highly liquid nature and because these securities represent the investment of cash that is available for current operations. As of October 31, 2007, we concluded that it was appropriate to classify certain of our investments previously classified as cash and cash equivalents as marketable securities. To conform to the current period presentation, we have reclassified \$56.6 million from cash and cash equivalents to marketable securities as of April 30, 2007.

*Stock-Based Compensation*

The Company has employee compensation plans under which various types of stock-based instruments are granted. These instruments, as more fully described below, principally include stock options, stock appreciation rights (SARs), restricted stock, and an Employee Stock Purchase Plan (ESPP). The Company accounts for stock-based instruments in accordance with Statement of Financial Accounting Standards No. 123(R), Share-Based Payment (SFAS No. 123(R)).



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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED STATEMENTS (Continued)**

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

The following table reflects the components of stock-based compensation expense recognized in the Company's condensed consolidated statements of income for the three and six months ended October 31, 2007 and 2006:

	<b>Three Months Ended</b>	<b>Six Months Ended</b>
	<b>October 31,</b>	<b>October 31,</b>
	<b>2007</b>	<b>2006</b>