

*Annual
Report
2018*

KFORCE®



Great results through strategic partnership and knowledge sharing.®

KFORCE®

is a professional staffing services and solutions firm that specializes in the areas of Technology, and Finance and Accounting. Each year, our network of over 50 offices and two national recruiting centers provides opportunities for 34,000 highly skilled professionals who work with over 4,000 clients, including 70% of the Fortune 100. Founded in 1962, our name stands for KnowledgeForce® which describes the customer-centric Kforce Knowledge Process that delivers high-touch, relationship-driven results backed by progressive technologies. At Kforce, our promise is to deliver great results through strategic partnership and knowledge sharing.

TECHNOLOGY

As the 5th largest technology staffing firm in the U.S., we engage more than 16,000 consultants annually in technology roles on a temporary, consulting and direct-hire basis. Our Technology professionals range from project managers to developers to data and network architects and technicians:

- **PROJECT MANAGEMENT AND BUSINESS ANALYSIS** offers a full suite of functional professionals to support the full scope of your initiative.
- **APPLICATION DEVELOPMENT** supports applications and systems software creation and maintenance.
- **ENTERPRISE DATA MANAGEMENT** supports any operating environment from unstructured to mature Big Data.
- **INFRASTRUCTURE** specializes in providing reliable infrastructure support to build and maintain the backbone of your organization.

FINANCE AND ACCOUNTING

As the 4th largest finance and accounting staffing firm in the U.S., we engage more than 18,000 highly skilled professionals annually in finance and accounting roles on a temporary, consulting and direct-hire basis. Our Finance and Accounting professionals range from strategic and operational to transactional and professional administration:

- **OPERATIONAL AND TECHNICAL** professionals perform day-to-day accounting and staff-level analysis, which includes directing, controlling and planning.
- **TRANSACTIONAL** functions include accounts receivable, accounts payable and payroll.
- **PROFESSIONAL ADMINISTRATION** tasks include loan servicing, benefits administration, customer service/call center, data entry, human resources and professional administrative support.

GOVERNMENT SOLUTIONS

Kforce Government Solutions, a wholly-owned subsidiary of Kforce, is a government contracting services and solutions provider that has offered a comprehensive portfolio of solutions to a wide range of Federal and Defense agencies since 1970. Headquartered in Fairfax, VA with offices in San Antonio, TX and Tampa, FL:

- **GS** offers a full range of solutions in the areas of Healthcare Informatics, Financial Management and Accounting, Enterprise Technology, Engineering and Intelligence.

This Annual Report contains forward-looking statements (within the meaning of the federal securities laws). Please see the "Cautionary Note Regarding Forward-Looking Statements" contained in the introductory portion of our Annual Report on Form 10-K for the year ended December 31, 2018 for additional information regarding forward looking statements.

The total shareholder return ("TSR") on our stock has been 892%, outperforming the Russell 2000 Index, which has returned 349% over the same period.



Kforce stock performance vs. Russell 2000 from 8/15/95 (IPO) to 12/31/18

TO OUR FELLOW SHAREHOLDERS, CLIENTS, CONSULTANTS AND EMPLOYEES:

As we reflect on 2018 and the overall strong results we delivered, we are immensely proud of what our team has accomplished. During the year we made significant progress in building our business. Our largest business, Tech Flex, is now growing at greater than twice the market rate. We have deepened client relationships, and, in many cases, we have become a trusted advisor in helping companies meet their ever-growing technology needs.

Total revenue of \$1.42 billion in 2018 grew 4.0% on a billing day basis year-over-year. We were also able to expand operating margins by 70 basis points and generate earnings per share of \$2.30, as compared to \$1.30 in 2017. We expect profitability to continue to improve as we grow and are firmly on track to reach our next milestone of 7.5% operating margins when quarterly revenues reach \$400 million. Shareholders continue to benefit from this strong performance as total shareholder return of 24.7% in 2018 was the best in our peer group.

Our strong cash flows in the year and positive outlook allowed us not only to continue to repurchase stock, but to also increase our quarterly dividend midway through the year to 18 cents per share. All told, we returned \$31 million to our shareholders through repurchases and dividends while also reducing debt by \$45 million. Our healthy cash flows, minimal capex requirements, low debt levels and \$300 million Credit Facility collectively provide flexibility to execute quickly on strategic or tuck-in acquisitions or other ventures and strategic partnerships while continuing to return significant capital to our shareholders through both a healthy dividend and share repurchases.

Revenue by Segment

- Revenues for our largest business, Tech Flex, of \$971.3 million represented 68.5% of our total revenue. We experienced strong results throughout 2018 with 9.0% year-over-year revenue growth on a billing day basis. We continued to benefit from positive trends in the length of our average assignment, improving bill rates and hours worked per consultant. We believe this success is driven by our ability to identify and deliver high caliber, qualified and skilled IT talent and a growing trend for clients to retain scarce talent for longer periods.
- Revenues for our FA Flex business of \$286.9 million represented 20.2% of our total revenue. FA Flex revenues decreased 10.2% on a billing day basis in 2018 over 2017. We continue to reposition

this business and place greater emphasis on higher bill rate opportunities within skill sets less susceptible to disruptions from technology enhancements.

- Revenues for our GS business of \$114.4 million represented 8.1% of our total revenue. GS revenues increased 9.3% on a billing day basis in 2018 compared to 2017. Our GS segment provides staffing services and solutions to the Federal Government as both a prime contractor and subcontractor in the fields of information technology and finance and accounting, as well as a product business specializing in manufacturing and delivering trauma-training manikins. Despite the instability in our political environment, our GS management team has done an admirable job building a strong, qualified pipeline of new business pursuits and is positioned for significant growth. GS derived 58% of revenues from work as a prime contractor in 2018 compared to 53% a year ago.
- Direct Hire revenues of \$45.7 million represented 3.2% of our total revenue. Direct Hire revenues decreased 4.6% on a billing day basis in 2018 over 2017. We provide direct hire services to our clients in both Tech and FA. Direct Hire remains a small but important part of our business that allows us to meet the talent needs of our clients through whatever means they prefer, whether on a flexible or permanent basis.

Our Customers

Fortune 1000 companies continue to be the largest consumers of flexible technology talent. Our revenue growth in 2018 was largely a result of our broader diversification efforts beyond our largest clients and deeper into other Fortune 1000 customers where we have established relationships. This focus on significant users of flexible staffing services has better enabled us to understand the technology issues and craft solutions for these sophisticated and substantial consumers of our services.

In both the \$30+ billion market for Technology staffing and the \$100+ billion market for IT solutions, where staffing companies are increasingly gaining a foothold, there are limited providers with the infrastructure to not only provide quality and timely talent at scale, but to also meet increasingly stringent compliance requirements. Our capabilities represent significant competitive advantages in today's war for talent. It is people serving people.

Our People

The stabilization of our team after several years of significant change, in combination with our technology and process investments, have led to improved productivity of our revenue-generating talent, which has improved greater than 10% each of the past three years. The size of our associate population was roughly unchanged in 2018 by design and we expect headcount levels to remain relatively constant in the near term. As we refine our model, we continue to identify opportunities for improving productivity, and therefore have not made material additions to associate headcount beyond those areas where productivity levels warrant additions as we believe significant capacity exists to continue to grow revenue at our targeted levels.

Technology Investments

Changing technologies are impacting staffing as new tools become available and non-traditional competitors enter the industry. At Kforce, our strategy is to embrace technologies that will enable our associates to focus on serving our customers with trusted relationships. We believe that technology will facilitate enhanced productivity and improved customer service in the sophisticated and complex world of professional and technical staffing. Technology investments during 2018 included continued enhancements to our CRM system and our Business Intelligence platform. A key technology initiative in 2019 will be the initial rollout of our Talent Relationship Management system, which we expect to go live late in the year. We have also continued to incorporate other technologies into our processes which could further enhance our capabilities. We expect the pace of change from a business model and technology standpoint to continue and we believe that we, like virtually every organization, need to maintain high levels of technology investment for the foreseeable future.

Looking Ahead

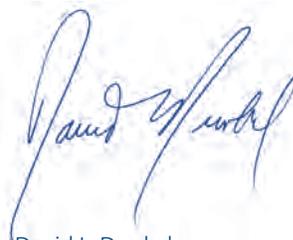
The demand environment continues to be very constructive and our outlook for 2019 is quite positive. With respect to the macroeconomic environment, significant market volatility and political uncertainty have persisted. Contrary to the concern that we might be late in the cycle however, the strength in recent employment reports point to the increasing need for skilled talent. Trends in our business as

well as others in our space support the notion that secular drivers in technology will transcend traditional cyclical patterns as business models are transformed. Non-traditional competitors are entering new end markets; thus, putting increased pressure on companies to invest in innovation and evolve. Big data, artificial intelligence and machine learning continue to be in high demand, as well as cloud computing, cybersecurity, mobility and digital marketing. Consequently, we foresee 2019 to be a year where we will continue to grow our core Tech Flex business at well above market rates and drive further improvements in profitability.

Stewardship

Stewardship and Community is an important core value to Kforce, and our Great People continue to give back by supporting local charities, organizations, and people in need by contributing through time, talent, and treasure. In 2018, our Kforce employees spent more than 10,000 hours supporting over 150 various charities nationwide. Additionally, our Day of Giving program expanded across all Kforce offices to allow our people the opportunity to dedicate time during the workday to give back to their communities. We could not be prouder of our people and how they keep the spirit of Stewardship and Community alive.

Thank you for your interest in and support of Kforce. The results that we are experiencing are the result of a lot of hard work, and tough decisions, by our team and I am grateful for their tenacity. While we have much more to do, I would like to say thank you to each and every member of our field and corporate teams, and to our consultants and our clients, for allowing us the privilege of serving you.



David L. Dunkel
*Chairman and
Chief Executive Officer*



Joseph J. Liberatore
President

SELECTED FINANCIAL DATA

The information set forth below is not necessarily indicative of the results of future operations and should be read in conjunction with Kforce's Consolidated Financial Statements and the related notes thereto incorporated into this Annual Report, hereinafter collectively referred to as the "Consolidated Financial Statements."

Years Ended December 31,	2018 ⁽¹⁾	2017 ⁽¹⁾	2016 ⁽²⁾	2015	2014 ⁽³⁾
<i>(In thousands, except per share amounts)</i>					
Revenue	\$1,418,353	\$1,357,940	\$1,319,706	\$1,319,238	\$1,217,331
Gross profit	418,608	408,056	408,499	414,114	374,581
Selling, general and administrative expenses	329,126	331,172	340,742	330,034	314,966
Depreciation and amortization	7,831	8,255	8,701	9,831	9,894
Other expense, net	4,498	4,535	3,101	2,577	1,764
Income from continuing operations, before income taxes	77,153	64,094	55,955	71,672	47,957
Income tax expense	19,173	30,809	23,182	28,848	18,559
Income from continuing operations	57,980	33,285	32,773	42,824	29,398
Income from discontinued operations, net of tax	—	—	—	—	61,517
Net income	\$ 57,980	\$ 33,285	\$ 32,773	\$ 42,824	\$ 90,915
Earnings per share—basic, continuing operations	\$2.34	\$1.32	\$1.26	\$1.53	\$0.94
Earnings per share—diluted, continuing operations	\$2.30	\$1.30	\$1.25	\$1.52	\$0.93
Earnings per share—basic	\$2.34	\$1.32	\$1.26	\$1.53	\$2.89
Earnings per share—diluted	\$2.30	\$1.30	\$1.25	\$1.52	\$2.87
Weighted average shares outstanding—basic	24,738	25,222	26,099	27,910	31,475
Weighted average shares outstanding—diluted	25,251	25,586	26,274	28,190	31,691
Dividends declared per share	\$0.60	\$0.48	\$0.48	\$0.45	\$0.41
As of December 31,	2018	2017	2016	2015	2014
<i>(In thousands)</i>					
Working capital	\$ 158,104	\$ 161,726	\$ 135,353	\$ 122,270	\$ 125,246
Total assets	\$ 379,908	\$ 384,304	\$ 365,421	\$ 351,822	\$ 363,922
Total outstanding borrowings on credit facility	\$ 71,800	\$ 116,523	\$ 111,547	\$ 80,472	\$ 93,333
Total long-term liabilities	\$ 121,219	\$ 166,308	\$ 160,332	\$ 124,449	\$ 130,351
Stockholders' equity	\$ 168,331	\$ 134,277	\$ 121,736	\$ 139,627	\$ 139,388

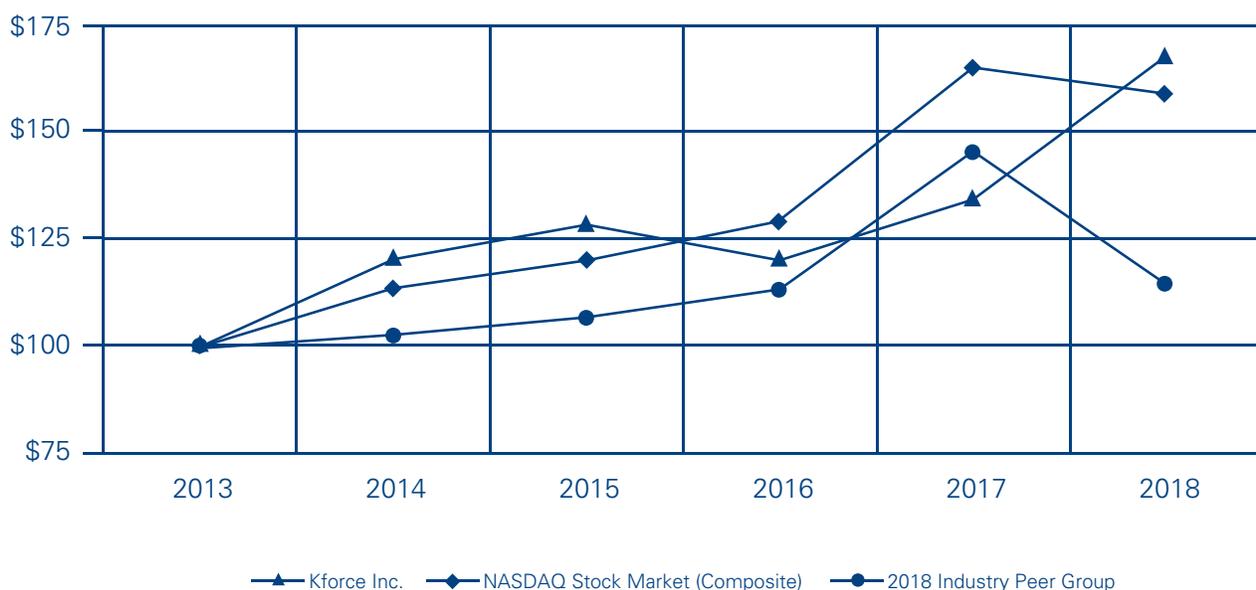
(1) The Tax Cuts and Jobs Act ("TCJA") was enacted in December 2017, which reduced the U.S. federal corporate tax rate from 35.0% to 21.0% in 2018. As a result, we revalued our net deferred income tax assets and recorded \$5.4 million of additional income tax expense during the year ended December 31, 2017.

(2) During 2016, Kforce incurred approximately \$6.0 million in severance costs associated with realignment activities focused on further streamlining our organization, which were recorded in Selling, general and administrative expenses ("SG&A").

(3) During 2014, Kforce disposed of Kforce Healthcare, Inc. ("KHI"), a wholly-owned subsidiary of Kforce Inc. The results of operations for KHI have been presented as discontinued operations for the year ended December 31, 2014.

STOCK PRICE PERFORMANCE

The following graph compares the cumulative five-year total return on our common stock, our 2018 Industry Peer Group and the NASDAQ Stock Market (U.S.) Index using the value of an investment of \$100 on December 31, 2013 with dividends fully reinvested. All returns are weighted based on market capitalization at the end of each discrete measurement period. Historical stock prices of our common stock are not necessarily indicative of future stock price performance.



Index	2013	2014	2015	2016	2017	2018
Kforce Inc.	\$100.0	\$120.2	\$128.3	\$120.1	\$134.3	\$167.4
NASDAQ Stock Market (Composite)	100.0	113.4	119.9	128.9	165.3	158.9
2018 Industry Peer Group (1)	100.0	102.3	106.4	113.0	145.7	114.1

(1) 2018 Industry Peer Group (no changes from 2017):

ASGN Incorporated	ManpowerGroup, Inc.	TrueBlue Inc.
Computer Task Group, Inc.	Resources Connection, Inc.	
Kelly Services, Inc.	Robert Half International Inc.	

In determining the industry peer group, we focus on selecting publicly-traded professional staffing companies active in recruiting and placing similar skill sets at similar types of clients. The specialty staffing industry is made up of thousands of companies, most of which are small local firms providing limited service offerings to a relatively small local client base. A report published by Staffing Industry Analysts in 2018 indicated that Kforce is one of the 10 largest publicly-traded specialty staffing firms in the U.S.

In addition to the specific staffing industry in which we operate, other primary criteria for this peer group selection includes customers, revenue footprint (i.e., revenue derived from different industries as a percentage of total revenue), geographical presence, talent, domestic presence, complexity of operating model and companies with which we compete for executive level talent. Most importantly, we consider the companies in the industry peer group as our direct business competitors on a day-to-day basis and, as a result, their size and scope vary considerably.

MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Holders of Common Stock

Our common stock trades on the NASDAQ using the ticker symbol "KFRC." As of February 21, 2019, there were approximately 150 holders of record.

Purchases of Equity Securities by the Issuer

On October 26, 2018, the Board approved an increase in our stock repurchase authorization bringing the then available authorization to \$100.0 million. The following table presents information with respect to our repurchases of Kforce common stock during the three months ended December 31, 2018:

Period	Total Number of Shares Purchased (1) (2)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs
October 1, 2018 to October 31, 2018	—	\$ —	—	\$100,000,000
November 1, 2018 to November 30, 2018	26,107	\$31.57	19,048	\$ 99,399,824
December 1, 2018 to December 31, 2018	317,087	\$29.81	216,708	\$ 92,940,594
Total	343,194	\$29.95	235,756	\$ 92,940,594

(1) Includes 7,059 shares of stock received upon vesting of restricted stock to satisfy tax withholding requirements for the period November 1, 2018 to November 30, 2018.

(2) Includes 100,379 shares of stock received upon vesting of restricted stock to satisfy tax withholding requirements for the period December 1, 2018 to December 31, 2018.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In addition to the inherent operational risks, Kforce is exposed to certain market risks, primarily related to changes in interest rates. As of December 31, 2018, we had \$71.8 million outstanding under our credit facility. Refer to Note 10—"Credit Facility" in the Notes to Consolidated Financial Statements, included in this Annual Report, for further details on our credit facility. A hypothetical 10% increase in interest rates on variable debt in effect at December 31, 2018 would have an increase to annual interest expense of less than \$0.2 million.

On April 21, 2017, Kforce entered into a forward-starting interest rate swap agreement with Wells Fargo Bank, N.A. to mitigate the risk of rising interest rates on the Firm's financial statements. The Swap rate is 1.81%, which is added to our interest rate margin to determine the fixed rate that the Firm will pay to the counterparty during the term of the Swap based on the notional amount of the Swap. The effective date of the Swap is May 31, 2017 and the maturity date is April 29, 2022. The notional amount of the Swap is \$65.0 million for the first three years and decreases to \$25.0 million for years four and five.

BUSINESS OVERVIEW

Company Overview

Kforce Inc. and its subsidiaries (collectively, “Kforce”) provide professional staffing services and solutions to clients through the following segments: Technology (“Tech”); Finance and Accounting (“FA”); and Government Solutions (“GS”). Kforce provides staffing services and solutions on both a temporary (“Flex”) and permanent (“Direct Hire”) basis. We operate through our corporate headquarters in Tampa, Florida with approximately 60 field offices located throughout the U.S. Kforce was incorporated in 1994 but its predecessor companies have been providing staffing services since 1962. Kforce completed its Initial Public Offering in August 1995.

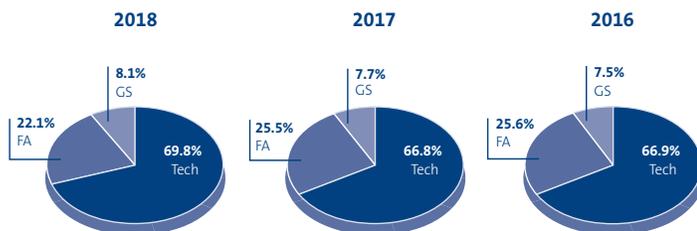
Kforce serves clients across many industries and geographies as well as companies of all sizes with a particular focus on Fortune 1000 and similarly-sized companies. We also provide services and solutions as a prime contractor and subcontractor to the U.S. Federal Government (the “Federal Government”) as well as state and local governments. We believe that our portfolio of service offerings is focused in areas of expected growth and are a key contributor to our long-term financial stability. Our 10 largest clients represented approximately 25% of revenue and no single client accounted for more than 5% of total revenue for the year ended December 31, 2018.

Substantially all of our revenues are derived from U.S. domestic operations. The asset sale of Kforce Global Solutions, Inc., (“Global”) a wholly-owned subsidiary located in the Philippines, was completed in September 2017. This sale did not meet the definition of discontinued operations. Global was included in our Tech segment and contributed approximately 1% of revenue in 2017 and 2016.

Our quarterly operating results can be affected by:

- the number of billing days in a particular quarter;
- the seasonality of our clients’ businesses;
- increased holidays and vacation days taken, which is usually highest in the fourth quarter of each calendar year; and
- increased costs as a result of certain annual U.S. state and federal employment tax resets that occur at the beginning of each calendar year, which negatively impacts our gross profit and overall profitability in the first fiscal quarter of each calendar year.

The following charts depict the percentage of our total revenue for each of our segments for the years ended December 31, 2018, 2017 and 2016:



For additional segment financial data see Note 2—“Reportable Segments” in the Notes to Consolidated Financial Statements, included in this Annual Report.

Tech Segment

Our largest segment, Tech, provides both Flex and Direct Hire services to our clients, focusing primarily on areas of information technology such as systems/applications architecture and development, project management, enterprise data management, business intelligence, artificial intelligence, machine learning, network architecture and security. Within our Tech segment, we provide service to clients in a variety of industries with a strong footprint in the financial services, communications and insurance services and also to Federal government integrators. Revenue for our Tech segment increased 9.1% to \$990.1 million in 2018 on a year-over-year basis. The average bill rate for our Tech segment in 2018 was approximately \$73 per hour.

The September 2018 report published by Staffing Industry Analysts (“SIA”) stated that temporary technology staffing is expected to experience growth of 3% in 2019. Digital transformation, as a general trend, is driving organizations across all industries to increase their technology investments as competition and the speed of change intensifies. Nontraditional competitors are also entering new end markets; thus, putting increased pressure on companies to invest in innovation and the evolution of their business models. We believe these secular drivers will transcend traditional cyclical patterns as our clients’ business models adjust. At the macro level, demand is also being driven by an ever-changing and complex regulatory and employment law environment, which increases the overall cost of employment for many companies. These factors, among others, are continuing to drive companies to look to temporary staffing providers, such as Kforce, to meet their human capital needs.

FA Segment

Our FA segment provides both Flex and Direct Hire services to our clients in areas such as general accounting, business analysis, accounts payable, accounts receivable, financial analysis and reporting, taxation, budget preparation and analysis, mortgage and loan processing, cost analysis, professional administration, outsourced functional support, credit and collections, audit services and systems and controls analysis and documentation. Within our FA segment, we provide services to clients in a variety of industries with a strong footprint in the financial services, healthcare and government sectors. Revenue for our FA segment decreased 9.3% to \$313.8 million in 2018 on a year-over-year basis. The average bill rate for our FA segment in 2018 was approximately \$35 per hour. The September 2018 report published by SIA stated that finance and accounting temporary staffing is expected to experience growth of 4% in 2019.

GS Segment

Our GS segment provides staffing services and solutions to the Federal Government as both a prime contractor and a subcontractor in the fields of information technology and finance and accounting. GS offers integrated business solutions to its clients in areas including but not limited to: information technology infrastructure transformation, healthcare informatics, data and knowledge management and analytics, research and development, audit readiness, financial management and accounting. GS contracts are concentrated among clients, such as the U.S. Department of Veteran Affairs, and the types of services and support that have historically been less likely to be impacted by sequestration threats and budget constraints, though a prolonged government shutdown could be expected to negatively impact GS revenue. Revenue for our GS segment increased 9.7% to \$114.4 million in 2018. Our GS segment also includes a product business specialized in manufacturing and delivering trauma-training manikins, which accounted for approximately 14% of total GS revenue in 2018. The majority of GS services are supplied to the Federal Government (or through a prime contractor to the Federal Government) through field offices located in the Washington, D.C. metropolitan area and San Antonio and Austin, Texas.

Our backlog represents only those U.S. government contracts and subcontracts for which funding has been provided, excluding renewal option years. Our backlog was \$47.4 million as of December 31, 2018 as compared to \$59.3 million as of December 31, 2017.

Flex Revenue

Flex revenue represents approximately 96% of total revenue over the last three fiscal years. We provide our clients with qualified individuals (“consultants”) on a temporary basis when it is determined that they have the appropriate skills and experience and are the right match for our clients. We utilize a diversified set of recruitment platforms and databases to identify consultants who are actively seeking employment. These consultants can either be directly employed by Kforce, qualified independent contractors or foreign nationals sponsored by Kforce. Our success is dependent upon our internal employees’ (“associates”) ability to: (1) acknowledge, understand and participate in creating solutions for our clients’ needs; (2) determine and understand the experience and capabilities of the consultants being recruited; and (3) ensure excellence in delivering and managing the client-consultant relationship. We believe proper execution by our associates and consultants directly impacts the longevity of the assignments, increases the likelihood of generating repeat business with our clients and fosters a better experience for our consultants, which has a direct correlation to their redeployment.

The key drivers of Flex revenue are the number of consultant assignments and billable hours, the bill rate per hour and, to a limited extent, the amount of billable expenses incurred by Kforce. Our Flex gross profit is determined by deducting related costs of employment for consultants, including compensation, payroll taxes, certain fringe benefits and subcontractor costs from Flex revenue. Associate and field management compensation, payroll taxes and other fringe benefits are included in SG&A, along with other customary costs such as administrative and corporate costs. The Flex business model involves attempting to maximize the number of billable hours and bill rates, while managing consultant pay rates and benefit costs, as well as compensation and benefits for our associates.

Direct Hire Revenue

Our Direct Hire business involves locating qualified individuals (“candidates”) for permanent placement with our clients. Direct Hire revenue represents less than 4% of total revenue over the last three fiscal years; although it is a smaller portion of our business, it continues to be an important capability in ensuring that we can meet the talent needs of our clients through whatever means they prefer. We recruit candidates using methods that are consistent with Flex consultants. Candidate searches are generally performed on a contingency basis (as opposed to a retained search), therefore fees are only earned if the candidates are ultimately hired by our clients. The typical fee structure is based upon a percentage of the candidate’s annual compensation in their first year of employment, which is known or can be estimated at the time of placement.

The key drivers of Direct Hire revenue are the number of placements and the associated placement fee. Direct Hire revenue also includes conversion revenue, which may occur when a consultant initially assigned to a client on a temporary basis is later converted to a permanent placement for a fee. Direct Hire revenue is recognized net of an allowance for “fallouts,” which occur when candidates do not complete the applicable contingency period (typically 90 days or less). There are no consultant payroll costs associated with Direct Hire placements, thus, all Direct Hire revenue increases gross profit by the full amount of the fee. Direct Hire associate commissions, compensation and benefits are included in SG&A.

Industry Overview

The professional staffing industry is made up of thousands of companies, most of which are small local firms providing limited service offerings to a relatively small local client base. A report published by SIA in 2018 indicated that Kforce is one of the 10 largest publicly-traded specialty staffing firms in the U.S.

Based upon previous economic cycles experienced by Kforce, we believe that times of sustained economic recovery generally stimulate demand for additional temporary workers in the U.S. and, conversely, an economic slowdown results in a contraction in demand for additional temporary workers in the U.S. From an economic standpoint, temporary employment figures and trends are important indicators of staffing demand, which continued to be positive during 2018, based on data published by the Bureau of Labor Statistics and SIA. The percentage of temporary staffing to total employment (penetration rate) and unemployment rate was 2.1% and 3.9%, respectively, in December 2018. Total non-farm employment was up 1.8% year-over-year as of December 2018, and temporary help employment was up 3.3% year-over-year. In addition, the college-level unemployment rate, which we believe serves as a proxy for professional employment and therefore aligns well with the consultant and candidate population that Kforce most typically serves, was 2.1% in December 2018. Further, we believe that the unemployment rate in the specialties we serve, especially in certain technology skill sets, is lower than the published averages, which we believe speaks to the demand environment in which we are operating.

According to a SIA in September 2018, the technology temporary staffing industry and finance and accounting temporary staffing industry are expected to generate projected revenues of \$32.0 billion and \$8.5 billion, respectively, in 2019 and based on these projected revenues, our current market share is approximately 3% and 4%, respectively. Our business strategies are sharply focused around expanding our share of the U.S. temporary staffing industry and further penetrating our existing clients' human capital needs.

Business Strategies

Our primary objectives are driving long-term shareholder value by achieving above-market revenue growth, making prudent investments to enhance efficiency and effectiveness within our operating model and significantly improving levels of operating profitability. We believe the following strategies will help us achieve our objectives.

Improving Productivity of our Talent. We believe that it is critical to provide our associates with high quality tools to effectively and efficiently perform their roles, to better evaluate business opportunities and to advance the value we bring to our clients and consultants. We continue to enhance our sales methodologies and processes in ways we believe will allow us to better evaluate and shape business opportunities with our clients as well as train our sales associates on our consistent and uniform methodology.

During 2018, we completed the deployment of a new time and expense application for our consultants and clients as well as a new expense application for our associates. In addition, we continue to make enhancements to our business and data intelligence capabilities as well as our customer relationship management system. We also began investing in a new talent relationship management system that we expect will better leverage our delivery strategies and processes and improve our capabilities. These investments are part of a multi-year effort to replace and upgrade our technology tools to equip our associates with improved capabilities to deliver exceptional service to our clients, consultants and candidates and improve the productivity of our associates and the scalability of our organization.

Enhancing our Client Relationships. We strive to differentiate ourselves by working collaboratively with our clients to better understand their business challenges and help them attain their organizational objectives. This collaboration focuses on building a consultative partnership rather than a transactional client relationship, which increases the intimacy with our clients and improves our ability to offer higher value and a broader array of services and support to our clients. To accomplish this, we align our revenue-generating talent with the appropriate clients based on their experience with markets, products and industries.

We measure our success in building long-lasting relationships with our clients using staffing industry benchmarks and surveys conducted by a specialized, independent third-party provider. Our client ratings compare very favorably against staffing industry averages and give us helpful insights directly from our clients on how to continue improving our relationships. We believe long-lasting relationships with our clients is a critical element in revenue growth.

Improving the Job Seeker Experience. Our consultants are a critical component to our business and essential in sustaining our client relationships. We are focused on effective and efficient processes and tools to find and attract prospective consultants, matching them to a client assignment and supporting them during their tenure with Kforce. Our success in this regard would be expected to positively influence the tenure and loyalty of our consultants and be their employer of choice, thus enabling us to deliver the highest quality talent to our clients.

We measure the quality of our service to and support of our consultants using staffing industry benchmarks and surveys conducted by a specialized, independent third-party provider. Our consultant ratings, similar to our client ratings, compare very favorably against staffing industry averages and give us helpful insights directly from our consultants on where and how we can continue improving our service during the various phases of our relationship.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS ("MD&A")

This section is intended to help the reader understand Kforce, our operations, and our present business environment. This MD&A should be read in conjunction with our Consolidated Financial Statements and the accompanying notes thereto contained in this Annual Report as well as Business Overview for an overview of our operations and business environment.

This overview summarizes the MD&A, which includes the following sections:

- *Executive Summary*—An executive summary of our results of operations for 2018.
- *Results of Operations*—An analysis of Kforce's consolidated results of operations for the three years presented in the consolidated financial statements. To assist the reader in understanding our business as a whole, certain metrics are presented for each of our segments.
- *Liquidity and Capital Resources*—An analysis of our cash flows, credit facility, off-balance sheet arrangements, stock repurchases, contractual obligations and commitments.
- *Critical Accounting Estimates*—A discussion of the accounting estimates that are most critical to aid in fully understanding and evaluating our reported financial results and that require management's most difficult, subjective or complex judgments.
- *New Accounting Standards*—A discussion of recently issued accounting standards and the potential impact on our consolidated financial statements.

EXECUTIVE SUMMARY

The following is an executive summary of what Kforce believes are highlights for 2018, which should be considered in the context of the additional discussions herein and in conjunction with the consolidated financial statements and notes thereto.

- Revenue increased 4.4% to \$1.42 billion in 2018 from \$1.36 billion in 2017. Revenue increased 9.1% and 9.7% for Tech and GS, respectively, and decreased 9.3% for FA.
- Flex revenue increased 4.5% to \$1.36 billion in 2018 from \$1.30 billion in 2017. Flex revenue increased 9.4% and 6.5% for Tech and GS, respectively, and decreased 9.9% for FA.
- Direct Hire revenue decreased 4.2% to \$45.7 million in 2018 from \$47.7 million in 2017.
- Flex gross profit margin decreased 40 basis points to 26.8% in 2018 from 27.2% in 2017. Flex gross profit margin increased 10 basis points for FA and decreased 10 basis points and 430 basis points for Tech and GS, respectively. Our GS business is operating in a cost competitive environment and, as such, has experienced reduced profitability in certain of its more recently awarded contracts.
- SG&A expenses as a percentage of revenue for the year ended December 31, 2018 decreased to 23.2% from 24.4% in 2017. The 120 basis point decrease was primarily driven by increased leverage as a result of enhancements to our performance-based compensation plans; improved associate productivity; reduced costs as a result of previous realignment activities; and a continued focus on expense discipline.

- Net income for the year ended December 31, 2018 increased 74.2% to \$58.0 million from \$33.3 million in 2017 and diluted earnings per share for the year ended December 31, 2018 increased to \$2.30 from \$1.30 per share in 2017, primarily driven by the factors noted above as well as the reduction in our effective tax rate due to the enactment of the TCJA.
- During 2018, Kforce repurchased 553 thousand shares of common stock on the open market at a total cost of approximately \$15.7 million. On October 26, 2018, the Board approved an increase in our stock repurchase authorization bringing the then available authorization to \$100.0 million.
- In the second half of 2018, the Board approved a 50% increase to the quarterly dividend, bringing it to \$0.18 per share, up from \$0.12 per share in the first half of 2018. The Firm declared and paid dividends totaling \$0.60 per share during the year ended December 31, 2018, resulting in a total cash payout of \$14.9 million.
- The total amount outstanding under our Credit Facility decreased \$44.7 million to \$71.8 million as of December 31, 2018 as compared to \$116.5 million as of December 31, 2017.
- Cash provided by operating activities was \$87.7 million during the year ended December 31, 2018 compared to \$29.3 million for 2017 primarily due to increasing levels of profitability and improved collections of our accounts receivable.

RESULTS OF OPERATIONS

In 2018, we continued to make progress on our strategic initiatives including:

- Implementing new and upgrading existing technologies that we believe will allow us to more effectively and efficiently serve our clients, consultants and candidates and improve the scalability of our organization. We completed the deployment of a new time and expense application for our consultants and clients as well as a new expense application for our associates. In addition, we continue to make enhancements to our business and data intelligence capabilities as well as our customer relationship management system. We expect these initiatives to benefit us in 2019 and beyond.
- Improving our alignment of revenue-generating talent to the markets, products, industries and clients that present the greatest opportunity for profitable revenue growth.
- Executing a Kforce brand refresh to reinforce our core values with a consistent message and identity.

To align the discussion of our Operating Results with Note 3—“Revenue” in the Notes to the Consolidated Financial Statements, included in this Annual Report, we have disaggregated our GS product business and modified the presentation to exclude it from Flex revenue and Flex gross profit. Prior periods have been adjusted to align with the current presentation.

The following table presents certain items in our Consolidated Statements of Operations and Comprehensive Income as a percentage of revenue for the years ended:

December 31,	2018	2017	2016
Revenue by segment:			
Tech	69.8%	66.8%	66.9%
FA	22.1	25.5	25.6
GS	8.1	7.7	7.5
Total Revenue	100.0%	100.0%	100.0%
Revenue by type:			
Flex	95.6%	95.6%	95.0%
Direct Hire	3.2	3.5	3.8
Product	1.2	0.9	1.2
Total Revenue	100.0%	100.0%	100.0%
Gross profit	29.5%	30.0%	31.0%
Selling, general and administrative expenses	23.2%	24.4%	25.8%
Depreciation and amortization	0.6%	0.6%	0.7%
Income from operations	5.8%	5.1%	4.5%
Income before income taxes	5.4%	4.7%	4.2%
Net income	4.1%	2.5%	2.5%

Revenue. The following table presents revenue by type for each segment and percentage change from the prior period for the years ended December 31 (in thousands):

	2018	Increase (Decrease)	2017	Increase (Decrease)	2016
Tech					
Flex revenue	\$ 971,310	9.4%	\$ 887,675	2.8%	\$ 863,434
Direct Hire revenue	18,779	(5.3)%	19,836	(1.0)%	20,043
Total Tech revenue	\$ 990,089	9.1%	\$ 907,511	2.7%	\$ 883,477
FA					
Flex revenue	\$ 286,939	(9.9)%	\$ 318,294	3.6%	\$ 307,245
Direct Hire revenue	26,909	(3.3)%	27,841	(8.3)%	30,356
Total FA revenue	\$ 313,848	(9.3)%	\$ 346,135	2.5%	\$ 337,601
GS					
Flex revenue	\$ 98,214	6.5%	\$ 92,241	11.9%	\$ 82,427
Product revenue	16,202	34.4%	12,053	(25.6)%	16,201
Total GS revenue	\$ 114,416	9.7%	\$ 104,294	5.7%	\$ 98,628
Total Flex revenue	\$1,356,463	4.5%	\$1,298,210	3.6%	\$1,253,106
Total Direct Hire revenue	45,688	(4.2)%	47,677	(5.4)%	50,399
Total Product revenue	16,202	34.4%	12,053	(25.6)%	16,201
Total Revenue	\$1,418,353	4.4%	\$1,357,940	2.9%	\$1,319,706

Our quarterly operating results are affected by the number of billing days in a quarter. The following quarterly information presents the year-over-year revenue growth rates, on a billing day basis, for the last five quarters:

	Year-Over-Year Revenue Growth Rates (Per Billing Day)				
	Q4 2018	Q3 2018	Q2 2018	Q1 2018	Q4 2017
Billing days	62	63	64	64	61
Tech Flex	9.0%	10.3%	9.8%	6.7%	5.4%
FA Flex	(11.7)%	(11.8)%	(9.4)%	(7.9)%	0.3%
GS Flex	(13.3)%	(0.6)%	18.2%	24.5%	27.9%
Total Flex	2.3%	4.2%	5.6%	4.2%	5.5%
Total Firm	2.8%	4.2%	5.4%	3.7%	5.1%

Flex Revenue. The key drivers of Flex revenue are the number of consultants on assignment and billable hours, the bill rate per hour and, to a limited extent, the amount of billable expenses incurred by Kforce.

Flex revenue for our largest segment, Tech, increased 9.4% during the year ended December 31, 2018 as compared to 2017 and increased 2.8% in 2017 from 2016. We believe the secular drivers of technology spend remain intact with many companies becoming increasingly dependent on the efficiencies provided by technology and the need for innovation to support business strategies and sustain relevancy in today's rapidly changing marketplace. Our belief in the strength in the demand environment within Tech Flex has not changed; thus, we expected continued growth in 2019 in this segment.

Our FA segment experienced a decrease in Flex revenue of 9.9% during the year ended December 31, 2018 as compared to 2017 and increased 3.6% in 2017 from 2016. The year-over-year decrease in 2018 from 2017 was primarily due to reduced volume of lower bill rate assignments as we begin to shift our focus towards higher skillset opportunities. In 2019, we expect FA Flex revenue to remain stable or slightly decrease year-over-year.

The following table presents the key drivers for the change in Flex revenue for our Tech and FA segments over the prior period (in thousands):

Year Ended December 31,	2018 vs. 2017		2017 vs. 2016	
	Tech	FA	Tech	FA
Key Drivers—Increase (Decrease)				
Volume—hours billed	\$18,284	\$(44,912)	\$ 9,710	\$ 3,915
Bill rate	62,036	13,298	14,563	7,053
Billable expenses	3,315	259	(32)	81
Total change in Flex revenue	\$83,635	\$(31,355)	\$24,241	\$11,049

These key drivers were impacted by the sale of Global's assets, which occurred in the third quarter of 2017. During 2017, Global contributed approximately 4% of the total hours billed but only 1% of the revenue for Tech Flex. The volume previously contributed by Global has been replaced by organic growth in the remainder of our portfolio at significantly higher bill rates.

The following table presents total Flex hours billed for our Tech and FA segments and percentage change over the prior period for the years ended December 31 (in thousands):

	2018	Increase (Decrease)	2017	Increase (Decrease)	2016
Tech	13,145	2.1%	12,878	1.1%	12,735
FA	8,241	(14.1)%	9,595	1.3%	9,474
Total Flex hours billed	21,386	(4.8)%	22,473	1.2%	22,209

Direct Hire Revenue. The key drivers of Direct Hire revenue are the number of placements and the associated placement fee. Direct Hire revenue also includes conversion revenue, which may occur when a consultant initially assigned to a client on a temporary basis is later converted to a permanent placement for a fee. Our GS segment does not make permanent placements.

Direct Hire revenue decreased 4.2% during the year ended December 31, 2018 as compared to 2017 and decreased 5.4% in 2017 from 2016. These decreases are primarily the result of management's strategy to make selective investments only where client needs exist.

The following table presents the key drivers for the change in Direct Hire revenue over the prior period (in thousands):

Year Ended December 31,	2018 vs. 2017		2017 vs. 2016	
	Tech	FA	Tech	FA
Key Drivers—Increase (Decrease)				
Volume—number of placements	\$(1,743)	\$(3,280)	\$(861)	\$(2,118)
Placement fee	686	2,348	654	(397)
Total change in Direct Hire revenue	\$(1,057)	\$ (932)	\$(207)	\$(2,515)

The following table presents the total number of placements for our Tech and FA segments and percentage change over the prior period for the years ended December 31:

	2018	Increase (Decrease)	2017	Increase (Decrease)	2016
Tech	1,039	(8.8)%	1,139	(4.4)%	1,191
FA	2,077	(11.8)%	2,355	(7.0)%	2,531
Total number of placements	3,116	(10.8)%	3,494	(6.1)%	3,722

The following table presents the average fee per placement for our Tech and FA segments and percentage change over the prior period for the years ended December 31:

	2018	Increase (Decrease)	2017	Increase (Decrease)	2016
Tech	\$18,070	3.8%	\$17,410	3.4%	\$16,836
FA	\$12,957	9.6%	\$11,826	(1.4)%	\$11,994
Total average placement fee	\$14,662	7.4%	\$13,646	0.8%	\$13,543

Gross Profit. Gross profit is determined by deducting direct costs (primarily consultant compensation, payroll taxes, payroll-related insurance and certain fringe benefits, as well as subcontractor costs) from total revenue. In addition, there are no consultant payroll costs associated with Direct Hire placements; thus, all Direct Hire revenue increases gross profit by the full amount of the placement fee.

The following table presents the gross profit percentage (gross profit as a percentage of total revenue) for each segment and percentage change over the prior period for the years ended December 31:

	2018	Increase (Decrease)	2017	Increase (Decrease)	2016
Tech	28.0%	(1.1)%	28.3%	(2.4)%	29.0%
FA	34.8%	1.8%	34.2%	(4.2)%	35.7%
GS	28.1%	(9.6)%	31.1%	(4.6)%	32.6%
Total gross profit percentage	29.5%	(1.7)%	30.0%	(3.2)%	31.0%

Total gross profit percentage decreased 50 basis points for the year ended December 31, 2018 as compared to 2017.

- The 30 basis point decrease for Tech was due to a lower mix of Direct Hire revenue and a slight decline in Flex gross profit percentage.
- The 60 basis point increase for FA was due to a higher mix of Direct Hire revenue and a slight increase in Flex gross profit percentage.
- The 300 basis point decrease for GS was due to a large decrease in Flex gross profit, offset by a higher mix of Product revenue to Flex revenue.

The change in total gross profit percentage for 2017 as compared to 2016 was primarily the result of a lower mix of Direct Hire revenues to total revenues as well as declines in our Flex gross profit percentage.

Flex gross profit percentage (Flex gross profit as a percentage of Flex revenue) provides management with helpful insight into the other drivers of total gross profit percentage driven by our Flex business such as changes in the spread between the consultants' bill rate and pay rate.

The following table presents the Flex gross profit percentage for each segment and percentage change over the prior period for the years ended December 31:

	2018	Increase (Decrease)	2017	Increase (Decrease)	2016
Tech	26.6%	(0.4)%	26.7%	(2.2)%	27.3%
FA	28.6%	0.4%	28.5%	(3.1)%	29.4%
GS	22.7%	(15.9)%	27.0%	2.7%	26.3%
Total Flex gross profit percentage	26.8%	(1.5)%	27.2%	(1.8)%	27.7%

The 40 basis point decrease in Flex gross profit percentage for the year ended December 31, 2018 as compared to 2017 was primarily driven by the decrease for GS. Tech and FA remained fairly stable year-over-year. GS Flex gross profit margin decreased 430 basis points primarily due to compression in bill and pay spreads as well as higher benefit costs. GS business is operating in a cost competitive environment and, as such, has experienced reduced profitability in certain of its more recently awarded contracts.

The decrease in Flex gross profit percentage of 50 basis points in 2017 from 2016 was due primarily to compression in the spread between our consultants' bill rates and pay rates and higher health insurance and other benefit costs, as well as the impact of Hurricanes Harvey and Irma.

The following table presents the key drivers for the change in Flex gross profit for our Tech and FA segments over the prior period (in thousands):

Year Ended December 31,	2018 vs. 2017		2017 vs. 2016	
	Tech	FA	Tech	FA
Key Drivers—Increase (Decrease)				
Volume—hours billed	\$22,356	\$(8,929)	\$ 6,620	\$ 3,244
Bill rate	(1,029)	481	(5,137)	(2,801)
Total change in Flex gross profit	\$21,327	\$(8,448)	\$ 1,483	\$ 443

Kforce continues to focus on training our revenue-generating associates on effective pricing and optimizing the spread between bill rates and pay rates. We believe this will serve to obtain the optimal volume, rate, effort and duration of assignment, while ultimately maximizing the benefit for our clients, our consultants and Kforce.

SG&A Expenses. Total compensation, commissions, payroll taxes and benefit costs as a percentage of SG&A represented 83.5%, 84.8%, and 84.0% of SG&A for the years ended December 31, 2018, 2017 and 2016, respectively. Commissions and other bonus incentives for our revenue-generating talent are variable costs driven primarily by revenue and gross profit levels, and associate performance. Therefore, as gross profit levels change, these expenses would also generally be anticipated to change, but remain relatively consistent as a percentage of revenue.

The following table presents certain components of SG&A as a percentage of total revenue for the years ended December 31 (in thousands):

	2018	% of Revenue	2017	% of Revenue	2016	% of Revenue
Compensation, commissions, payroll taxes and benefits costs	\$274,767	19.4%	\$280,721	20.7%	\$286,261	21.7%
Other (1)	54,359	3.8%	50,451	3.7%	54,481	4.1%
Total SG&A	\$329,126	23.2%	\$331,172	24.4%	\$340,742	25.8%

(1) Includes items such as bad debt expense, lease expense, professional fees, travel, telephone, computer and certain other expenses.

SG&A as a percentage of revenue decreased 120 basis points in 2018 compared to 2017, primarily driven by increased leverage as a result of enhancements to our performance-based compensation plans; improved associate productivity; lower revenue-generating headcount; reduced costs as a result of previous realignment activities; and a continued focus on expense discipline. Additionally, during 2017, Kforce recorded a \$3.3 million gain on the sale of Global's assets, which was partially offset by a \$1.0 million disaster relief contribution to support recovery efforts related to Hurricanes Harvey and Irma.

SG&A as a percentage of revenue decreased 140 basis points in 2017 compared to 2016, which was driven primarily by \$6.0 million in severance costs recognized in 2016 related to realignment activities, improving associate productivity levels in 2017, and overall continued discipline in areas of travel and office related expenses. These benefits were partially offset by an increase in information technology investments.

Depreciation and Amortization. The following table presents depreciation and amortization expense and percentage change over the prior period by major category for the years ended December 31 (in thousands):

	2018	Increase (Decrease)	2017	Increase (Decrease)	2016
Fixed asset depreciation (includes capital leases)	\$6,303	(9.2)%	\$6,939	4.2%	\$6,660
Capitalized software amortization	1,183	21.8%	971	(32.9)%	1,448
Intangible asset amortization	345	—%	345	(41.8)%	593
Total Depreciation and amortization	\$7,831	(5.1)%	\$8,255	(5.1)%	\$8,701

Other Expense, Net. Other expense, net was \$4.5 million in 2018, \$4.5 million in 2017 and \$3.1 million in 2016, and consisted primarily of interest expense related to outstanding borrowings under our credit facility.

Income Tax Expense. Income tax expense as a percentage of income before income taxes (our “effective tax rate”) for the year ended December 31, 2018, was 24.9%. Our effective tax rate for 2018 was positively impacted by the TCJA. For the year ended December 31, 2017, our effective tax rate was 48.1%, which was unfavorably impacted by the revaluation of our net deferred tax assets as a result of the TCJA. For the year ended December 31, 2016, our effective tax rate was 41.4%, which was unfavorably impacted by certain one-time non-cash adjustments.

NON-GAAP FINANCIAL MEASURES

Free Cash Flow. “Free Cash Flow”, a non-GAAP financial measure, is defined by Kforce as net cash provided by operating activities determined in accordance with GAAP, less capital expenditures. Management believes this provides an additional way of viewing our liquidity that, when viewed with our GAAP results, provides a more complete understanding of factors and trends affecting our cash flows and is useful information to investors as it provides a measure of the amount of cash generated from the business that can be used for strategic opportunities including investing in our business, making acquisitions, repurchasing common stock or paying dividends. Free cash flow has limitations due to the fact that it does not represent the residual cash flow available for discretionary expenditures.

Therefore, we believe it is important to view free cash flow as a complement to our Consolidated Statements of Cash Flows. The following table presents Free Cash Flow (in thousands):

Years Ended December 31,	2018	2017	2016
Net income	\$ 57,980	\$ 33,285	\$ 32,773
Non-cash provisions and other	22,643	29,134	21,093
Changes in operating assets/liabilities	7,100	(33,080)	(14,043)
Net cash provided by operating activities	87,723	29,339	39,823
Capital expenditures	(5,170)	(5,846)	(12,420)
Free cash flow	82,553	23,493	27,403
Proceeds from sale of Global’s assets	1,000	1,000	—
Change in debt	(44,723)	4,976	31,075
Repurchases of common stock	(22,187)	(14,622)	(46,013)
Cash dividends	(14,871)	(12,144)	(12,447)
Other	(2,039)	(3,806)	(33)
Change in cash and cash equivalents	\$ (267)	\$ (1,103)	\$ (15)

Adjusted EBITDA. “Adjusted EBITDA”, a non-GAAP financial measure, is defined by Kforce as net income before depreciation and amortization, stock-based compensation expense, interest expense, net and income tax expense. Adjusted EBITDA should not be considered a measure of financial performance under GAAP. Items excluded from Adjusted EBITDA are significant components in understanding and assessing our past and future financial performance, and this presentation should not be construed as an inference by us that our future results will be unaffected by those items excluded from Adjusted EBITDA. Adjusted EBITDA is a key measure used by management to assess our operations including our ability to generate cash flows and our ability to repay our debt obligations. Management believes it is useful information to investors as it provides a good metric of our core profitability in comparing our performance to our competitors, as well as our

performance over different time periods. The measure should not be considered in isolation or as an alternative to net income, cash flows or other financial statement information presented in the consolidated financial statements as indicators of financial performance or liquidity. The measure is not determined in accordance with GAAP and is susceptible to varying calculations, and as presented, may not be comparable to similarly titled measures of other companies.

In addition, although we excluded amortization of stock-based compensation expense because it is a non-cash expense, we expect to continue to incur stock-based compensation in the future and the associated stock issued may result in an increase in our outstanding shares of stock, which may result in the dilution of our shareholder ownership interest. We suggest that you evaluate these items and the potential risks of excluding such items when analyzing our financial position.

The following table presents Adjusted EBITDA and includes a reconciliation of Adjusted EBITDA to net income (in thousands):

Years Ended December 31,	2018	2017	2016
Net income	\$57,980	\$33,285	\$32,773
Depreciation and amortization	8,265	8,508	8,796
Stock-based compensation expense	8,797	7,600	6,705
Interest expense, net	4,455	5,039	3,050
Income tax expense	19,173	30,809	23,182
Adjusted EBITDA	\$98,670	\$85,241	\$74,506

LIQUIDITY AND CAPITAL RESOURCES

To meet our capital and liquidity requirements, we primarily rely on operating cash flow, as well as borrowings under our Credit Facility. At December 31, 2018, Kforce had \$158.1 million in working capital compared to \$161.7 million at December 31, 2017.

Cash Flows

We are principally focused on achieving an appropriate balance of cash flow across several areas of opportunity such as: generating positive cash flow from operating activities; returning capital to our shareholders through our quarterly dividends and common stock repurchase program; maintaining appropriate leverage under our Credit Facility; investing in our infrastructure to allow sustainable growth via capital expenditures; and maintaining sufficient liquidity to complete acquisitions or other strategic investments.

The following table presents a summary of our net cash flows from operating, investing and financing activities (in thousands):

Years Ended December 31,	2018	2017	2016
Cash provided by (used in):			
Operating activities	\$ 87,723	\$ 29,339	\$ 39,823
Investing activities	(4,170)	(4,846)	(12,420)
Financing activities	(83,820)	(25,596)	(27,418)
Change in cash and cash equivalents	\$ (267)	\$ (1,103)	\$ (15)

Operating Activities

Our largest source of operating cash flows is the collection of trade receivables and our largest use of operating cash flows is the payment of our consultant and associate compensation. When comparing cash flows from operating activities, the increase in cash provided by operating activities during the year ended December 31, 2018, as compared to 2017 was primarily due to increased levels of profitability and improved collections of our accounts receivable as well as \$11.0 million related to the decreased effective tax rate as a result of the enactment of the TCJA and the receipt of a \$6.8 million income tax refund. The decrease in cash provided by operating activities during the year ended December 31, 2017 as compared to 2016 was primarily due to an increase in accounts receivable, which was primarily driven by the revenue growth in our business, the timing of collections and continued pressure from certain larger clients for extended payment terms.

Investing Activities

Capital expenditures for the years ended December 31, 2018, 2017 and 2016, which exclude equipment acquired under capital leases, were \$5.2 million, \$5.8 million and \$12.4 million, respectively. We continually review our portfolio of businesses and their operations in comparison to our internal strategic and performance objectives. As part of this review, we may acquire other businesses and further invest in, fully divest and/or sell parts of our current businesses.

Financing Activities

The increase in cash used for financing activities in 2018 compared to 2017 was primarily driven by a reduction in our Credit Facility balance as well as an increase in cash used for common stock repurchases and dividends.

The decrease in cash used for financing activities in 2017 as compared to 2016 was primarily due to a reduction in our Credit Facility balance, offset by fewer common stock repurchases in 2017 than 2016.

The following table presents the cash flow impact of the common stock repurchase activity for the years ended December 31 (in thousands):

	2018	2017	2016
Open market repurchases	\$ 16,069	\$ 12,276	\$ 44,109
Repurchase of shares related to tax withholding requirements for vesting of restricted stock	6,118	2,346	1,904
Total cash flow impact of common stock repurchases	\$ 22,187	\$ 14,622	\$ 46,013
Cash paid in current year for settlement of prior year repurchases	\$ 3,323	\$ 935	\$ 1,012

During the years ended December 31, 2018, 2017 and 2016, Kforce declared and paid dividends of \$14.9 million (\$0.60 per share), \$12.1 million (\$0.48 per share), and \$12.4 million (\$0.48 per share), respectively. During the year ended December 31, 2018, the Board approved a 50% increase to our quarterly dividend, bringing the payout to \$0.18 per share in the second half of 2018, as compared to a quarterly dividend of \$0.12 per share for the first half of 2018. During the years ended December 31, 2017 and 2016, Kforce declared and paid a quarterly dividend of \$0.12 per share for all shares outstanding. The declaration, payment and amount of future dividends are discretionary and will be subject to determination by Kforce's Board each quarter following its review of, among other things, the Firm's current and expected financial performance as well as the ability to pay dividends under applicable law.

We believe that existing cash and cash equivalents, cash flow from operations and available borrowings under our Credit Facility will be adequate to meet the capital expenditure and working capital requirements of our operations for at least the next 12 months. However, a material deterioration in the economic environment or market conditions, among other things, could negatively impact operating results and liquidity, as well as the ability of our lenders to fund borrowings.

Actual results could also differ materially from those indicated as a result of a number of factors, including the use of currently available resources for potential acquisitions and additional stock repurchases.

Credit Facility

On May 25, 2017, the Firm entered into a credit agreement with Wells Fargo Bank, National Association, as administrative agent, Wells Fargo Securities, LLC, as lead arranger and bookrunner, Bank of America, N.A., as syndication agent, Regions Bank and BMO Harris Bank, N.A., as co-documentation agents, and the lenders referred to therein (the "Credit Facility"). Under the Credit Facility, the Firm has a maximum borrowing capacity of \$300.0 million, which may, subject to certain conditions and the participation of the lenders, be increased up to an aggregate additional amount of \$150.0 million (the "Commitment"), which is available to the Firm in the form of revolving credit loans, swingline loans and letters of credit. Letters of credit and swingline loans under the Credit Facility are subject to sublimits of \$10.0 million. The maturity date of the Credit Facility is

May 25, 2022. Borrowings under the Credit Facility are secured by substantially all of the tangible and intangible assets of the Firm, excluding the Firm's corporate headquarters and certain other designated executed collateral. As of December 31, 2018, \$71.8 million was outstanding and \$225.0 million was available, subject to the covenants described below and as of December 31, 2017, \$116.5 million was outstanding.

The Firm is subject to certain affirmative and negative covenants including (but not limited to), the maintenance of a fixed charge coverage ratio of no less than 1.25 to 1.00 and the maintenance of a total leverage ratio of no greater than 3.25 to 1.00. The numerator in the fixed charge coverage ratio is defined pursuant to the Credit Facility as earnings before interest expense, income taxes, depreciation and amortization, stock-based compensation expense and other permitted items pursuant to our Credit Facility (disclosed as "Consolidated EBITDA"), less cash paid for capital expenditures, income taxes and dividends. The denominator is defined as Kforce's fixed charges such as interest expense and principal payments paid or payable on outstanding debt other than borrowings under the Credit Facility. The total leverage ratio is defined pursuant to the Credit Facility as total indebtedness divided by Consolidated EBITDA. Our ability to make distributions or repurchases of equity securities could be limited if an event of default has occurred. Furthermore, our ability to repurchase equity securities could be limited if: (a) the total leverage ratio is greater than 2.75 to 1.00; and (b) the Firm's availability, inclusive of unrestricted cash, is less than \$25.0 million. At December 31, 2018, Kforce was not limited in making distributions and executing repurchases of our equity securities. Refer to Note 10—"Credit Facility" in the Notes to Consolidated Financial Statements, included in this Annual Report for a complete discussion of our credit facility.

Kforce entered into a forward-starting interest rate swap agreement (the "Swap") to mitigate the risk of rising interest rates and the Swap has been designated as a cash flow hedge. As of December 31, 2018 and 2017, the fair value of the Swap asset was \$0.9 million and \$0.5 million, respectively. Refer to Note 11—"Derivative Instrument and Hedging Activity" in the Notes to Consolidated Financial Statements, included in this Annual Report for a complete discussion of our interest rate swap.

Stock Repurchases

The following table presents the open market repurchase activity under the Board-authorized common stock repurchase program for the years ended December 31 (in thousands):

	2018 (1)		2017	
	Shares	\$	Shares	\$
Open market repurchases	553	\$ 15,727	526	\$ 12,239

(1) On October 26, 2018, our Board approved an increase in our stock repurchase authorization bringing the then available authorization to \$100.0 million.

As of December 31, 2018 and 2017, \$92.9 million and \$38.5 million, respectively, remained available for further repurchases under the Board-authorized common stock repurchase program.

Off-Balance Sheet Arrangements

Kforce provides letters of credit to certain vendors in lieu of cash deposits. At December 31, 2018, Kforce had letters of credit outstanding for workers' compensation and other insurance coverage totaling \$2.8 million, and for facility lease deposits totaling \$0.3 million. Aside from certain obligations more fully described in the Contractual Obligations and Commitments section below, we do not have any additional off-balance sheet arrangements that have had, or are expected to have, a material effect on our consolidated financial statements.

Contractual Obligations and Commitments

The following table presents our expected future contractual obligations as of December 31, 2018 (in thousands):

	Payments due by period				
	Total	Less than 1 year	1-3 Years	3-5 Years	More than 5 years
Credit facility (1)	\$ 80,699	\$ 2,380	\$ 5,187	\$73,132	\$ —
Operating lease obligations	21,988	6,994	9,908	3,887	1,199
Capital lease obligations	944	764	177	3	—
Purchase obligations (2)	16,293	10,619	5,393	281	—
Notes and interest payable (3)	2,211	1,005	1,206	—	—
Deferred compensation plans liability (4)	30,706	1,791	4,827	4,016	20,072
Supplemental Executive Retirement Plan (5)	17,760	—	13,351	—	4,409
Liability for unrecognized tax positions (6)	—	—	—	—	—
Total	\$170,601	\$23,553	\$40,049	\$81,319	\$25,680

(1) Our credit facility matures May 25, 2022. Our weighted average interest rate as of December 31, 2018 was utilized to forecast the expected future interest rate payments. These payments are inherently uncertain due to fluctuations in interest rates and outstanding borrowings that will occur over the remaining term of the credit facility.

(2) Purchase obligations include agreements to purchase goods and services that are enforceable, legally binding and specify all significant terms.

(3) Our notes payable as of December 31, 2018 are classified in Other current liabilities if payable within the next year or in Long-term debt—other if payable after the next year in the accompanying Consolidated Balance Sheets. The interest rate on the notes range from 2.58% to 2.80% and expire between November 2020 and October 2021.

(4) Kforce maintains various non-qualified deferred compensation plans pursuant to which eligible management and highly-compensated key employees may elect to defer all or part of their compensation to later years. These amounts are included in the accompanying Consolidated Balance Sheets and classified as Accounts payable and other accrued liabilities and Other long-term liabilities, as appropriate, and are payable based upon the elections of the plan participants (e.g. retirement, termination of employment, change-in-control). Amounts payable upon the retirement or termination of employment may become payable during the next five years if covered employees schedule a distribution, retire or terminate during that time.

(5) There is no funding requirement associated with our Supplemental Executive Retirement Plan ("SERP") and, as a result, no contributions have been made through the year ended December 31, 2018. Kforce does not currently anticipate funding our SERP during 2019. Kforce has included the total undiscounted projected benefit payments, as determined at December 31, 2018, in the table above.

(6) Kforce's liability for unrecognized tax positions as of December 31, 2018 was \$0.9 million. This balance has been excluded from the table above due to the significant uncertainty with respect to the timing and amount of settlement, if any.

Kforce has no material unrecorded commitments, losses, contingencies or guarantees associated with any related parties or unconsolidated entities.

CRITICAL ACCOUNTING ESTIMATES

Our significant accounting policies are discussed in Note 1—“Summary of Significant Accounting Policies” in the Notes to Consolidated Financial Statements, included in this Annual Report. Our consolidated financial statements are prepared in accordance with GAAP. In connection with the preparation of our consolidated financial statements, we are required to make assumptions and estimates about future events, and apply judgments that affect the reported amount of assets, liabilities, revenues, expenses and the related disclosures. We base our assumptions, estimates and judgments on historical experience, current trends and other factors that management believes to be relevant at the time our consolidated

financial statements are prepared. On a regular basis, management reviews the accounting policies, estimates, assumptions and judgments to ensure that our consolidated financial statements are presented fairly and in accordance with GAAP. However, because future events and their effects cannot be determined with certainty, actual results could differ from our assumptions and estimates, and such differences could be material. Management believes that the following accounting estimates are the most critical to aid in fully understanding and evaluating our reported financial results, and they require management's most difficult, subjective or complex judgments, resulting from the need to make estimates about the effect of matters that are inherently uncertain. We have not made any material changes in our accounting methodologies used from the prior years.

Allowance for Doubtful Accounts

Management performs an ongoing analysis of factors in establishing its allowance for doubtful accounts including recent write-off and delinquency trends, a specific analysis of significant receivable balances that are past due, the concentration of accounts receivable among clients and higher-risk sectors, and the current state of the U.S. economy.

Accounting for Income Taxes

Our consolidated effective income tax rate is influenced by tax planning opportunities available to us in the various jurisdictions in which we conduct business. Significant judgment is required in determining our effective tax rate and in evaluating our tax positions, including those that may be uncertain.

We are also required to exercise judgment with respect to the realization of our net deferred tax assets. Management evaluates all positive and negative evidence and exercises judgment regarding past and future events to determine if it is more likely than not that all or some portion of the deferred tax assets may not be realized. If appropriate, a valuation allowance is recorded against deferred tax assets to offset future tax benefits that may not be realized.

Refer to Note 5—“Income Taxes” in the Notes to Consolidated Financial Statements, included in this Annual Report for a complete discussion of the components of Kforce’s income tax expense, as well as the temporary differences that exist as of December 31, 2018.

Self-Insured Liabilities

We are self-insured for certain losses related to health insurance and workers’ compensation claims that are below insurable limits. However, we obtain third-party insurance coverage to limit our exposure to claims in excess of insurable limits. When estimating our self-insured liabilities, we consider a number of factors, including historical claims experience, plan structure, internal claims management activities, demographic factors and severity factors. Periodically, management reviews its assumptions to determine the adequacy of our self-insured liabilities.

Our self-insured liabilities contain uncertainties because management is required to make assumptions and to apply judgment to estimate the ultimate total cost to settle reported claims and claims incurred but not reported (“IBNR”) as of the balance sheet date.

Defined Benefit Pension Plan

The SERP is a defined benefit pension plan that benefits certain named executive officers. The SERP was not funded as of December 31, 2018 or 2017. When estimating the obligation for our pension benefit plan, management is required to make certain assumptions and to apply judgment with respect to determining an appropriate discount rate, bonus percentage assumptions and expected effect of future compensation increases for the participants in the plan.

Refer to Note 9—“Employee Benefit Plans” in the Notes to Consolidated Financial Statements, included in this Annual Report for a complete discussion of the terms of this plan.

Goodwill Impairment

Goodwill is tested at the reporting unit level which is generally an operating segment, or one level below the operating segment level, where a business operates and for which discrete financial information is available and reviewed by segment management. We evaluate goodwill for impairment annually or more frequently whenever events or circumstances indicate that the fair value of a reporting unit is below its carrying value. We monitor the existence of potential impairment indicators throughout the year. It is our policy to conduct impairment testing based on our current business strategy in light of present industry and economic conditions, as well as future expectations.

When performing a quantitative assessment, we determine the fair value of our reporting units using widely accepted valuation techniques, including the discounted cash flow, guideline transaction and guideline company methods. These types of analyses contain uncertainties because they require management to make significant assumptions and judgments including: (1) an appropriate rate to discount the expected future cash flows; (2) the inherent risk in achieving forecasted operating results; (3) long-term growth rates; (4) expectations for future economic cycles; (5) market comparable companies and appropriate adjustments thereto; and (6) market multiples. When performing a qualitative assessment, we assess qualitative factors to determine whether the existence of events or circumstances indicated that it was more likely than not that the fair value of the reporting unit was less than its carrying amount.

For all of our segments (Tech, FA and GS) reporting units, Kforce assessed the qualitative factors of each reporting unit to determine if it was more likely than not that the fair value of the reporting unit was less than its carrying amount. Based on the qualitative assessments, management determined that it was not more likely than not that the fair values of the reporting units were less than the carrying values. A deterioration in any of the assumptions could result in an impairment charge in the future.

See Note 6—“Goodwill and Other Intangible Assets” in the Notes to Consolidated Financial Statements, included in this Annual Report for a complete discussion of the valuation methodologies employed.

NEW ACCOUNTING STANDARDS

Refer to Note 1—“Summary of Significant Accounting Policies” in the Notes to Consolidated Financial Statements, included in this Annual Report for a discussion of new accounting standards.

MANAGEMENT REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Kforce is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) of the Exchange Act. Kforce's internal control system was designed to provide reasonable assurance to Kforce's management and the Board regarding the preparation and fair presentation of published financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Under the supervision and with the participation of the CEO and the CFO, Kforce's management assessed the effectiveness of Kforce's internal control over financial reporting as of December 31, 2018. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control—Integrated Framework (2013). Based on our assessment we believe that, as of December 31, 2018, Kforce's internal control over financial reporting is effective based on those criteria.

Kforce's independent registered public accounting firm, Deloitte & Touche LLP, has issued an audit report on our internal control over financial reporting. This report follows.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of Kforce Inc.

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Kforce Inc. and subsidiaries (“Kforce”) as of December 31, 2018 and 2017, the related consolidated statements of operations and comprehensive income, changes in stockholders’ equity, and cash flows, for each of the three years in the period ended December 31, 2018, and the related notes (collectively referred to as the “financial statements”). We also have audited Kforce’s internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Kforce as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, Kforce maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control—Integrated Framework (2013) issued by COSO.

Basis for Opinions

Kforce’s management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on Kforce’s internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to Kforce in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures to respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.



Tampa, Florida
February 22, 2019

We have served as Kforce’s auditor since 2000.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

(In thousands, except per share amounts)

Years Ended December 31,	2018	2017	2016
Revenue	\$1,418,353	\$1,357,940	\$1,319,706
Direct costs	999,745	949,884	911,207
Gross profit	418,608	408,056	408,499
Selling, general and administrative expenses	329,126	331,172	340,742
Depreciation and amortization	7,831	8,255	8,701
Income from operations	81,651	68,629	59,056
Other expense, net	4,498	4,535	3,101
Income before income taxes	77,153	64,094	55,955
Income tax expense	19,173	30,809	23,182
Net income	57,980	33,285	32,773
Other comprehensive income (loss):			
Defined benefit pension plans, net of tax	881	(373)	(134)
Change in fair value of interest rate swap, net of tax	315	289	—
Comprehensive income	\$ 59,176	\$ 33,201	\$ 32,639
Earnings per share—basic	\$2.34	\$1.32	\$1.26
Earnings per share—diluted	\$2.30	\$1.30	\$1.25
Weighted average shares outstanding—basic	24,738	25,222	26,099
Weighted average shares outstanding—diluted	25,251	25,586	26,274
Dividends declared per share	\$0.60	\$0.48	\$0.48

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

CONSOLIDATED BALANCE SHEETS

(In thousands)

December 31,	2018	2017
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 112	\$ 379
Trade receivables, net of allowances of \$2,800 and \$2,333, respectively	234,895	225,865
Income tax refund receivable	319	7,116
Prepaid expenses and other current assets	13,136	12,085
Total current assets	248,462	245,445
Fixed assets, net	35,818	39,680
Other assets, net	36,957	38,598
Deferred tax assets, net	9,751	11,316
Intangible assets, net	2,952	3,297
Goodwill	45,968	45,968
Total assets	\$ 379,908	\$ 384,304
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and other accrued liabilities	\$ 38,606	\$ 34,873
Accrued payroll costs	45,262	46,886
Other current liabilities	1,632	1,960
Income taxes payable	4,858	—
Total current liabilities	90,358	83,719
Long-term debt—credit facility	71,800	116,523
Long-term debt—other	1,359	2,597
Other long-term liabilities	48,060	47,188
Total liabilities	211,577	250,027
Commitments and contingencies (Note 14)		
Stockholders' equity:		
Preferred stock, \$0.01 par; 15,000 shares authorized, none issued and outstanding	—	—
Common stock, \$0.01 par; 250,000 shares authorized, 71,856 and 71,494 issued and outstanding, respectively	719	715
Additional paid-in capital	447,337	437,394
Accumulated other comprehensive income	1,296	100
Retained earnings	237,308	195,143
Treasury stock, at cost; 45,822 and 45,167 shares, respectively	(518,329)	(499,075)
Total stockholders' equity	168,331	134,277
Total liabilities and stockholders' equity	\$ 379,908	\$ 384,304

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

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

<i>(In thousands)</i>	Common Stock	
	Shares	Amount
Balance, December 31, 2015	70,558	\$705
Net income	—	—
Issuance for stock-based compensation and dividend equivalents, net of forfeitures	695	8
Exercise of stock options	15	—
Stock-based compensation expense	—	—
Income tax benefit from stock-based compensation	—	—
Employee stock purchase plan	—	—
Dividends (\$0.48 per share)	—	—
Defined benefit pension plans, net of tax benefit of \$89	—	—
Repurchases of common stock	—	—
Balance, December 31, 2016	71,268	713
Net income	—	—
Cumulative effect of new accounting standard (Note 13)	—	—
Issuance for stock-based compensation and dividend equivalents, net of forfeitures	221	2
Exercise of stock options	5	—
Stock-based compensation expense	—	—
Employee stock purchase plan	—	—
Dividends (\$0.48 per share)	—	—
Defined benefit pension plans, net of tax benefit of \$207	—	—
Change in fair value of interest rate swap, net of tax of \$189	—	—
Repurchases of common stock	—	—
Balance, December 31, 2017	71,494	715
Net income	—	—
Cumulative effect of new accounting standard (Note 1), net of tax of \$63	—	—
Issuance for stock-based compensation and dividend equivalents, net of forfeitures	357	4
Exercise of stock options	5	—
Stock-based compensation expense	—	—
Employee stock purchase plan	—	—
Dividends (\$0.60 per share)	—	—
Defined benefit pension plan, net of tax of \$314	—	—
Change in fair value of interest rate swap, net of tax of \$107	—	—
Repurchases of common stock	—	—
Balance, December 31, 2018	71,856	\$719

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

Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Treasury Stock		Total Stockholders' Equity
			Shares	Amount	
\$ 420,276	\$ 318	\$ 155,096	42,130	\$(436,768)	\$ 139,627
—	—	32,773	—	—	32,773
447	—	(455)	—	—	—
172	—	—	3	(63)	109
6,705	—	—	—	—	6,705
307	—	—	—	—	307
305	—	—	(34)	364	669
—	—	(12,447)	—	—	(12,447)
—	(134)	—	—	—	(134)
—	—	—	2,370	(45,873)	(45,873)
428,212	184	174,967	44,469	(482,340)	121,736
—	—	33,285	—	—	33,285
769	—	(469)	—	—	300
494	—	(496)	—	—	—
72	—	—	—	—	72
7,600	—	—	—	—	7,600
247	—	—	(25)	275	522
—	—	(12,144)	—	—	(12,144)
—	(373)	—	—	—	(373)
—	289	—	—	—	289
—	—	—	723	(17,010)	(17,010)
437,394	100	195,143	45,167	(499,075)	134,277
—	—	57,980	—	—	57,980
—	—	(179)	—	—	(179)
762	—	(766)	—	—	—
46	—	—	1	(46)	—
8,797	—	—	—	—	8,797
338	—	—	(19)	211	549
—	—	(14,870)	—	—	(14,870)
—	881	—	—	—	881
—	315	—	—	—	315
—	—	—	673	(19,419)	(19,419)
\$447,337	\$1,296	\$237,308	45,822	\$(518,329)	\$168,331

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

Years Ended December 31,	2018	2017	2016
Cash flows from operating activities:			
Net income	\$ 57,980	\$ 33,285	\$ 32,773
Adjustments to reconcile net income to cash provided by operating activities:			
Deferred income tax provision, net	989	12,243	2,007
Provision for bad debt	1,820	1,031	976
Depreciation and amortization	8,265	8,508	8,796
Stock-based compensation expense	8,797	7,600	6,705
Defined benefit pension plans expense	1,821	937	1,733
Loss on deferred compensation plan investments, net	563	510	597
Gain on sale of Global's assets	—	(3,148)	—
Other	388	1,453	279
(Increase) decrease in operating assets			
Trade receivables, net	(10,851)	(20,535)	(8,403)
Income tax refund receivable	6,797	(6,944)	354
Prepaid expenses and other current assets	(2,050)	(1,471)	(1,631)
Other assets, net	994	(556)	(495)
Increase (decrease) in operating liabilities			
Accounts payable and other accrued liabilities	3,932	(1,537)	(1,920)
Accrued payroll costs	1,350	1,954	(1,320)
Income taxes payable	4,858	(221)	(489)
Other long-term liabilities	2,070	(3,770)	(139)
Cash provided by operating activities	87,723	29,339	39,823
Cash flows from investing activities:			
Capital expenditures	(5,170)	(5,846)	(12,420)
Proceeds from sale of Global's assets	1,000	1,000	—
Cash used in investing activities	(4,170)	(4,846)	(12,420)
Cash flows from financing activities:			
Proceeds from credit facility	450,400	1,038,593	937,083
Payments on credit facility	(495,123)	(1,033,617)	(906,008)
Payments on other financing arrangements	(2,039)	(2,148)	(1,830)
Repurchases of common stock	(22,187)	(14,622)	(46,013)
Cash dividends	(14,871)	(12,144)	(12,447)
Payments of loan financing fees	—	(1,730)	(158)
Proceeds from exercise of stock options, net of shares tendered in payment of exercise	—	72	172
Proceeds from other financing arrangements	—	—	1,783
Cash used in financing activities	(83,820)	(25,596)	(27,418)
Change in cash and cash equivalents	(267)	(1,103)	(15)
Cash and cash equivalents at beginning of year	379	1,482	1,497
Cash and cash equivalents at end of year	\$ 112	\$ 379	\$ 1,482

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements have been prepared in conformity with GAAP and the rules of the SEC.

Principles of Consolidation

The consolidated financial statements include the accounts of Kforce Inc. and its subsidiaries. All intercompany transactions and balances have been eliminated in consolidation. References in this document to “Kforce,” “the Company,” “we,” “the Firm,” “management,” “our” or “us” refer to Kforce Inc. and its subsidiaries, except where the context indicates otherwise.

Use of Estimates

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 financial statements and the reported amounts of revenues and expenses during the reporting period. The most important of these estimates and assumptions relate to the following: allowance for doubtful accounts; income taxes; self-insured liabilities for workers' compensation and health insurance; obligations for pension plans and goodwill and any related impairment. Although these and other estimates and assumptions are based on the best available information, actual results could be materially different from these estimates.

Revenue Recognition

All of our revenue and trade receivables are generated from contracts with customers and substantially all of our revenues are derived from U.S. domestic operations. The following section describes the accounting policies that we believe have significant judgment, or changes in judgment, as a result of adopting Topic 606.

Revenue is recognized when control of the promised goods or services is transferred to our customers at an amount that reflects the consideration to which we expect to be entitled to in exchange for those goods or services. Revenue is recorded net of sales or other transaction taxes collected from clients and remitted to taxing authorities.

For substantially all of our revenue transactions, we have determined that gross reporting of revenues as a principal versus net as an agent is the appropriate accounting treatment because Kforce: (i) is primarily responsible for fulfilling the promise to provide the specified good or service to the customer, (ii) has discretion in selecting and assigning the temporary workers to particular jobs and establishing the bill rate, and (iii) bears the risk and rewards of the transaction, including credit risk if the customer fails to pay for services performed.

Flex Revenue

Flex revenue is recognized over time as temporary staffing services are provided by our consultants at the contractually established bill rates, net of applicable variable consideration. Reimbursements of travel and out-of-pocket expenses (“billable expenses”) are also recorded within Flex revenue when incurred and the equivalent amount of expense is recorded in Direct costs in the Consolidated Statements of Operations and Comprehensive Income.

Certain temporary staffing services are provided under time-and-material and fixed-price arrangements. For time-and-materials contracts, we recognize revenue in the amount of consideration to which we have the right to invoice when it corresponds directly to the services transferred to the customer satisfied over time. For fixed-price contracts, which are most frequently utilized in our GS segment, revenue is recognized over time using the input method based on costs incurred as a proportion of estimated total costs. Incurred costs represent work performed, which corresponds with, and thereby best depicts, the transfer of control to the customer. Management uses significant judgments when estimating the total labor hours expected to complete the contract performance obligation.

Direct Hire Revenue

Direct Hire revenue is recognized at the agreed upon rate at the point in time when the performance obligation is considered complete. Our policy requires the following criteria to be met in order for the performance obligation to be considered complete: (i) the candidate accepted the position; (ii) the candidate resigned from their current employer; and (iii) the agreed upon start date falls within the following month. Since the client has accepted the candidate and can direct the use of and obtains the significant risk and rewards of the placement, we consider this point as the transfer of control to our client.

Product Revenue

Revenue for our product business, which accounts for approximately 1% of total revenue for each of the years ended December 31, 2018, 2017 and 2016, is recognized after the transfer of control to the customer, which typically occurs upon delivery.

Variable Consideration

Transaction prices for Flex revenue include variable consideration, such as customer rebates and discounts. Management evaluates the facts and circumstances of each contract to estimate the variable consideration using the most likely amount method which utilizes management's expectation of the volume of services to be provided over the applicable period. Direct Hire revenue is recorded net of a fallout reserve. Direct Hire fallouts occur when a candidate does not remain employed with the client through the respective contingency period (typically 90 days or less). Management uses the expected value method to estimate the fallout reserve based on a combination of past experience and current trends. Variable consideration reduces revenue, but may be constrained to the extent that it is probable a significant reversal will not occur. These balances are recorded in Accounts payable and other accrued liabilities in the Consolidated Balance Sheets.

Under Topic 605, the Direct Hire fallout reserve was recorded as a Trade receivables allowance and under Topic 606, it is recorded within Accounts payable and other accrued liabilities in the Consolidated Balance Sheets. As of December 31, 2018 and 2017, the Direct Hire fallout reserve was \$0.6 million and \$0.5 million, respectively.

Payment Terms

Our payment terms and conditions vary by arrangement, although terms are typically less than 90 days. Generally, the timing between the satisfaction of the performance obligation and the payment is not significant and we do not currently have any significant financing components.

Unsatisfied Performance Obligations

We do not disclose the value of unsatisfied performance obligations for contracts if either the original expected length is one year or less or if revenue is recognized at the amount to which we have the right to invoice for services performed.

Contract Balances

We record accounts receivable when our right to consideration becomes unconditional. Other than our trade receivable balance, we do not have any material contract assets as of January 1, 2018 and December 31, 2018.

We record a contract liability when we receive consideration from a customer prior to transferring goods or services to the customer or if we have an unconditional right and services have been performed. We recognize the contract liability as revenue after we have transferred control of the goods or services to the customer. Contract liabilities are recorded within Accounts payable and other accrued liabilities if expected to be recognized in less than one year and Other long-term liabilities, if over one year, in the Consolidated Balance Sheets. We do not have any material contract liabilities as of January 1, 2018 and December 31, 2018.

Cost of Services

Direct costs are composed of all related costs of employment for consultants, including compensation, payroll taxes, certain fringe benefits and subcontractor costs. Direct costs exclude depreciation and amortization expense (except for the product business), which is presented on a separate line in the accompanying Consolidated Statements of Operations and Comprehensive Income.

Associate and field management compensation, payroll taxes and fringe benefits are included in selling, general and administrative expenses ("SG&A"), along with other customary costs such as administrative and corporate costs.

Commissions

Our associates make placements and earn commissions as a percentage of gross profit for Flex or Direct Hire revenues pursuant to a commission plan. The amount of associate commissions paid increases as volume increases. Commissions are accrued at an amount equal to the percent of total expected commissions payable to total revenue or gross profit for the commission-plan period, as applicable. We generally expense sales commissions and any other incremental costs of obtaining a contract as incurred because the amortization period is typically less than one year.

Stock-Based Compensation

Stock-based compensation is measured using the grant-date fair value of the award of equity instruments. The expense is recognized over the requisite service period. Effective January 1, 2017, the Firm changed its accounting policy regarding forfeitures and elected to recognize as incurred.

Income Taxes

Income taxes are recorded using the asset and liability approach for deferred tax assets and liabilities and the expected future tax consequences of differences between carrying amounts and the tax basis of assets and liabilities. A valuation allowance is recorded unless it is more likely than not that the deferred tax asset can be utilized to offset future taxes. Effective January 1, 2017, excess tax benefits or deficiencies of deductions attributable to employees' vesting of restricted stock are reflected in Income tax expense in the accompanying Consolidated Statements of Operations and Comprehensive Income.

Management evaluates tax positions taken or expected to be taken in our tax returns and records a liability for uncertain tax positions. We recognize tax benefits from uncertain tax positions when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes. The Company recognizes interest and penalties related to uncertain tax positions in income tax expense in the accompanying Consolidated Statements of Operations and Comprehensive Income.

Cash and Cash Equivalents

All highly liquid investments with original maturity dates of three months or less at the time of purchase are classified as cash equivalents. Cash and cash equivalents consist of cash on hand with banks, either in commercial accounts or overnight interest-bearing money market accounts and at times may exceed federally insured limits. Cash and cash equivalents are stated at cost, which approximates fair value because of the short-term nature of these instruments.

Trade Receivables and Related Reserves

Trade receivables are recorded net of allowance for doubtful accounts. The allowance for doubtful accounts is determined based on factors including recent write-off and delinquency trends, a specific analysis of significant receivable balances that are past due, the concentration of trade receivables among clients and higher-risk sectors, and the current state of the U.S. economy. Trade receivables are written off after all reasonable collection efforts have been exhausted. Trade accounts receivable reserves as a percentage of gross trade receivables was 1.0% at December 31, 2018 and 2017.

Fixed Assets

Fixed assets are carried at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. The cost of leasehold improvements is amortized using the straight-line method over the lesser of the estimated useful lives of the assets or the terms of the related leases. Upon sale or disposition of our fixed assets, the cost and accumulated depreciation are removed and any resulting gain or loss, net of proceeds, is reflected within SG&A in the Consolidated Statements of Operations and Comprehensive Income.

Leases

Leases for our field offices, which are located throughout the U.S., range from three to seven-year terms, although a limited number of leases contain short-term renewal provisions that range from month-to-month to one year.

For leases that contain escalations of the minimum rent, we recognize the related rent expense on a straight-line basis over the lease term. We record any difference between the straight-line rent amounts and amounts payable under the leases as a deferred rent liability in Accounts payable and other accrued liabilities or Other long-term liabilities, as appropriate, in the Consolidated Balance Sheets.

The Company records incentives provided by landlords for leasehold improvements in Accounts payable and other accrued liabilities or Other long-term liabilities, as appropriate, in the Consolidated Balance Sheets and records a corresponding reduction in rent expense on a straight-line basis over the lease term.

Goodwill and Other Intangible Assets

Goodwill

Management has determined that the reporting units for the goodwill analysis is consistent with our reporting segments. We evaluate goodwill for impairment either through a qualitative or quantitative approach annually, or more frequently if an event occurs or circumstances change that indicate the carrying value of a reporting unit may not be recoverable. If we perform a quantitative assessment that indicates the carrying amount of a reporting unit exceeds its fair market value, an impairment loss is recognized to reduce the carrying amount to its fair market value. Kforce determines the fair market value of each reporting unit based on a weighting of the present value of projected future cash flows (the “income approach”) and the use of comparative market approaches under both the guideline company method and guideline transaction method (collectively, the “market approach”). Fair market value using the income approach is based on estimated future cash flows on a discounted basis. The market approach compares each reporting unit to other comparable companies based on valuation multiples derived from operational and transactional data to arrive at a fair value. Factors requiring significant judgment include, among others, the assumptions related to discount rates, forecasted operating results, long-term growth rates, the determination of comparable companies, and market multiples. Changes in economic and operating conditions or changes in Kforce’s business strategies that occur after the annual impairment analysis may impact these assumptions and result in a future goodwill impairment charge, which could be material to our consolidated financial statements.

Other Intangible Assets

Identifiable intangible assets arising from certain of Kforce’s acquisitions include non-compete and employment agreements, contractual relationships, client contracts, technology, and GS’s Data Confidence trademark. Our trade names and trademarks, and derivatives thereof, including GS’s Data Confidence trademark, are important to our business and are registered with the U.S. Patent and Trademark Office.

For definite-lived intangible assets, amortization is computed using the straight-line method over the period of expected benefit, which ranges from one to fifteen years. The impairment evaluation for indefinite-lived intangible assets is conducted on an annual basis or more frequently if events or changes in circumstances indicate that an asset may be impaired.

Impairment of Long-Lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability of long-lived assets is measured by a comparison of the carrying amount of the asset group to the future undiscounted net cash flows expected to be generated by those assets. If an analysis indicates the carrying amount of these long-lived assets exceeds the fair value, an impairment loss is recognized to reduce the carrying amount to its fair market value, as determined based on the present value of projected future cash flows.

Capitalized Software

Kforce purchases, develops and implements software to enhance the performance of our technology infrastructure. Direct internal costs, such as payroll and payroll-related costs, and external costs incurred during the development stage are capitalized and classified as capitalized software. Capitalized software development costs and the associated accumulated amortization are classified as Other assets, net in the accompanying Consolidated Balance Sheets. Amortization is computed using the straight-line method over the estimated useful lives of the software, which range from one to seven years.

Workers’ Compensation

Kforce retains the economic burden for the first \$250 thousand per occurrence in workers’ compensation claims except: (1) in states that require participation in state-operated insurance funds and (2) for Kforce Government Solutions, Inc. which is fully insured for workers’ compensation claims. Workers’ compensation includes ongoing health care and indemnity coverage for claims and may be paid over numerous years following the date of injury. Workers’ compensation expense includes insurance premiums paid, claims administration fees charged by Kforce’s workers’ compensation administrator, premiums paid to state-operated insurance funds and an estimate for Kforce’s liability for IBNR claims and for the ongoing development of existing claims.

Management estimates its workers’ compensation liability based upon historical claims experience, actuarially determined loss development factors, and qualitative considerations such as claims management activities.

Health Insurance

Except for certain fully insured health insurance lines of coverage, Kforce retains the risk of loss for each health insurance plan participant up to \$350 thousand in claims annually. Additionally, for all claim amounts exceeding \$350 thousand, Kforce retains the risk of loss up to an aggregate annual loss of those claims of \$700 thousand. For its partially self-insured lines of coverage, health insurance costs are accrued using estimates to approximate the liability for reported claims and IBNR claims, which are primarily based upon an evaluation of historical claims experience, actuarially-determined completion factors and a qualitative review of our health insurance exposure including the extent of outstanding claims and expected changes in health insurance costs.

Defined Benefit Pension Plans

The unfunded status of its defined benefit pension plan is recorded as a liability in its Consolidated Balance Sheets. Because our plan is unfunded as of December 31, 2018, actuarial gains and losses may arise as a result of the actuarial experience of the plan, as well as changes in actuarial assumptions in measuring the associated obligation as of year-end, or an interim date if any re-measurement is necessary. The net after-tax impact of unrecognized actuarial gains and losses related to our defined benefit pension plan is recorded in Accumulated other comprehensive income (loss) in our consolidated financial statements.

Amortization of a net unrecognized gain or loss in accumulated other comprehensive income (loss) is included as a component of net periodic benefit cost if, as of the beginning of the year, that net gain or loss exceeds 10% of the projected benefit obligation. If amortization is required, the minimum amortization shall be that excess divided by the average remaining service period of active plan participants. The interest cost component of the net periodic benefit cost is included in Other expense, net in the Consolidated Statements of Operations and Comprehensive Income.

Earnings per Share

Basic earnings per share is computed as net income divided by the weighted average number of common shares outstanding ("WASO") during the period. WASO excludes unvested shares of restricted stock. Diluted earnings per share is computed by dividing net income by diluted WASO. Diluted WASO includes the dilutive effect of unvested shares of restricted stock using the treasury stock method, except where the effect of including potential common shares would be anti-dilutive.

For the years ended December 31, 2018, 2017 and 2016, there were 513 thousand, 364 thousand, and 175 thousand common stock equivalents, respectively, included in the diluted WASO. For the years ended December 31, 2018, 2017 and 2016, there were nil, 527 thousand and 32 thousand, respectively, of anti-dilutive common stock equivalents.

Treasury Stock

The Board may authorize share repurchases of our common stock. Shares repurchased under Board authorizations are held in treasury for general corporate purposes, including issuances under the 2009 Employee Stock Purchase Plan. Treasury shares are accounted for under the cost method and reported as a reduction of stockholders' equity in the accompanying consolidated financial statements.

Derivative Instrument

Our interest rate swap derivative instrument has been designated as a cash flow hedge and is recorded at fair value on the Consolidated Balance Sheets. The effective portion of the gain or loss on the derivative instrument is recorded as a component of Accumulated other comprehensive income (loss), net of tax, and reclassified into earnings when the hedged item affects earnings and into the line item of the hedged item. Any ineffective portion of the gain or loss is recognized immediately into Other expense, net on the Consolidated Statements of Operations and Comprehensive Income. Cash flows from the derivative instrument are classified in the Consolidated Statements of Cash Flows in the same category as the hedged item.

Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy uses a framework which requires categorizing assets and liabilities into one of three levels based on the inputs used in valuing the asset or liability.

- Level 1 inputs are unadjusted, quoted market prices in active markets for identical assets or liabilities.
- Level 2 inputs are observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets or quoted prices for identical assets or liabilities in inactive markets.
- Level 3 inputs include unobservable inputs that are supported by little, infrequent or no market activity and reflect management's own assumptions about inputs used in pricing the asset or liability.

Level 1 provides the most reliable measure of fair value, while Level 3 generally requires significant management judgment. Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

Fair value measurements include, but are not limited to: the impairment testing of goodwill, other intangible assets and other long-lived assets; stock-based compensation; the interest rate swap and contingent consideration liability. The carrying values of cash and cash equivalents, trade receivables, other current assets and accounts payable and other accrued liabilities approximate fair value because of the short-term nature of these instruments. Using available market information and appropriate valuation methodologies, Management has determined the estimated fair value measurements; however, considerable judgment is required in interpreting data to develop the estimates of fair value.

New Accounting Standards

Recently Adopted Accounting Standards

In May 2014, the FASB issued authoritative guidance regarding revenue from contracts with customers, which specifies that revenue should be recognized when control of the promised goods or services is transferred to our customers at an amount that reflects the consideration to which we expect to be entitled to in exchange for those goods or services. Topic 606 is effective for annual and interim reporting periods beginning after December 15, 2017. We adopted Topic 606 using the modified retrospective transition method for all contracts that were not completed as of January 1, 2018. The cumulative impact of adopting Topic 606 was recorded as a reduction to the opening balance of retained earnings of \$0.2 million, net of tax, as of January 1, 2018 with the offset recorded as a contract liability. The adjustment is related to a change in the revenue recognition pattern for the performance obligations under certain GS contracts including standard warranty revenues related to our product business and a contract that provides our customer with a material right to a future discount. As of and for the year ended December 31, 2018, the consolidated financial statements were not materially impacted as a result of the application of Topic 606 compared to Topic 605. The comparative information continues to be reported under the accounting standards in effect for the period presented.

Accounting Standards Not Yet Adopted

In August 2018, the FASB issued authoritative guidance regarding customer's accounting for implementation costs incurred in a cloud computing arrangement that is a service contract. These amendments align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software, and defer these costs over the noncancelable term of the cloud computing arrangements plus any option renewal periods that are reasonably certain to be exercised. This amendment also requires entities to present cash flows, capitalized costs and amortization expense in the same financial statement line items as the service costs incurred for such hosting arrangements. The guidance is effective for fiscal periods beginning after December 15, 2019 with retrospective application or prospective to all implementation costs incurred after the date of adoption. We plan to early adopt this standard in the first quarter of 2019 and expect certain presentation changes, which are not expected to be material to the consolidated financial statements.

In August 2018, the FASB issued authoritative guidance regarding changes to the disclosure requirement for defined benefit plans including additions and deletions to certain disclosure requirements for employers that sponsor defined benefit pension or other post-retirement plans. The guidance is effective for fiscal periods beginning after December 15, 2020. The adoption of this guidance will modify our disclosures and is not expected to have a material effect on our consolidated financial statements.

In August 2018, the FASB issued authoritative guidance regarding changes to the disclosure requirements for fair value measurement. The amendments on changes in unrealized gains and losses, the weighted average and range of significant unobservable inputs used to develop Level 3 fair value measurements, and the narrative description of measurement uncertainty should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. The guidance is effective for fiscal periods beginning after December 15, 2019. The adoption of this guidance will modify our disclosures and is not expected to have a material effect on our consolidated financial statements.

In February 2018, the FASB issued authoritative guidance regarding the reclassification of certain stranded tax effects from accumulated other comprehensive income to retained earnings as a result of the change in tax rates related to the Tax Cuts and Jobs Act. The guidance is effective for fiscal periods beginning after December 15, 2018 and should be applied either in the period of adoption or retrospectively. Kforce will adopt this standard using the period of adoption method with an adjustment of approximately \$168 thousand to retained earnings on January 1, 2019.

In August 2017, the FASB issued authoritative guidance targeting improvements to accounting for hedging activities by simplifying the rules around hedge accounting and improving

the disclosure requirements. The guidance is effective for annual periods beginning after December 15, 2018. The hedge accounting guidance should be implemented using a modified retrospective approach for any hedges that exist on the date of adoption, while the presentation and disclosure requirements must be applied prospectively. Kforce will adopt this standard in the first quarter of 2019; it will modify our disclosures but is not expected to have a material effect on our consolidated financial statements.

In June 2016, the FASB issued authoritative guidance on accounting for credit losses on financial instruments, including trade receivables. The guidance requires the application of a current expected credit loss model, which measures credit losses based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts. The guidance is effective for annual periods beginning after December 15, 2019. The guidance requires companies to apply the requirements using a modified retrospective approach. We are currently evaluating the potential impact on our consolidated financial statements, especially with respect to our disclosures.

In February 2016, the FASB issued authoritative guidance regarding the accounting for leases, and has since issued subsequent updates to the initial guidance. The amended guidance requires the recognition of assets and liabilities for operating leases with terms longer than 12 months. The guidance is effective for annual periods beginning after December 15, 2018. We will adopt this standard in the first quarter of 2019 utilizing the optional transition method in the period of adoption without retrospective application to comparative periods. We anticipate recording approximately \$17.6 million and \$21.0 million in right-of-use assets and lease liabilities, respectively, on our consolidated balance sheets on January 1, 2019. We will take advantage of the package of practical expedients permitted in the new standard as well as the practical expedients for short term leases and not separating lease and nonlease components.

2. REPORTABLE SEGMENTS

Kforce's reportable segments are as follows: (1) Tech; (2) FA; and (3) GS. Historically, and for the year ended December 31, 2018, Kforce has generated only sales and gross profit information on a segment basis. We do not report total assets or income from continuing operations separately by segment as our operations are largely combined.

For the years ended December 31, 2017 and 2016, our Tech segment included the results of operations for Global, a wholly-owned subsidiary located in Manila, Philippines. During the year ended December 31, 2017, Kforce completed the sale of Global's assets. This sale did not meet the definition of discontinued operations. Kforce recorded a \$3.3 million gain on sale of Global's assets, which was recorded in Selling, general and administrative expenses within the accompanying Consolidated Statements of Operations and Comprehensive Income for the year ended December 31, 2017.

The following table provides information concerning the operations of our segments for the years ended December 31 (in thousands):

	Tech	FA	GS	Total
2018				
Revenue	\$990,089	\$313,848	\$114,416	\$1,418,353
Gross profit	\$277,388	\$109,099	\$ 32,121	\$ 418,608
Operating and other expenses				341,455
Income before income taxes				\$ 77,153
2017				
Revenue	\$907,511	\$346,135	\$104,294	\$1,357,940
Gross profit	\$257,118	\$118,479	\$ 32,459	\$ 408,056
Operating and other expenses				343,962
Income before income taxes				\$ 64,094
2016				
Revenue	\$883,477	\$337,601	\$ 98,628	\$1,319,706
Gross profit	\$255,842	\$120,551	\$ 32,106	\$ 408,499
Operating and other expenses				352,544
Income before income taxes				\$ 55,955

3. REVENUE

Disaggregation of Revenue

The following table provides information about disaggregated revenue by segment and revenue type for the years ended December 31, 2018, 2017 and 2016 (in thousands):

	Tech	FA	GS	Total
2018				
Revenue by type:				
Flex revenue	\$971,310	\$286,939	\$ 98,214	\$1,356,463
Direct Hire revenue	18,779	26,909	—	45,688
Product revenue	—	—	16,202	16,202
Total Revenue	\$ 990,089	\$ 313,848	\$ 114,416	\$1,418,353
2017				
Revenue by type:				
Flex revenue	\$887,675	\$318,294	\$ 92,241	\$1,298,210
Direct Hire revenue	19,836	27,841	—	47,677
Product revenue	—	—	12,053	12,053
Total Revenue	\$907,511	\$346,135	\$104,294	\$1,357,940
2016				
Revenue by type:				
Flex revenue	\$863,434	\$307,245	\$ 82,427	\$1,253,106
Direct Hire revenue	20,043	30,356	—	50,399
Product revenue	—	—	16,201	16,201
Total Revenue	\$883,477	\$337,601	\$ 98,628	\$1,319,706

GS Flex revenue includes 41.9% and 34.3% of revenue recognized from fixed-price contracts for the years ended December 31, 2018 and 2017, respectively.

4. FIXED ASSETS

The following table presents major classifications of fixed assets and related useful lives (in thousands):

December 31,	Useful Life	2018	2017
Land		\$ 5,892	\$ 5,892
Building and improvements	3-40 years	25,755	25,733
Furniture and equipment	1-20 years	17,467	17,285
Computer equipment	1-5 years	6,289	9,231
Leasehold improvements	3-7 years	12,497	13,424
		67,900	71,565
Less accumulated depreciation		(32,082)	(31,885)
Total Fixed assets, net		\$ 35,818	\$ 39,680

Computer equipment as of December 31, 2018 and 2017 includes equipment acquired under capital leases of \$2.3 million and \$3.5 million, respectively, and related accumulated depreciation of \$1.4 million and \$2.1 million, respectively. Depreciation expense, which includes capital leases, during the years ended December 31, 2018, 2017 and 2016 was \$6.3 million, \$6.9 million, and \$6.7 million, respectively.

5. INCOME TAXES

The Tax Cuts and Jobs Act was enacted in December 2017, which reduced the U.S. federal corporate tax rate from 35.0% to 21.0% effective January 1, 2018. As a result, we revalued our net deferred income tax assets and recorded \$5.4 million of additional Income tax expense in the Consolidated Statement of Operations and Comprehensive Income for the year ended December 31, 2017.

The provision for income taxes from continuing operations consists of the following (in thousands):

Years Ended December 31,	2018	2017	2016
Current tax expense:			
Federal	\$ 12,730	\$ 15,060	\$ 16,677
State	5,454	3,244	3,829
Deferred tax expense (1)	989	12,505	2,676
Total Income tax expense	\$ 19,173	\$ 30,809	\$ 23,182

(1) Includes the impact of TCJA for the year ended December 31, 2017.

The provision for income taxes from continuing operations shown above varied from the statutory federal income tax rate for those periods as follows:

Years Ended December 31,	2018	2017	2016
Federal income tax rate	21.0%	35.0%	35.0%
State income taxes, net of Federal tax effect	5.7	3.8	6.8
Non-deductible compensation and meals and entertainment	1.0	0.7	1.2
Tax credits	(2.2)	(2.2)	(2.1)
Valuation allowance on foreign tax credit	—	2.5	—
Enactment of TCJA	—	9.1	—
Other	(0.6)	(0.8)	0.5
Effective tax rate	24.9%	48.1%	41.4%

The 2018 effective tax rate was favorably impacted by the TCJA. The 2017 effective tax rate was unfavorably impacted due to the revaluation of our net deferred tax assets as a result of TCJA. The 2016 effective tax rate was unfavorably impacted by certain one-time non-cash adjustments.

Deferred tax assets and liabilities are composed of the following (in thousands):

December 31,	2018	2017
Deferred tax assets:		
Accounts receivable reserves	\$ 738	\$ 611
Accrued liabilities	1,825	1,953
Deferred compensation obligation	5,545	5,423
Stock-based compensation	723	598
Pension and post-retirement benefit plans	3,471	3,767
Goodwill and intangible assets	—	526
Foreign tax credit	1,630	1,632
Other	344	289
Deferred tax assets	14,276	14,799
Deferred tax liabilities:		
Prepaid expenses	(190)	(251)
Fixed assets	(1,277)	(1,482)
Goodwill and intangible assets	(1,057)	—
Other	(254)	(17)
Deferred tax liabilities	(2,778)	(1,750)
Valuation allowance	(1,747)	(1,733)
Deferred tax assets, net	\$ 9,751	\$ 11,316

At December 31, 2018, Kforce had approximately \$3.4 million of state tax net operating losses ("NOLs") which will be carried forward to be offset against future state taxable income. The state tax NOLs expire in varying amounts through 2037.

In evaluating the realizability of Kforce's deferred tax assets, management assesses whether it is more likely than not that some portion, or all, of the deferred tax assets, will be realized. Management considers, among other things, the ability to generate future taxable income (including reversals of deferred tax liabilities) during the periods in which the related temporary differences will become deductible. The valuation allowance includes a foreign tax credit, which we expect may not be realizable as a result of reduction in our foreign income.

Kforce is periodically subject to IRS audits, as well as state and other local income tax audits for various tax years. During 2018, the IRS commenced an audit for the tax year ended December 31, 2016. No adjustments have been proposed to date. During 2018, the Company also received a notice of examination by the North Carolina Department of Revenue for the years ended December 31, 2016, 2015 and 2014. No adjustments have been proposed to date. The Company has not received a notice of examination by any other jurisdictions for any other tax year open under statute. Although Kforce has not experienced any material liabilities in the past due to income tax audits, Kforce can make no assurances concerning any future income tax audits.

Uncertain Income Tax Positions

The following table presents a reconciliation of the beginning and ending balance of unrecognized tax benefits for the years ended (in thousands):

December 31,	2018	2017	2016
Unrecognized tax benefits, beginning	\$1,127	\$1,115	\$ 788
Additions for prior year tax positions	41	50	454
Additions for current year tax positions	—	29	—
Lapse of statute of limitations	(248)	(67)	(102)
Reductions for tax positions of prior years	(14)	—	(25)
Unrecognized tax benefits, ending	\$ 906	\$1,127	\$1,115

As of December 31, 2018, the amount of unrecognized tax benefit that would impact the effective tax rate, if recognized, is \$0.7 million. Kforce does not expect any significant changes to its uncertain tax positions in the next 12 months.

Kforce and its subsidiaries file income tax returns in the U.S. federal jurisdiction and various states. Global files income tax returns in the Philippines. With a few exceptions, Kforce is no longer subject to federal, state, local, or non-U.S. income tax examinations by tax authorities for years before 2016.

6. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill

The following table presents the gross amount and accumulated impairment losses for each of our reporting units as of December 31, 2018, 2017 and 2016 (in thousands):

	Technology	Finance and Accounting	Government Solutions	Total
Goodwill, gross amount	\$ 156,391	\$ 19,766	\$104,596	\$ 280,753
Accumulated impairment losses	(139,357)	(11,760)	(83,668)	(234,785)
Goodwill, carrying value	\$ 17,034	\$ 8,006	\$ 20,928	\$ 45,968

There was no impairment expense related to goodwill for each of the years ended December 31, 2018, 2017 and 2016.

Throughout 2018, we considered the qualitative and quantitative factors associated with each of our reporting units and determined that there was no indication that the carrying values of any of our reporting units were likely impaired.

Management performed its annual impairment assessment of the carrying value of goodwill as of December 31, 2018. For each of our reporting units, we assessed qualitative factors to determine whether the existence of events or circumstances indicated that it was more likely than not that the fair value of the reporting units was less than its carrying amount. We concluded that it was more likely than not that the fair value of these reporting units was more than their carrying amounts at December 31, 2018.

Kforce performed a quantitative analysis for each reporting unit and compared the carrying value for each to the respective estimated fair values as of December 31, 2017. Discounted cash flows, which serve as the primary basis for the income approach, were based on a discrete financial forecast developed by management. Cash flows beyond the discrete forecast period of five years were estimated using a terminal value calculation, which incorporated historical and forecasted financial trends and also considered long-term earnings growth rates for publicly-traded peer companies, as well as the

risk-free rate of return. The market approach consists of: (1) the guideline company method and (2) the guideline transaction method. The guideline company method applies pricing multiples derived from publicly-traded guideline companies that are comparable to the reporting unit to determine its value. The guideline transaction method applies pricing multiples derived from recently completed acquisitions that we believe are reasonably comparable to the reporting unit to determine fair value. Kforce concluded there were no indications of impairment for its reporting units for the year ended December 31, 2017.

As of December 31, 2016, for our Technology and Finance and Accounting reporting units, we assessed qualitative factors to determine whether the existence of events or circumstances indicated that it was more likely than not that the fair value of the reporting units was less than its carrying amount. Based on the qualitative assessments, management determined that it was not more likely than not that the fair values of the reporting units were less than the carrying values. As of December 31, 2016, for our Government Solutions reporting unit, we performed a quantitative analysis and compared the carrying value to the estimated fair value, using a similar approach as described above noting no indications of impairment.

Other Intangible Assets

Our other intangible assets balance includes an indefinite-lived trademark of \$2.2 million as of December 31, 2018 and 2017 and is recorded in Intangible assets, net in the accompanying Consolidated Balance Sheets. As of December 31, 2018 and 2017, our definite-lived intangible assets balance of \$0.7 million and \$1.1 million, respectively, included accumulated amortization of \$27.9 million and \$27.5 million, respectively. There was no impairment expense related to our other intangible assets during the years ended December 31, 2018, 2017 and 2016.

7. ACCOUNTS PAYABLE AND OTHER ACCRUED LIABILITIES

Accounts payable and other accrued liabilities consisted of the following (in thousands):

December 31,	2018	2017
Accounts payable	\$22,900	\$21,591
Accrued liabilities	15,706	13,282
Total Accounts payable and other accrued liabilities	\$38,606	\$34,873

Our accounts payable balance includes vendor and independent contractor payables. Our accrued liabilities balance includes the current portion of our deferred compensation plans liability, contract liabilities from contracts with customers (such as customer rebates), and other accrued liabilities.

8. ACCRUED PAYROLL COSTS

Accrued payroll costs consisted of the following (in thousands):

December 31,	2018	2017
Payroll and benefits	\$39,690	\$37,788
Payroll taxes	1,842	5,270
Health insurance liabilities	2,714	2,596
Workers' compensation liabilities	1,016	1,232
Total Accrued payroll costs	\$45,262	\$46,886

9. EMPLOYEE BENEFIT PLANS

401(k) Savings Plans

The Firm maintains various qualified defined contribution 401(k) retirement savings plans for eligible employees. Assets of these plans are held in trust for the sole benefit of employees and/or their beneficiaries. Employer matching contributions are discretionary and are funded annually as approved by the Board.

Kforce accrued matching 401(k) contributions of \$1.8 million and \$1.6 million as of December 31, 2018 and 2017, respectively. The plans held a combined 146 thousand and 167 thousand shares of Kforce's common stock as of December 31, 2018 and 2017, respectively.

Employee Stock Purchase Plan

Kforce's employee stock purchase plan allows all eligible employees to enroll each quarter to purchase Kforce's common stock at a 5% discount from its market price on the last day of the quarter. Kforce issued 19 thousand, 25 thousand, and 34 thousand shares of common stock at an average purchase price of \$28.93, \$20.65, and \$19.37 per share during the years ended December 31, 2018, 2017 and 2016, respectively. All shares purchased under the employee stock purchase plan were settled using Kforce's treasury stock.

Deferred Compensation Plans

The Firm maintains various non-qualified deferred compensation plans, pursuant to which eligible management and highly compensated key employees, as defined by IRS regulations, may elect to defer all or part of their compensation to later years. These amounts are classified in Accounts payable and other accrued liabilities if payable within the next year or in Other long-term liabilities if payable after the next year, upon retirement or termination of employment in the accompanying Consolidated Balance Sheets. At December 31, 2018 and 2017, amounts related to the deferred compensation plans included in Accounts payable and other accrued liabilities were \$1.8 million and \$2.9 million, respectively, and \$28.9 million was included in Other long-term liabilities at December 31, 2018 and 2017 in the Consolidated Balance Sheets. For the years ended December 31, 2018, 2017 and 2016, we recognized compensation expense for the plans of \$876 thousand, \$722 thousand and \$881 thousand, respectively.

Kforce maintains a Rabbi Trust and holds life insurance policies on certain individuals to assist in the funding of the deferred compensation liability. If necessary, employee distributions are funded through proceeds from the sale of assets held within the Rabbi Trust. The balance of the assets within the Rabbi Trust, including the cash surrender value of the Company-owned life insurance policies, was \$29.1 million and \$31.4 million as of December 31, 2018 and 2017, respectively, and is recorded in Other assets, net in the accompanying Consolidated Balance Sheets. As of December 31, 2018, the life insurance policies had a cumulative face value of \$213.1 million. Kforce had no realized gains or losses attributable to investments in trading securities for the years ended December 31, 2018, 2017 and 2016.

Supplemental Executive Retirement Plan

Kforce maintains a SERP for the benefit of certain executive officers. The primary goals of the SERP are to create an additional wealth accumulation opportunity, restore lost qualified pension benefits due to government limitations and retain our covered executive officers. The SERP is a non-qualified benefit plan and does not include elective deferrals of covered executive officers' compensation.

Normal retirement age under the SERP is defined as age 65; however, certain conditions allow for early retirement as early as age 55 or upon a change in control. Vesting under the plan is defined as 100% upon a participant's attainment of age 55 and 10 years of service and 0% prior to a participant's attainment of age 55 and 10 years of service. Full vesting also occurs if a participant

with five years or more of service is involuntarily terminated by Kforce without cause or upon death, disability or a change in control. The SERP will be funded entirely by Kforce, and benefits are taxable to the covered executive officer upon receipt and will be deductible by Kforce when paid. Benefits payable under the SERP upon the occurrence of a qualifying distribution event, as defined, are targeted at 45% of the covered executive officers' average salary and bonus, as defined, from the three years in which the covered executive officer earned the highest salary and bonus during the last 10 years of employment, which is subject to adjustment for retirement prior to the normal retirement age and the participant's vesting percentage. The benefits under the SERP are reduced for a participant that has not reached age 62 with 10 years of service or age 55 with 25 years of service with a percentage reduction up to the normal retirement age.

Benefits under the SERP are based on the lump sum present value but may be paid over the life of the covered executive officer or 10-year annuity, as elected by the covered executive officer upon commencement of participation in the SERP. None of the benefits earned pursuant to the SERP are attributable to services provided prior to the effective date of the plan. For purposes of the measurement of the benefit obligation as of December 31, 2018, Kforce has assumed that all participants will elect to take the lump sum present value option based on historical trends.

Actuarial Assumptions

Due to the SERP being unfunded as of December 31, 2018 and 2017, it is not necessary for Kforce to determine the expected long-term rate of return on plan assets. The following table presents the weighted average actuarial assumptions used to determine the actuarial present value of projected benefit obligations at:

December 31,	2018	2017
Discount rate	4.00%	3.25%
Rate of future compensation increase	2.90%	2.90%

The following table presents the weighted average actuarial assumptions used to determine net periodic benefit cost for the years ended:

December 31,	2018	2017	2016
Discount rate	3.25%	4.00%	4.00%
Rate of future compensation increase	2.90%	3.60%	4.00%

The discount rate was determined using the Moody's Aa long-term corporate bond yield as of the measurement date with a maturity commensurate with the expected payout of the SERP obligation. This rate is also compared against the Citigroup Pension Discount Curve and Liability Index to ensure the rate used is reasonable and may be adjusted accordingly. This index is widely used by companies throughout the U.S. and is considered to be one of the preferred standards for establishing a discount rate.

The assumed rate of future compensation increases is based on a combination of factors, including the historical compensation increases for its covered executive officers and future target compensation levels for its covered executive officers taking into account the covered executive officers' assumed retirement date.

The periodic benefit cost is based on actuarial assumptions that are reviewed on an annual basis; however, management monitors these

assumptions on a periodic basis to ensure that they accurately reflect current expectations of the cost of providing retirement benefits.

Net Periodic Benefit Cost

The following table presents the components of net periodic benefit cost for the years ended (in thousands):

December 31,	2018	2017	2016
Service cost	\$1,353	\$319	\$1,310
Interest cost	468	537	453
Net periodic benefit cost	\$1,821	\$856	\$1,763

Changes in Benefit Obligation

The following table presents the changes in the projected benefit obligation for the years ended (in thousands):

December 31,	2018	2017
Projected benefit obligation, beginning	\$14,409	\$13,436
Service cost	1,353	319
Interest cost	468	537
Actuarial experience and changes in actuarial assumptions	(1,195)	117
Projected benefit obligation, ending	\$15,035	\$14,409

There were no payments made under the SERP during the years ended December 31, 2018 and 2017, respectively. The projected benefit obligation is recorded in Other long-term liabilities in the accompanying Consolidated Balance Sheets. The accumulated benefit obligation is the actuarial present value of all benefits attributed to past service, excluding future salary increases. The accumulated benefit obligation as of December 31, 2018 and 2017 was \$15.0 million and \$14.3 million, respectively.

Contributions

There is no requirement for Kforce to fund the SERP and, as a result, no contributions have been made to the SERP through the year ended December 31, 2018. Kforce does not currently anticipate funding the SERP during the year ending December 31, 2019.

Estimated Future Benefit Payments

Undiscounted benefit payments by the SERP, which reflect the anticipated future service of participants, expected to be paid are as follows during the years ended December 31 (in thousands):

	Projected Annual Benefit Payments
2019	\$ —
2020	—
2021	13,351
2022	—
2023	—
2024-2027	—
Thereafter	4,409

10. CREDIT FACILITY

On May 25, 2017, the Firm entered into a credit agreement with Wells Fargo Bank, National Association, as administrative agent, Wells Fargo Securities, LLC, as lead arranger and bookrunner, Bank of America, N.A., as syndication agent, Regions Bank and BMO Harris Bank, N.A., as co-documentation agents, and the lenders referred to therein (the "Credit Facility"). Under the Credit Facility, the Firm has a maximum borrowing capacity of \$300.0 million, which may, subject to certain conditions and the participation of the lenders, be increased up to an aggregate additional amount of \$150.0 million (the "Commitment"), which is available to the Firm in the form of revolving credit loans, swingline loans, and letters of credit. Letters of credit and swingline loans under the Credit Facility are subject to sublimits of \$10.0 million. The maturity date of the Credit Facility is May 25, 2022. Borrowings under the Credit Facility are secured by substantially all of the tangible and intangible assets of the Firm, excluding the Firm's corporate headquarters and certain other designated executed collateral.

Revolving credit loans under the Credit Facility bears interest at a rate equal to: (a) the Base Rate (as described below) plus the Applicable Margin (as described below); or (b) the LIBOR Rate plus the Applicable Margin. Swingline loans under the Credit Facility bears interest at a rate equal to the Base Rate plus the Applicable Margin. The Base Rate is the highest of: (i) the Wells Fargo Bank, National Association prime rate; (ii) the federal funds rate plus 0.50%; or (iii) one-month LIBOR plus 1.00%, and the LIBOR Rate is reserve-adjusted LIBOR for the applicable interest period, but not less than zero. The Applicable Margin is based on the Firm's total leverage ratio. The Applicable Margin for Base Rate loans ranges from 0.25% to 0.75% and the Applicable Margin for LIBOR Rate loans ranges from 1.25% to 1.75%. The Firm will pay a quarterly non-refundable commitment fee equal to the Applicable Margin on the average daily unused portion of the Commitment (swingline loans do not constitute usage for this purpose). The Applicable Margin for the commitment fee is based on the Firm's total leverage ratio and ranges between 0.20% and 0.35%.

The Firm is subject to certain affirmative and negative covenants including (but not limited to), the maintenance of a fixed charge coverage ratio of no less than 1.25 to 1.00 and the maintenance of a total leverage ratio of no greater than 3.25 to 1.00. The numerator in the fixed charge coverage ratio is defined pursuant to the Credit Facility as earnings before interest expense, income taxes, depreciation and amortization, stock-based compensation expense and other permitted items pursuant to our Credit Facility (disclosed as "Consolidated EBITDA"), less cash paid for capital expenditures, income taxes and dividends. The denominator is defined as Kforce's fixed charges such as interest expense and principal payments paid or payable on outstanding debt other than borrowings under the Credit Facility. The total leverage ratio is defined pursuant to the Credit Facility as total indebtedness divided by Consolidated EBITDA. Our ability to make distributions or repurchases of equity securities could be limited if an event of default has occurred. Furthermore, our ability to repurchase equity securities could be limited if: (a) the total leverage ratio is greater than 2.75 to 1.00; and (b) the Firm's availability, inclusive of unrestricted cash, is less than \$25.0 million. At December 31, 2018, Kforce was not limited in making distributions and executing repurchases of our equity securities.

As of December 31, 2018 and 2017, \$71.8 million and \$116.5 million was outstanding, respectively. Kforce had \$3.2 million of outstanding letters of credit at December 31, 2018 and 2017 which, pursuant to the Credit Facility, reduces the availability.

11. DERIVATIVE INSTRUMENT AND HEDGING ACTIVITY

Kforce is exposed to interest rate risk as a result of our corporate borrowing activities. The Firm uses an interest rate swap derivative as a risk management tool to mitigate the potential impact of rising interest rates on variable rate debt.

On April 21, 2017, Kforce entered into a forward-starting interest rate swap agreement with Wells Fargo Bank, N.A. The Swap rate is 1.81%, which is added to our interest rate margin to determine the fixed rate that the Firm will pay to the counterparty during the term of the Swap based on the notional amount of the Swap. The Swap was effective May 31, 2017 and matures April 29, 2022. The notional amount of the Swap is \$65.0 million for the first three years and decreases to \$25.0 million for years four and five.

The Swap has been designated as a cash flow hedge and was effective as of December 31, 2018. The change in the fair value of the Swap was recorded as a component of Accumulated other comprehensive income (loss), net of tax, in the Consolidated Statements of Operations and Comprehensive Income. As of December 31, 2018 and 2017, the fair value of the Swap asset was \$0.9 million and \$0.5 million, respectively, and is recorded in Other assets, net within the accompanying Consolidated Balance Sheets.

12. FAIR VALUE MEASUREMENTS

Kforce's interest rate swap is measured at fair value using readily observable inputs, such as the LIBOR interest rate, which are considered to be Level 2 inputs. Refer to Note 11—"Derivative Instrument and Hedging Activity" in the Notes to the Consolidated Financial Statements, included in this Annual Report for a complete discussion of the Firm's derivative instrument.

Our contingent consideration liability relates to a non-significant business acquisition within our GS reporting segment, which is measured on a recurring basis and recorded at fair value using the discounted cash flow method. The inputs used to calculate the fair value of the contingent consideration liability are considered to be Level 3 inputs due to the lack of relevant market activity and significant management judgment. An increase in future cash flows may result in a higher estimated fair value while a decrease in future cash flows may result in a lower estimated fair value of the contingent consideration liability. Remeasurements to fair value are recorded in Other expense, net within the Consolidated Statements of Operations and Comprehensive Income. For the years ended December 31, 2018 and 2017, approximately \$4 thousand and \$565 thousand of income, respectively, was recognized due to the remeasurement of our contingent consideration liability. The contingent consideration liability is recorded in Other long-term liabilities within the Consolidated Balance Sheets and the estimated fair value as of December 31, 2018 and 2017 was \$187 thousand and \$191 thousand, respectively.

Certain assets, in specific circumstances, are measured at fair value on a non-recurring basis utilizing Level 3 inputs such as goodwill, other intangible assets and other long-lived assets. For these assets, measurement at fair value in periods subsequent to their initial recognition would be applicable if one or more of these assets were determined to be impaired.

The following table sets forth by level, within the fair value hierarchy, estimated fair values on a recurring basis at December 31, 2018 and 2017 were as follows (in thousands):

Assets/(Liabilities) Measured at Fair Value:	Asset/ (Liability)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
At December 31, 2018				
Recurring basis:				
Interest rate swap derivative instrument	\$ 900	\$—	\$900	\$ —
Contingent consideration liability	\$(187)	\$—	\$ —	\$(187)
<i>At December 31, 2017</i>				
Recurring basis:				
Interest rate swap derivative instrument	\$ 479	\$—	\$479	\$ —
Contingent consideration liability	\$(191)	\$—	\$ —	\$(191)

There were no transfers into or out of Level 1, 2 or 3 assets or liabilities during the years ended December 31, 2018 and 2017.

13. STOCK INCENTIVE PLANS

On April 18, 2017, the Kforce shareholders approved the 2017 Stock Incentive Plan ("2017 Plan"). The 2017 Plan allows for the issuance of stock options, stock appreciation rights, restricted stock (including restricted stock awards ("RSAs") and restricted stock units ("RSUs")) and other stock-based awards. The aggregate number of shares of common stock that are subject to awards under the 2017 Plan is approximately 3.0 million shares. The 2017 Plan terminates on April 18, 2027. Prior to the effective date of the 2017 Plan, the Company granted stock awards to eligible participants under our 2016 Stock Incentive Plan and 2013 Stock Incentive Plan (collectively the "Prior Plans"). No additional awards may be granted pursuant to the Prior Plans; however, awards outstanding as of the effective date will continue to vest in accordance with the terms of the Prior Plans.

In March 2016, the FASB issued authoritative guidance regarding the accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liability, and classification in the statement of cash flows. This guidance was effective for us on January 1, 2017. An entity is allowed to make a policy election as to whether it will include an estimate for awards expected to be forfeited or whether it will account for forfeitures as incurred. The Firm elected to change its policy on accounting for forfeitures and to recognize as incurred. This policy election was applied using a modified retrospective approach with a cumulative-effect adjustment to retained earnings as of the effective date. The impact to the beginning balance of retained earnings was \$0.5 million, which is net of taxes of \$0.3 million, on January 1, 2017.

During the years ended December 31, 2018, 2017 and 2016, stock-based compensation expense was \$8.8 million, \$7.6 million, and \$6.7 million, respectively. The related tax benefit for the years ended December 31, 2018, 2017 and 2016 was \$2.2 million, \$3.0 million, and \$2.8 million, respectively.

Restricted Stock

Restricted stock (including RSAs and RSUs) are granted to executives and management either: for awards related to Kforce's annual long-term incentive ("LTI") compensation program, or as part of a compensation package in order to retain directors, executives and management. The LTI award amounts are generally based on total shareholder return performance goals. The LTI restricted stock granted during the year ended December 31, 2018 will vest ratably over a period between three to four years. Other restricted stock granted during the year ended December 31, 2018 will vest ratably over a period of between one to ten years.

RSAs contain the same voting rights as other common stock as well as the right to forfeitable dividends in the form of additional RSAs at the same rate as the cash dividend on common stock and containing the same vesting provisions as the underlying award. RSUs contain no voting rights, but have the right to forfeitable dividend equivalents in the form of additional RSUs at the same rate as the cash dividend on common stock and containing the same vesting provisions as the underlying award. The distribution of shares of common stock for each RSU, pursuant to the terms of the Kforce Inc. Director's Restricted Stock Unit Deferral Plan, can be deferred to a date later than the vesting date if an appropriate election was made. In the event of such deferral, vested RSUs have the right to dividend equivalents.

The following table presents the restricted stock activity for the years ended December 31, 2018, 2017 and 2016 (in thousands, except per share amounts):

	Number of Restricted Stock	Weighted Average Grant Date Fair Value	Total Intrinsic Value of Restricted Stock Vested
Outstanding at December 31, 2015	1,293	\$20.89	
Granted (1)	1,048	\$22.46	
Forfeited/Canceled	(353)	\$21.04	
Vested	(280)	\$20.67	\$ 6,434
Outstanding at December 31, 2016	1,708	\$21.86	
Granted	427	\$24.03	
Forfeited/Canceled	(206)	\$21.70	
Vested (2)	(574)	\$21.60	\$13,668
Outstanding at December 31, 2017	1,355	\$22.67	
Granted	447	\$29.72	
Forfeited/Canceled	(90)	\$22.81	
Vested	(392)	\$23.03	\$11,935
Outstanding at December 31, 2018	1,320	\$18.19	

(1) The increase in shares granted during the year ended December 31, 2016 was due to a change in the grant date practice for our annual LTI awards. Kforce has historically granted these annual awards on the first business day of the year following the end of the performance period; however, for the performance period ending December 31, 2016 and thereafter, the grant date was shifted to the last day of the performance period. This administrative change resulted in two annual grants being made during the year ended December 31, 2016 (a grant on January 4, 2016 for the performance period ending December 31, 2015 and a grant on December 31, 2016 for the performance period ending December 31, 2016).

(2) The increase in shares vested during the year ended December 31, 2017 was due to a shift in the vesting date of our outstanding annual LTI awards from January 2, 2018 and January 4, 2018 to December 31, 2017 as a tax planning strategy.

The fair market value of restricted stock is determined based on the closing stock price of Kforce's common stock at the date of grant, and is amortized on a straight-line basis over the requisite service period. As of December 31, 2018, total unrecognized stock-based compensation expense related to restricted stock was \$29.6 million, which will be recognized over a weighted average remaining period of 3.9 years.

14. COMMITMENTS AND CONTINGENCIES

Lease Commitments

Kforce leases office space and operating assets under operating and capital leases expiring at various dates, with some leases cancelable upon 30 to 90 days' notice and with some leases containing escalation in rent clauses. In addition to rental payments, certain leases require payments for taxes, insurance and maintenance costs.

Future minimum lease payments, inclusive of accelerated lease payments, under non-cancelable capital and operating leases are summarized as follows (in thousands):

	2019	2020	2021	2022	2023	Thereafter	Total
Capital leases							
Present value of payments	\$ 721	\$ 154	\$ 18	\$ 3	\$ —	\$ —	\$ 896
Interest	43	4	1	—	—	—	48
Total Capital lease payments	\$ 764	\$ 158	\$ 19	\$ 3	\$ —	\$ —	\$ 944
Operating lease payments	\$6,994	\$6,177	\$3,731	\$2,142	\$1,745	\$1,199	\$21,988
Total Lease payments	\$7,758	\$6,335	\$3,750	\$2,145	\$1,745	\$1,199	\$22,932

The present value of the minimum lease payments for capital lease obligations has been classified in Other current liabilities and Long-term debt—other in the accompanying Consolidated Balance Sheets, according to their respective maturities. Rental expense under operating leases was \$7.7 million for each of the years ended December 31, 2018, 2017 and 2016.

Purchase Commitments

Kforce has various commitments to purchase goods and services in the ordinary course of business. These commitments are primarily related to software and online application licenses and hosting. As of December 31, 2018, these purchase commitments amounted to approximately \$16.3 million and are expected to be paid as follows: \$10.6 million in 2019; \$3.2 million in 2020; \$2.2 million in 2021; and \$0.3 million in 2022.

Letters of Credit

Kforce provides letters of credit to certain vendors in lieu of cash deposits. At December 31, 2018, Kforce had letters of credit outstanding for workers' compensation and other insurance coverage totaling \$2.8 million, and for facility lease deposits totaling \$0.3 million.

Litigation

We are involved in legal proceedings, claims and administrative matters that arise in the ordinary course of our business. We have made accruals with respect to certain of these matters, where appropriate, that are reflected in our consolidated financial statements but are not, individually or in the aggregate, considered material. For other matters for which an accrual has not been made, we have not yet determined that a loss is probable, or the amount of loss cannot be reasonably estimated. While the ultimate outcome of the matters cannot be determined, we currently do not expect that these proceedings and claims, individually or in the aggregate, will have a material effect on our financial position, results of operations, or cash flows. The outcome of any litigation is inherently uncertain, however, and if decided adversely to us, or if we determine that settlement of particular litigation is appropriate, we may be subject to liability that could have a material adverse effect on our financial position, results of operations, or cash flows. Kforce maintains liability insurance in amounts and with such coverage and deductibles as management believes is reasonable. The principal liability risks that

Kforce insures against are workers' compensation, personal injury, bodily injury, property damage, directors' and officers' liability, errors and omissions, cyber liability, employment practices liability and fidelity losses. There can be no assurance that Kforce's liability insurance will cover all events or that the limits of coverage will be sufficient to fully cover all liabilities. Legal costs incurred in connection with loss contingencies are expensed as incurred.

Employment Agreements

Kforce has employment agreements with certain executives that provide for minimum compensation, salary and continuation of certain benefits for a six-month to a three-year period after their employment ends under certain circumstances. Certain of the agreements also provide for a severance payment ranging from one to three times annual salary and one-half to three times average annual bonus if such an agreement is terminated without good cause by Kforce or for good reason by the executive subject to certain post-employment restrictive covenants. At December 31, 2018, our liability would be approximately \$32.6 million if, following a change in control, all of the executives under contract were terminated without good cause by the employer or if the executives resigned for good reason and \$14.1 million if, in the absence of a change in control, all of the executives under contract were terminated by Kforce without good cause or if the executives resigned for good reason.

15. QUARTERLY FINANCIAL DATA (UNAUDITED)

The following table provides quarterly information for the years ended December 31, 2018 and 2017 (in thousands, except per share amounts):

Three Months Ended	March 31,	June 30,	September 30,	December 31,
2018				
Revenue	\$346,293	\$358,624	\$355,452	\$357,984
Gross profit	100,188	107,483	104,381	106,556
Net income	9,175	16,272	16,177	16,356
Earnings per share—basic	\$0.37	\$0.66	\$0.65	\$0.66
Earnings per share—diluted	\$0.37	\$0.65	\$0.64	\$0.65
2017				
Revenue	\$333,992	\$340,309	\$341,053	\$342,586
Gross profit	97,135	103,919	104,375	102,627
Net income	5,902	11,144	10,099	6,140
Earnings per share—basic	\$0.23	\$0.44	\$0.40	\$0.25
Earnings per share—diluted	\$0.23	\$0.44	\$0.40	\$0.24

16. SUPPLEMENTAL CASH FLOW INFORMATION

The following table provides information regarding supplemental cash flows for the years ended December 31 (in thousands):

	2018	2017	2016
Cash paid during the year for:			
Income taxes	\$13,442	\$24,330	\$21,324
Interest, net	\$ 3,814	\$ 3,518	\$ 2,101
Non-Cash Financing and Investing Transactions:			
Unsettled repurchases of common stock	\$ 556	\$ 898	\$ 935
Employee stock purchase plan	\$ 549	\$ 522	\$ 669
Equipment acquired under capital leases	\$ —	\$ 937	\$ 1,153
Receivable for sale of Global's assets	\$ —	\$ 1,979	\$ —
Shares tendered in payment of exercise price of stock options	\$ —	\$ —	\$ 63

During the year ended December 31, 2018, cash provided by operating activities included the receipt of an income tax refund in the amount of \$6.8 million. Our effective tax rate for the year ended December 31, 2018 was positively impacted by the TCJA.



CORPORATE INFORMATION

BOARD OF DIRECTORS

David L. Dunkel
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Chief Executive Officer,
Kforce Inc.*

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President, A.R.G., Inc.

Richard M. Cocchiaro

Ann E. Dunwoody
*President
First 2 Four, LLC*

Mark F. Furlong
*President and
Chief Executive Officer (Ret.),
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Randall A. Mehl
*President and
Chief Investment Officer,
Stewardship Capital Advisors, LLC*

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*Nonexecutive Chair of the Board,
Assurant, Inc.
Chair of the Board,
The Kresge Foundation*

N. John Simmons
*COO/CFO
DeMert Brands, Inc.*

Ralph E. Struzziero
Consultant

Howard W. Sutter
*Vice Chairman,
Kforce Inc.*

A. Gordon Tunstall
*President and
Chief Executive Officer,
Tunstall Consulting, Inc.*

EXECUTIVE AND SENIOR OFFICERS

David L. Dunkel
*Chairman and
Chief Executive Officer*

Joseph J. Liberatore
President

David M. Kelly
*Chief Financial Officer
and Secretary*

Kye L. Mitchell
Chief Operations Officer

Andrew G. Thomas
Chief Marketing Officer

Michael R. Blackman
Chief Corporate Development Officer

Denis Edwards
Chief Information Officer

CORPORATE COUNSEL
Holland & Knight LLP
Tampa, Florida

INDEPENDENT AUDITORS
Deloitte & Touche LLP
Tampa, Florida

TRANSFER AGENT

Computershare Investor Services
P.O. Box 505000
Louisville, KY 40233-5000
www.computershare.com/investor
Shareholder services:
1 (877) 373-6374

FORM 10-K AVAILABLE

A copy of the Kforce Inc.'s Annual Report on Form 10-K (excluding exhibits thereto) is available to any investor without charge upon written request to:

Michael R. Blackman
Chief Corporate Development Officer
Kforce Inc.
1001 East Palm Avenue
Tampa, Florida 33605

Or call Investor Relations:
1 (813) 552-2927

ANNUAL MEETING

The annual meeting of shareholders will be held on April 23, 2019 at 8:00 a.m. EST at Kforce Inc. headquarters in Tampa, Florida.

WEBSITE INFORMATION

For a comprehensive profile of Kforce Inc., visit the Firm's website at: www.kforce.com.



KFORCE—OVER 50 OFFICES TO SERVE YOU.

To find the location nearest you, visit our Website at www.kforce.com or call (800) 395-5575.

Corporate Headquarters: 1001 East Palm Avenue, Tampa, Florida 33605, (813) 552-5000

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San Ramon

COLORADO

Greenwood Village (Denver)

CONNECTICUT

East Hartford
Shelton
Stamford

DISTRICT OF COLUMBIA

Washington

FLORIDA

Doral (Miami)
Jacksonville
Orlando
Sunrise (Ft. Lauderdale)
Tampa

GEORGIA

Atlanta (2)

ILLINOIS

Chicago
Rolling Meadows

KANSAS

Overland Park (Kansas City)

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MARYLAND

Linthicum (Baltimore)

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NORTH CAROLINA

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Providence

TEXAS

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Austin (2)
Fort Worth
Houston
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