HEIDRICK & STRUGGLES INTERNATIONAL INC
Form 10-K
March 23, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2016

OR

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

Commission File No. 0-25837

HEIDRICK & STRUGGLES
INTERNATIONAL, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware	36-2681268
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

233 South Wacker Drive, Suite 4900, Chicago, Illinois 60606-6303
(Address of principal executive offices) (Zip Code)
(312) 496-1200
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange On Which Registered
Common Stock, $.01 par value	The Nasdaq Stock Market

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 of Section 15(d) of the Act. Yes ¨ No x

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K Yes x No ¨.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The aggregate market value of the registrant's Common Stock held by non-affiliates (excludes shares held by executive officers, directors and beneficial owners of 10% or more of the registrant's outstanding Common Stock) on June 30, 2016 was approximately $313,583,642 based upon the closing market price of $16.88 on that date of a share of Common Stock as reported on the Nasdaq Global Stock Market. As of March 10, 2017, there were 18,670,901 shares of the Company's Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement for its Annual Meeting of Stockholders to be held on May 25, 2017, are incorporated by reference into Part III of this Form 10-K.

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES

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PART I

ITEM 1. BUSINESS

Overview

Heidrick & Struggles International, Inc. ("Heidrick & Struggles") is a leadership advisory firm providing executive search, leadership consulting and culture shaping services to businesses and business leaders worldwide. When we use the terms "Heidrick & Struggles," "The Company," "we," "us" and "our," in this Form 10-K, we mean Heidrick & Struggles International, Inc. a Delaware corporation, and its consolidated subsidiaries. We provide our services to a broad range of clients through the expertise of over 300 consultants located in major cities around the world. Heidrick & Struggles and its predecessors have been a leadership advisor for more than 60 years. Heidrick & Struggles was formed as a Delaware corporation in 1999 when two of our predecessors merged to form Heidrick & Struggles.

Our service offerings include the following:

Executive Search. We partner with respected organizations globally to build and sustain the best leadership teams in the world, with a specialized focus on the placement of top-level senior executives. We believe focusing on top-level senior executives provides the opportunity for several advantages including access to and influence with key decision makers, increased potential for recurring search and consulting engagements, higher fees per search, enhanced brand visibility, and a leveraged global footprint. Working at the top of client organizations also facilitates the attraction and retention of high-caliber consultants who desire to serve top industry executives and their leadership needs. Our executive search services derive revenue through the fees generated for each search engagement, which generally are based on the annual compensation for the placed executive. We provide our executive search services primarily on a retained basis, recruiting senior executives whose first year base salary and bonus averaged approximately $340,000 in 2016 on a worldwide basis.

The executive search industry is highly fragmented, consisting of several thousand executive search firms worldwide. Executive search firms are generally separated into two broad categories: retained search and contingency search. Retained executive search firms fulfill their clients' senior leadership needs by identifying potentially qualified candidates and assisting clients in evaluating and assessing these candidates. Retained executive search firms generally are compensated for their services regardless of whether the client employs a candidate identified by the search firm and are generally retained on an exclusive basis. Typically, retained executive search firms are paid a retainer for their services equal to approximately one-third of the estimated first year compensation for the position to be filled. In addition, if the actual compensation of a placed candidate exceeds the estimated compensation, executive search firms often are authorized to bill the client for one-third of the excess. In contrast, contingency search firms are compensated only upon successfully placing a recommended candidate.

We are a retained executive search firm. Our search process typically consists of the following steps:

- Analyzing the client's business needs in order to understand its organizational structure, relationships, and culture; advising the client as to the required set of skills and experiences for the position; and identifying with the client the other characteristics desired of the successful candidate

- Selecting, contacting, interviewing and evaluating candidates on the basis of experience and potential cultural fit with the client organization

- Presenting confidential written reports on the candidates who potentially fit the position specification

- Scheduling a mutually convenient meeting between the client and each candidate
- Completing references on the final candidate selected by the client
- Assisting the client in structuring compensation packages and supporting the successful candidate’s integration into the client team

On August 4, 2016, we acquired JCA Group Limited ("JCA"), a UK-based provider of executive search, succession planning and coaching services.

Leadership Consulting. Our leadership consulting services include succession planning, executive assessment and top team and board effectiveness. Our leadership consulting services generate revenue primarily through the professional fees generated

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for each engagement which are generally based on the size of the project and scope of services. On September 1, 2016, we acquired Philosophy IB, LLP ("Philosophy IB"), a leadership, organizational development and management consulting firm. On February 29, 2016, we acquired Decision Strategies International, Inc. ("DSI"), which specializes in advising organizations and institutions on strategic planning and decision making in certain operating environments, leadership development and talent strategy. On October 1, 2015, we acquired Co Company Limited, an organizational development consulting firm.

Culture Shaping. Our culture shaping business uses its proprietary technology to analyze and interpret organizational cultures and drivers, and partner with clients to administer methods that develop alignment on leadership teams and desired organizational outcomes. Chief executive officers seek our guidance through our culture shaping services to create thriving organizational cultures in a variety of business situations, including:

- Shaping the culture to support new strategies and structures
- Aligning executive teams when there are new leaders and/or new roles
- Integrating cultures following mergers and acquisitions
- Helping minimize cultural barriers to change when implementing major organizational systems or processes
- Creating greater organizational agility to meet the challenges of a changing marketplace.

On December 31, 2012 we acquired Senn-Delaney Leadership Consulting Group, LLC ("Senn Delaney"), a global leader of corporate culture shaping.

Our culture shaping services generate revenue through a combination of professional service and license fees related to the engagement. Culture Shaping is currently less than 10% of our net revenue.

Client base. For many of our clients, our global access to and knowledge of regional and functional markets and candidate talent is an important differentiator of our business. Our clients generally fall into one of the following categories:

- Fortune 1000 companies
- Major U.S. and non-U.S. companies
- Middle market and emerging growth companies
- Governmental, higher education and not-for-profit organizations
- Other leading private and public entities

Available Information

We maintain an Internet website at http://www.heidrick.com. We make available free of charge through the investor relations section of our website, annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the U.S. Securities Exchange Act of 1934 (Exchange Act), as well as proxy statements, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission (“SEC”). Also posted on our website, and available in print upon request of any shareholder to our Investor Relations Officer, are our certificate of incorporation and by-laws, charters for our Audit and Finance Committee, Human Resources and Compensation Committee, and Nominating and Board Corporate Governance Committee, our Policy Regarding Director Independence Determinations, our Policy on Reporting of Concerns Regarding Accounting and Other Matters, our Corporate Governance Guidelines and our Code of Business Conduct and Ethics governing our directors, officers and employees. Within the time period required by the SEC, we will post on our website any amendment to the Code of Business Conduct and Ethics and any waiver applicable to any executive officer, director or senior financial officer.

In addition, our website includes information concerning purchases and sales of our equity securities by our executive officers and directors, as well as disclosure relating to certain non-GAAP financial measures (as defined in the SEC's Regulation G) that we may make public orally, telephonically, by webcast, by broadcast or by similar means from time to time.

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Our Investor Relations Officer can be contacted at Heidrick & Struggles International, Inc., 233 South Wacker Drive, Suite 4900, Chicago, Illinois, 60606, Attn: Investor Relations Officer, telephone: 312-496-1200, e-mail: InvestorRelations@heidrick.com.

Organization

Our organizational structure, which is arranged by geography, service offering and industry and functional practices, is designed to enable us to better understand our clients' cultures, operations, business strategies, industries and regional markets for leadership talent.

Geographic Structure. We provide senior-level executive search, leadership consulting and culture shaping services to our clients worldwide through a network of 47 offices in 25 countries. Each office size varies; however, major locations are staffed with consultants, research associates, administrative assistants and other support staff. Administrative functions are centralized where possible, although certain support and research functions are situated regionally because of variations in local requirements. We face risks associated with political instability, legal requirements and currency fluctuations in our international operations. Examples of such risks include difficulties in managing global operations, social and political instability, regulations and potential adverse tax consequences. For a more complete description of the risks associated with our business please see the Section in this Form 10-K entitled "Risk Factors".

Our worldwide network includes affiliate relationships in Finland, South Africa, Turkey and Portugal. We have no financial investment in these affiliates but receive licensing fees from them for the use of our name and our databases. Licensing fees are less than 1% of our net revenue.

Information by Geography. We operate our executive search services in three geographic regions: the Americas (which includes the countries in North and South America); Europe (which includes the continents of Europe and Africa); and Asia Pacific (which includes Asia and the region generally known as the Middle East). Our leadership consulting segment operates globally and our culture shaping segment operates in the Americas and Europe.

Americas Executive Search. As of December 31, 2016, we had 158 consultants in our Americas segment. The largest offices in this segment, as defined by net revenue, are located in New York, Chicago and Boston.

Europe Executive Search. As of December 31, 2016, we had 95 consultants in our European segment. The largest countries in this segment, as defined by net revenue, are the United Kingdom, France and Germany.

Asia Pacific Executive Search. As of December 31, 2016, we had 82 consultants in our Asia Pacific segment. The largest countries in this segment, as defined by net revenue, are China (including Hong Kong), Australia and Singapore.

Leadership Consulting. As of December 31, 2016, we had 22 consultants in our Leadership Consulting segment. The largest countries in this segment, as defined by net revenue, are the United Kingdom, United States and Singapore.

Culture Shaping. As of December 31, 2016, we had 17 consultants in our Culture Shaping segment. The culture shaping consultants are primarily based in Huntington Beach, CA and approximately 81% of the net revenue is generated in the United States.

The relative percentages of net revenue attributable to each segment were as follows:

Year Ended
December 31,

	2016	2015	2014
Executive Search			
Americas	53 %	55 %	51 %
Europe	19 %	17 %	21 %
Asia Pacific	15 %	17 %	17 %
Leadership Consulting	7 %	4 %	4 %
Culture Shaping	6 %	7 %	7 %

For financial information relating to each segment, see Note 16, Segment Information, in the Notes to Consolidated Financial Statements.

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Global Industry Practices. Our executive search and leadership consulting businesses operate in six broad industry groups listed below. These industry categories and their relative sizes, as measured by billings for 2016, 2015 and 2014, are as follows:

	Percentage of Billings		
Global Industry Practices	2016	2015	2014
Financial Services	28 %	27 %	26 %
Industrial	21	21	23
Global Technology & Services	21	22	21
Consumer Markets	17	16	18
Healthcare & Life Sciences	11	10	8
Education, Non-Profit & Social Enterprise	2	4	4
	100%	100%	100%

Within each broad industry group are a number of industry sub-sectors. Consultants often specialize in one or more sub sectors to provide clients with market intelligence and candidate knowledge specific to their industry. For example, within the Financial Services sector our business is diversified amongst a number of industry sub sectors including Asset & Wealth Management, Consumer & Commercial Finance, Commodities, Corporate and Transaction Banking, Global Markets, Hedge Fund, Infrastructure, Investment Banking, Insurance, Private Equity Investment Professionals and Real Estate.

We service our clients with global industry interests and needs through unified global executive search teams who specialize in industry practices. This go-to-market strategy allows us to leverage our global diversity and market intelligence and is designed to provide better client service. Each client is served by one global account team, which we believe is a key differentiator from our competition.

Global Functional Practices. Our executive search consultants also specialize in searches for specific “C-level” functional positions, which are roles that generally report directly to the chief executive officer.

Our Global Functional Practices include Chief Executive Officer & Board of Directors; Human Resources Officers; Financial Officers; Information and Technology Officers; Legal, Risk, Compliance & Government Affairs; Marketing, Sales and Strategy Officers and Supply Chain and Operations.

Our team of executive search consultants may service clients from any one of our offices around the world. For example, an executive search for a chief financial officer of an industrial company located in the United Kingdom may involve a consultant in the United Kingdom with an existing relationship with the client, another executive search consultant in the United States with expertise in our Industrial practice and a third executive search consultant with expertise in recruiting chief financial officers. This same industrial client may also engage us to perform skill-based assessments for each of its senior managers, which could require the expertise of one of our leadership advisory consultants trained in this service.

Seasonality

There is no discernible seasonality in our business, although as a percentage of total annual net revenue, the first quarter is typically the lowest. Revenue and operating income have historically varied by quarter and are hard to predict from quarter to quarter. In addition, the volatility in the global economy and business cycles can impact our quarterly revenue and operating income.

Clients and Marketing

Our consultants market the firm's executive search, leadership consulting and culture shaping services through two principal means: targeted client calling and industry networking with clients and referral sources. These efforts are supported by proprietary databases, which provide our consultants with information as to contacts made by their colleagues with particular referral sources, candidates and clients. In addition, we benefit from a significant number of referrals generated by our reputation for high quality service and successfully completed assignments, as well as repeat business resulting from our ongoing client relationships.

In support of client calling and networking, the practice teams as well as individual consultants also author and publish articles and white papers on a variety of leadership and talent topics and trends around the world. Our consultants often present research findings and talent insights at notable conferences and events as well. Our insights are sometimes acknowledged by major media outlets and trade journalists. These efforts aid in the marketing of our services as well.

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Either by agreement with the clients or to maintain strong client relationships, we may refrain from recruiting employees of a client, or possibly other entities affiliated with that client, for a specified period of time but typically not more than one year from the commencement of a search. We seek to mitigate any adverse effects of these off-limits arrangements by strengthening our long-term relationships, allowing us to communicate our belief to prospective clients that we can conduct searches without these off-limits arrangements impeding the quality of our work.

No single client accounted for more than 1% of our net revenue in 2016, 2015 or 2014. As a percentage of total revenue, our top ten clients in aggregate accounted for approximately 7% in 2016, 2015 and 2014.

Information Management Systems

We rely on technology to support our consultants and staff in the search process. Our technology infrastructure consists of internally developed databases containing candidate profiles and client records, coupled with online services, industry reference sources, and Leadership Signature, an internally developed assessment tool. We use technology to manage and share information on current and potential clients and candidates, to communicate to both internal and external constituencies and to support administrative functions.

Our culture shaping business' proprietary Web-based system, SD Connect™ is integral to the culture-shaping process. This technology platform enables our consultants to administer, analyze and interpret online Corporate Culture Profiles™ (CCP) surveys to develop clarity around team and organizational need and desired outcomes. In addition, we gather data using our online Culture Impact Survey™ (CIS) to determine which culture-shaping concepts are being utilized by individuals and the team as a whole.

Professional Staff and Employees

Our professionals are generally categorized either as consultants or associates. Associates assist consultants by providing research support, coordinating candidate contact and performing other engagement-related functions. As of December 31, 2016, we had head count of 1,814, consisting of 374 consultants with 335 consultants related to executive search, 22 consultants related to leadership consulting and 17 consultants related to culture shaping, 538 associates and 902 other search, support and Global Operations Support staff.

We promote our associates to consultants during the annual consultant promotion process and we recruit our consultants from other executive search or human capital firms, or in the case of executive search, consultants new to search who have worked in industries or functions represented by our practices. In the latter case, these are often seasoned executives with extensive contacts and outstanding reputations who are entering the search profession as a second career and whom we train in our techniques and methodologies. Our culture shaping consultants are recruited for their executive business experience as well as their skills in consulting and leadership advisory and often are former clients who are familiar with our culture shaping methodology. We are not a party to any U.S. based collective bargaining agreement, and we consider relations with our employees to be good.

Competition

The executive search industry is highly competitive. While we face competition to some degree from all firms in the industry, we believe our most direct competition comes from four established global retained executive search firms that conduct searches primarily for the most senior-level positions within an organization. In particular, our competitors include Egon Zehnder International, Korn Ferry International, Russell Reynolds Associates, Inc. and Spencer Stuart & Associates. To a lesser extent, we also face competition from smaller boutique firms that specialize in certain regional markets or industry segments and Internet-based firms. Each firm with which we compete is also a competitor in the marketplace for effective search consultants.

Overall, the search industry has relatively few barriers to entry; however, there are higher barriers to entry to compete with global retained executive search firms that can provide leadership consulting services at the senior executive level. At this level, clients rely more heavily on a search firm’s reputation, global access and the experience level of its consultants. We believe that the segment of executive search in which we compete is more quality-sensitive than price-sensitive. As a result, we compete on the level of service we offer, reflected by our client services specialties and, ultimately, by the quality of our search results. We believe that our emphasis on senior-level executive search, the depth of experience of our search consultants and our global presence enable us to compete favorably with other executive search firms.

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Competition in the leadership consulting services and culture shaping markets in which we operate is highly fragmented, with no universally recognized market leaders.

Regulation

We are subject to the U.S. securities laws and general corporate and commercial laws and regulations of the locations which we serve. These include regulations regarding anti-bribery, privacy and data protection, intellectual property, data security, data retention, personal information, economic or other trade prohibitions or sanctions. In particular, we are subject to federal, state, and foreign laws regarding privacy and protection of people's data. Foreign data protection, privacy, and other laws and regulations can be more restrictive than those in the United States. U.S. federal and state and foreign laws and regulations, which in some cases can be enforced by private parties in addition to government entities, are constantly evolving and can be subject to change.

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EXECUTIVE OFFICERS

Below is the name, age, present title, principal occupation and certain biographical information for each of our executive officers as of the date of this report. All of our executive officers have been appointed by and serve at the pleasure of our board of directors. There are no family relationships between any executive officer or director.

Tracy R. Wolstencroft (58) Mr. Wolstencroft has been our President and Chief Executive Officer since February 3, 2014, and a director since February 6, 2014. From 1994 until his retirement in 2010, Mr. Wolstencroft served as a partner for Goldman Sachs & Co. ("Goldman"), concluding a twenty-five year career with the firm. During his service to Goldman, Mr. Wolstencroft served on the Firmwide Partnership Committee, the Investment Banking Operating Committee, and the Asia Management Committee. During his career, he led a wide range of businesses in the United States and abroad, including Investment Banking Services, Environmental Markets, Latin America, Public Sector and Infrastructure Banking, and Fixed Income Capital Markets. While living in Asia from 1998 to 2002, Mr. Wolstencroft was President of GS Singapore, co-head of investment banking in Japan, head of Asia financial institutions, and a leader of the firm's strategy in China. Mr. Wolstencroft also served as an Advisory Director for Goldman and as Chairman of the firm's Clean Technology and Renewables business. He currently serves as a Trustee of the Brookings Institution, the National Geographic Society and the International Rescue Committee.

Richard W. Pehlke (63) Mr. Pehlke has been our Executive Vice President and Chief Financial Officer since August 2011 after serving as interim Chief Financial Officer since May 2011. Previously, Mr. Pehlke was Executive Vice President and Chief Financial Officer at Grubb & Ellis Company, a commercial real estate firm, from 2007 to 2010. During his extensive career, he also has held senior financial positions in the business services, telecommunications, financial services, food and consumer products and executive search and staffing industries. Mr. Pehlke currently serves on the board of directors of Ideal Industries.

Stephen W. Beard (45) Mr. Beard has been our Executive Vice President, General Counsel and Chief Administrative Officer since January 1, 2013. During his more than 10 years with the Company he has served in several senior leadership capacities, including serving as our General Counsel and Corporate Secretary (2011 to 2013) and Deputy General Counsel and Chief Compliance Officer (2008 to 2011).

Colin Price (58) Mr. Price has been our Executive Vice President and Managing Partner - Leadership Consulting since December 2015 and a member of our Executive Committee on January 1, 2016. Previously, Mr. Price served as Chairman of Co Company Limited, an organizational development consulting firm acquired by Heidrick & Struggles in 2015. He previously was a Director in McKinsey & Company's London office and led McKinsey's Global Organisation Practice (1999 through July 2014.)

Krishnan Rajagopalan (56) Mr. Rajagopalan has been our Executive Vice President and Managing Partner - Executive Search since January 2016. Previously, he served as Head of Global Practices beginning in April 2014 and was appointed an Executive Vice President on January 1, 2015. Mr. Rajagopalan has served in other leadership roles including Global Practice Managing Partner, Technology and Services (2010 to 2014) and Global Practice Managing Partner, Business/Professional Services (2007 to 2010). Mr. Rajagopalan joined the firm in 2001 in executive search.

Richard W. Greene (53) Mr. Greene has been our Executive Vice President and Chief Human Resources Officer since January 1, 2015. Previously, Mr. Greene was the global Head of Talent Management and a global segment HR executive at Bunge, an agribusiness and food production company (2011 to 2014). Mr. Greene previously managed Heidrick & Struggles' Leadership Consulting and Human Resources practices in the Americas (2006 to 2011).

Michael Marino (65) Mr. Marino has served as the the President and Chief Executive Officer, Senn Delaney and Executive Vice President and Managing Partner - Culture Shaping since January 1, 2017. Mr. Marino has served on the leadership team at Senn Delaney for more than twenty years.

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ITEM 1A. RISK FACTORS

In addition to other information in this Form 10-K, the following risk factors should be carefully considered in evaluating our business because such factors may have a material impact on our business, operating results, cash flows and financial condition. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties that we are unaware of, or that we currently believe are not material, may also become important factors that adversely affect our business.

We depend on attracting, integrating, managing, and retaining qualified consultants and senior leaders.

Our success depends upon our ability to attract, develop, manage and retain quality consultants with the skills and experience necessary to fulfill our clients' needs and achieve our operational and financial goals. Our ability to hire and retain qualified consultants could be impaired by any diminution of our reputation, disparity in compensation relative to our competitors, modifications to our total compensation philosophy or competitor hiring programs. If we cannot attract, hire, develop and retain qualified consultants, our business, financial condition and results of operations may suffer. Our future success also depends upon our ability to complete the integration of newly-hired consultants successfully into our operations and to manage the performance of our consultants. Failure to successfully integrate newly-hired consultants or to manage the performance of our consultants could affect our profitability by causing operating inefficiencies that could increase operating expenses and reduce operating income. There is also a risk that unanticipated turnover in senior leadership coupled with an inadequate succession plan stalls company activity, interrupts strategic vision or lowers productive output which may adversely impact our financial condition and results of operations.

We may not be able to prevent our consultants from taking our clients with them to another firm.

Our success depends upon our ability to develop and maintain strong, long-term relationships with our clients. Although we work on building these relationships between our firm and our clients, in many cases, one or two consultants have primary responsibility for a client relationship. When a consultant leaves one executive search firm and joins another, clients who have established relationships with the departing consultant may move their business to the consultant's new employer. We may also lose clients if the departing consultant has widespread name recognition or a reputation as a specialist in executing searches in a specific industry or management function. If we fail to retain important client relationships when a consultant departs our firm, our business, financial condition and results of operations may be adversely affected.

Our success depends on our ability to maintain our professional reputation and brand name.

We depend on our overall professional reputation and brand name recognition to secure new engagements and hire qualified consultants. Our success also depends on the individual reputations of our consultants. We obtain many of our new engagements from existing clients or from referrals by those clients. A client who is dissatisfied with our work can adversely affect our ability to secure new engagements. If any factor, including poor performance, hurts our reputation we may experience difficulties in competing successfully for both new engagements and qualified consultants. Failure to maintain our professional reputation and brand name could seriously harm our business, financial condition and results of operations.

Our net revenue may be affected by adverse economic conditions.

Demand for our services is affected by global economic conditions and the general level of economic activity in the geographic regions in which we operate. During periods of slowed economic activity many companies hire fewer permanent employees, and our financial condition and results of operations can be adversely affected. If unfavorable changes in economic conditions occur, our business, financial condition and results of operations could suffer.

Because our clients may restrict us from recruiting their employees, we may be unable to fill or obtain new executive search assignments.

Clients frequently require us to refrain from recruiting certain of their employees when conducting executive searches on behalf of other clients. These restrictions generally remain in effect for no more than one year following the commencement of an engagement. However, the specific duration and scope of the off-limits arrangements depend on the length of the client relationship, the frequency with which the client engages us to perform searches, the number of assignments we have performed for the client and the potential for future business with the client.

Client restrictions on recruiting their employees could hinder us from fulfilling executive searches. Additionally, if a prospective client believes that we are overly restricted by these off-limits arrangements from recruiting the employees of our existing clients, these prospective clients may not engage us to perform their executive searches. As a result, our business, financial condition and results of operations may suffer.

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We face aggressive competition.

The global executive search industry is highly competitive and fragmented. We compete with other large global executive search firms, smaller specialty firms, and more recently with Internet-based firms and social media. Specialty firms can focus on regional or functional markets or on particular industries. Some of our competitors may possess greater resources, greater name recognition and longer operating histories than we do in particular markets or practice areas, or be willing to reduce their fees or agree to alternative pricing practices in order to attract clients and increase market share. Our competitors may be further along in the development and design of technological solutions to meet client requirements.

There are limited barriers to entry into the search industry and new search firms continue to enter the market. Many executive search firms that have a smaller client base may be subject to fewer off-limits arrangements. In addition, our clients or prospective clients may decide to perform executive searches using in-house personnel. Also, as internet-based firms continue to evolve, they may develop offerings similar to or more expansive than ours, thereby increasing competition for our services or more broadly causing market disruption in the executive search industry. We may not be able to continue to compete effectively with existing or potential competitors and we may not be able to implement our leadership strategy effectively. Our inability to meet these competitive challenges could have an adverse impact on our business, financial condition and results of operations.

We rely heavily on information management systems.

Our success depends upon our ability to store, retrieve, process and manage substantial amounts of information. To achieve our goals, we must continue to improve and upgrade our information management systems. We may be unable to license, design and implement, in a cost-effective and timely manner, improved information systems that allow us to compete effectively. In addition, business process reengineering efforts may result in a change in software platforms and programs. Such efforts may result in an acceleration of depreciation expense over the shortened expected remaining life of the software and present transitional problems. Problems or issues with our proprietary search system or other factors may result in interruptions or loss in our information processing capabilities which may cause our business, financial condition and results of operations to suffer.

We face the risk of liability in the services we perform.

We are exposed to potential claims with respect to the executive search process. A client could assert a claim for violations of off-limits arrangements, breaches of confidentiality agreements or professional malpractice. The growth and development of our culture shaping and other leadership advisory services brings with it the potential for new types of claims. In addition, candidates and client employees could assert claims against us. Possible claims include failure to maintain the confidentiality of the candidate’s employment search or for discrimination or other violations of the employment laws or malpractice. In various countries, we are subject to data protection laws impacting the processing of candidate information. We maintain professional liability insurance in amounts and coverage that we believe are adequate; however, we cannot guarantee that our insurance will cover all claims or that coverage will always be available. Significant uninsured liabilities could have a negative impact on our business, financial condition and results of operations.

Our multinational operations may be adversely affected by social, political, regulatory, legal and economic risks.

We generate substantial revenue outside the United States. We offer our services through a network of offices in 25 countries around the world. Our ability to effectively serve our clients is dependent upon our ability to successfully leverage our operating model across all of these and any future locations, maintain effective management controls over all of our locations to ensure, among other things, compliance with applicable laws, rules and regulations, and instill our core values in all of our personnel at each of these and any future locations. We are exposed to the risk of changes in social, political, legal and economic conditions inherent in our operations, which could have a significant impact on our business, financial condition and results of operations. In addition, we conduct business in countries where the legal systems, local laws and trade practices are unsettled and evolving. Commercial laws in these countries are sometimes vague, arbitrary and inconsistently applied. Under these circumstances, it is difficult for us to determine at all times the exact requirements of such local laws. If we fail to comply with local laws, our business, financial condition and results of operations could suffer. In addition, the global nature of our operations poses challenges to our management, and financial and accounting systems. Failure to meet these challenges could seriously harm our business, financial condition and results of operations.

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A significant currency fluctuation between the U.S. dollar and other currencies could adversely impact our operating income.

With our operations in the Americas, Europe and Asia Pacific, we conduct business using various currencies. In 2016, approximately 41% of our net revenue was generated outside the United States. As we typically transact business in the local currency of our subsidiaries, our profitability may be impacted by the translation of foreign currency financial statements into U.S. dollars. Significant long-term fluctuations in relative currency values, in particular an increase in the value of the U.S. dollar against foreign currencies, could have an adverse effect on our profitability and financial condition.

We may not be able to align our cost structure with net revenue.

We must ensure that our costs and workforce continue to be in proportion to demand for our services. Failure to align our cost structure and headcount with net revenue could adversely affect our business, financial condition, and results of operations.

Unfavorable tax law changes and tax authority rulings may adversely affect results.

We are subject to income taxes in the United States and in various foreign jurisdictions. Domestic and international tax liabilities are subject to the allocation of income among various tax jurisdictions. Our effective tax rate could be adversely affected by changes in the mix of earnings among countries with differing statutory tax rates, or changes in the valuation allowance of deferred tax assets or tax laws. The amount of income taxes and other taxes are subject to ongoing audits by U.S. federal, state and local tax authorities and by non-U.S. authorities. If these audits result in assessments different from amounts recorded, future financial results may include unfavorable tax adjustments.

We may not be able to generate sufficient profits to realize the benefit of our net deferred tax assets.

We establish valuation allowances against deferred tax assets when there is insufficient evidence that we will be able to realize the benefit of these deferred tax assets. We reassess our ability to realize deferred tax assets as facts and circumstances dictate. If after future assessments of our ability to realize the deferred tax assets, we determine that a lesser or greater allowance is required, we record a reduction or increase to the income tax expense and the valuation allowance in the period of such determination. The uncertainty surrounding the future realization of our net deferred tax assets could adversely impact our results of operations.

We may experience impairment of our goodwill, other intangible assets and other long-lived assets.

In accordance with generally accepted accounting principles, we perform assessments of the carrying value of our goodwill at least annually and we review our goodwill, other intangible assets and other long-lived assets for impairment whenever events occur or circumstances indicate that a carrying amount of these assets may not be recoverable. These events and circumstances include a significant change in business climate, attrition of key personnel, changes in financial condition or results of operations, a prolonged decline in our stock price and market capitalization, competition, and other factors. In performing these assessments, we must make assumptions regarding the estimated fair value of our goodwill and other intangible assets. These assumptions include estimates of future market growth and trends, forecasted revenue and costs, capital investments, discount rates, and other variables. If the fair market value of one of our reporting units or other long term assets is less than the carrying amount of the related assets, we would be required to record an impairment charge. Due to continual changes in market and general business conditions, we cannot predict whether, and to what extent, our goodwill and long-lived intangible assets may be impaired in future periods. Any resulting impairment loss could have an adverse impact on our business, financial condition and results of operations.

Our ability to execute and integrate future acquisitions, if any, could negatively affect our business and profitability.
Our future success may depend in part on our ability to complete the integration of acquisition targets successfully into our operations. The process of executing and integrating an acquired business may subject us to a number of risks, including:

- diversion of management attention;
- failure to successfully further develop the acquired business;
- amortization of intangible assets, adversely affecting our reported results of operations;
- inability to retain and/or integrate the management, key personnel and other employees of the acquired business;
- inability to properly integrate businesses resulting in operating inefficiencies;

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- inability to establish uniform standards, disclosure controls and procedures, internal control over financial reporting and other systems, procedures and policies in a timely manner;
- inability to retain the acquired company's clients;
- exposure to legal claims for activities of the acquired business prior to acquisition; and
- inability to generate revenues to offset any new liabilities assumed and expenses associated with an acquired business.

If our acquisitions are not successfully executed and integrated, our business, financial condition and results of operations, as well as our professional reputation, could be adversely affected.

We have anti-takeover provisions that make an acquisition of us difficult and expensive.

Anti-takeover provisions in our Certificate of Incorporation, our Bylaws and the Delaware laws make it difficult and expensive for someone to acquire us in a transaction which is not approved by our Board of Directors. Some of the provisions in our Certificate of Incorporation and Bylaws include:

- limitations on the removal of directors
- limitations on stockholder actions
- the ability to issue one or more series of preferred stock by action of our Board of Directors

These provisions could discourage an acquisition attempt or other transaction in which stockholders could receive a premium over the current market price for the common stock.

Our ability to access additional credit could be limited.

Banks can be expected to strictly enforce the terms of our credit agreement. Although we are currently in compliance with the financial covenants of our revolving credit facility, a deterioration of economic conditions may negatively impact our business resulting in our failure to comply with these covenants, which could limit our ability to borrow funds under our credit facility or from other borrowing facilities in the future. In such circumstances, we may not be able to secure alternative financing or may only be able to do so at significantly higher costs.

Increased cybersecurity requirements, vulnerabilities, threats and more sophisticated and targeted cyber-related attacks could pose a risk to our systems, networks, solutions, services and data.

Increased global cybersecurity vulnerabilities, threats and more sophisticated and targeted cyber-related attacks pose a risk to the security of our systems and networks and the confidentiality, availability and integrity of our data. We have a program in place to detect and respond to data security incidents. However, we remain potentially vulnerable to additional known or unknown threats. We also have access to sensitive, confidential or personal data or information that is subject to privacy and security laws, regulations and client-imposed controls. Despite our efforts to protect sensitive, confidential or personal data or information, we may be vulnerable to security breaches, theft, lost data, employee errors and/or malfeasance that could potentially lead to the compromising of sensitive, confidential or personal data or information, improper use of our systems or networks, unauthorized access, use, disclosure, modification or destruction of information. In addition, a cyber-related attack could result in other negative consequences, including damage to our reputation or competitiveness, remediation or increased protection costs, litigation or regulatory action which could result in a negative impact to our results of operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our corporate headquarters is located in Chicago, Illinois. We have leased office space in 47 cities in 25 countries around the world. All of our offices are leased. We do not own any real estate. The aggregate square footage of office space under lease was 465,715 as of December 31, 2016. Our office leases call for future minimum lease payments of approximately $164.2 million and have terms that expire between 2017 and 2026, exclusive of renewal options that we can exercise. Approximately 7,000 square feet of office space has been sublet to third parties.

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Our office space by geographic segment as of December 31, 2016 is as follows:

	Square Footage
Americas	251,139
Asia Pacific	111,429
Europe	103,147
Total	465,715

ITEM 3. LEGAL PROCEEDINGS

We have contingent liabilities from various pending claims and litigation matters arising in the ordinary course of our business, some of which involve claims for damages that may be substantial in amount. Some of these matters are covered by insurance. Based upon information currently available, we believe the ultimate resolution of such claims and litigation, including the “UK Employee Benefits Trust” matter discussed below, will not have a material adverse effect on our financial condition, results of operations or liquidity.

UK Employee Benefits Trust

On January 27, 2010, HM Revenue & Customs (“HMRC”) in the United Kingdom notified us that it was challenging the tax treatment of certain of our contributions in the United Kingdom to an Employee Benefits Trust between 2002 and 2008. HMRC alleges that these contributions should have been subject to Pay As You Earn tax and Class 1 National Insurance Contributions in the United Kingdom; and HMRC is proposing an adjustment to our payroll tax liability for the affected years. The aggregate amount of HMRC’s proposed adjustment is approximately £3.9 million (equivalent to $4.8 million at December 31, 2016). We have appealed the proposed adjustment. At this time, we believe that the likelihood of an unfavorable outcome with respect to the proposed adjustment is not probable and the potential amount of any loss cannot be reasonably estimated. We also believe that the amount of a final adjustment, if any, would not be material to our financial condition.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market for Registrant's Common Equity

Our common stock is listed on the Nasdaq Global Stock Market under the symbol "HSII." The following table sets forth the high and low stock price per share of the common stock for the periods indicated, as reported on the Nasdaq Global Stock Market.

Year Ended December 31, 2016	High	Low
First Quarter	$26.91	$22.22
Second Quarter	24.69	16.36
Third Quarter	21.15	16.73
Fourth Quarter	24.50	17.55
Year Ended December 31, 2015		
First Quarter	$24.78	$22.16
Second Quarter	26.59	23.13
Third Quarter	26.26	19.16
Fourth Quarter	29.77	19.43

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Performance Graph

We have presented below a graph which compares the cumulative total stockholder return on our common shares with the cumulative total stockholder return of the Standard & Poor's SmallCap 600 Index and the Standard & Poor's Composite 1500 Human Resource and Employment Services Index. The S&P Composite 1500 Human Resource & Employment Services Index includes 11 companies in related businesses, including Heidrick & Struggles. Cumulative total return for each of the periods shown in the performance graph is measured assuming an initial investment of $100 on December 31, 2011.

The stock price performance depicted in this graph is not necessarily indicative of future price performance. This graph will not be deemed to be filed as part of this Form 10-K and will not be deemed to be incorporated by reference by any general statement incorporating this Form 10-K into any filing by us under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent we specifically incorporate this information by reference.

* Assuming $100 invested on 12/31/11 in HSII or index, including reinvestment of dividends.
Prepared by: Zacks Investment Research, Inc.
Copyright: Standard and Poor's, Inc.

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Dividends

Since September 2007, we have paid a quarterly cash dividend of $0.13 per share as approved by our Board of Directors. In 2016, the total cash dividend paid was $0.52 per share.

The following table outlines the record date, payment date and amount of quarterly cash dividends paid during 2015 and 2016:

Quarter	Record Date	Payment Date	Dividends (in millions)
Q1 2015	February 6, 2015	February 20, 2015	$2.4
Q2 2015	May 1, 2015	May 15, 2015	2.4
Q3 2015	August 7, 2015	August 21, 2015	2.4
Q4 2015	November 6, 2015	November 20, 2015	2.4
Q1 2016	February 5, 2016	February 19, 2016	2.4
Q2 2016	May 6, 2016	May 20, 2016	2.4
Q3 2016	August 5, 2016	August 19, 2016	2.4
Q4 2016	November 4, 2016	November 18, 2016	2.4

In December 2016, our Board of Directors declared a quarterly dividend of $0.13 per share on our common stock which was paid on February 17, 2017 to shareholders of record as of February 3, 2017. Cash dividends payable of $2.4 million related to the fourth quarter 2016 cash dividend, which was paid in the first quarter of 2017, is accrued in the Consolidated Balance Sheets as of December 31, 2016. Cash dividends payable of $2.4 million related to the fourth quarter 2015 cash dividend, was paid in the first quarter of 2016.

In connection with the quarterly cash dividend, we also pay a dividend equivalent on outstanding restricted stock units. The amounts related to the dividend equivalent payments for restricted stock units are accrued over the vesting period and paid upon vesting. In 2016 and 2015 we paid $0.3 million and $0.2 million, respectively, in dividend equivalent payments.

Issuer Purchases of Equity Securities

On February 11, 2008, we announced that our Board of Directors authorized management to repurchase shares of our common stock with an aggregate purchase price up to $50 million. We intend from time to time and as business conditions warrant, to purchase shares of our common stock on the open market or in negotiated or block trades. No time limit has been set for completion of this program. We did not repurchase any shares of our common stock in 2016. As of December 31, 2016 and December 31, 2015, we have purchased 1,038,670 shares of our common stock for a total of $28.3 million and $21.7 million remains available for future purchases under the authorization. For further information of our share repurchase activity, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources.”

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ITEM 6. SELECTED FINANCIAL DATA

The selected financial data presented below have been derived from our audited consolidated financial statements. The data as of December 31, 2016 and 2015 and for the years ended December 31, 2016, 2015 and 2014 are derived from the audited current and historical consolidated financial statements, which are included elsewhere in this Form 10-K. Other than noted below, the data as of December 31, 2014, 2013 and 2012 and for the years ended December 31, 2013 and 2012 are derived from audited historical consolidated financial statements, which are not included in this report. The data set forth is qualified in its entirety by, and should be read in conjunction with, "Management's Discussion and Analysis of Financial Condition and Results of Operations," the audited consolidated financial statements, the notes thereto, and the other financial data and statistical information included in this Form 10-K.

	Year Ended December 31,				
	2016	2015	2014	2013	2012
	(in thousands, except per share and other operating data)				
Statements of Operations Data:					
Revenue:					
Revenue before reimbursements (net revenue)	$582,390	$531,139	$494,292	$461,995	$443,777
Reimbursements	18,516	17,172	18,947	18,998	21,304
Total revenue	600,906	548,311	513,239	480,993	465,081
Operating expenses:					
Salaries and employee benefits	400,070	369,385	337,448	319,499	309,502
General and administrative expenses	147,087	127,692	130,191	126,931	113,826
Reimbursed expenses	18,516	17,172	18,947	18,998	21,304
Restructuring charges	—	—	—	—	810 (2)
Total operating expenses	565,673	514,249	486,586	465,428	445,442
Operating income	35,233	34,062	26,653	15,565	19,639
Non-operating (expense) income:					
Interest, net	244	(122)	(358)	(175)	1,118
Other, net	2,289	(2,386)	(2,108)	(2,002)	(495)
Net non-operating (expense) income	2,533	(2,508)	(2,466)	(2,177)	623
Income before income taxes	37,766	31,554	24,187	13,388	20,262
Provision for income taxes	22,353	14,422	17,390	7,041	14,022
Net income	$15,413	$17,132	$6,797	$6,347	$6,240
Basic weighted average common shares outstanding	18,540	18,334	18,210	18,077	17,971
Diluted weighted average common shares outstanding	18,939	18,715	18,432	18,232	18,120
Basic earnings per common share	$0.83	$0.93	$0.37	$0.35	$0.35
Diluted earnings per common share	$0.81	$0.92	$0.37	$0.35	$0.34
Cash dividends paid per share	$0.52	$0.52	$0.52	$0.39	$0.65
Balance Sheet Data (at end of period):					
Working capital (1)	$77,838	$79,533	$112,387	$107,177	$66,030
Total assets (1)	581,502	572,718	568,621	552,937	494,890
Long-term debt, less current maturities	—	—	23,500	29,500	—
Stockholders' equity	258,590	254,802	244,664	247,873	248,347
Other Operating Data:					
Average number of consultants during the period	347	326	313	341	342

Notes to Selected Financial Data:

(1) As adjusted for the adoption of ASU 2015-17, Income Taxes: Balance Sheet Classification of Deferred Taxes.

(2) In 2012, we recorded restructuring charges of $0.8 million in Europe related to adjustments associated with our 2011 restructuring plan. These charges consist of $1.1 million of employee-related costs associated with severance

arrangements, partially offset by $0.3 million of adjustments to premise-related costs.

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's Discussion and Analysis of Financial Condition and Results of Operations as well as other sections of this annual report on Form 10-K contain forward-looking statements. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Forward-looking statements are not historical facts, but instead represent only our beliefs, assumptions, expectations, estimates, forecasts and projections regarding future events, many of which, by their nature, are inherently uncertain and outside our control. These statements include statements other than historical information or statements of current condition and may relate to our future plans and objectives and results. By identifying these statements for you in this manner, we are alerting you to the possibility that our actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these forward-looking statements. Important factors that could cause our actual results and financial condition to differ from those indicated in the forward-looking statements include, among others, those discussed under the Section heading "Risk Factors" in Part I, Item 1A of this Form 10-K.

Factors that may affect the outcome of the forward-looking statements include, among other things, leadership changes, our ability to attract, integrate, manage and retain qualified consultants and senior leaders; our ability to develop and maintain strong, long-term relationships with our clients; fluctuations in the global and local economies and our ability to execute successfully our strategies;social or political instability in markets where we operate, the impact of the U.K. referendum to leave the European Union (Brexit); the impact of foreign currency exchange rate fluctuations; unfavorable tax law changes and tax authority rulings; price competition; the ability to forecast, on a quarterly basis, variable compensation accruals that ultimately are determined based on the achievement of annual results; our ability to realize our tax losses; the timing of the establishment or reversal of valuation allowance on deferred tax assets; the mix of profit and loss by country; our ability to integrate future acquisitions; our reliance on information management systems; any impairment of our goodwill, other intangible assets and other long-lived assets; and the ability to align our cost structure and headcount with net revenue. We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

Executive Overview

Our Business

We are a leadership advisory firm providing executive search, leadership consulting and culture shaping services. We help our clients build leadership teams by facilitating the recruitment, management and development of senior executives. We believe focusing on top-level services offers us several advantages that include access to and influence with key decision makers, increased potential for recurring search consulting engagements, higher fees per search, enhanced brand visibility, and a leveraged global footprint, which create added barriers to entry for potential competitors. Working at the top of client organizations also allows us to attract and retain high-caliber consultants. On August 4, 2016, we acquired JCA Group Limited, a UK-based provider of executive search, succession planning and coaching services.

In addition to executive search, we provide leadership consulting expertise and culture shaping services including executive leadership assessment; leadership, team and board development; succession planning; talent strategy; people performance; inter-team collaboration; and organizational transformation. On September 1, 2016, we acquired Philosophy IB, LLP, a leadership, organizational development and management consulting firm. On August 4, 2016, we acquired JCA Group Limited, a UK-based provider of executive search, succession planning and coaching services. On February 29, 2016, we acquired Decision Strategies International, Inc., which specializes in advising organizations and institutions on strategic planning and decision making in certain operating environments, leadership development and talent strategy. On October 1, 2015, we acquired Co Company Limited, an organizational development consulting firm.

In the fourth quarter of 2016, we restructured our operating segments. Given the significant growth of the Company's Leadership Consulting service line, our chief operating decision maker began to regularly assess performance and make resource allocation decisions separately for Executive Search and Leadership Consulting. Therefore, we now report Executive Search and Leadership Consulting as separate operating segments. We currently operate our executive search business in the Americas; Europe (which includes Africa); and Asia Pacific (which includes the Middle East) and operate our leadership consulting and culture shaping businesses as separate segments. Previously reported operating segment results for the years ended December 31, 2015 and 2014 have been recast to conform to the new operating segment structure.

We provide our services to a broad range of clients through the expertise of over 300 consultants located in major cities around the world. Our executive search services are provided on a retained basis. Revenue before reimbursements of out-of-pocket expenses ("net revenue") consists of retainers and indirect expenses billed to clients. Typically, we are paid a retainer for

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our executive search services equal to approximately one-third of the estimated first year compensation for the position to be filled. In addition, if the actual compensation of a placed candidate exceeds the estimated compensation, we often are authorized to bill the client for one-third of the excess. Indirect expenses are calculated as a percentage of the retainer with certain dollar limits per search.

Key Performance Indicators

We manage and assess Heidrick & Struggles' performance through various means, with the primary financial and operational measures including net revenue, operating income, operating margin, Adjusted EBITDA (non-GAAP), and Adjusted EBITDA margin (non-GAAP). Executive Search and Leadership Consulting performance is also measured using consultant headcount. Specific to Executive Search, confirmation trends, consultant productivity and average revenue per search are used to measure performance.

Revenue is driven by market conditions and a combination of the number of executive search engagements and leadership consulting and culture shaping projects and the average revenue per search or project. With the exception of compensation expense, incremental increases in revenue do not necessarily result in proportionate increases in costs, particularly operating and administrative expenses, thus potentially improving operating margins.

The number of consultants, confirmation trends, number of searches or projects completed, productivity levels and the average revenue per search or project will vary from quarter to quarter, affecting net revenue and operating margin.

Our Compensation Model

At the Executive Search consultant level there are fixed and variable components of compensation. Individuals are rewarded for their performance based on a system that directly ties a portion of their compensation to the amount of net revenue for which they are responsible. A portion of the reward may be based upon individual performance against a series of non-financial measures. Credit towards the variable portion of an executive search consultant's compensation is earned by generating net revenue for winning and executing work. Each quarter, we review and update the expected annual performance of all Executive Search consultants and accrue variable compensation accordingly. The amount of variable compensation that is accrued for each Executive Search consultant is based on a tiered payout model. Overall Company performance determines the amount available for total variable compensation. The more net revenue that is generated by the consultant, the higher the percentage credited towards the consultant's variable compensation and thus accrued by our Company as expense. The mix of individual consultants who generate the revenue can significantly affect the total amount of compensation expense recorded, which directly impacts operating margin. As a result, the variable portion of the compensation expense may fluctuate significantly from quarter to quarter. The total variable compensation is discretionary and is based on Company-wide financial targets approved by the Human Resources and Compensation Committee of the Board of Directors.

A portion of our Executive Search consultants' and management cash bonuses is deferred and paid over a three-year vesting period. The compensation expense related to the amounts being deferred is recognized on a graded vesting attribution method over the requisite service period. This service period begins on January 1 of the respective fiscal year and continues through the deferral date, which coincides with our bonus payments in the first quarter of the following year, and for an additional three year vesting period. The deferrals are recorded in Accrued salaries and employee benefits in the Consolidated Balance Sheets.

2016 Overview

Consolidated net revenue was $582.4 million for the year ended December 31, 2016, an increase of $51.2 million or 9.6% compared to December 31, 2015. Consultant productivity measured by net executive search and leadership consulting revenue per consultant was $1.6 million and $1.5 million for the years ended December 31, 2016 and 2015. Average revenue per executive search was $117,700 for the year ended December 31, 2016 compared to $115,300 for the year ended December 31, 2015.

Operating income as a percentage of net revenue was 6.0% in 2016 compared to 6.4% in 2015. Operating income was driven by an increase in net revenue of $51.2 million, partially offset by an increase in salaries and employee benefits expense of $30.7 million and an increase in general and administrative expense of $19.4 million. Salaries and employee benefits expense as a percentage of net revenue was 68.7% in 2016 and 69.5% in 2015. General and administrative expense as a percentage of net revenue was 25.3% in 2016 and 24.0% in 2015.

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We ended the year with combined cash and cash equivalents of $165.0 million, a decrease of $25.4 million compared to $190.5 million at December 31, 2015. The decrease is primarily due to bonus payments, payments for the DSI, Philosophy and JCA acquisitions, capital expenditures, tax extension payments, cash dividend payments and earnout payments, partially offset by cash collections. We pay the majority of bonuses in the first quarter following the year in which they were earned. Employee bonuses are accrued throughout the year and are based on the Company’s performance and the performance of the individual employee. We expect to pay approximately $128.0 million in bonuses related to 2016 performance in March and April 2017. In February 2017, we paid approximately $12.0 million in cash bonuses deferred in prior years.

2017 Outlook

We are currently forecasting 2017 first quarter net revenue of between $140 million and $150 million. Our 2017 first quarter guidance is based upon, among other things, management’s assumptions for the anticipated volume of new executive search confirmations and leadership consulting and culture shaping projects, the current backlog, consultant productivity, consultant retention, the seasonality of our business and average currency rates from December 2016.

Our 2017 first quarter guidance is subject to a number of risks and uncertainties, including those disclosed under Risk Factors (See Item 1A. Risk Factors) and Management’s Discussion and Analysis of Financial Condition and Results of Operations included in this Form 10-K. As such, actual results could vary from these projections.

Results of Operations

The following table summarizes, for the periods indicated, the results of operations (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Revenue			
Revenue before reimbursements (net revenue)	$582,390	$531,139	$494,292
Reimbursements	18,516	17,172	18,947
Total revenue	600,906	548,311	513,239
Operating Expenses			
Salaries and employee benefits	400,070	369,385	337,448
General and administrative	147,087	127,692	130,191
Reimbursed expenses	18,516	17,172	18,947
Total operating expenses	565,673	514,249	486,586
Operating income	35,233	34,062	26,653
Non-operating income (expense)			
Interest, net	244	(122)	(358)
Other, net	2,289	(2,386)	(2,108)
Net non-operating income (expense)	2,533	(2,508)	(2,466)
Income before taxes	37,766	31,554	24,187
Provision for income taxes	22,353	14,422	17,390
Net income	$15,413	$17,132	$6,797
Basic weighted average common shares outstanding	18,540	18,334	18,210
Diluted weighted average common shares outstanding	19,038	18,715	18,432
Basic net income per common share	$0.83	$0.93	$0.37
Diluted net income per common share	$0.81	$0.92	$0.37
Cash dividends paid per share	$0.52	$0.52	$0.52

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The following table summarizes, for the periods indicated, our results of operations as a percentage of revenue before reimbursements (net revenue):

	Year Ended December 31,		
	2016	2015	2014
Revenue:			
Revenue before reimbursements (net revenue)	100.0 %	100.0 %	100.0 %
Reimbursements	3.2	3.2	3.8
Total revenue	103.2	103.2	103.8
Operating expenses:			
Salaries and employee benefits	68.7	69.5	68.3
General and administrative expenses	25.3	24.0	26.3
Reimbursed expenses	3.2	3.2	3.8
Total operating expenses	97.1	96.8	98.4
Operating income	6.0	6.4	5.4
Non-operating expense			
Interest, net	— %	— %	— %
Other, net	0.4	(0.4)	(0.4)
Net non-operating expense	0.4	(0.5)	(0.5)
Income before income taxes	6.5	5.9	4.9
Provision for income taxes	3.8	2.7	3.5
Net income	2.6 %	3.2 %	1.4 %

Note: Totals and subtotals may not equal the sum of individual line items due to rounding.

We operate our executive search services in the Americas; Europe (which includes Africa); and Asia Pacific (which includes the Middle East) and operate our leadership consulting and culture shaping businesses as separate segments (See Note 16, Segment Information).

The following table sets forth, for the periods indicated, our revenue and operating income by segment (in thousands):

	Year Ended December 31,		
	2016	2015	2014
Revenue:			
Executive Search			
Americas	$313,292	$294,606	$253,718
Europe	108,754	92,135	103,416
Asia Pacific	85,319	89,026	83,537
Total Executive Search	507,365	475,767	440,671
Leadership Consulting	38,806	19,045	18,870
Culture Shaping	36,219	36,327	34,751
Revenue before reimbursements (net revenue)	582,390	531,139	494,292
Reimbursements	18,516	17,172	18,947
Total	$600,906	$548,311	$513,239
Operating income (loss):			
Executive Search			
Americas	$73,857	$68,043	$57,370
Europe	6,851	3,644	6,013
Asia Pacific	4,799	5,909	4,348
Total Executive Search	85,507	77,596	67,731
Leadership Consulting	(1,495)	(1,847)	(357)
Culture Shaping	(1,558)	4,913	4,621
Total Segments	82,454	80,662	71,995
Global Operations Support	(47,221)	(46,600)	(45,342)
Total	$35,233	$34,062	$26,653

Year Ended December 31, 2016 compared to year ended December 31, 2015

Total revenue. Consolidated total revenue increased $52.6 million, or 9.6%, to $600.9 million in 2016 from $548.3 million in 2015. The increase in total revenue was primarily due to the increase in revenue before reimbursements (net revenue).

Revenue before reimbursements (net revenue). Consolidated net revenue increased $51.2 million or 9.6%, to $582.4 million in 2016 from $531.1 million in 2015. Foreign exchange rate fluctuations decreased revenue by $11.4 million, or 2.1%. Executive Search net revenue was $507.4 million in 2016, an increase of $31.6 million compared to 2015. The increase in Executive Search net revenue was the result of growth in the Americas and Europe. Leadership Consulting net revenue increased $19.8 million, or 103.8%, to $38.8 million in 2016 from $19.0 million in 2015. The increase in Leadership Consulting net revenue was primarily the result of the Co Company, DSI and Philosophy IB acquisitions. Culture Shaping net revenue was $36.2 million in 2016, a decrease of $0.1 million compared to 2015. The number of Executive Search and Leadership Consulting consultants was 335 and 22, respectively, as of December 31, 2016 compared to 308 and 26, respectively, as of December 31, 2015. Specific to Executive Search, our largest business, productivity as measured by annualized net Executive Search revenue per consultant was $1.6 million and $1.5 million for the years ended December 31, 2016 and 2015, respectively. The number of confirmed searches increased 7.1% compared to 2015. The average revenue per executive search increased to $117,700 for the year ended December 31, 2016 compared to $115,300 for the year ended December 31, 2015.

Salaries and employee benefits. Consolidated salaries and employee benefits expense increased $30.7 million or 8.3%, to $400.1 million in 2016 from $369.4 million in 2015. The increase was due to higher fixed compensation of $31.7 million partially offset by lower variable compensation of $1.0 million. Fixed compensation increased due to higher compensation related to our four recent acquisitions, new hires over the last year with incentives and minimum guarantees that are part of the consultant hiring process, $6.7 million of investments in new and existing partners in our Culture Shaping business and severance related to the repositioning of the Leadership Consulting business. As a result of higher fixed compensation expense

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and an increase in the use of third-party consultants, whose costs are included in General and administrative expenses, variable compensation decreased $1.0 million reflecting the overall profitability of the business. Foreign exchange rate fluctuations decreased total salaries and employee benefits by $6.2 million or 1.7%.

In 2016, we had an average of 1,716 employees, compared to an average of 1,563 employees in 2015. As a percentage of net revenue, salaries and employee benefits expense was 68.7% in 2016, compared to 69.5% in 2015.

General and administrative expenses. Consolidated general and administrative expenses increased $19.4 million, or 15.2%, to $147.1 million for the year ended December 31, 2016 from $127.7 million for the year ended December 31, 2015. More than half of the increase was due to ongoing general and administrative expenses related to our four recent acquisitions including the use of third-party consultants in these businesses to execute work. The increase in general and administrative expenses also reflects the repositioning of our Leadership Consulting business of $1.5 million, higher professional service fees supporting technology implementation and training and development fees, higher unbilled travel and business development expense, and an increase in technology subscription costs reflecting additional headcount throughout the business for cloud-based services.

Foreign exchange rate fluctuations decreased total general and administrative expenses by $3.2 million or 2.5%.

As a percentage of net revenue, general and administrative expenses were 25.3% in 2016, compared to 24.0% in 2015.

Operating income. Our consolidated operating income was $35.2 million in 2016 compared to $34.1 million in 2015. The impacts of foreign exchange rate fluctuations reduced operating income by $1.9 million.

Net non-operating income (expense). Net non-operating income was $2.5 million for 2016, an increase of $5.0 million from net non-operating expense of $2.5 million in 2015.

Net interest income was $0.2 million in 2016, a $0.3 million increase from net interest expense of $0.1 million in 2015. Interest expense decreased $0.3 million due the repayment of outstanding debt in the third quarter of 2015, which had been outstanding during the year ended December 31, 2015.

Other, net was income of $2.3 million in 2016 and expense of $2.4 million in 2015. Other, net increased due to lower net losses on available for sale securities compared to the prior year and decreased losses on the disposal of fixed assets.

Income taxes. See Note 15, Income Taxes.

Executive Search

Americas

The Americas segment reported net revenue of $313.3 million in 2016, an increase of 6.3% from $294.6 million in 2015. The increase in net revenue was due to an increase average revenue per search in addition to an increase in consultant headcount. All practice groups contributed to the increased net revenue with the exception of the Financial Services practice group. The number of consultants was 158 as of December 31, 2016, compared to 146 as of December 31, 2015.

Salaries and employee benefits expense increased $10.9 million from 2015. Fixed compensation increased $11.3 million primarily due to higher base salaries and payroll taxes of $4.2 million, higher minimum guarantee and sign-on bonuses of $1.4 million, higher retirement and benefits and increased deferred compensation due to market fluctuations. Variable compensation decreased $0.4 million primarily due to lower bonus accruals.

General and administrative expenses increased $2.0 million primarily due to professional service fees, office occupancy expenses and internal travel costs.

Operating income was $73.9 million in 2016, an increase of $5.8 million compared to $68.0 million in 2015.

Europe

Europe reported net revenue of $108.7 million in 2016, an increase of 18.0% from $92.1 million in 2015. The increase in net revenue was driven by a 24.7% increase in the number of executive search confirmations as compared to the prior year and an increase in consultant headcount. Our acquisition of JCA Group in August 2016 also contributed to the year-over-year growth in net revenue. Foreign exchange rate fluctuations decreased revenue by $6.7 million or 7.3%. All industry practice groups contributed to net revenue growth except for the Education, Nonprofit & Social Enterprise practice group. The number of consultants was 95 as of December 31, 2016 as compared to 78 as of December 31, 2015.

Salaries and employee benefits expense increased $10.7 million from 2015. Fixed compensation increased $9.2 million due to higher base salaries and payroll taxes of $5.3 million primarily from merit increases, additional headcount related to the JCA Group acquisition and higher minimum guarantees of $3.5 million. Variable compensation increased $1.5 million due to higher bonus accruals for consultant performance.

General and administrative expense increased $2.7 million from 2015 due to higher internal travel costs, amortization and accretion related to the JCA group acquisition and higher professional service fees, partially offset by lower office occupancy costs.

The Europe segment reported operating income of $6.9 million in 2016, an increase of $3.3 million compared to $3.6 million in 2015.

Asia Pacific

Asia Pacific reported net revenue of $85.3 million in 2016, a decrease of 4.2% compared to $89.0 million in 2015. The decrease in net revenue was due to lower average revenue per search and lower consultant headcount. The Consumer Markets and Financial Services practice groups increased net revenue, which was offset by decreases in the Global Technology & Services, Healthcare & Life Sciences, Industrial and Education and Social Enterprise practice groups. The number of consultants was 82 as of December 31, 2016, compared to 84 as of December 31, 2015.

Salaries and employee benefits expense decreased $3.0 million. The decrease in salaries and employee benefits expense is due to lower variable compensation of $4.8 million from lower bonus accruals for consultant performance partially offset by an increase in fixed compensation of $1.8 million as a result of headcount increases and the timing of merit increases.

General and administrative expenses increased $0.4 million primarily due to higher office occupancy expenses and internal travel costs.

The Asia Pacific segment reported operating income of $4.8 million in 2016, a decrease of $1.1 million compared to 2015.

Leadership Consulting

The Leadership Consulting segment reported net revenue of $38.8 million in 2016, an increase of 103.8% compared to $19.0 million in 2015. The increase in net revenue was primarily driven by our DSI and Philosophy IB acquisitions in addition to a full year of results for Co Company, which was acquired in October 2015. Foreign exchange rate fluctuations decreased net revenues by $2.7 million or 14.2%. There were 22 Leadership Consulting consultants at December 31, 2016 compared to 26 at December 31, 2015.

Salaries and employee benefits expense increased $6.0 million compared to the prior year. Fixed compensation increased $4.9 million due to additional headcount related to the DSI and Philosophy IB acquisitions in addition to a full year of expense for Co Company. Variable compensation increased $1.1 million as compared to the prior year.

General and administrative expenses increased $13.4 million primarily as a result of ongoing general and administrative expenses related to our recent acquisitions of DSI, Philosophy and Co Company and their use of third-party consultants to execute work, $1.5 million of costs associated with repositioning of our Leadership Consulting business and higher office occupancy costs.

The Leadership Consulting segment reported an operating loss of $1.5 million in 2016, an improvement of $0.3 million compared to an operating loss of $1.8 million in 2015.

Culture Shaping

The Culture Shaping segment reported net revenue of $36.2 million in 2016, a decrease of 0.3% compared to $36.3 million in 2015. Net revenue decreased due to a decline in the volume of client work.

Salaries and employee benefits expense increased $4.6 million due to $6.7 million of investments in new and existing consultants.

General and administrative expenses increased $1.8 million primarily due to third-party external consultant costs and professional service fees.
The Culture Shaping segment reported an operating loss of $1.6 million in 2016, a decrease of $6.5 million compared to $4.9 million of operating income in 2015.

Global Operations Support
Global Operations Support expenses in 2016 increased $0.6 million or 1.3% to $47.2 million from $46.6 million in 2015.

Salaries and employee benefits expense increased $1.4 million due to additional stock-based compensation expense related to meeting the vesting requirements of the performance share awards for the chief executive officer, higher retirement and benefits expense and higher separation costs.

General and administrative expense decreased $0.8 million due to decreases in internal travel costs, office occupancy expenses and professional service fees that were partially offset by increased taxes and licenses, hiring fees and temporary labor costs.

Year ended December 31, 2015 compared to year ended December 31, 2014

Total revenue. Consolidated total revenue increased $35.1 million, or 6.8%, to $548.3 million in 2015 from $513.2 million in 2014. The increase in total revenue was primarily due to the increase in revenue before reimbursements (net revenue).

Revenue before reimbursements (net revenue). Consolidated net revenue increased $36.8 million or 7.5%, to $531.1 million in 2015 from $494.3 million in 2014. Foreign exchange rate fluctuations decreased revenue by $24.2 million, or 4.9%. Executive Search net revenue was $475.8 million in 2015, an increase of $35.1 million compared to 2014. The increase in Executive Search net revenue was the result of strong growth in all practice groups. Leadership Consulting net revenue increased $0.1 million, or 0.9%, to $19.0 million in 2015 from $18.9 million in 2014. Culture Shaping net revenue was $36.3 million in 2015, an increase of $1.6 million compared to 2014.
The number of Executive Search and Leadership Consulting consultants was 308 and 26, respectively, as of December 31, 2015 compared to 286 and 21, respectively, as of December 31, 2014. Specific to Executive Search, our largest business, productivity as measured by annualized net Executive Search revenue per consultant was $1.5 million for each of the years ended December 31, 2015 and 2014. The number of confirmed searches increased 7.3% compared to 2014. The average revenue per executive search decreased to $115,300 for the year ended December 31, 2015 compared to $116,000 for the year ended December 31, 2015.

Salaries and employee benefits. Consolidated salaries and employee benefits expense increased $32.0 million or 9.5%, to $369.4 million in 2015 from $337.4 million in 2014. Variable compensation increased $18.0 million due to increased production, partially offset by foreign exchange rate fluctuations of $4.5 million. Fixed compensation increased $13.9 million due to higher average headcount and minimum guarantees for new consultant hires. The increase in fixed compensation was partially offset by foreign exchange rate fluctuations of $12.4 million and lower severance costs. Foreign exchange rate fluctuations decreased total salaries and employee benefits by $16.9 million or 5.0%.

In 2015, we had an average of 1,538 employees, compared to an average of 1,477 employees in 2014. As a percentage of net revenue, salaries and employee benefits expense was 69.5% in 2015, compared to 68.3% in 2014.

General and administrative expenses. Consolidated general and administrative expenses decreased $2.5 million, or 1.9%, to $127.7 million for the year ended December 31, 2015 from $130.2 million for the year ended December

31, 2014. The decrease was primarily due to the impact of foreign exchange rates of $5.0 million, lower amortization and accretion expense of $1.2 million and the 2014 state franchise tax matter of $1.3 million, which occurred in 2014 and did not reoccur in 2015. These decreases were partially offset by expenses related to Co Company, higher IT-related costs of $1.4 million, higher legal fees of $1.1 million and higher training costs.

As a percentage of net revenue, general and administrative expenses were 24.0% in 2015, compared to 26.3% in 2014.

Operating income. Our consolidated operating income was $34.1 million in 2015 compared to $26.7 million in 2014. The impacts of foreign exchange rate fluctuations reduced operating income by $2.2 million.

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Net non-operating expense. Net non-operating expense was $2.5 million for 2015 and 2014.

Net interest expense was $0.1 million and $0.4 million in 2015 and 2014, respectively. Interest expense of $0.5 million associated with the Term Loan was partially offset by interest income of $0.4 million for the year ended December 31, 2015.Interest expense of $0.9 million associated with the Term Loan was partially offset by interest income of $0.5 million for the year ended December 31, 2014.

Other, net expense was $2.4 million and $2.1 million in 2015 and 2014. For the year ended December 31, 2015, net other non-operating expense consists primarily of $1.2 million exchange losses from balances which are denominated in non-functional currencies and are not considered permanent in nature, $0.8 million of losses on disposals of fixed assets and $0.6 million of minority interest. For the year ended December 31, 2014, net other non-operating expense consisted primarily of exchange losses from balances which were denominated in non-functional currencies and not considered permanent in nature.

Income taxes. See Note 15, Income Taxes.

Executive Search

Americas

The Americas segment reported net revenue of $294.6 million in 2015, an increase of 16.1% from $253.7 million in 2014. The increase in net revenue was due to higher confirmations and higher average revenue per search. The Financial Services, Healthcare & Life Sciences, Global Technology & Services and Industrial practice groups contributed to the increased net revenue, partially offset by the Consumer Markets practice group. The number of consultants was 146 as of December 31, 2015, compared to 140 as of December 31, 2014.

Salaries and employee benefits expense increased $27.3 million from 2014. Fixed compensation increased $15.0 million due to higher average headcount and minimum guarantees for new consultants hires. Variable compensation increased $12.3 million primarily due to higher production.

General and administrative expenses increased $2.9 million primarily due to higher IT-related costs of $1.0 million, regional conference expenses of $0.7 million, and higher other professional service fees.

Operating income was $68.0 million in 2015, an increase of $10.6 million compared to $57.4 million in 2014.

Europe

Europe reported net revenue of $92.1 million in 2015, a decrease of 10.9% from $103.4 million in 2014. The decrease in revenue was due to foreign exchange rate fluctuations which decreased revenue by $11.2 million, or 10.8%. The decrease in net revenue was across all industry practice groups except the Global Technology & Services practice group. The number of consultants was 78 as of December 31, 2015 and 89 as of December 31, 2014.

Salaries and employee benefits expense decreased $4.9 million from 2014 primarily due to the impact of foreign exchange rate fluctuations of $7.7 million. Fixed compensation decreased $2.2 million due to foreign exchange impacts, partially offset by higher average headcount and minimum guarantees for new consultant hires. Variable compensation decreased $2.7 million due foreign exchange fluctuations.

General and administrative expense decreased $4.0 million from 2014 due to a $2.3 million benefit of foreign currency fluctuations, lower hiring fees and bad debt expense and the non-recurring benefit from 2014 related to the value added tax charge of $0.5 million, partially offset $0.6 million of costs associated with the regional conference in 2015.

The Europe segment reported operating income of $3.6 million in 2015, a decrease of $2.4 million compared to $6.0 million in 2014.

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Asia Pacific

Asia Pacific reported net revenue of $89.0 million in 2015, an increase of 6.6% compared to $83.5 million in 2014. The increase in net revenue was partially offset by the impact of foreign exchange rate fluctuations which lowered net revenue by $7.0 million in 2015. The increase in net revenue was due to higher average revenue per Executive Search. The Global Technology & Services, Healthcare & Life Sciences and Financial Services practice groups increased net revenue, partially offset by the Consumer Markets practice group. The number of consultants was 84 as of December 31, 2015, compared to 78 as of December 31, 2014.

Salaries and employee benefits expense increased $4.6 million. Variable compensation increased $5.8 million due to higher production. Fixed compensation decreased $1.1 million due to foreign exchange rate fluctuations and lower separation costs, partially offset by the cost of higher headcount and minimum guarantees for new consultant hires.

General and administrative expenses decreased $0.7 million primarily due to the benefit of foreign currency fluctuations of $1.1 million, partially offset by $0.5 million of costs associated with the regional conference in 2015.

The Asia Pacific segment reported operating income of $5.9 million in 2015, an increase of $1.6 million compared to 2014.

Leadership Consulting

The Leadership Consulting segment reported net revenue of $19.0 million in 2015, an increase of 0.9% compared to $18.9 million in 2014. The increase in net revenue was primarily driven by our acquisition of Co Company in October 2015. Foreign exchange rate fluctuations decreased net revenues by $1.9 million or 9.8%. There were 26 Leadership Consulting consultants at December 31, 2015 compared to 21 at December 31, 2014.

Salaries and employee benefits expense increased $0.3 million compared to the prior year. Fixed compensation decreased $1.3 million due to foreign exchange rate fluctuations, partially offset by additional headcount related to the Co Company acquisition and higher minimum guarantees. Variable compensation increased $1.6 million as compared to the prior year.

General and administrative expenses increased $1.3 million primarily as a result of ongoing general and administrative expenses related to the acquisition of Co Company in October 2015.

The Leadership Consulting segment reported an operating loss of $1.8 million in 2015, an decrease of $1.4 million compared to an operating loss of $0.4 million in 2015. The impacts of foreign exchange rate fluctuations reduced operating income by $0.5 million.

Culture Shaping

The Culture Shaping segment reported net revenue of $36.3 million in 2015, an increase of 4.5% compared to $34.8 million in 2014. Net revenue increased due to additional projects. Net revenue in 2014 excluded $0.4 million of pre-acquisition deferred revenue that we were unable to recognize as a result of purchase accounting.

Salaries and employee benefits expense increased $2.2 million due to higher average headcount and variable compensation.

General and administrative expenses decreased $0.9 million due to lower amortization and accretion expense of $1.4 million, partially offset by internal meeting costs.

The Culture Shaping segment reported operating income of $4.9 million in 2015, a increase of $0.3 million compared to $4.6 million in 2014.

Global Operations Support

Global Operations Support expenses in 2015 increased $1.3 million or 2.8% to $46.6 million from $45.3 million in 2014.

Salaries and employee benefits expense increased $2.4 million. The increase in salaries and employee benefits expense was due to increases in fixed compensation of $2.2 million from higher support staff headcount and from higher stock-based compensation expense, which increased due to higher performance share unit compensation and a prior year forfeiture of equity awards.

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General and administrative expense decreased $1.1 million. The decrease in general and administrative expense was primarily due to the prior year expense for the global partner meeting of $1.8 million and the state franchise tax matter of $1.3 million, partially offset by higher legal costs of $1.3 million and higher training costs of $1.1 million in 2015.

Liquidity and Capital Resources

General. We continually evaluate our liquidity requirements, capital needs and availability of capital resources based on our operating needs. We believe that our available cash balances together with the funds expected to be generated from operations and funds available under our committed revolving credit facility will be sufficient to finance our operations for the foreseeable future, as well as to finance the cash payments associated with our cash dividends and stock repurchase program.

We pay the non-deferred portion of annual bonuses in the first quarter following the year in which they are earned. Employee bonuses are accrued throughout the year and are based on our performance and the performance of the individual employee.

Lines of Credit. On June 30, 2015, we entered into a Second Amended and Restated Credit Agreement (the “Restated Credit Agreement”) (See Note 10, Line of Credit in the Notes to Consolidated Financial Statements), and replaced our revolving facility and term facility (“Existing Facility”) with a single senior unsecured revolving line of credit. The Restated Credit Agreement has an aggregate commitment of up to $100 million, which includes a sublimit of $25 million for letters of credit, and a $50 million expansion feature. On the amendment date, an aggregate of $26.5 million of term loans
outstanding under the Existing Facility remained outstanding as revolving borrowings under the Replacement Facility. On September 30, 2015, the Company repaid the full outstanding $26.5 million balance of the revolver, in order to reduce the Company's interest expense.
There were no other borrowings made during the years ended 2016 and 2015. During 2016 and 2015 we were in compliance with the financial and other covenants under the Restated Credit Agreement, respectively, and no event of default existed.

Cash and cash equivalents. Cash and cash equivalents at December 31, 2016 were $165.0 million, a decrease of $25.4 million compared to $190.5 million at December 31, 2015. The $165.0 million of cash and cash equivalents at December 31, 2016 includes $76.7 million held by our foreign subsidiaries. A portion of the $76.7 million is considered permanently reinvested in these foreign subsidiaries. If these funds were required to satisfy obligations in the U.S., the repatriation of these funds could cause us to incur additional U.S. income taxes or foreign withholding taxes. Any additional taxes could be offset, in part or in whole, by foreign tax credits. The amount of such taxes and application of tax credits would be dependent on the income tax laws and other circumstances at the time these amounts are repatriated. Based on these variables, it is not practicable to determine the income tax liability that might be incurred if these earnings were to be repatriated. We expect to pay approximately $128.0 million in variable compensation related to 2016 performance in March and April 2017. In February 2017, we paid approximately $12.0 million in variable compensation that was deferred in prior years.

Cash flows provided by operating activities. In 2016, cash provided by operating activities was $24.8 million, primarily reflecting depreciation and amortization expense of $16.4 million, net income of $15.4 million, stock based compensation expense of $6.4 million and an increase in the net retirement and pension plan liability of $4.2 million, partially offset by an increase in accounts receivable of $14.4 million, a change in other assets and liabilities of $3.0 million and an increase in prepaid expenses of $2.3 million.

In 2015, cash provided by operating activities was $57.6 million, principally reflecting an increase in accrued expenses of $37.2 million, higher net income of $17.1 million and depreciation and amortization expense of $13.7

million, partially offset by an increase in accounts receivable of $8.7 million. The accrued expense increase reflects approximately $113 million of bonus payments for 2014 and prior year cash deferrals partially offset by 2015 bonus accruals of $148 million. The accounts receivable increase reflects higher revenue in the fourth quarter of 2015 compared to the fourth quarter of 2014.

In 2014, cash provided by operating activities was $56.8 million, principally reflecting an increase in accrued expenses of $30.0 million, net income of $6.8 million and a valuation adjustment to our German pension plan, partially offset by a decrease in other assets and liabilities of $8.2 million. The accrued expense increase reflects approximately $108 million of bonus accruals for 2014 partially offset by bonus payments of $86 million.

Cash flows used in investing activities. Cash used in investing activities was $27.8 million for the year ended December 31, 2016 primarily due to the acquisitions of JCA Group, DSI and Philosophy IB. This use of cash was partially offset by a

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reduction in restricted cash of $7.2 million primarily due to a release of funds for the retention bonuses paid to certain key executives related to the Senn Delaney acquisition.

Cash used in investing activities was $27.5 million in 2015 primarily due to capital expenditures of $16.4 million, the acquisition of Co Company for $10.3 million, and net purchases of available for sale securities of $0.8 million. Capital expenditures primarily related to office build outs or renovations for eight offices, of which $4.3 million was reimbursed as tenant improvement allowances and reflected as an operating activity. Our capital expenditures consist mostly of office build outs and investments in technology.

Cash used in investing activities was $3.3 million in 2014 primarily due to capital expenditures of $3.4 million.

Cash flows used in financing activities. Cash used in financing activities in 2016 was $20.1 million due to cash dividend payments of $10.0 million, earnout payments for the Senn Delaney, Scambler MacGregor and Co Company acquisitions of $6.8 million, $0.4 million and $0.2 million, respectively, and the payment of employee tax withholdings on equity transactions of $2.7 million.

Cash used in financing activities in 2015 was $46.3 million primarily due to debt repayments of $29.5 million, quarterly cash dividend payments to shareholders of $10.0 million and earnout payments of $5.5 million related to the Senn Delaney and Scambler MacGregor acquisitions.

Cash used in financing activities in 2014 was $19.7 million primarily due quarterly cash dividend payments to shareholders of $9.9 million, debt repayments of $6.0 million, an earnout payment of $3.4 million related to the Senn Delaney acquisition and employee tax withholdings on equity transactions of $0.4 million.

On February 11, 2008, we announced that our Board of Directors authorized management to repurchase shares of our common stock with an aggregate total amount up to $50 million. We intend from time to time and as business conditions warrant, to purchase shares of our common stock on the open market or in negotiated or block trades. No time limit has been set for completion of this program. We did not repurchase any shares of our common stock in 2016. As of December 31, 2016 and December 31, 2015, we have purchased 1,038,670 shares of our common stock for a total of $28.3 million and $21.7 million remains available for future purchases under the authorization. Unless terminated or extended earlier by resolution of the board of directors, the program will expire when the amount authorized for repurchases has been spent.

Off-Balance Sheet Arrangements. We do not have material off-balance sheet arrangements, special purpose entities, trading activities of non-exchange traded contracts or transactions with related parties.

Contractual obligations. The following table presents our known contractual obligations as of December 31, 2016 and the expected timing of cash payments related to these contractual obligations (in millions):

	Payments due for the years ended December 31,						
	2017	2018	2019	2020	2021	Thereafter	Total
Contractual obligations:							
Operating lease obligations	$31.4	$30.7	$29.1	$21.1	$17.4	$ 36.7	$166.4
Asset retirement obligations (1)	0.2	0.2	0.1	0.2	—	1.9	2.6
Total	$31.6	$30.9	$29.2	$21.3	$17.4	$ 38.6	$169.0

(1) Represents the fair value of the obligation associated with the retirement of tangible long-lived assets, primarily related to our obligation at the end of the lease term to return office space to the landlord in its original condition.

In addition to the contractual obligations included in the above table, we have liabilities related to certain employee benefit plans. These liabilities are recorded in our Consolidated Balance Sheet at December 31, 2016. The obligations related to these employee benefit plans are described in Note 11, Employee Benefit Plans, and Note 12, Pension Plan and Life Insurance Contract, in the Notes to Consolidated Financial Statements. As the timing of cash disbursements related to these employee benefit plans is uncertain, we have not included these obligations in the above table. The table excludes our liability for uncertain tax positions including accrued interest and penalties, which totaled $1.0 million as of December 31, 2016, since we cannot predict with reasonable reliability the timing of cash settlements to the respective taxing authorities.

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Application of Critical Accounting Policies and Estimates

General. Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our Consolidated Financial Statements, which have been prepared using accounting principles generally accepted in the United States of America. Our significant accounting policies are discussed in Note 2, Summary of Significant Accounting Policies, in the Notes to Consolidated Financial Statements. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. If actual amounts are ultimately different from previous estimates, the revisions are included in our results of operations for the period in which the actual amounts become known.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, if different estimates that reasonably could have been used, or if changes in the accounting estimates that are reasonably likely to occur periodically, that could materially impact the financial statements. Management believes the following critical accounting policies reflect its more significant estimates and assumptions used in the preparation of the Consolidated Financial Statements.

Revenue recognition. Revenue before reimbursements of out-of-pocket expenses ("net revenue") consists of retainers and indirect expenses billed to clients. For each assignment, we and our client enter into a contract that outlines the general terms and conditions of the assignment. Typically, we are paid a retainer for our executive search services equal to approximately one-third of the estimated first year compensation for the position to be filled. In addition, generally, if the actual compensation of a placed candidate exceeds the estimated compensation, we often are authorized to bill the client for one-third of the excess. Indirect expenses are calculated as a percentage of the retainer with certain dollar limits per search. We generally bill our clients for our retainer and indirect expenses in one-third increments over a three-month period commencing in the month of a client's acceptance of the contract.

Net revenue is recognized when earned and realizable and therefore when the following criteria have been met: (a) persuasive evidence of an arrangement exists, (b) services have been rendered, (c) the fee to our client is fixed or determinable, and (d) collectability is reasonably assured. Taxes collected from clients and remitted to governmental authorities are presented on a net basis. Typically, net revenue from standard executive search engagements is recognized over the expected average period of performance, in proportion to the estimated personnel time incurred to fulfill our obligations under the arrangements. Net revenue in excess of the retainer, resulting from actual compensation of the placed candidate exceeding the estimated compensation, is recognized upon completion of the executive search when the amount of the additional fee is known.

Net revenue associated with culture shaping consulting is recognized proportionally as services are performed. Net revenue associated with licenses to use our culture shaping proprietary materials is typically recognized over the term of the arrangement.

Depending on the terms of that agreement, net revenue from certain leadership consulting and non-standard executive search engagements is either recognized proportionally as services are performed or in accordance with the completion of the engagement deliverables.

Income taxes. Determining the consolidated provision for income tax expense, income tax liabilities and deferred tax assets and liabilities involves judgment. As a global company, we calculate and provide for income taxes in each of the tax jurisdictions in which we operate. This involves estimating current tax exposures in each jurisdiction as well as making judgments regarding the recoverability of deferred tax assets. Tax exposures can involve complex issues and may require an extended period to resolve. Changes in the geographic mix or estimated level of annual income before taxes can affect the overall effective tax rate.

We apply an estimated annual effective tax rate to our cumulative quarterly operating results to determine the provision for income tax expense. In the event there are significant unusual or infrequent items recognized in our quarterly operating results, the tax attributable to that item is recorded in the interim period in which it occurs.

The recognition of deferred tax assets is based on management's belief that it is more likely than not that the tax benefits associated with temporary differences, net operating loss carryforwards and tax credits will be utilized. We assess the recoverability of the deferred tax assets on an ongoing basis. In making this assessment, we consider all positive and negative evidence, and all potential sources of taxable income including scheduled reversals of deferred tax liabilities, tax-planning strategies, projected future taxable income and recent financial performance.

Deferred taxes have been recorded for U.S. income taxes and foreign withholding taxes related to undistributed foreign earnings that are not permanently reinvested. Annually, we assess material changes in estimates of cash, working capital and long-term investment requirements in order to determine whether these earnings should be distributed. If so, an additional provision for taxes may apply, which could materially affect our future effective tax rate.

Goodwill and other intangible assets. We review goodwill for impairment annually. We also review goodwill and long-lived assets; including identifiable intangible assets for impairment whenever events or changes in circumstances indicate that it is more-likely-than-not that the fair value has fallen below the carrying amount of an asset. We review factors such as a significant change in business climate, attrition of key personnel, changes in financial condition or results of operations, a prolonged decline in our stock price and market capitalization, competition, and other factors to determine if an impairment test is necessary. Our annual impairment test begins with a qualitative assessment to determine whether it is necessary to perform the first step of the two-step, fair value based goodwill impairment test. The qualitative assessment includes evaluating whether events and circumstances indicate that it is more-likely-than-not that fair values of reporting units are greater than the carrying values. If the qualitative factors do not indicate that it is more-likely-than-not that the fair values of the reporting units are greater than the carrying values then we perform step 1 of the two-step test. The first step compares the fair value of a reporting unit with its carrying amount, including goodwill. The second step measures the impairment charge and is performed only if the carrying amount of a reporting unit exceeds its fair value as determined in step one. To measure the amount of the impairment loss, the implied fair value of a reporting unit’s goodwill is compared to the carrying amount of that goodwill. If the carrying amount of a reporting unit’s goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination.

The impairment test is considered for each of the Company’s reporting units that have goodwill as defined in the accounting standard for goodwill and intangible assets. The Company has historically operated four reporting units: the Americas; Europe, which includes Africa; Asia Pacific, which includes the Middle East; and Culture Shaping. During the fourth quarter of 2016, the Company revised its reporting unit structure based on the manner in which the Company's chief operating decision maker allocates resources and assesses performance. Under the revised reporting unit structure, the Company operates five reporting units: Americas Executive Search; Europe Executive Search, which includes Africa; Asia Pacific Executive Search, which includes the Middle East; Leadership Consulting; and Culture Shaping. As a result of the change in reporting units, the Company conducted it's annual impairment evaluation for both the former and revised reporting unit structures as required by the accounting standard for goodwill and intangible assets.

During the first step, the fair value of each of our reporting units is determined using a discounted cash flow methodology.

The discounted cash flow approach is dependent on a number of factors including estimates of future market growth and trends, forecasted revenue and costs, capital investments, appropriate discount rates, certain assumptions to allocate shared costs, assets and liabilities, historical and projected performance of our reporting units, the outlook for the executive search industry, and the macroeconomic conditions affecting each of our reporting units. We base our fair value estimates on assumptions we believe to be reasonable, but which are unpredictable and inherently uncertain. The fair value of our reporting units is also impacted by our overall market capitalization and may be impacted by volatility in our stock price and assumed control premium, among other factors. As a result, actual future results may differ from those estimates and may result in a future impairment charge. These assumptions are updated annually, at a minimum, to reflect information concerning our reportable segments.

Additionally, we review long-lived assets, such as property, equipment, and purchased intangibles subject to amortization for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge, equal to the amount by which the carrying amount of the asset exceeds the fair value of the asset, is recognized.

We believe that the accounting estimate related to goodwill and other intangible asset impairment is a critical accounting estimate because the assumptions used are highly susceptible to changes in the operating results and cash flows of our reportable segments.

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Recently Adopted Financial Accounting Standards

In March 2016, the FASB issued ASU No. 2016-09, Stock Compensation: Improvements to Employee Share-Based Payment Accounting, which is intended to simplify several aspects of the accounting for share-based payment transactions including the income tax accounting, classification of awards as either equity or liabilities, the accounting for forfeitures and classification on the statement of cash flows. The standard is effective for annual reporting periods beginning after December 15, 2016 with early adoption permitted. The Company early adopted this standard during the fourth quarter of 2016. The adoption of this standard reduced tax expense by approximately $0.7 million for the year ended December 31, 2016.

Recent Financial Accounting Standards

In November 2016, the Financial Accounting Standards Board ("FASB") issued accounting Standards Update ("ASU") No. 2016-18, Statement of Cash Flows: Restricted Cash, which requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore amounts generally described as restricted cash should be included with cash and cash equivalents when recording the beginning of period and end of period total amounts shown on the statement of cash flows. The Company currently does not include restricted cash amounts in the beginning and ending cash amounts and will change the presentation of the cash flow statement to include restricted cash in the beginning and ending cash totals. The standard is effective for annual reporting periods beginning after December 15, 2017 with early adoption permitted.The Company has not yet determined when it will adopt this guidance. The impact of this change is not expected to be significant to the classification of these activities on the Consolidated Statement of Cash Flows.
In August 2016, the Financial Accounting Standards Board ("FASB") issued accounting Standards Update ("ASU") No. 2016-15, Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments, which is intended to reduce diversity in practice as to how certain cash receipts and cash payments should be presented and classified. The standard is effective for interim and annual reporting periods beginning after December 15, 2017 with early adoption permitted. The Company has evaluated the standard and noted the guidance for contingent consideration payments made after a business combination are applicable to the Condensed Consolidated Statements of Cash Flows. The Company currently classifies all contingent consideration payments as financing activities. The impact of this change is not expected to be significant to the classification of these activities on the Consolidated Statements of Cash Flows.

In February 2016, the FASB issued ASU No. 2016-02, Leases, intended to improve financial reporting about leasing transactions. The new guidance will require entities that lease assets to recognize on their balance sheets the assets and liabilities for the rights and obligations created by those leases and to disclose key information about the leasing arrangements. ASU 2016-02 is effective for interim and annual periods beginning after December 15, 2018 with early adoption permitted. The guidance requires lessees and lessors to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Company is currently evaluating the impact of this accounting guidance. The effect is not known or reasonably estimable at this time.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments: Recognition and Measurement of Financial Assets and Financial Liabilities, which addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments including the recognition of unrealized changes in fair value within net income. The standard is effective for annual reporting periods beginning after December 15, 2017. The Company is currently evaluating the impact of this accounting guidance. The effect is not known or reasonably estimable at this time.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. The ASU requires that an entity recognizes revenue to depict the transfer of promised goods or services to customer in an amount that reflects

the consideration to which the Company expects to be entitled in exchange for these goods or services. The effective date has been deferred for one year to the interim and annual reporting periods beginning after December 15, 2017. The guidance permits the use of either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients or (ii) a retrospective approach with the cumulative effect upon initial adoption recognized at the date of adoption. The Company will adopt the guidance on January 1, 2018 and will apply the modified retrospective method.
The Company is performing its evaluation of ASU No. 2014-09. The Company is paid a retainer for its executive search services equal to approximately one-third of the estimated first year compensation for the position to be filled. If the actual compensation of a placed candidate exceeds the estimated compensation, the Company is often authorized to bill the client for one-third of the excess. The Company currently recognizes revenue associated with the difference between the estimated

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compensation and actual compensation at the time this amount is determinable. Under ASU 2014-09, the difference between estimated compensation and actual compensation is considered variable consideration. The Company will be required to estimate the amount of variable consideration for its executive search services at the time the contract is executed and recognize this variable consideration as the Company delivers services to the client. The Company is still evaluating the financial impact of this change. The Company is currently evaluating the impact of this accounting guidance for its other revenue streams. The effect is not known or reasonably estimable at this time.

Quarterly Financial Information (Unaudited)

The following table sets forth certain financial information for each quarter of 2016 and 2015. The information is derived from our quarterly consolidated financial statements which are unaudited but which, in the opinion of management, have been prepared on the same basis as the audited annual consolidated financial statements included in this document. The consolidated financial data shown below should be read in conjunction with the consolidated financial statements and notes thereto. The operating results for any quarter are not necessarily indicative of results for any future period.

	Quarter Ended							
	2016				2015			
	Mar. 31	Jun. 30	Sept. 30	Dec. 31	Mar. 31	Jun. 30	Sept. 30	Dec. 31
Revenue before reimbursements (net revenue)	$130,189	$148,861	$143,519	$159,821	$115,153	$133,045	$138,421	$144,520
Operating income	3,868	11,694	12,006	7,665	6,672	9,172	12,933	5,285
Income before income taxes	3,989	11,781	12,388	9,608	6,526	9,118	11,137	4,773
Provision for income taxes	2,664	5,126	5,448	9,115	3,100	4,162	3,647	3,513
Net income	$1,325	$6,655	$6,940	$493	$3,426	$4,956	$7,490	$1,260
Basic earnings per common share	$0.07	$0.36	$0.37	$0.03	$0.19	$0.27	$0.41	$0.07
Diluted earnings per common share	$0.07	$0.35	$0.37	$0.01	$0.18	$0.27	$0.40	$0.07
Cash dividends paid per share	$0.13	$0.13	$0.13	$0.13	$0.13	$0.13	$0.13	$0.13

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Currency market risk. With our operations in the Americas, Europe and Asia Pacific, we conduct business using various currencies. Revenue earned in each country is generally matched with the associated expenses incurred, thereby reducing currency risk to earnings. However, because certain assets and liabilities are denominated in currencies other than the U.S. dollar, changes in currency rates may cause fluctuations in the valuation of such assets and liabilities. As the local currency of our subsidiaries has generally been designated as the functional currency, we are affected by the translation of foreign currency financial statements into U.S. dollars. A 10% change in the average exchange rate for currencies of all foreign countries in which we operate would have increased or decreased our 2016 net income by approximately $0.7 million. For financial information by segment, see Note 16, Segment Information, in the Notes to Consolidated Financial Statements.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Heidrick & Struggles International, Inc.:

We have audited the accompanying consolidated balance sheets of Heidrick & Struggles International, Inc. and subsidiaries (the Company) as of December 31, 2016 and 2015, and the related consolidated statements of comprehensive income, changes in stockholders’ equity, and cash flows for each of the years in the three-year period ended December 31, 2016. We also have audited the Company’s internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company’s management is responsible for these consolidated 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’s Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company’s internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. 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.

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.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Heidrick & Struggles International, Inc. and subsidiaries as of December 31, 2016 and 2015, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) .

/s/ KPMG LLP

Chicago, Illinois
March 23, 2017

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	December 31, 2016	December 31, 2015
Current assets:		
Cash and cash equivalents	$165,011	$190,452
Accounts receivable, net	93,191	76,058
Prepaid expenses	21,602	19,197
Other current assets	13,779	18,447
Income taxes recoverable	4,847	4,809
Total current assets	298,430	308,963
Non-current assets:		
Property and equipment, net	35,099	36,498
Assets designated for retirement and pension plans	15,698	16,857
Investments	17,346	14,145
Other non-current assets	9,322	11,115
Goodwill	151,844	131,122
Other intangible assets, net	20,690	18,687
Deferred income taxes	33,073	35,331
Total non-current assets	283,072	263,755
Total assets	$581,502	$572,718
Current liabilities:		
Accounts payable	$7,952	$6,150
Accrued salaries and employee benefits	155,523	158,875
Deferred revenue, net	28,367	29,724
Other current liabilities	24,133	31,239
Income taxes payable	4,617	3,442
Total current liabilities	220,592	229,430
Non-current liabilities:		
Accrued salaries and employee benefits	34,993	32,690
Retirement and pension plans	39,039	35,949
Other non-current liabilities	28,288	19,847
Total non-current liabilities	102,320	88,486
Total liabilities	322,912	317,916
Commitments and contingencies (Note 18)		
Stockholders' equity:		
Preferred stock, $0.01 par value, 10,000,000 shares authorized, no shares issued at December 31, 2016 and December 31, 2015	—	—
Common stock, $0.01 par value, 100,000,000 shares authorized, 19,585,777 shares issued, 18,578,176 and 18,379,398 shares outstanding at December 31, 2016 and December 31, 2015, respectively	196	196
Treasury stock at cost, 1,007,601 and 1,206,379 shares at December 31, 2016 and December 31, 2015, respectively	(32,915)	(39,583)
Additional paid in capital	229,957	232,358
Retained earnings	58,030	52,572
Accumulated other comprehensive income	3,322	9,259
Total stockholders' equity	258,590	254,802

Total liabilities and stockholders’ equity	$581,502	$572,718

The accompanying notes to Consolidated Financial Statements are an integral part of these statements.

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands, except per share amounts)

	December 31, 2016	2015	2014
Revenue:			
Revenue before reimbursements (net revenue)	$582,390	$531,139	$494,292
Reimbursements	18,516	17,172	18,947
Total revenue	600,906	548,311	513,239
Operating expenses:			
Salaries and employee benefits	400,070	369,385	337,448
General and administrative expenses	147,087	127,692	130,191
Reimbursed expenses	18,516	17,172	18,947
Total operating expenses	565,673	514,249	486,586
Operating income	35,233	34,062	26,653
Non-operating income (expense):			
Interest, net	244	(122)	(358)
Other, net	2,289	(2,386)	(2,108)
Net non-operating income (expense)	2,533	(2,508)	(2,466)
Income before income taxes	37,766	31,554	24,187
Provision for income taxes	22,353	14,422	17,390
Net income	15,413	17,132	6,797
Other comprehensive (loss) income, net of tax:			
Foreign currency translation adjustment	(6,271)	(1,811)	(1,235)
Net unrealized gain (loss) on available-for-sale investments	1,035	(789)	262
Pension gain (loss) adjustment	(701)	714	(2,736)
Unrealized loss on cash flow hedge	—	(78)	(37)
Other comprehensive loss, net of tax	(5,937)	(1,964)	(3,746)
Comprehensive income	$9,476	$15,168	$3,051
Basic weighted average common shares outstanding	18,540	18,334	18,210
Diluted weighted average common shares outstanding	19,038	18,715	18,432
Basic net income per common share	$0.83	$0.93	$0.37
Diluted net income per common share	$0.81	$0.92	$0.37
Cash dividends paid per share	$0.52	$0.52	$0.52

The accompanying notes to Consolidated Financial Statements are an integral part of these statements.

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HEIDRICK & STRUGGLES INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(In thousands)

	Common Stock		Treasury Stock		Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares	Amount	Shares	Amount				
Balance at December 31, 2013	19,586	$ 196	1,452	$(47,811)	$232,008	$48,511	$ 14,969	$247,873
Net income	—	—	—	—	—	6,797	—	6,797
Other comprehensive loss, net of tax	—	—	—	—	—	—	(3,746)	(3,746)
Treasury and common stock transactions:								
Stock-based compensation	—	—	—	—	3,579	—	—	3,579
Vesting of equity, net of tax withholdings	—	—	(82)	2,737	(3,142)	—	—	(405)
Re-issuance of treasury stock	—	—	(24)	813	(363)	—	—	450
Cash dividends declared ($0.52 per share)	—	—	—	—	—	(9,481)	—	(9,481)
Dividend equivalents on restricted stock units	—	—	—	—	—	(396)	—	(396)
Tax deficit related to stock-based compensation	—	—	—	—	(7)	—	—	(7)
Balance at December 31, 2014	19,586	196	1,346	(44,261)	232,075	45,431	11,223	244,664
Net income	—	—	—	—	—	17,132	—	17,132
Other comprehensive loss, net of tax	—	—	—	—	—	—	(1,964)	(1,964)
Treasury and common stock transactions:								
Stock-based compensation	—	—	—	—	5,066	—	—	5,066
Vesting of equity, net of tax withholdings	—	—	(123)	4,094	(4,972)	—	—	(878)
Re-issuance of treasury stock	—	—	(17)	584	(135)	—	—	449
Cash dividends declared ($0.52 per share)	—	—	—	—	—	(9,550)	—	(9,550)
Dividend equivalents on restricted stock units	—	—	—	—	—	(441)	—	(441)
Tax surplus related to stock-based compensation	—	—	—	—	324	—	—	324
Balance at December 31, 2015	19,586	196	1,206	(39,583)	232,358	52,572	9,259	254,802
Net income	—	—	—	—	—	15,413	—	15,413
Other comprehensive loss, net of tax	—	—	—	—	—	—	(5,937)	(5,937)
Treasury and common stock transactions:								

Stock-based compensation	—	—	—	—	6,393	—	—	6,393
Vesting of equity, net of tax withholdings	—	—	(167)	5,636	(8,324)	—	—	(2,688)
Re-issuance of treasury stock	—	—	(31)	1,032	(470)	—	—	562
Cash dividends declared ($0.52 per share)	—	—	—	—	—	(9,668)	—	(9,668)
Dividend equivalents on restricted stock units	—	—	—	—				