

COMPUTER TASK GROUP INC

Form 10-Q

August 02, 2012

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED June 29, 2012

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

FOR THE TRANSITION PERIOD FROM TO

Commission file number 001-9410

COMPUTER TASK GROUP, INCORPORATED

(Exact name of Registrant as specified in its charter)

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New York
(State of incorporation)

16-0912632
(IRS Employer Identification No.)

800 Delaware Avenue, Buffalo, New York
(Address of principal executive offices)

14209
(Zip Code)

Registrant's telephone number, including area code: (716) 882-8000

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

| Title of each class | Shares outstanding at July 19, 2012 |
|---|--|
| Common stock, par value \$.01 per share | 18,454,819 |

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****COMPUTER TASK GROUP, INCORPORATED****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(amounts in thousands, except per share data)

(Unaudited)

| | For the Quarter Ended | | For the Two Quarters Ended | |
|--|--------------------------|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| Revenue | \$ 106,705 | \$ 98,327 | \$ 210,072 | \$ 194,236 |
| Direct costs | 83,810 | 77,594 | 165,325 | 153,706 |
| Selling, general and administrative expenses | 16,752 | 16,056 | 33,005 | 31,254 |
| Operating income | 6,143 | 4,677 | 11,742 | 9,276 |
| Interest and other income | 476 | 32 | 520 | 63 |
| Interest and other expense | 92 | 80 | 186 | 148 |
| Income before income taxes | 6,527 | 4,629 | 12,076 | 9,191 |
| Provision for income taxes | 2,404 | 1,799 | 4,593 | 3,533 |
| Net income | \$ 4,123 | \$ 2,830 | \$ 7,483 | \$ 5,658 |
| Net income per share: | | | | |
| Basic | \$ 0.27 | \$ 0.19 | \$ 0.49 | \$ 0.38 |
| Diluted | \$ 0.25 | \$ 0.17 | \$ 0.45 | \$ 0.34 |
| Weighted average shares outstanding: | | | | |
| Basic | 15,123 | 15,050 | 15,147 | 14,909 |
| Diluted | 16,747 | 16,864 | 16,810 | 16,759 |

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

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COMPUTER TASK GROUP, INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(amounts in thousands)

(Unaudited)

| | For the Quarter Ended | | For the Two Quarters Ended | |
|---|--------------------------|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| Net income | \$ 4,123 | \$ 2,830 | \$ 7,483 | \$ 5,658 |
| Change in foreign currency | (989) | 255 | (578) | 1,163 |
| Change in pension loss, net of tax of \$28 and \$23 in the 2012 and 2011 second quarter, respectively, and \$58 and \$46 in the first two quarters of 2012 and 2011, respectively | 130 | 38 | 144 | 78 |
| Comprehensive income | \$ 3,264 | \$ 3,123 | \$ 7,049 | \$ 6,899 |

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

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COMPUTER TASK GROUP, INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEETS

(amounts in thousands, except share balances)

(Unaudited)

| | June 29, 2012 | Dec. 31, 2011 |
|---|-------------------|-------------------|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 23,624 | \$ 22,414 |
| Accounts receivable, net of allowances of \$871 and \$965 in 2012 and 2011, respectively | 71,928 | 67,801 |
| Prepaid and other current assets | 2,206 | 1,876 |
| Deferred income taxes | 1,130 | 1,221 |
| Total current assets | 98,888 | 93,312 |
| Property, equipment and capitalized software net of accumulated depreciation and amortization of \$18,469 and \$17,532 in 2012 and 2011, respectively | 7,249 | 7,969 |
| Goodwill | 35,678 | 35,678 |
| Deferred income taxes | 7,439 | 7,062 |
| Other assets | 3,918 | 2,921 |
| Investments | 683 | 550 |
| Total assets | \$ 153,855 | \$ 147,492 |
| Liabilities and Shareholders' Equity | | |
| Current Liabilities: | | |
| Accounts payable | \$ 11,768 | \$ 9,532 |
| Accrued compensation | 30,950 | 30,971 |
| Advance billings on contracts | 1,752 | 1,756 |
| Other current liabilities | 3,979 | 3,972 |
| Income taxes payable | 697 | 1,695 |
| Total current liabilities | 49,146 | 47,926 |
| Deferred compensation benefits | 9,938 | 10,231 |
| Other long-term liabilities | 532 | 530 |
| Total liabilities | 59,616 | 58,687 |
| Shareholders' Equity: | | |
| Common stock, par value \$0.01 per share, 150,000,000 shares authorized; 27,017,824 shares issued | 270 | 270 |
| Capital in excess of par value | 117,004 | 115,895 |
| Retained earnings | 90,962 | 83,479 |
| Less: Treasury stock of 8,558,442 and 8,540,864 shares at cost in 2012 and 2011, respectively | (49,989) | (47,320) |
| Stock Trusts of 3,363,351 shares at cost in both periods | (55,083) | (55,083) |
| Other | (260) | (206) |
| Accumulated other comprehensive loss | (8,665) | (8,230) |
| Total shareholders' equity | 94,239 | 88,805 |
| Total liabilities and shareholders' equity | \$ 153,855 | \$ 147,492 |

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

Table of Contents**COMPUTER TASK GROUP, INCORPORATED****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(amounts in thousands)

(Unaudited)

| | For the Two Quarters Ended | |
|---|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 |
| Cash flow from operating activities: | | |
| Net income | \$ 7,483 | \$ 5,658 |
| Adjustments: | | |
| Depreciation and amortization expense | 1,304 | 978 |
| Equity-based compensation expense | 985 | 696 |
| Deferred income taxes | (376) | (222) |
| Deferred compensation | 188 | (20) |
| (Gain) loss on sales of property and equipment | 5 | (2) |
| Changes in assets and liabilities: | | |
| Increase in accounts receivable | (4,651) | (7,922) |
| Increase in prepaid and other current assets | (365) | (170) |
| Increase in other assets | (997) | (1,428) |
| Increase (decrease) in accounts payable | 674 | (284) |
| Increase in accrued compensation | 195 | 619 |
| Decrease in income taxes payable | (962) | (1,492) |
| Increase (decrease) in advance billings on contracts | 10 | (837) |
| Increase in other current liabilities | 94 | 70 |
| Increase in other long-term liabilities | 8 | 18 |
| Net cash provided by (used in) operating activities | 3,595 | (4,338) |
| Cash flow from investing activities: | | |
| Additions to property and equipment | (623) | (846) |
| Additions to capitalized software | | (351) |
| Deferred compensation plan investments, net | (112) | (109) |
| Proceeds from sales of property and equipment | 2 | 22 |
| Net cash used in investing activities | (733) | (1,284) |
| Cash flow from financing activities: | | |
| Proceeds from stock option plan exercises | 434 | 1,778 |
| Excess tax benefits from equity-based compensation | 640 | 1,714 |
| Proceeds from Employee Stock Purchase Plan | 145 | 138 |
| Change in cash overdraft, net | 1,221 | 609 |
| Purchase of stock for treasury | (3,608) | (1,177) |
| Net cash provided by (used in) financing activities | (1,168) | 3,062 |
| Effect of exchange rates on cash and cash equivalents | (484) | 725 |
| Net increase (decrease) in cash and cash equivalents | 1,210 | (1,835) |
| Cash and cash equivalents at beginning of year | 22,414 | 14,837 |

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| | | |
|---|-----------|-----------|
| Cash and cash equivalents at end of quarter | \$ 23,624 | \$ 13,002 |
|---|-----------|-----------|

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

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COMPUTER TASK GROUP, INCORPORATED

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Financial Statements

The condensed consolidated financial statements included herein reflect, in the opinion of the management of Computer Task Group, Incorporated (CTG or the Company), all normal recurring adjustments necessary to present fairly the condensed consolidated financial position, results of operations and comprehensive income, and cash flows for the periods presented.

The Company's fiscal year-end is December 31. During the year, the quarters generally consist of a 13-week fiscal quarter where the last day of each of the first three quarters is a Friday. The 2012 second quarter began on March 31, 2012 and ended on June 29, 2012. The 2011 second quarter began on April 2, 2011 and ended July 1, 2011. There were 64 billable days in both the second quarters of 2012 and 2011, and 128 and 129 billable days in the first two quarters of 2012 and 2011, respectively.

2. Summary of Significant Accounting Policies

Basis of Presentation

These condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to the SEC rules and regulations. The preparation of financial statements and related disclosures in conformity with U.S. generally accepted accounting principles requires the Company's management to make estimates, judgments and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. Such estimates include, but are not limited to, the valuation of goodwill, valuation allowances for deferred tax assets, actuarial assumptions including discount rates and expected rates of return on assets, as applicable, for the Company's defined benefit and postretirement benefit plans, the allowance for doubtful accounts receivable, assumptions underlying stock option valuation, investment valuation, legal matters, other contingencies, and progress toward completion and direct profit or loss on contracts. Management believes that the information and disclosures provided herein are adequate to present fairly the condensed consolidated financial position, results of operations and comprehensive income, and cash flows of the Company. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's latest Annual Report on Form 10-K filed with the SEC.

The Company operates in one industry segment, providing Information Technology (IT) services to its clients. These services include IT solutions and IT staffing. CTG provides these primary services to all of the markets that it serves. The services provided typically encompass the IT business solution life cycle, including phases for planning, developing, implementing, managing, and ultimately maintaining the IT solution. A typical customer is an organization with large, complex information and data processing requirements.

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IT solutions and IT staffing revenue as a percentage of total revenue for the quarter and two quarters ended June 29, 2012 and July 1, 2011 are as follows:

| | For the Quarter Ended | | For the Two Quarters Ended | |
|--------------|--------------------------|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| IT solutions | 42% | 37% | 41% | 36% |
| IT staffing | 58% | 63% | 59% | 64% |
| Total | 100% | 100% | 100% | 100% |

The Company promotes a significant portion of its services through four vertical market focus areas: Technology Service Providers, Healthcare (which includes services provided to healthcare providers, health insurers, and life sciences companies), Energy and Financial Services. The Company focuses on these four vertical areas as it believes that these areas are either higher growth markets than the general IT services market and the general economy, or are areas that provide greater potential for the Company's growth due to the size of the vertical market. The remainder of CTG's revenue is derived from general markets.

The Company's revenue by vertical market as a percentage of total revenue for the quarter and two quarters ended June 29, 2012 and July 1, 2011 are as follows:

| | For the Quarter Ended | | For the Two Quarters Ended | |
|------------------------------|--------------------------|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| Healthcare | 33% | 29% | 32% | 28% |
| Technology service providers | 31% | 35% | 32% | 35% |
| Financial services | 6% | 6% | 6% | 7% |
| Energy | 6% | 6% | 6% | 6% |
| General markets | 24% | 24% | 24% | 24% |
| Total | 100% | 100% | 100% | 100% |

Fair Value

Fair value is defined as the exchange price that would be received for an asset or paid for a liability in the principal or most advantageous market for the asset or liability, in an orderly transaction between market participants. The Company utilizes a fair value hierarchy for its assets and liabilities, as applicable, based upon three levels of input, which are:

Level 1 quoted prices in active markets for identical assets or liabilities (observable)

Level 2 inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in inactive markets, or other inputs that are observable or can be supported by observable market data for essentially the full term of the asset or liability (observable)

Level 3 unobservable inputs that are supported by little or no market activity, but are significant to determining the fair value of the asset or liability (unobservable)

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At June 29, 2012 and December 31, 2011, the reported balances of the Company's cash and cash equivalents of \$23.6 million and \$22.4 million, respectively, approximated fair value.

The Company is also allowed to elect an irrevocable option to measure, on a contract by contract basis, specific financial instruments and certain other items that are currently not being measured at fair value. The Company did not elect to measure on a fair value basis any of its individual contracts during the quarters or year-to-date periods ended June 29, 2012 or July 1, 2011.

Life Insurance Policies

The Company has purchased life insurance on the lives of certain plan participants in the non-qualified defined-benefit Executive Supplemental Benefit Plan. Those policies have generated cash surrender value, and the Company has taken loans against the policies. At June 29, 2012 and December 31, 2011, these insurance policies have a gross cash surrender value of \$26.9 million and \$27.4 million, loans have been taken totaling \$24.1 million and \$25.6 million, respectively, and the net cash surrender value balance of \$2.8 million and \$1.8 million, respectively, is included on the condensed consolidated balance sheet in "Other Assets" under non-current assets.

During the 2012 second quarter, one of the plan participants passed away. The company received non-taxable net proceeds and recorded a gain, included in interest and other income, from the participant's life insurance in the 2012 second quarter totaling approximately \$0.4 million.

Taxes Collected from Customers

In instances where the Company collects taxes from its customers for remittance to governmental authorities, primarily in its European operations, revenue and expenses are not recorded at gross amounts as such taxes are presented on a net basis.

Cash and Cash Equivalents, and Cash Overdrafts

For the purposes of the statement of cash flows, cash and cash equivalents are defined as cash on hand, demand deposits, and short-term, highly liquid investments with a maturity of three months or less. The Company had no cash equivalents at June 29, 2012 or December 31, 2011. Additionally, as the Company does not fund its bank accounts for checks it has written until the checks are presented to the bank for payment, the balance representing change in cash overdraft, net on the condensed consolidated statements of cash flows represents the increase or decrease in outstanding checks for the periods presented.

Capitalized Software Costs - Projects Developed for Internal Use

The Company did not record any capitalized software costs during the quarter or two quarters ended June 29, 2012, and as of that date had capitalized a total of \$5.1 million. Accumulated amortization for these projects, with amortization periods ranging from three to five years, totaled \$2.2 million as of June 29, 2012.

During the quarter and two quarters ended July 1, 2011, the Company recorded capitalized software costs of \$0.1 million and \$0.4 million, respectively, and as of that date had capitalized a total of \$5.1 million. Accumulated amortization for these projects totaled \$0.8 million as of July 1, 2011.

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The Company has several guarantees in place in our European operations which support office leases and performance under government projects. These guarantees totaled approximately \$2.1 million at June 29, 2012.

3. Net Income Per Share

Basic and diluted earnings per share for the quarter and two quarters ended June 29, 2012 and July 1, 2011 are as follows:

| | For the Quarter Ended | | For the Two Quarters Ended | |
|--|---|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| | (amounts in thousands, except share data) | | | |
| Weighted-average number of shares outstanding during period | 15,123 | 15,050 | 15,147 | 14,909 |
| Common stock equivalents - incremental shares, primarily stock options | 1,624 | 1,814 | 1,663 | 1,850 |
| Number of shares on which earnings per share is based | 16,747 | 16,864 | 16,810 | 16,759 |
| Net income | \$ 4,123 | \$ 2,830 | \$ 7,483 | \$ 5,658 |
| Net income per share: | | | | |
| Basic | \$ 0.27 | \$ 0.19 | \$ 0.49 | \$ 0.38 |
| Diluted | \$ 0.25 | \$ 0.17 | \$ 0.45 | \$ 0.34 |

Certain options representing 0.5 million and 0.2 million shares of common stock were outstanding at June 29, 2012 and July 1, 2011, respectively, but were not included in the computation of diluted earnings per share as they were anti-dilutive.

4. Investments

The Company's investments consist of mutual funds which are part of the Computer Task Group, Incorporated Non-qualified Key Employee Deferred Compensation Plan and the Non-employee Director Deferred Compensation Plan. At June 29, 2012 and December 31, 2011, the Company's investment balances, which are classified as trading securities, totaled approximately \$0.7 million and \$0.6 million, respectively, and are measured at fair value. As there is an active trading market for these funds, fair value was determined using Level 1 inputs (see Fair Value in Note 2). Unrealized gains and losses on these securities are recorded in earnings and were nominal in both the 2012 and 2011 second quarters and year-to-date periods.

Table of Contents**5. Accumulated Other Comprehensive Loss**

The components that make up accumulated other comprehensive loss on the condensed consolidated balance sheets at June 29, 2012 and December 31, 2011 are as follows:

| | June 29, 2012 | Dec. 31, 2011 |
|---|--------------------------|--------------------------|
| | (amounts in thousands) | |
| Foreign currency adjustment | \$ (5,202) | \$ (4,624) |
| Pension loss adjustment, net of tax of \$1,377 in 2012, and \$1,436 in 2011 | (3,463) | (3,606) |
| Accumulated other comprehensive loss | \$ (8,665) | \$ (8,230) |

6. Income Taxes

The Company's effective tax rate (ETR) is calculated quarterly based upon current assumptions relating to the full year's estimated operating results and various tax-related items. The Company's normal annual ETR typically ranges from 38% to 42% of pre-tax income. The 2012 second quarter ETR was 36.8% and the 2012 year-to-date ETR was 38.0%. The Company received \$0.4 million of non-taxable life insurance proceeds for one of its previous chief executive officers that passed away in the 2012 second quarter. The 2011 second quarter ETR was 38.9% and the 2011 year-to-date ETR was 38.4%, both of which were within the Company's expected normal annual ETR.

7. Deferred Compensation and Other Benefits

The Company maintains a non-qualified defined-benefit Executive Supplemental Benefit Plan (ESBP) that provides certain former key executives with deferred compensation benefits, based on years of service and base compensation, payable during retirement. The ESBP was amended as of November 1994 to freeze benefits for participants at that time.

Net periodic pension cost for the quarter and two quarters ended June 29, 2012 and July 1, 2011 for the ESBP are as follows:

| | For the Quarter Ended | | For the Two Quarters Ended | |
|---------------------------------------|----------------------------------|-------------------------|---------------------------------------|-------------------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| | (amounts in thousands) | | | |
| Interest cost | \$ 85 | \$ 102 | \$ 170 | \$ 204 |
| Amortization of unrecognized net loss | 70 | 52 | 140 | 104 |
| Net periodic pension cost | \$ 155 | \$ 154 | \$ 310 | \$ 308 |

The ESBP is deemed to be unfunded as the Company has not specifically identified assets to be used to discharge the deferred compensation benefit liabilities. The Company has purchased insurance on the lives of certain plan participants in amounts deemed to be sufficient to reimburse the Company for the costs associated with the plan for those participants. The Company does not anticipate making contributions to the plan other than for benefit payments as required for the remainder of 2012 or in future years.

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The Company also retained a contributory defined-benefit plan for its previous employees located in The Netherlands (NDBP) when the Company disposed of its subsidiary CTG Nederland B.V. Benefits paid are a function of a percentage of career average pay. The plan was curtailed for additional contributions in January 2003. Net periodic pension cost was approximately \$16,000 and \$1,000 in the 2012 and 2011 second quarters, respectively, and \$32,000 and \$2,000 in the year-to-date periods ended June 29, 2012 and July 1, 2011, respectively.

The Company does not anticipate making significant contributions to the NDBP in 2012 or future years as the NDBP is nearly fully funded. The assets for the NDBP are held by Aegon, a financial services firm located in The Netherlands. The assets for the plan are included in a general portfolio of government bonds, a portion of which is allocated to the NDBP based upon the estimated pension liability associated with the plan. The fair market value of the plan's assets equals the amount allocated to the NDBP at any point in time. The fair value of the assets is determined using a Level 3 methodology (see note 2 Fair Value), including using assumptions such as expected market rates of return, equity and interest rate volatility, credit risk, correlations of market returns, and discount rates. The plan investments have a targeted minimum return to the Company of 4%, which is consistent with historical returns and the 4% return guaranteed to the participants of the plan. The Company, in conjunction with Aegon, continues to maintain the current investment strategy of investing plan assets solely in government bonds throughout 2012.

The change in the fair value of the plan assets for the NDBP for the two quarters ended June 29, 2012 and July 1, 2011 are as follows:

| | For the Two Quarters Ended | |
|---|---------------------------------------|-------------------------|
| | June 29, 2012 | July 1, 2011 |
| | (amounts in thousands) | |
| Fair value of plan assets at beginning of year | \$ 7,811 | \$ 7,831 |
| Return on plan assets | 156 | 166 |
| Contributions | | 42 |
| Benefits paid | (55) | (53) |
| Effect of exchange rate changes | (300) | 692 |
| Fair value of plan assets at end of quarter | \$ 7,612 | \$ 8,678 |

The Company maintains the Key Employee Non-Qualified Deferred Compensation Plan, a defined-contribution plan for certain key executives. Company contributions to this plan, if any, are based on annually defined financial performance objectives. The Company made contributions to this plan for amounts earned in 2011 totaling \$0.4 million in the 2012 first quarter. The investments in the plan are included in the total assets of the Company, and are discussed in Note 4, Investments. Participants in the plan have the ability to exchange a portion of their investments for stock units which represent shares of the Company's common stock. In exchange for the funds received, the Company will issue stock out of treasury stock equivalent to the number of share units received by each participant. These shares of common stock are not entitled to any voting rights and the holders will not receive dividends if any are paid. The shares are being held by the Company, and will be released to the participants as prescribed by their respective payment elections under the plan.

The Company maintains the Non-Employee Director Deferred Compensation Plan for its non-employee directors. Cash contributions to the plan for one of these directors during the 2012 second quarter and year-to-date period were \$0.1 million. At the time the contributions were made, the non-employee director elected to exchange his cash contributions to the plan for stock units which represent shares of the Company's common stock. Consistent with the Key Employee Non-Qualified Deferred Compensation Plan, in exchange for funds received, the Company issued stock out of treasury stock equivalent to the number of share units received by the participant. These shares of common stock are not entitled to any voting rights and the holder will not receive dividends if any are paid. The shares are being held by the Company, and will be released to the non-employee director as prescribed by their respective payment election under the plan.

Table of Contents**8. Equity-based Compensation**

During both the second quarters of 2012 and 2011, the Company granted stock options to certain of its independent directors, and in 2012, to one of its employees. The Company utilizes the Black-Scholes option-pricing model to estimate the fair value of stock options granted on the date of grant. The stock options granted, the weighted-average fair value of an option, and the weighted-average assumptions used to calculate the fair value of a stock option for the respective quarters are as follows:

| | For the | |
|-----------------------------|------------------|-----------------|
| | Quarter ended | |
| | June 29, 2012 | July 1, 2011 |
| Stock options granted | 106,500 | 120,000 |
| Weighted-average fair value | \$ 3.75 | \$ 2.83 |
| Expected volatility | 58.4% | 47.9% |
| Risk-free interest rate | 0.17% | 0.20% |
| Expected term (years) | 1.5 | 1.2 |
| Expected dividend yield | 0.0% | 0.0% |

The exercise price of stock options granted by the Company is equal to the closing market price on the date of grant. The Company used historical volatility calculated using daily closing prices for its common stock over periods that match the expected term of the granted option to estimate the expected volatility for its stock option grants. The risk-free interest rate assumption was based upon U.S. Treasury yields appropriate for the expected term of the Company's stock options based upon the date of grant. The expected term of the stock options granted was based upon the options' expected vesting schedule and historical exercise patterns. The expected dividend yield was based upon the Company's recent history of not paying dividends, and the expectation of not paying dividends in the foreseeable future.

9. Treasury Stock

During the 2012 second quarter, the Company used approximately \$2.7 million to purchase 204,000 shares of its stock for treasury pursuant to the Company's share repurchase program. For the year-to-date period ended June 29, 2012, the Company used approximately \$3.6 million to purchase 263,000 shares pursuant to the repurchase program. At June 29, 2012, approximately 0.6 million shares remained authorized for future purchases. The Company issued approximately 45,000 shares and 297,000 shares out of treasury stock primarily to fulfill the share requirements from stock option exercises and restricted stock grants during the 2012 second quarter and year-to-date period, respectively.

During the 2011 second quarter, the Company used approximately \$0.6 million to purchase 44,000 shares of its stock for treasury pursuant to the Company's share repurchase program. For the year-to-date period ended July 1, 2011, the Company used approximately \$1.2 million to purchase 94,000 shares pursuant to the repurchase program. At July 1, 2011, approximately 1.1 million shares remained authorized for future purchases. The Company issued approximately 320,000 shares and 791,000 shares out of treasury stock primarily to fulfill the share requirements from stock option exercises and restricted stock grants during the 2011 second quarter and year-to-date period, respectively.

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10. Significant Customer

In the 2012 second quarter, International Business Machines Corporation (IBM) was the Company's largest customer, and accounted for \$29.0 million or 27.2% of consolidated revenue as compared with \$29.6 million or 30.0% of revenue in the comparable 2011 period. In the first two quarters of 2012, IBM accounted for \$57.4 million or 27.3% of consolidated revenue, compared with \$58.1 million or 29.9% of consolidated revenue in the comparable 2011 period.

During the 2011 fourth quarter, the National Technical Services Agreement (NTS Agreement) with IBM was renewed for three years to December 31, 2014. As part of the NTS Agreement, the Company provides its services as a predominant supplier to IBM's Integrated Technology Services unit and as sole provider to the Systems and Technology Group business unit. The Company's accounts receivable from IBM at June 29, 2012 and July 1, 2011 totaled \$13.7 million and \$15.0 million, respectively. No other customer accounted for more than 10% of the Company's revenue in the second quarter or year-to-date periods of 2012 or 2011.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations for the Quarter and Two Quarters Ended June 29, 2012****Forward-Looking Statements**

This quarterly report on Form 10-Q contains forward-looking statements made by the management of Computer Task Group, Incorporated (CTG, the Company or the Registrant) that are subject to a number of risks and uncertainties. These forward-looking statements are based on information as of the date of this report. The Company assumes no obligation to update these statements based on information from and after the date of this report. Generally, forward-looking statements include words or phrases such as anticipates, believes, estimates, expects, intends, plans, projects, could, may, might, should, will and words and phrases of similar impact. The forward-looking statements include, but are not limited to, statements regarding future operations, industry trends or conditions and the business environment, and statements regarding future levels of, or trends in, revenue, operating expenses, capital expenditures, and financing. The forward-looking statements are made pursuant to safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Numerous factors could cause actual results to differ materially from those in the forward-looking statements, including the following: (i) the availability to CTG of qualified professional staff, (ii) renegotiations, nullification, or breaches of contracts with customers, vendors, subcontractors or other parties, (iii) the partial or complete loss of the revenue the Company generates from International Business Machines Corporation (IBM), (iv) risks associated with operating in foreign jurisdictions, (v) the change in valuation of recorded goodwill balances, (vi) the impact of current and future laws and government regulation, as well as repeal or modification of such, affecting the IT solutions and staffing industry, taxes and the Company's operations in particular, (vii) industry and economic conditions, including fluctuations in demand for information technology (IT) services, (viii) consolidation among the Company's competitors or customers, (ix) domestic and foreign industry competition for customers and talent, (x) the need to supplement or change our IT services in response to new offerings in the industry, and (xi) the risks described in Item 1A of the most recently filed Form 10-K and from time to time in the Company's reports filed with the Securities and Exchange Commission (SEC).

Industry Trends

The Company operates in one industry segment, providing IT services to its clients. These services include IT solutions and IT staffing. The market demand for the Company's services is heavily dependent on IT spending by major corporations, organizations and government entities in the markets and regions that it serves. The pace of technological change and changes in business requirements and practices of the Company's clients all have a significant impact on the demand for the services that we provide. Competition for new engagements and pricing pressure has been and, management believes, will continue to be strong.

IT solutions and IT staffing revenue as a percentage of total revenue for the quarter and two quarters ended June 29, 2012 and July 1, 2011 are as follows:

| | For the Quarter Ended | | For the Two Quarters Ended | |
|--------------|--------------------------|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| IT solutions | 42% | 37% | 41% | 36% |
| IT staffing | 58% | 63% | 59% | 64% |
| Total | 100% | 100% | 100% | 100% |

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The Company promotes a significant portion of its services through four vertical market focus areas: Technology Service Providers, Healthcare (which includes services provided to healthcare providers, health insurers, and life sciences companies), Energy, and Financial Services. The Company focuses on these four vertical areas as it believes that these areas are either higher growth markets than the general IT services market and the general economy, or are areas that provide greater potential for the Company's growth due to the size of the vertical market. The remainder of CTG's revenue is derived from general markets.

The Company's revenue by vertical market as a percentage of total revenue for the quarter and two quarters ended June 29, 2012 and July 1, 2011 are as follows:

| | For the Quarter Ended | | For the Two Quarters Ended | |
|------------------------------|--------------------------|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| Healthcare | 33% | 29% | 32% | 28% |
| Technology service providers | 31% | 35% | 32% | 35% |
| Financial services | 6% | 6% | 6% | 7% |
| Energy | 6% | 6% | 6% | 6% |
| General markets | 24% | 24% | 24% | 24% |
| Total | 100% | 100% | 100% | 100% |

The IT services industry is extremely competitive and characterized by continuous changes in customer requirements and improvements in technologies. The Company's competition varies significantly by geographic region, as well as by the type of service provided. Many of the Company's competitors are larger than CTG, and have greater financial, technical, sales and marketing resources. In addition, the Company frequently competes with a client's own internal IT staff. Our industry is being impacted by the growing use of lower-cost offshore delivery capabilities (primarily India and other parts of Asia). There can be no assurance that CTG will be able to continue to compete successfully with existing or future competitors or that future competition will not have a material adverse effect on our results of operations and financial condition.

Revenue and Cost Recognition

The Company recognizes revenue when persuasive evidence of an arrangement exists, when the services have been rendered, when the price is determinable, and when collectability of the amount due is reasonably assured. For time-and-material contracts, revenue is recognized as hours are incurred and costs are expended. For contracts with periodic billing schedules, primarily monthly, revenue is recognized as services are rendered to the customer. Revenue for fixed price contracts is recognized as per the proportional method of accounting using an input-based approach whereby salary and indirect labor costs incurred are measured and compared with the total estimate of costs at completion of a project. Revenue is recognized based upon the percent complete calculation of total incurred costs to total estimated costs. The Company's estimate of the total labor costs it expects to incur over the term of the contract is based on the nature of the project and our past experience on similar projects, and includes management judgments and estimates which affect the amount of revenue recognized on fixed-price contracts in any accounting period.

The Company entered into a series of contracts with a customer that provide for application customization and integration services, specifically utilizing one of the software tools the Company has internally developed. As the contracts are closely interrelated and dependent on each other, for accounting purposes the contracts are considered to be one arrangement. Additionally, as the project includes significant modification and customization services to transform the previously developed software tool into an expanded tool that meets the customer's requirements, the percentage-of-completion method of contract accounting is being utilized for the project.

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The Company's revenue from contracts accounted for under time-and-material, progress billing and percentage-of-completion methods for the quarter and two quarters ended June 29, 2012 and July 1, 2011 are as follows:

| | For the Quarter Ended | | For the Two Quarters Ended | |
|--------------------------|--------------------------|-----------------|-------------------------------|-----------------|
| | June 29, 2012 | July 1, 2011 | June 29, 2012 | July 1, 2011 |
| Time-and-material | 90% | 90% | 91% | 91% |
| Progress payment | 8% | 8% | 8% | 7% |
| Percentage-of-completion | 2% | 2% | 1% | 2% |
| Total | 100% | 100% | 100% | 100% |

Results of Operations

The table below sets forth data as contained in the condensed consolidated statements of income with the percentage information calculated as a percentage of consolidated revenue.

| | June 29, 2012 | | July 1, 2011 | |
|---|------------------------|------------|--------------|-----------|
| | (amounts in thousands) | | | |
| For the Quarter Ended: | | | | |
| Revenue | 100.0% | \$ 106,705 | 100.0% | \$ 98,327 |
| Direct costs | 78.5% | 83,810 | 78.9% | 77,594 |
| Selling, general, and administrative expenses | 15.7% | 16,752 | 16.3% | 16,056 |
| Operating income | 5.8% | 6,143 | 4.8% | 4,677 |
| Interest and other income (expense), net | 0.4% | 384 | (0.1)% | (48) |
| Income before income taxes | 6.2% | 6,527 | 4.7% | 4,629 |
| Provision for income taxes | 2.3% | 2,404 | 1.8% | 1,799 |
| Net income | 3.9% | \$ 4,123 | 2.9% | \$ 2,830 |

| | June 29, 2012 | | July 1, 2011 | |
|---|------------------------|------------|--------------|------------|
| | (amounts in thousands) | | | |
| For the Two Quarters Ended: | | | | |
| Revenue | 100.0% | \$ 210,072 | 100.0% | \$ 194,236 |
| Direct costs | 78.7% | 165,325 | 79.1% | 153,706 |
| Selling, general, and administrative expenses | 15.7% | 33,005 | 16.1% | 31,254 |
| Operating income | 5.6% | 11,742 | 4.8% | 9,276 |
| Interest and other income (expense), net | 0.2% | 334 | (0.1)% | (85) |
| Income before income taxes | 5.8% | 12,076 | 4.7% | 9,191 |
| Provision for income taxes | 2.2% | 4,593 | 1.8% | 3,533 |
| Net income | 3.6% | \$ 7,483 | 2.9% | \$ 5,658 |

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The Company recorded revenue in the 2011 and 2012 periods as follows:

| | June 29, 2012 | | July 1, 2011 | | Year-over -Year Change |
|-------------------------------|------------------------|------------|--------------|-----------|------------------------------|
| | (amounts in thousands) | | | | |
| For the Quarter Ended: | | | | | |
| North America | 84.3% | \$ 89,938 | 82.4% | \$ 80,990 | 11.0% |
| Europe | 15.7% | 16,767 | 17.6% | 17,337 | (3.3%) |
| Total | 100.0% | \$ 106,705 | 100.0% | \$ 98,327 | 8.5% |

There were 64 billable days in both the 2012 and 2011 second quarters. The Company's revenue included reimbursable expenses billed to customers which totaled \$3.7 million in the second quarter of 2012 and \$3.1 million in the second quarter of 2011.

| | June 29, 2012 | | July 1, 2011 | | Year-over -Year Change |
|------------------------------------|------------------------|------------|--------------|------------|------------------------------|
| | (amounts in thousands) | | | | |
| For the Two Quarters Ended: | | | | | |
| North America | 83.8% | \$ 176,130 | 82.3% | \$ 159,820 | 10.2% |
| Europe | 16.2% | 33,942 | 17.7% | 34,416 | (1.4%) |
| Total | 100.0% | \$ 210,072 | 100.0% | \$ 194,236 | 8.2% |

There were 128 billable days and 129 billable days in the 2012 and 2011 year-to-date periods, respectively. Reimbursable expenses billed to customers and included in revenue totaled \$6.9 million and \$6.3 million in the 2012 and 2011 year-to-date periods, respectively.

The revenue increase in North America in the 2012 second quarter and first two quarters as compared with the corresponding 2011 period was due to significant demand for the Company's IT solutions services. IT solutions revenue increased 23.3% and 22.7% in the 2012 second quarter and year-to-date period, respectively, as compared with the corresponding 2011 periods. The IT solutions revenue increase was primarily driven by an increase in electronic medical records work for providers in the Company's healthcare vertical market. IT staffing revenue in the 2012 second quarter and year-to-date period was consistent with the revenue recorded in the corresponding 2011 period. The Company's headcount was approximately 3,800 employees at June 29, 2012, which was a 3% increase from approximately 3,700 employees at both December 31, 2011 and July 1, 2011.

The decrease in revenue in the Company's European operations in both the 2012 second quarter and first two quarters as compared with the corresponding 2011 periods was primarily due the weakness relative to the U.S. dollar of the currencies of Belgium, Luxembourg, and the United Kingdom, the countries in which the Company's European subsidiaries operate, offset by modest strength in the Company's staffing business. In Belgium and Luxembourg, the functional currency is the Euro, while in the United Kingdom the functional currency is the British Pound. In the 2012 second quarter as compared with the 2011 second quarter, the average value of the Euro decreased 10.7% while the average value of the British Pound decreased 2.9%. A significant portion of the Company's revenue from its European operations is generated in Belgium and Luxembourg. If there had been no change in these exchange rates from the 2011 second quarter to the 2012 second quarter, total European revenue would have been approximately \$1.9 million higher, or \$18.7 million as compared with the \$16.8 million reported. In the first two quarters of 2012 as compared with the first two quarters of 2011, the average value of the Euro decreased 7.5% while the average value of the British Pound decreased 2.4%. If there had been no change in the exchange rates from the first two quarters of 2011 to the corresponding 2012 period, total European revenue would have been approximately \$2.7 million higher, or \$36.6 million as compared with the \$33.9 million reported. Additionally, operating income in both the 2012 second quarter and year-to-date period would have been approximately \$0.1 million higher if there had been no change in the exchange rates year-over-year.

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In the 2012 second quarter, IBM was the Company's largest customer, accounting for \$29.0 million or 27.2% of consolidated revenue as compared with \$29.5 million or 30.0% of revenue in the comparable 2011 period. In the first two quarters of 2012, IBM accounted for \$57.4 million or 27.3% of consolidated revenue, compared with \$58.1 million or 29.9% in the comparable 2011 period. During the 2011 fourth quarter, the National Technical Services Agreement (NTS Agreement) with IBM was renewed for three years to December 31, 2014. As part of the NTS Agreement, the Company provides its services as a predominant supplier to IBM's Integrated Technology Services unit and as sole provider to the Systems and Technology Group business unit. The Company's accounts receivable from IBM at June 29, 2012 and July 1, 2011 totaled \$13.7 million and \$15.0 million, respectively. No other customer accounted for more than 10% of the Company's revenue in the second quarter or first two quarters of 2012 or 2011.

Direct costs, defined as the costs for billable staff including billable out-of-pocket expenses, were 78.5% of revenue in the 2012 second quarter as compared with 78.9% of revenue in the 2011 second quarter, and 78.7% of revenue in the first two quarters of 2012 as compared with 79.1% in the corresponding 2011 period. The Company's direct costs as a percentage of revenue fell in the 2012 second quarter and year-to-date period as compared with the corresponding 2011 periods due to a shift in the Company's business mix to a higher level of solutions business, which incurs lower direct costs as a percentage of revenue than the Company's staffing business.

Selling, general and administrative (SG&A) expenses were 15.7% of revenue in the 2012 second quarter and 16.3% in the corresponding 2011 period, and 15.7% in the first two quarters of 2012 as compared with 16.1% in the corresponding 2011 period. The decrease in SG&A expenses as a percentage of revenue in the 2012 second quarter and first two quarters as compared with the corresponding 2011 periods is primarily due to continued disciplined cost management.

Operating income was 5.8% of revenue in the 2012 second quarter as compared with 4.8% in the 2011 second quarter, and 5.6% of revenue in the first two quarters of 2012 as compared with 4.8% in the corresponding 2011 period. The increase in operating income as a percentage of revenue in the 2012 second quarter and year-to-date period as compared with the second quarter and year-to-date period of 2011 is primarily due to the favorable change in business mix from the prior periods. Operating income from North American operations was \$10.3 million and \$7.7 million in the first two quarters of 2012 and 2011, respectively. European operations recorded operating income of \$1.4 million and \$1.6 million, respectively, in the corresponding 2012 and 2011 periods.

Interest and other income (expense) was 0.4% of revenue in the 2012 second quarter as compared with (0.1)% in the 2011 second quarter, and 0.2% of revenue in the first two quarters of 2012 as compared with (0.1)% in the corresponding 2011 period. The increase in net interest and other income in both the 2012 second quarter and year-to-date period resulted from receipt of life insurance proceeds of approximately \$0.4 million for one of the Company's previous chief executive officers who passed away in the 2012 second quarter.

The Company's normal annual effective tax rate (ETR) typically ranges from 38% to 42% of pre-tax income. The 2012 second quarter ETR was 36.8% and the 2012 year-to-date ETR was 38.0%. The Company received \$0.4 million of non-taxable life insurance proceeds for one of its previous chief executive officers that passed away in the 2012 second quarter. The 2011 second quarter ETR was 38.9% and the 2011 year-to-date ETR was 38.4%, both of which were within the Company's expected normal annual ETR.

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Net income for the 2012 second quarter was 3.9% of revenue or \$0.25 per diluted share, compared with net income of 2.9% of revenue or \$0.17 per diluted share in the 2011 second quarter. Net income for the first two quarters of 2012 was 3.6% of revenue or \$0.45 per diluted share, compared with net income of 2.9% of revenue or \$0.34 per diluted share in the corresponding 2011 period. Net income in the 2012 second quarter and year-to-date period included approximately \$0.03 per share from the life insurance proceeds mentioned above. Diluted earnings per share was calculated using 16.7 million and 16.9 million weighted-average equivalent shares outstanding for the quarters ended June 29, 2012 and July 1, 2011, respectively. Diluted earnings per share was calculated using 16.8 million weighted-average equivalent shares outstanding for both of the year-to-date periods ended June 29, 2012 and July 1, 2011.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with U.S. generally accepted accounting principles requires the Company's management to make estimates, judgments and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. The Company's significant accounting policies, along with the underlying assumptions and judgments made by the Company's management in their application, have a significant impact on the Company's condensed consolidated financial statements. The Company identifies its most critical accounting policies as those that are the most pervasive and important to the portrayal of the Company's financial position and results of operations, and that require the most difficult, subjective and/or complex judgments by management regarding estimates about matters that are inherently uncertain. The Company's most critical accounting policies are those related to income taxes, specifically relating to deferred taxes and valuation allowances, and goodwill valuation.

Income Taxes **Deferred Taxes and Valuation Allowances** At June 29, 2012, the Company had a total of \$8.6 million of current and non-current deferred tax assets, net of deferred tax liabilities, recorded on its consolidated balance sheet. The changes in deferred tax assets and liabilities from period to period are determined based upon the changes in differences between the basis of assets and liabilities for financial reporting purposes and the basis of assets and liabilities for tax purposes, as measured by the enacted tax rates when these differences are estimated to reverse. The Company has made certain assumptions regarding the timing of the reversal of these assets and liabilities, and whether taxable income in future periods will be sufficient to recognize all or a part of any gross deferred tax asset of the Company.

At June 29, 2012, the Company had deferred tax assets recorded resulting from net operating losses totaling approximately \$1.1 million. Management of the Company has analyzed each jurisdiction's tax position, including forecasting potential taxable income in future periods, and the expiration of the net operating loss carryforwards as applicable, and determined that it is unclear whether some of these deferred tax assets will be realized at any point in the future. At June 29, 2012, the Company has offset substantially all of these deferred tax assets with a valuation allowance totaling \$1.0 million, resulting in a net deferred tax asset from net operating loss carryforwards of approximately \$0.1 million.

The Company's deferred tax assets and their potential realizability are evaluated each quarter to determine if any changes should be made to the valuation allowance. Any change in the valuation allowance in the future could result in a change in the Company's effective tax rate (ETR). A 1% change in the ETR in the 2012 second quarter would have increased or decreased net income in the quarter by approximately \$65,000.

Goodwill Valuation The Company has a goodwill balance of \$35.7 million related to its healthcare vertical market recorded as of June 29, 2012. As of the fiscal month-end October 2011, with the assistance of an independent appraisal company, the Company completed its annual valuation of the business to which the Company's goodwill relates. The valuation indicated that the estimated fair value of the business was substantially in excess of its carrying value by approximately 116%. Additionally, no facts or circumstances have arisen since October 2011 which have led management to believe the goodwill may be impaired.

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Other Estimates The Company has also made a number of estimates and assumptions relating to the reporting of other assets and liabilities and the disclosure of contingent assets and liabilities to prepare the consolidated financial statements pursuant to the rules and regulations of the SEC. Such estimates primarily relate to actuarial assumptions including discount rates and expected rates of return on assets, as applicable, for the Company's defined benefit and postretirement benefit plans, an allowance for doubtful accounts receivable, assumptions underlying stock option valuation, investment valuation, legal matters, other contingencies, and progress toward completion and direct profit or loss on contracts. As future events and their effects can not be determined with precision, actual results could differ from these estimates. Changes in the economic climates in which the Company operates may affect these estimates and will be reflected in the Company's financial statements in the event they occur.

Financial Condition and Liquidity

Operating activities provided cash of \$3.6 million in the first two quarters of 2012 (2012 period), and used \$4.3 million of cash in the first two quarters of 2011 (2011 period). In the 2012 period, net income totaled \$7.5 million, while other non-cash adjustments, primarily consisting of depreciation and amortization expense, equity-based compensation expense, deferred income taxes, and deferred compensation totaled a net of \$2.1 million. In the 2011 period, net income was \$5.7 million, while the corresponding non-cash adjustments netted to \$1.4 million. Accounts receivable balances increased \$4.7 million in the 2012 period, and increased \$7.9 million in the 2011 period. The increase in the accounts receivable balance in the 2012 period primarily resulted from a 9% increase in revenue year-over-year, offset by a one day decrease in days sales outstanding (DSO). DSO decreased one day to 61 days at June 29, 2012, from 62 days at December 31, 2011. The increase in accounts receivable in the 2011 period primarily resulted from a 22% increase in revenue year-over-year and an increase in DSO to 62 days at July 1, 2011, as compared with 57 days at July 2, 2010.

Other assets increased \$1.0 million in the 2012 period and \$1.4 million in the 2011 period primarily due to the timing of payment of insurance premiums prior to quarter-end. Accrued compensation increased \$0.2 million in the 2012 period primarily due to an increase in headcount of 100 people, or 3%, in the 2012 period, and increased \$0.6 million in the 2011 period due to an increase in employee headcount of approximately 300, or 9% in the 2011 period. Income taxes payable decreased \$1.0 million in the 2012 period and \$1.5 million in the 2011 period due to the timing of payments and the excess tax benefit received from equity-based compensation transactions. Advance billings decreased \$0.8 million in the 2011 period due to the timing of invoices sent to customers near quarter-end.

Investing activities used \$0.7 million in the 2012 period as compared with \$1.3 million in the 2011 period. The cash used in the 2012 period represented additions to property and equipment of \$0.6 million and net contributions to the Company's deferred compensation plans totaling \$0.1 million. Additions to property, equipment and capitalized software in the 2011 period totaled approximately \$1.2 million, while contributions to deferred compensation plans totaled approximately \$0.1 million. The Company has no significant commitments for the purchase of property or equipment at June 29, 2012.

Financing activities used \$1.2 million of cash in the 2012 period as compared with providing \$3.1 million in the 2011 period. The cash used in the 2012 period primarily resulting from \$3.6 million used for the purchase of stock for treasury, offset by \$0.4 million received from the exercise of stock options under the Company's equity-based compensation plans, excess tax benefits from the company's equity-based compensation transactions of \$0.6 million, and a \$1.2 million net change in cash overdrafts. In the 2011 period, the Company received \$1.8 million from the exercise of stock options, \$1.7 million from excess tax benefits for equity-based compensation transactions, \$0.6 million for the net change in cash overdrafts, offset by \$1.2 million used for the purchase of stock for treasury.

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The Company's credit agreement expires in April 2014 and allows the Company to borrow up to \$35.0 million. At both June 29, 2012 and July 1, 2011, there were no amounts outstanding under the credit agreement. Although there were no borrowings outstanding, at both June 29, 2012 and July 1, 2011, there were \$0.4 million of letters of credit issued under the credit agreement. The Company borrows or repays its revolving debt as needed based upon its working capital obligations, including the timing of the U.S. bi-weekly payroll. During the 2012 period, the Company did not borrow any funds under its revolving credit agreement, while the average outstanding balance under this line of credit was \$0.5 million in the 2011 period.

The Company is required to meet certain financial covenants in order to maintain borrowings under its revolving credit line, pay dividends, and make acquisitions. The covenants are measured quarterly, and at June 29, 2012 include a leverage ratio which must be no more than 2.75 to 1, a calculation of minimum tangible net worth which must be no less than \$47.8 million, and total expenditures for property, equipment and capitalized software can not exceed \$5.0 million annually. The Company was in compliance with these covenants at June 29, 2012 as its leverage ratio was 0.0, tangible net worth was \$59.1 million, and expenditures for property and equipment in the 2012 period were \$0.6 million. The Company was also in compliance with its required covenants at July 1, 2011. When considering current market conditions and operating results, and the Company's current estimate of future operating results, the Company believes it will be able to meet its covenants, as applicable, for the remainder of 2012 and in future years.

During the 2012 period, the Company used approximately \$3.6 million to purchase 263,000 shares of its stock for treasury. At June 29, 2012, a total of approximately 0.6 million shares are authorized for future purchases. During the 2011 period, the Company used approximately \$1.2 million to purchase 94,000 shares of its stock for treasury.

Of the total cash and cash equivalents reported on the consolidated balance sheet at June 29, 2012 of \$23.6 million, approximately \$11.6 million was held by the Company's foreign operations and is considered to be indefinitely reinvested in those operations. The Company has not repatriated any of its cash and cash equivalents from its foreign operations in the past five years, and has no intention of doing so in the foreseeable future as the funds are required to meet the working capital needs of our foreign operations.

The Company believes existing internally available funds, cash potentially generated from future operations, and borrowings available under the Company's revolving line of credit totaling \$34.6 million at June 29, 2012 are sufficient to meet foreseeable working capital and capital expenditure needs, fund stock repurchases, and allow for future internal growth and expansion.

Off-Balance Sheet Arrangements

The Company did not have off-balance sheet arrangements or transactions in the second quarter or year-to-date periods of 2012 or 2011 other than the guarantees in our European operations that support office leases and performance under government contracts.

Contractual Obligations

The Company did not enter into any significant contractual obligations during the quarter or year-to-date period ended June 29, 2012.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company's primary market risk exposure consists of foreign currency exchange risk associated with the Company's European operations.

The decrease in revenue in the Company's European operations in both the 2012 second quarter and first two quarters as compared with the corresponding 2011 periods was primarily due the weakness relative to the U.S. dollar of the currencies of Belgium, Luxembourg, and the United Kingdom, the countries in which the Company's European subsidiaries operate, offset by modest strength in the Company's staffing business. In Belgium and Luxembourg, the functional currency is the Euro, while in the United Kingdom the functional currency is the British Pound. In the 2012 second quarter as compared with the 2011 second quarter, the average value of the Euro decreased 10.7% while the average value of the British Pound decreased 2.9%. A significant portion of the Company's revenue from its European operations is generated in Belgium and Luxembourg. If there had been no change in these exchange rates from the 2011 second quarter to the 2012 second quarter, total European revenue would have been approximately \$1.9 million higher, or \$18.7 million as compared with the \$16.8 million reported. In the first two quarters of 2012 as compared with the first two quarters of 2011, the average value of the Euro decreased 7.5% while the average value of the British Pound decreased 2.4%. If there had been no change in the exchange rates from the first two quarters of 2011 to the corresponding 2012 period, total European revenue would have been approximately \$2.7 million higher, or \$36.6 million as compared with the \$33.9 million reported. Additionally, operating income in both the 2012 second quarter and year-to-date period would have been approximately \$0.1 million higher if there had been no change in the exchange rates year-over-year.

The Company has historically not used any market risk sensitive instruments to hedge its foreign currency exchange risk. The Company believes the market risk related to intercompany balances in future periods will not have a material affect on its results of operations.

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Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The Company's management has evaluated, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, the effectiveness of the design and operations of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this periodic report.

Changes in Internal Control over Financial Reporting

The Company reviews its internal controls on a continuous basis. The Company's management, including its Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's internal control over financial reporting as of the end of the period covered by this report, and concluded that the Company's internal control over financial reporting was effective as of the end of the period covered by this report. There were no changes in the Company's internal control over financial reporting that occurred during the period covered by this report, which ended on June 29, 2012, that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Table of Contents**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

None

Item 1A. Risk Factors

There were no material changes in the Company's risk factors from those previously disclosed in the Company's Form 10-K for the period ended December 31, 2011.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**Issuer Purchases of Equity Securities**

| Period | Total Number of Shares Purchased | Average Price Paid per Share ** | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares that may yet be Purchased Under the Plans or Programs* |
|---------------------|--|------------------------------------|--|---|
| March 31 - April 30 | 60,187 | \$ 14.55 | 60,187 | 741,418 |
| May 1 - May 31 | 109,095 | \$ 13.09 | 109,095 | 632,323 |
| June 1 - June 29 | 34,400 | \$ 12.53 | 34,400 | 597,923 |
| Total | 203,682 | \$ 13.43 | 203,682 | |

* The Company's share repurchase program (originally announced on May 12, 2005) does not have an expiration date, nor was it terminated during the 2012 second quarter. The information in this table does not include shares tendered to the Company either to satisfy the exercise cost for the cashless exercise of employee stock options, or tax withholding obligations associated with employee equity awards.

** Excludes broker commissions

Item 3. Default Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None

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Item 6. Exhibits

| Exhibit | Description | Page |
|---------|--|------|
| 31. (a) | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | 28 |
| 31. (b) | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | 29 |
| 32. | Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | 30 |
| 101. | Interactive data files pursuant to Rule 405 of Regulation S-T: the Condensed Consolidated Statements of Income for the quarter and six-month periods Ending June 29, 2012 and July 1, 2011, the Condensed Consolidated Statements of Comprehensive Income for the quarter and six-month periods Ending June 29, 2012 and July 1, 2011, the Condensed Consolidated Balance Sheets as of June 29, 2012 and December 31, 2011, the Condensed Consolidated Statements of Cash Flows for the six-month periods ended June 29, 2012 and July 1, 2011, and the Notes to the Condensed Consolidated Financial Statements | |

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

COMPUTER TASK GROUP, INCORPORATED

By: */s/ BRENDAN M. HARRINGTON*
Brendan M. Harrington

Title: **Chief Financial Officer**

Date: August 2, 2012