

FAIR ISAAC CORP
Form 10-Q
May 08, 2008

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2008

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
[NO FEE REQUIRED]**

For the transition period from _____ to _____

Commission File Number 0-16439

Fair Isaac Corporation

(Exact name of registrant as specified in its charter)

Delaware

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

94-1499887

*(I.R.S. Employer
Identification No.)*

**901 Marquette Avenue, Suite 3200
Minneapolis, Minnesota**

(Address of principal executive offices)

55402-3232

(Zip Code)

Registrant's telephone number, including area code:

612-758-5200

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐
(Do not check if a 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

The number of shares of common stock outstanding on April 30, 2008 was 48,623,492 (excluding 40,233,291 shares held by the Company as treasury stock).

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FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except par value data)
(Unaudited)

	March 31, 2008	September 30, 2007
Assets		
Current assets:		
Cash and cash equivalents	\$ 59,963	\$ 95,284
Marketable securities available for sale, current portion	48,918	125,327
Accounts receivable, net	159,337	169,293
Prepaid expenses and other current assets	18,429	23,008
Deferred income taxes	1,391	
Current assets of discontinued operations	10,989	9,839
Total current assets	299,027	422,751
Marketable securities available for sale, less current portion	79,066	13,776
Other investments	12,374	12,374
Property and equipment, net	49,835	51,007
Goodwill	701,178	685,452
Intangible assets, net	60,919	54,733
Deferred income taxes	14,938	14,828
Other assets	4,335	4,040
Long-term assets of discontinued operations	9,083	16,810
	\$ 1,230,755	\$ 1,275,771
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 13,221	\$ 15,204
Senior convertible notes	367,259	390,963
Accrued compensation and employee benefits	33,228	43,418
Other accrued liabilities	26,596	30,119
Deferred revenue	36,989	42,010
Current liabilities of discontinued operations	4,433	4,210
Total current liabilities	481,726	525,924
Revolving line of credit	213,000	170,000
Other liabilities	16,854	13,533
Total liabilities	711,580	709,457

Commitments and contingencies

Stockholders' equity:

Preferred stock (\$0.01 par value; 1,000 shares authorized; none issued and outstanding)

Common stock (\$0.01 par value; 200,000 shares authorized, 88,857 shares issued and 48,589 and 51,064 shares outstanding at March 31, 2008 and September 30, 2007, respectively)

Paid-in-capital

Treasury stock, at cost (40,268 and 37,793 shares at March 31, 2008 and September 30, 2007, respectively)

Retained earnings

Accumulated other comprehensive income

Total stockholders' equity

486	511
1,105,335	1,097,327
(1,375,025)	(1,290,393)
776,772	745,054
11,607	13,815
519,175	566,314
\$ 1,230,755	\$ 1,275,771

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except per share data)
(Unaudited)

	Quarter Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
Revenues	\$ 193,234	\$ 190,675	\$ 383,340	\$ 388,839
Operating expenses:				
Cost of revenues (1)	72,946	65,239	139,918	127,515
Research and development	20,662	17,431	40,131	34,825
Selling, general and administrative (1)	61,365	67,138	128,124	134,215
Amortization of intangible assets (1)	3,621	5,869	6,684	11,752
Restructuring	6,124		5,679	
Gain on sale of product line assets		(1,541)		(1,541)
Total operating expenses	164,718	154,136	320,536	306,766
Operating income	28,516	36,539	62,804	82,073
Interest income	1,685	3,341	4,235	6,905
Interest expense	(3,837)	(3,230)	(8,258)	(5,906)
Other income, net	874	491	617	38
Income from continuing operations before income taxes	27,238	37,141	59,398	83,110
Provision for income taxes	9,464	15,510	20,788	29,869
Income from continuing operations	17,774	21,631	38,610	53,241
Loss from discontinued operations, net of tax	(4,287)	(193)	(4,937)	(578)
Net income	\$ 13,487	\$ 21,438	\$ 33,673	\$ 52,663
Basic earnings per share:				
Continuing operations	\$ 0.36	\$ 0.38	\$ 0.78	\$ 0.93
Discontinued operations	(0.08)		(0.10)	(0.01)
Total	\$ 0.28	\$ 0.38	\$ 0.68	\$ 0.92

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Diluted earnings per share:				
Continuing operations	\$ 0.36	\$ 0.37	\$ 0.77	\$ 0.90
Discontinued operations	(0.08)		(0.10)	(0.01)
Total	\$ 0.28	\$ 0.37	\$ 0.67	\$ 0.89

Shares used in computing earnings per share:				
Basic	48,760	56,940	49,404	57,504
Diluted	48,961	58,659	50,084	59,328

(1) Cost of revenues and selling, general and administrative expenses exclude the amortization of intangible assets. See Note 2 to the accompanying condensed consolidated financial statements.

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY AND
COMPREHENSIVE INCOME

(In thousands)
(Unaudited)

	Common Stock Shares	Par Value	Paid-In- Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholders' Equity	Comprehensive Income
Balance at September 30, 2007	51,064	\$ 511	\$ 1,097,327	\$ (1,290,393)	\$ 745,054	\$ 13,815	\$ 566,314	
Share-based compensation			14,926				14,926	
Exercise of stock options	450	4	(4,477)	15,389			10,916	
Tax benefit from exercised stock options			327				327	
Forfeitures of restricted stock	(18)		573	(573)				
Repurchases of common stock	(3,121)	(31)		(106,809)			(106,840)	
Issuance of ESPP shares from treasury	172	2	(1,214)	5,906			4,694	
Issuance of restricted stock to employees from treasury	42		(2,127)	1,455			(672)	
Dividends paid					(1,955)		(1,955)	
Net income					33,673		33,673	\$ 33,673
Unrealized gains on investments						500	500	500
Cumulative translation adjustments						(2,708)	(2,708)	(2,708)
Balance at March 31, 2008	48,589	\$ 486	\$ 1,105,335	\$ (1,375,025)	\$ 776,772	\$ 11,607	\$ 519,175	\$ 31,465

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended March 31,	
	2008	2007
Cash flows from operating activities:		
Net income	\$ 33,673	\$ 52,663
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	19,863	26,867
Share-based compensation	14,926	20,080
Deferred income taxes	1,020	2,001
Tax benefit from exercised stock options	327	13,529
Excess tax benefits from share-based payment arrangements	(1,216)	(10,079)
Gain on repurchase of senior convertible notes	(356)	
Net amortization (accretion) of premium (discount) on marketable securities	177	(822)
Provision for doubtful accounts	1,753	2,804
Loss on sale of discontinued operations	6,921	
Gain on sale of product line assets		(1,541)
Net gain on sales of property and equipment	(37)	(1)
Changes in operating assets and liabilities, net of acquisition and disposition effects:		
Accounts receivable	8,133	(16,846)
Prepaid expenses and other assets	3,427	(1,159)
Accounts payable	571	2,986
Accrued compensation and employee benefits	(10,134)	4,558
Other liabilities	(4,393)	(4,952)
Deferred revenue	(4,386)	(1,684)
Net cash provided by operating activities	70,269	88,404
Cash flows from investing activities:		
Purchases of property and equipment	(13,432)	(11,651)
Cash proceeds from sale of product line assets		13,904
Cash proceeds from sales of property and equipment	1,543	
Cash paid for acquisitions, net of cash acquired	(31,941)	
Purchases of marketable securities	(112,204)	(132,512)
Proceeds from sales of marketable securities	2,008	14,250
Proceeds from maturities of marketable securities	121,000	130,999
Investment in cost-method investees		(213)
Net cash provided by (used in) investing activities	(33,026)	14,777
Cash flows from financing activities:		
Proceeds from revolving line of credit	43,000	70,000
Repurchases of senior convertible notes	(23,348)	
Debt issuance costs		(408)

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Proceeds from issuances of common stock under employee stock option and purchase plans	14,938	61,838
Dividends paid	(1,955)	(2,284)
Repurchases of common stock	(106,840)	(196,443)
Excess tax benefits from share-based payment arrangements	1,216	10,079
Net cash used in financing activities	(72,989)	(57,218)
Effect of exchange rate changes on cash	425	1,330
Increase (decrease) in cash and cash equivalents	(35,321)	47,293
Cash and cash equivalents, beginning of period	95,284	75,154
Cash and cash equivalents, end of period	\$ 59,963	\$ 122,447
Supplemental disclosures of cash flow information:		
Cash paid for income taxes, net of refunds	\$ 9,015	\$ 13,796
Cash paid for interest	\$ 9,037	\$ 3,807

See accompanying notes to condensed consolidated financial statements.

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FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Nature of Business

Fair Isaac Corporation

Incorporated under the laws of the State of Delaware, Fair Isaac Corporation is a provider of analytic, software and data management products and services that enable businesses to automate, improve and connect decisions. Fair Isaac Corporation provides a range of analytical solutions, credit scoring and credit account management products and services to banks, credit reporting agencies, credit card processing agencies, insurers, retailers, telecommunications providers, healthcare organizations and government agencies.

In these consolidated financial statements, Fair Isaac Corporation is referred to as we, us, our, and Fair Isaac.

Principles of Consolidation and Basis of Presentation

We have prepared the accompanying unaudited interim condensed consolidated financial statements in accordance with the instructions to Form 10-Q and the standards of accounting measurement set forth in Accounting Principles Board (APB) Opinion No. 28 and any amendments thereto adopted by the Financial Accounting Standards Board (FASB). Consequently, we have not necessarily included in this Form 10-Q all information and footnotes required for audited financial statements. In our opinion, the accompanying unaudited interim condensed consolidated financial statements in this Form 10-Q reflect all adjustments (consisting only of normal recurring adjustments, except as otherwise indicated) necessary for a fair presentation of our financial position and results of operations. These unaudited condensed consolidated financial statements and notes thereto should be read in conjunction with our audited consolidated financial statements and notes thereto presented in our Annual Report on Form 10-K for the year ended September 30, 2007. The interim financial information contained in this report is not necessarily indicative of the results to be expected for any other interim period or for the entire fiscal year.

The condensed consolidated financial statements include the accounts of Fair Isaac and its subsidiaries. All intercompany accounts and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. These estimates and assumptions include, but are not limited to, assessing the following: the recoverability of accounts receivable, goodwill and other intangible assets, software development costs and deferred tax assets; estimated losses associated with contingencies and litigation; the ability to estimate hours in connection with fixed-fee service contracts, the ability to estimate transactional-based revenues for which actual transaction volumes have not yet been received, the determination of whether fees are fixed or determinable and collection is probable or reasonably assured; and the development of assumptions for use in the Black-Scholes model that estimates the fair value of our share-based awards and assessing forfeiture rates of share-based awards.

Adoption of Accounting Pronouncement

In June 2006 the FASB issued Financial Interpretation No. 48, *Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. It also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. We adopted FIN 48 on October 1, 2007. See Note 9 for more information about the impact of adoption of this guidance.

2. Amortization of Intangible Assets

Amortization expense associated with our intangible assets, which has been reflected as a separate operating expense caption within the accompanying condensed consolidated statements of income, consisted of the following:

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FAIR ISAAC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

	Quarter Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
	(In thousands)			
Cost of revenues	\$ 1,919	\$ 3,768	\$ 3,421	\$ 7,544
Selling, general and administrative expenses	1,702	2,101	3,263	4,208
	\$ 3,621	\$ 5,869	\$ 6,684	\$ 11,752

Cost of revenues reflects our amortization of completed technology, and selling, general and administrative expenses reflects our amortization of other intangible assets. Intangible assets were \$60.9 million and \$54.7 million, net of accumulated amortization of \$102.0 million and \$95.7 million, as of March 31, 2008 and September 30, 2007, respectively.

3. Restructuring and Acquisition-Related Expenses

The following table summarizes our restructuring and acquisition-related accruals associated with acquisitions and certain Fair Isaac facility closures. The current portion and non-current portion is recorded in accrued compensation and employee benefits, other accrued current liabilities and other long-term liabilities within the accompanying condensed consolidated balance sheets. These balances are expected to be paid by fiscal 2012.

	Accrual at September 30, 2007	Expense Additions	Cash Payments	Expense Reversal	Accrual at March 31, 2008
Facilities charges	\$ 10,294	\$ 807	\$ (1,582)	\$ (445)	\$ 9,074
Employee separation	1,012	5,317	(974)		5,355
	11,306	\$ 6,124	\$ (2,556)	\$ (445)	14,429
Less: current portion	(4,051)				(7,909)
Non-current	\$ 7,255				\$ 6,520

During the quarter ended December 31, 2007, we recorded a \$0.4 million expense reversal due to favorable sublease arrangements we entered into for office space that was vacated last year. During the quarter ended March 31, 2008, we incurred charges of \$5.3 million for severance costs associated with the elimination of 190 positions across the organization. Cash payments for these severance costs will be paid in the third quarter of 2008. We also vacated excess lease space located in Colorado and recorded a lease exit accrual for \$0.8 million.

4. Composition of Certain Financial Statement Captions

	March 31, 2008	September 30, 2007
	(In thousands)	
Property and equipment	\$ 195,307	\$ 189,158

