HARTE HANKS INC
Form 10-Q
May 07, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2013

or

o **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 001-7120

HARTE-HANKS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**74-1677284**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

9601 McAllister Freeway, Suite 610, San Antonio, Texas 78216

(Address of principal executive offices) (Zip Code)

Registrant s telephone number including area code **210/829-9000**

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 o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 o

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

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

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

The number of shares outstanding of each of the registrant s classes of common stock as of April 15, 2013 was 62,439,311 shares of common stock, all of one class.

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HARTE-HANKS, INC. AND SUBSIDIARIES

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FORM 10-Q REPORT

March 31, 2013

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Item 1. Interim Condensed Consolidated Financial Statements

Harte-Hanks, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets (in thousands, except share amounts)

	March 31, 2013 (Unaudited)	December 31, 2012 (Audited)
Assets		
Current assets		
Cash and cash equivalents	$ 61,011	$ 49,648
Accounts receivable *(less allowance for doubtful accounts of $2,931 at March 31, 2013 and $3,402 at December 31, 2012)*	126,579	141,347
Inventory	4,975	5,067
Prepaid expenses	10,854	9,178
Current deferred income tax asset	7,052	8,181
Prepaid income tax	1,583	4,491
Other current assets	10,344	7,588
Total current assets	222,398	225,500
Property, plant and equipment *(less accumulated depreciation of $232,170 at March 31, 2013 and $231,167 at December 31, 2012)*	57,646	61,971
Goodwill	408,715	408,715
Other intangible assets *(less accumulated amortization of $9,596 at March 31, 2013 and $9,541 at December 31, 2012)*	5,204	5,259
Other assets	5,018	4,767
Total assets	$ 698,981	$ 706,212
Liabilities and Stockholders Equity		
Current liabilities		
Current maturities of long-term debt	$ 12,250	$ 12,250
Accounts payable	41,510	42,187
Accrued payroll and related expenses	13,438	16,777
Deferred revenue and customer advances	35,381	36,924
Income taxes payable	1,987	1,518
Customer postage and program deposits	15,111	19,892
Other current liabilities	8,294	10,649
Total current liabilities	127,971	140,197
Long-term debt	94,938	98,000
Other long-term liabilities *(including deferred income taxes of $57,056 at March 31, 2013 and $53,935 at December 31, 2012)*	141,593	139,851
Total liabilities	364,502	378,048
Stockholders equity		
Common stock, $1 par value per share, 250,000,000 shares authorized. 118,956,799 shares issued at March 31, 2013 and 118,737,456 shares issued at December 31, 2012	118,957	118,737
Additional paid-in capital	341,837	341,586
Retained earnings	1,172,619	1,165,952
Less treasury stock: 56,451,821 shares at cost at March 31, 2013 and 56,348,026 shares at cost at December 31, 2012	(1,249,073)	(1,248,377)
Accumulated other comprehensive loss	(49,861)	(49,734)
Total stockholders equity	334,479	328,164
Total liabilities and stockholders equity	$ 698,981	$ 706,212

See Notes to Unaudited Condensed Consolidated Financial Statements.

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Harte-Hanks, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income (in thousands, except per share amounts)

(Unaudited)

	Three Months Ended March 31, 2013		Three Months Ended March 31, 2012	
Operating revenues	$	178,332	$	186,042
Operating expenses				
Labor		80,308		83,879
Production and distribution		67,587		67,669
Advertising, selling, general and administrative		15,326		15,313
Depreciation and software amortization		4,882		5,145
Intangible asset amortization		55		60
Total operating expenses		168,158		172,066
Operating income		10,174		13,976
Other expenses (income)				
Interest expense		803		1,019
Interest income		(35)		(29)
Other, net		(1,218)		655
Total other expenses (income)		(450)		1,645
Income from continuing operations before income taxes		10,624		12,331
Income tax expense		3,957		4,896
Income from continuing operations		6,667		7,435
Loss from discontinued operations, net of income taxes		0		(642)
Net income	$	6,667	$	6,793
Basic earnings (loss) per common share				
Continuing operations	$	0.11	$	0.12
Discontinued operations	$	0.00	$	(0.01)
Basic earnings per common share	$	0.11	$	0.11
Weighted-average common shares outstanding		62,471		62,910
Diluted earnings (loss) per common share				
Continuing operations	$	0.11	$	0.12
Discontinued operations	$	0.00	$	(0.01)
Diluted earnings per common share	$	0.11	$	0.11
Weighted-average common and common equivalent shares outstanding		62,669		63,273
Other comprehensive income (loss), net of tax				
Adjustment to pension liability	$	1,003	$	901
Foreign currency translation adjustments		(1,130)		886
Total other comprehensive income (loss), net of tax		(127)		1,787
Comprehensive income	$	6,540	$	8,580

See Notes to Unaudited Condensed Consolidated Financial Statements.

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Harte-Hanks, Inc. and Subsidiaries

Consolidated Statements of Cash Flows (in thousands)

(Unaudited)

	Three Months Ended March 31, 2013	2012
Cash Flows from Operating Activities		
Net income	$ 6,667	$ 6,793
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss from discontinued operations	0	642
Depreciation and software amortization	4,882	5,145
Intangible asset amortization	55	60
Stock-based compensation	1,288	993
Excess tax benefits from stock-based compensation	(5)	(42)
Net pension cost	346	506
Deferred income taxes	2,769	3,018
Other, net	(851)	3
Changes in operating assets and liabilities, net of acquisitions:		
Decrease in accounts receivable, net	14,768	22,414
Decrease in inventory	92	475
Increase in prepaid expenses and other current assets	(647)	(2,215)
Decrease in accounts payable	(4,462)	(6,987)
Decrease in other accrued expenses and other current liabilities	(9,031)	(17,828)
Other, net	(945)	(196)
Net cash provided by continuing operations	14,926	12,781
Net cash provided by discontinued operations	0	171
Net cash provided by operating activities	14,926	12,952
Cash Flows from Investing Activities		
Purchases of property, plant and equipment	(4,631)	(3,054)
Proceeds from sale of property, plant and equipment	4,781	8
Net cash provided by (used in) investing activities	150	(3,046)
Cash Flows from Financing Activities		
Repayment of borrowings	(3,062)	(61,532)
Issuance of common stock	82	361
Excess tax benefits from stock-based compensation	5	42
Purchase of treasury stock	(436)	0
Dividends paid	0	(5,405)
Net cash used in financing activities	(3,411)	(66,534)
Effect of exchange rate changes on cash and cash equivalents	(302)	217
Net increase (decrease) in cash and cash equivalents	11,363	(56,411)
Cash and cash equivalents at beginning of year	49,648	86,778
Cash and cash equivalents at end of period	$ 61,011	$ 30,367

See Notes to Unaudited Condensed Consolidated Financial Statements.

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Harte-Hanks, Inc. and Subsidiaries

Consolidated Statements of Changes in Equity (in thousands, except per share amounts)

(2013 Unaudited)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
Balance at December 31, 2011	118,487	341,149	1,276,266	(1,244,224)	(45,323)	446,355
Exercise of stock options and release of nonvested shares	250	410	0	(205)	0	455
Net tax effect of options exercised and release of nonvested shares	0	(3,082)	0	0	0	(3,082)
Stock-based compensation	0	3,412	0	0	0	3,412
Dividends paid ($0.43 per share)	0	0	(26,961)	0	0	(26,961)
Treasury stock issued	0	(303)	0	454	0	151
Purchase of treasury stock	0	0	0	(4,402)	0	(4,402)
Net loss	0	0	(83,353)	0	0	(83,353)
Other comprehensive income	0	0	0	0	(4,411)	(4,411)
Balance at December 31, 2012	$ 118,737	$ 341,586	$ 1,165,952	$ (1,248,377)	$ (49,734)	$ 328,164
Exercise of stock options and release of nonvested shares	220	(138)	0	(395)	0	(313)
Net tax effect of options exercised and release of nonvested shares	0	(801)	0	0	0	(801)
Stock-based compensation	0	1,288	0	0	0	1,288
Treasury stock issued	0	(98)	0	135	0	37
Purchase of treasury stock	0	0	0	(436)	0	(436)
Net income	0	0	6,667	0	0	6,667
Other comprehensive income	0	0	0	0	(127)	(127)
Balance at March 31, 2013	$ 118,957	$ 341,837	$ 1,172,619	$ (1,249,073)	$ (49,861)	$ 334,479

See Notes to Unaudited Condensed Consolidated Financial Statements.

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Harte-Hanks, Inc. and Subsidiaries

Notes to Unaudited Condensed Consolidated Financial Statements

Note A - Basis of Presentation

Consolidation

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of Harte-Hanks, Inc. and its subsidiaries (the Company). All intercompany accounts and transactions have been eliminated in consolidation.

As used in this report, the terms Harte-Hanks, we, us or our may refer to Harte-Hanks, one or more of its consolidated subsidiaries, or all of them taken as a whole.

Interim Financial Information

The financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2013 are not necessarily indicative of the results that may be expected for the year ending December 31, 2013. The information included in this Form 10-Q should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and notes thereto included in our annual report on Form 10-K for the year ended December 31, 2012.

Discontinued Operations

As discussed in Note M, *Discontinued Operations*, we sold the assets of our Florida Shoppers operations on December 31, 2012. The operating results of our Florida Shoppers are being reported as discontinued operations in the Consolidated Financial Statements. Unless otherwise stated, amounts related to the Florida Shoppers operations are excluded from the Notes to Consolidated Financial Statements for all periods presented.

Sale of Belgium Facility

In the first quarter of 2013, we sold the facility where our Hasselt, Belgium direct marketing business was located for net proceeds of $4.6 million. At the time of the sale, the book value of this facility was $3.7 million, and the transaction resulted in a $0.9 million gain. This gain is included in Other, net in the Consolidated Statements of Comprehensive Income. This direct marketing business now operates in leased space in Hasselt, Belgium.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results and outcomes could differ from those estimates and assumptions. On an ongoing basis management reviews its estimates based on currently available information. Changes in facts and circumstances could result in revised estimates and assumptions.

Operating Expense Presentation in Consolidated Statements of Comprehensive Income

Labor in the Consolidated Statements of Comprehensive Income includes all employee payroll and benefits, including stock-based compensation, along with temporary labor costs. Production and distribution and Advertising, selling, general and administrative do not include labor, depreciation or amortization.

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Note B - Recent Accounting Pronouncements

In the first quarter of 2013, we adopted Accounting Standards Update (ASU) 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.* ASU 2013-02 addresses the presentation of reclassification adjustments, which was deferred in the initial issuance of ASU 2011-05, *Presentation of Comprehensive Income*. ASU 2013-02 requires entities to disclose:

- For items reclassified out of accumulated other comprehensive income and into net income in their entirety, the effect of the reclassification on each affected net income line item, and

- For accumulated other comprehensive income reclassification items that are not reclassified in their entirety into net income, a cross reference to other required U.S. GAAP disclosures.

In connection with this adoption we have added the required disclosures in Note J, *Comprehensive Income*. The adoption of ASU 2013-02 did not affect our operating results, cash flows or financial position.

Note C - Fair Value of Financial Instruments

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 also establishes a fair value hierarchy that prioritizes the inputs used in valuation methodologies into three levels:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Because of their maturities and/or variable interest rates, certain financial instruments have fair values approximating their carrying values. These instruments include cash and cash equivalents, accounts receivable and trade payables. The fair value of our outstanding debt is disclosed in Note E, *Long-Term Debt.*

Note D - Goodwill

As of March 31, 2013 and December 31, 2012, we had goodwill of $408.7 million. Under the provisions of FASB ASC 350, *Intangibles-Goodwill and Other*, goodwill is tested for impairment at least annually, or more frequently if events or circumstances indicate that it is more likely than not that goodwill might be impaired. Such events could include a significant change in business conditions, a significant negative regulatory outcome or other events that could negatively affect our business and financial performance. We perform our annual goodwill impairment assessment as of November 30th of each year.

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Note E - Long-Term Debt

Our long-term debt obligations were as follows:

In thousands		March 31, 2013		December 31, 2012
2010 Revolving Credit Facility, various interest rates based on LIBOR, due August 12, 2013 ($60.5 million capacity at March 31, 2013)		0		0
2011 Term Loan Facility, various interest rates based on LIBOR (effective rate of 2.20% at March 31, 2013), due August 16, 2016		107,188		110,250
Total debt		107,188		110,250
Less current maturities		12,250		12,250
Total long-term debt	$	94,938	$	98,000

The carrying values and estimated fair values of our outstanding debt were as follows:

	March 31, 2013				December 31, 2012			
In thousands		Carrying Value		Fair Value		Carrying Value		Fair Value
Total debt	$	107,188	$	107,188	$	110,250	$	110,250

The estimated fair values were calculated using current rates provided to us by our bankers for debt of the same remaining maturity and characteristics. These current rates are considered Level 2 inputs under the fair value hierarchy established by FASB ASC 820, *Fair Value Measurements and Disclosures*, (ASC 820).

Note F - Stock-Based Compensation

We recognized $1.3 million and $1.0 million of stock-based compensation during the three months ended March 31, 2013 and 2012, respectively.

Our annual grant of stock-based awards occurred in the first quarter of 2013, consistent with the timing of previous annual grants. All stock-based awards granted in the first quarter of 2013 were granted under the 2005 Omnibus Incentive Plan (2005 Plan). These grants consisted of:

	Number	Weighted-Average Grant-Date

	of Shares		Fair Value
Stock options	668,600	$	2.09
Non-vested shares	461,210	$	7.73
Performance stock units	183,000	$	7.10

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. These options become exercisable in 25% increments on the first, second, third and fourth anniversaries of their date of grant, and expire on the tenth anniversary of their date of grant. All stock options granted in the first quarter of 2013 have exercise prices equal to the market value of the common stock on the date of grant. Market value is defined by the 2005 Plan as the closing price on the previous trading day. The weighted-average exercise price of options granted in the first quarter of 2013 was $7.72.

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The fair value of each non-vested share is estimated on the date of grant as the closing market price of our common stock on the date of grant. All non-vested shares granted in the first quarter of 2013 vest in three equal increments on the first, second and third anniversaries of their date of grant.

The fair value of each performance stock unit is estimated on the date of grant as the closing market price of our common stock on the date of grant, minus the present value of anticipated dividend payments. Performance stock units are a form of share-based awards similar to non-vested shares, except that the number of shares ultimately issued is based on our performance against specific performance goals over a three-year period. At the end of the performance period, the number of shares of stock issued will be determined by adjusting upward or downward from the maximum in a range between 0% and 100%.

Note G - Components of Net Periodic Pension Benefit Cost

Prior to January 1, 1999, we maintained a defined benefit pension plan for which most of our employees were eligible. We elected to freeze benefits under this defined benefit pension plan as of December 31, 1998.

In 1994, we adopted a non-qualified, unfunded, supplemental pension plan covering certain employees, which provides for incremental pension payments so that total pension payments equal those amounts that would have been payable from our principal pension plan if it were not for limitations imposed by income tax regulations. The benefits under this supplemental pension plan continue to accrue as