TERADATA CORP /DE/
Form 10-Q
August 02, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 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 30, 2013

OR

¨ **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 001-33458

TERADATA CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**75-3236470**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

10000 Innovation Drive

Dayton, Ohio 45342

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code: (866) 548-8348

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

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

Indicate by check mark 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	x	Accelerated filer	¨
Non-accelerated filer	¨	Smaller reporting company	¨

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

At July 26, 2013, the registrant had approximately 163.1 million shares of common stock outstanding.

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PART I FINANCIAL INFORMATION

PART II OTHER INFORMATION

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Part 1 FINANCIAL INFORMATION

Item 1. Financial Statements.
Teradata Corporation

Condensed Consolidated Statements of Income (Unaudited)

In millions, except per share amounts	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Revenue				
Product revenue	$ 303	$ 321	$ 552	$ 629
Service revenue	367	344	705	649
Total revenue	670	665	1,257	1,278
Costs and operating expenses				
Cost of products	101	99	194	202
Cost of services	190	184	379	356
Selling, general and administrative expenses	185	179	364	344
Research and development expenses	47	43	97	89
Total costs and operating expenses	523	505	1,034	991
Income from operations	147	160	223	287
Other expense, net	0	0	(1)	(1)
Income before income taxes	147	160	222	286
Income tax expense	39	48	55	83
Net income	$ 108	$ 112	$ 167	$ 203
Net income per weighted average common share				
Basic	$ 0.66	$ 0.66	$ 1.02	$ 1.21
Diluted	$ 0.65	$ 0.65	$ 1.00	$ 1.18
Weighted average common shares outstanding				
Basic	163.4	168.7	164.4	168.3
Diluted	166.3	172.3	167.4	172.0

See Notes to Condensed Consolidated Financial Statements (Unaudited).

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Teradata Corporation

Condensed Consolidated Statements of Comprehensive Income (Unaudited)

In millions	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Net income	$ 108	$ 112	$ 167	$ 203
Other comprehensive income:				
Foreign currency translation adjustments	(5)	(10)	(17)	(5)
Other comprehensive loss	(5)	(10)	(17)	(5)
Comprehensive income	$ 103	$ 102	$ 150	$ 198

See Notes to Condensed Consolidated Financial Statements (Unaudited).

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Teradata Corporation

Condensed Consolidated Balance Sheets (Unaudited)

In millions, except per share amounts	June 30, 2013	December 31, 2012
Assets		
Current Assets		
Cash and cash equivalents	$ 826	$ 729
Accounts receivable, net	514	668
Inventories	70	47
Other current assets	83	90
Total current assets	1,493	1,534
Property and equipment, net	156	150
Capitalized software, net	182	173
Goodwill	934	932
Acquired intangible assets, net	168	186
Deferred income taxes	24	29
Other assets	85	62
Total assets	$ 3,042	$ 3,066
Liabilities and stockholders equity		
Current liabilities		
Accounts payable	$ 105	$ 141
Payroll and benefits liabilities	116	158
Deferred revenue	422	375
Other current liabilities	131	132
Total current liabilities	774	806
Long-term debt	263	274
Pension and other postemployment plan liabilities	72	73
Long-term deferred revenue	29	30
Deferred tax liabilities	86	83
Other liabilities	28	21
Total liabilities	1,252	1,287
Commitments and contingencies (Note 7)		
Stockholders equity		
Preferred stock: par value $0.01 per share, 100.0 shares authorized, 0.0 shares issued and outstanding at June 30, 2013 and December 31, 2012	0	0
Common stock: par value $0.01 per share, 500.0 shares authorized, 190.2 and 189.5 shares issued at June 30, 2013 and December 31, 2012, respectively	2	2
Paid-in capital	941	898
Treasury stock: 27.1 and 23.8 shares at June 30, 2013 and December 31, 2012, respectively	(988)	(806)
Retained earnings	1,823	1,656
Accumulated other comprehensive income	12	29
Total stockholders equity	1,790	1,779
Total liabilities and stockholders equity	$ 3,042	$ 3,066

See Notes to Condensed Consolidated Financial Statements (Unaudited).

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Teradata Corporation

Condensed Consolidated Statements of Cash Flows (Unaudited)

In millions	Six Months Ended June 30, 2013	2012
Operating activities		
Net income	$ 167	$ 203
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	70	61
Stock-based compensation expense	27	21
Excess tax benefit from stock-based compensation	(4)	(24)
Deferred income taxes	6	22
Changes in assets and liabilities:		
Receivables	157	(1)
Inventories	(23)	26
Current payables and accrued expenses	(72)	(22)
Deferred revenue	46	72
Other assets and liabilities	9	(14)
Net cash provided by operating activities	383	344
Investing activities		
Expenditures for property and equipment	(31)	(31)
Additions to capitalized software	(34)	(38)
Business acquisitions and other investing activities, net	(39)	(238)
Net cash used in investing activities	(104)	(307)
Financing activities		
Repurchases of common stock	(184)	(37)
Repayments of long-term borrowings	(8)	(4)
Excess tax benefit from stock-based compensation	4	24
Other financing activities, net	15	36
Net cash (used in) provided by financing activities	(173)	19
Effect of exchange rate changes on cash and cash equivalents	(9)	(7)
Increase in cash and cash equivalents	97	49
Cash and cash equivalents at beginning of period	729	772
Cash and cash equivalents at end of period	$ 826	$ 821

See Notes to Condensed Consolidated Financial Statements (Unaudited).

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Notes to Condensed Consolidated Financial Statements (Unaudited)

1. Basis of Presentation

These statements have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC) and, in accordance with those rules and regulations, do not include all information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). In the opinion of management, the condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, necessary to fairly state the results of operations, financial position and cash flows of Teradata Corporation (Teradata or the Company) for the interim periods presented herein. The year-end 2012 condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make use of estimates and assumptions that affect the reported amounts and disclosures. Actual results may vary from these estimates.

These condensed consolidated interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Teradata s most recent Annual Report on Form 10-K for the fiscal year ended December 31, 2012 (the 2012 Annual Report). The results of operations for any interim period are not necessarily indicative of the results of operations to be expected for the full year.

2. New Accounting Pronouncements

Comprehensive Income. In February 2013, the Financial Accounting Standards Board (FASB) issued new guidance regarding the disclosure of comprehensive income. Under the new guidance, entities are required to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, entities are required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under GAAP that provide additional detail about those amounts. The amendments in this update do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This new guidance was adopted by the Company as of January 1, 2013 and is not expected to have a significant impact on the Company s disclosures.

3. Supplemental Financial Information

	As of	
In millions	**June 30, 2013**	**December 31, 2012**
Inventories		
Finished goods	$ 49	$ 26
Service parts	21	21
Total inventories	$ 70	$ 47
Deferred revenue		
Deferred revenue, current	$ 422	$ 375
Long-term deferred revenue	29	30
Total deferred revenue	$ 451	$ 405

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4. Goodwill and Acquired Intangible Assets

The following table identifies the activity relating to goodwill by operating segment:

In millions	Balance December 31, 2012	Additions	Currency Translation Adjustments	Balance June 30, 2013
Goodwill				
Americas	$ 616	$ 11	$ (1)	$ 626
International	316	3	(11)	308
Total goodwill	$ 932	$ 14	$ (12)	$ 934

The changes in goodwill for the six months ended June 30, 2013 were due to the impact of immaterial acquisitions executed during the period, as well as changes in foreign currency exchange rates.

Acquired intangible assets were specifically identified when acquired, and are deemed to have finite lives. The gross carrying amount and accumulated amortization for Teradata s acquired intangible assets were as follows:

		June 30, 2013			December 31, 2012		
In millions	Original Amortization Life (in Years)	Gross Carrying Amount	Accumulated Amortization	Currency Translation Adjustment	Gross Carrying Amount	Accumulated Amortization	Currency Translation Adjustment
Acquired intangible assets							
Intellectual property/developed technology	1 to 7	$ 153	$ (59)	$ 1	$ 153	$ (50)	$ 2
Customer relationships	3 to 10	77	(20)	1	77	(15)	1
Trademarks/trade names	3.5 to 5	15	(5)	0	15	(2)	0
In-process research and development	5	5	0	0	5	0	0
Non-compete agreements	1 to 3	1	(1)	0	1	(1)	0
Total	1 to 10	$ 251	$ (85)	$ 2	$ 251	$ (68)	$ 3

In the six months ended June 30, 2013, certain intangible assets previously acquired became fully amortized and were removed from the balance sheet. This was offset by the addition of newly acquired intangible assets associated with immaterial acquisitions in the current period.

The aggregate amortization expense (actual and estimated) for acquired intangible assets for the following periods is as follows:

	Six Months Ended	For the year ended (estimated)				
In millions	June 30, 2013	2013	2014	2015	2016	2017
Amortization expense	$ 22	$ 44	$ 42	$ 39	$ 26	$ 18

5. Income Taxes

Income tax provisions for interim periods are based on estimated annual income tax rates, adjusted to reflect the effects of any significant infrequent or unusual items which are required to be discretely recognized within the current interim period. The Company s intention is to permanently reinvest its foreign earnings outside of the United States. As a result, the effective tax rates in the periods presented are largely based upon the forecasted pre-tax earnings mix and allocation of certain expenses in various taxing jurisdictions where the Company conducts its business that apply a broad range of statutory income tax rates, certain of which are less than the U.S. statutory rate.

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The effective tax rate for the three months ended June 30, 2013 and June 30, 2012 was 26.5% and 30.0%, respectively. The effective tax rate for the six months ended June 30, 2013 and June 30, 2012 was 24.8% and 29.0%, respectively. The effective tax rate for the three and six months ended June 30, 2013 included the marginal rate benefit of the U.S. Federal Research and Development Tax Credit (the Federal R&D Tax Credit) for 2013. The effective tax rate for the six months ended June 30, 2013 also included a one-time discrete $4 million tax benefit associated with the Federal R&D Tax Credit for 2012, which was retroactively reinstated with the enactment of the American Taxpayer Relief Act of 2012 in January of 2013. There were no material discrete tax items, nor any tax benefit associated with the 2012 Federal R&D Tax Credit due to its expiration, reflected in the effective tax rate for the three and six months ended June 30, 2012.

6. Derivative Instruments and Hedging Activities

As a portion of the Company s operations is conducted outside the United States and in currencies other than the U.S. dollar, the Company is exposed to potential gains and losses from changes in foreign currency exchange rates. In an attempt to mitigate the impact of currency fluctuations, the Company uses foreign exchange forward contracts to hedge transactional exposures resulting predominantly from foreign currency denominated inter-company receivables and payables. The forward contracts are designated as fair value hedges of specified foreign currency denominated inter-company receivables and payables and generally mature in three months or less. The Company does not hold or issue derivative financial instruments for trading purposes, nor does it hold or issue leveraged derivative instruments. By using derivative financial instruments to hedge exposures to changes in exchange rates, the Company exposes itself to credit risk. The Company manages exposure to counterparty credit risk by entering into derivative financial instruments with highly rated institutions that can be expected to fully perform under the terms of the applicable contracts.

All derivatives are recognized in the Consolidated Balance Sheet at their fair value. The fair values of foreign exchange contracts are based on market spot and forward exchange rates and represent estimates of possible value that may not be realized in the future. Changes in the fair value of derivative financial instruments, along with the loss or gain on the hedged asset or liability, are recorded in current period earnings. The notional amounts represent agreed-upon amounts on which calculations of dollars to be exchanged are based, and are an indication of the extent of Teradata s involvement in such instruments. These notional amounts do not represent amounts exchanged by the parties and, therefore, are not a measure of the instruments. Across its portfolio of contracts, Teradata has both long and short positions relative to the U.S. dollar. As a result, Teradata s net involvement is less than the total contract notional amount of the Company s foreign exchange forward contracts.

The contract notional amount of the Company s foreign exchange forward contracts was $85 million ($25 million on a net basis) at June 30, 2013, and $140 million ($53 million on a net basis) at December 31, 2012. The fair value derivative assets and liabilities recorded in other current assets and accrued liabilities at June 30, 2013 and December 31, 2012, were not material.

Gains and losses from the Company s fair value hedges (foreign currency forward contracts and related hedged items) were immaterial for the three and six months ended June 30, 2013 and June 30, 2012. Gains and losses from foreign exchange forward contracts are fully recognized each period and reported along with the offsetting gain or loss of the related hedged item, either in cost of products or in other income, depending on the nature of the related hedged item.

7. Commitments and Contingencies

In the normal course of business, from time to time, the Company is involved in claims, lawsuits, investigations and proceedings incidental to its business operations which management expects will be resolved without a material impact on the Company s results of operations, cash flows or financial condition. No material amount of loss in excess of recorded amounts is believed to be reasonably possible as a result of such claims, lawsuits, investigations or proceedings.

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As previously reported in our 2012 Annual Report on Form 10-K, in January 2013, the Company settled a litigation matter in federal district court filed under the qui tam provisions of the civil False Claims Act for the $3 million previously accrued on the balance sheet as of December 31, 2012, and the court dismissed the action.

Guarantees and Product Warranties. Guarantees associated with the Company s business activities are reviewed for appropriateness and impact to the Company s financial statements. Periodically, the Company s customers enter into various leasing arrangements coordinated with a leasing company. In some instances, the Company guarantees the leasing company a minimum value at the end of the lease term on the leased equipment. As of June 30, 2013, the maximum future payment obligation of this guaranteed value and the associated liability balance was $3 million.

The Company provides its customers a standard manufacturer s warranty and records, at the time of the sale, a corresponding estimated liability for potential warranty costs. Estimated future obligations due to warranty claims are based upon historical factors such as labor rates, average repair time, travel time, number of service calls and cost of replacement parts. For each consummated sale, the Company recognizes the total customer revenue and records the associated warranty liability using pre-established warranty percentages for that product class.

The following table identifies the activity relating to the warranty reserve for the six months ended June 30:

In millions	2013	2012
Warranty reserve liability		
Beginning balance at January 1	$ 8	$ 6
Provisions for warranties issued	7	8
Settlements (in cash or in kind)	(8)	(7)
Balance at June 30	$ 7	$ 7

The Company also offers extended and/or enhanced coverage to its customers in the form of maintenance contracts. The Company accounts for these contracts by deferring the related maintenance revenue over the extended and/or enhanced coverage period. Costs associated with maintenance support are expensed as incurred. Amounts associated with these maintenance contracts are not included in the table above.

In addition, the Company provides its customers with certain indemnification rights. In general, the Company agrees to indemnify the customer if a third party asserts patent or other infringement on the part of the customer for its use of the Company s products. The Company has entered into indemnification agreements with the officers and directors of its subsidiaries. From time to time, the Company also enters into agreements in connection with its acquisition and divesture activities that include indemnification obligations by the Company. The fair value of these indemnification obligations is not readily determinable due to the conditional nature of the Company s potential obligations and the specific facts and circumstances involved with each particular agreement, and as such the Company has not recorded a liability in connection with these indemnification arrangements. Historically, payments made by the Company under these types of agreements have not had a material effect on the Company s consolidated financial condition, results of operations or cash flows.

8. Fair Value Measurements

GAAP has established a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets for identical assets or liabilities; Level 2, defined as significant other observable inputs, such as quoted prices in active markets for similar assets or liabilities, or quoted prices in less-active markets for identical assets; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

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The Company s assets and liabilities measured at fair value on a recurring basis include money market funds and foreign currency exchange contracts. A portion of the Company s excess cash reserves are held in money market funds which generate interest income based on the prevailing market rates. Money market funds are included in cash and cash equivalents in the Company s balance sheet. Money market fund holdings are measured at fair value using quoted market prices and are classified within Level 1 of the valuation hierarchy. When deemed appropriate, the Company minimizes its exposure to changes in foreign currency exchange rates through the use of derivative financial instruments, specifically, forward foreign exchange contracts. The fair value of these contracts are measured at the end of each interim reporting period using observable inputs other than quoted prices, specifically market spot and forward exchange rates. As such, these derivative instruments are classified within Level 2 of the valuation hierarchy. Fair value gains for open contracts are recognized as assets and fair value losses are recognized as liabilities. The fair value derivative assets and liabilities recorded in other current assets and accrued liabilities at June 30, 2013 and December 31, 2012, were not material. Any realized gains or losses would be mitigated by corresponding gains or losses on the underlying exposures.

The Company s assets measured at fair value on a recurring basis and subject to fair value disclosure requirements at June 30, 2013 and December 31, 2012 were as follows:

		Fair Value Measurements at Reporting Date Using		
In millions	**Total**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Assets				
Money market funds, June 30, 2013	$ 434	$ 434	$ 0	$ 0
Money market funds, December 31, 2012	$ 260	$ 260	$ 0	$ 0

9. Debt

In June 2012, Teradata entered into a five-year revolving credit agreement (the Credit Facility), under which the Company may borrow up to $300 million. The Credit Facility replaced a similar revolving credit agreement in the same maximum principal amount entered into by Teradata in 2007. The Credit Facility ends on June 15, 2017, at which point any remaining outstanding borrowings would be due for repayment unless extended by agreement of the parties for up to two additional one-year periods. The interest rate charged on borrowings pursuant to the Credit Facility can vary depending on the interest rate option the Company chooses to utilize and the Company s leverage ratio at the time of the borrowing. In the near term, Teradata would anticipate choosing a floating rate based on the London Interbank Offered Rate (LIBOR). The Credit Facility is unsecured and contains certain representations and warranties, conditions, affirmative, negative and financial covenants, and events of default customary for such facilities.

As of June 30, 2013, the Company had no borrowings outstanding under the Credit Facility, leaving $300 million in additional borrowing capacity available under the Credit Facility.

Teradata s senior unsecured $300 million five-year term loan is payable in quarterly installments, which commenced in June 2012, with all remaining principal due in April 2016. The outstanding principal amount of the term loan agreement bears interest at a floating rate based upon a negotiated base rate or a Eurodollar rate plus in each case a margin based on the leverage ratio of the Company. As of June 30, 2013, the term loan principal outstanding was $281 million, and carried an interest rate of 1.25%.

Teradata s term loan is recognized on the Company s balance sheet at its unpaid principal balance, and is not subject to fair value measurement. However, given that the loan carries a variable rate, the Company estimates that the unpaid principal balance of the term loan would approximate its fair value. If measured at fair value in the financial statements, the Company s term loan would be classified as Level 2 in the fair value hierarchy.

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10. Earnings Per Share

Basic earnings per share is calculated by dividing net income by the weighted average number of shares outstanding during the reported period. The calculation of diluted earnings per share is similar to basic earnings per share, except that the weighted average number of shares outstanding includes the dilution from potential shares resulting from stock options and unvested restricted stock awards.

The components of basic and diluted earnings per share are as follows:

In millions, except per share amounts	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Net income available for common stockholders	$ 108	$ 112	$ 167	$ 203
Weighted average outstanding shares of common stock	163.4	168.7	164.4	168.3
Dilutive effect of employee stock options and restricted stock	2.9	3.6	3.0	3.7
Common stock and common stock equivalents	166.3	172.3	167.4	172.0
Earnings per share:				
Basic	$ 0.66	$ 0.66	$ 1.02	$ 1.21
Diluted	$ 0.65	$ 0.65	$ 1.00	$ 1.18

Options to purchase 0.7 million and 0.4 million shares of common stock for the three and six months ended June 30, 2013 were not included in the computation of diluted earnings per share because their exercise prices were greater than the average market price of the common shares for the respective periods and, therefore, the effect would have been anti-dilutive. Because the average market price of common shares was greater than the exercise prices of outstanding awards, no stock options were excluded from the computation of diluted earnings per share for the three and six month periods ended June 30, 2012.

11. Segment and Other Supplemental Information

Effective January 1, 2013, Teradata combined the management of the Europe, Middle East and Africa, and the Asia Pacific and Japan regions into a new International region. This larger International region has greater critical mass and leverage of resources for deployment of the Company s integrated marketing management, big data analytics, and data warehouse solutions, and also possesses more knowledge depth for our numerous consulting and support services offers.

As a result, Teradata now manages its business in two geographic regions, which are also the Company s operating segments: (1) the North America and Latin America (Americas) region; and (2) the International region. Management evaluates the performance of its segments based on revenue and segment margin, and does not include segment assets for management reporting purposes. Corporate-related costs are fully allocated to the segments.

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The following table presents regional segment revenue and gross margin for the Company. For comparative purposes, prior-year amounts have been reclassified to conform to the current-year presentation:

In millions	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Revenue				
Americas	$ 405	$ 398	$ 760	$ 786
International	265	267	497	492
Total revenue	670	665	1,257	1,278
Gross margin				
Americas	240	242		