

ALLIANCE DATA SYSTEMS CORP

Form 10-Q

May 05, 2006

Table of Contents

**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, 2006
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

For the transition period from to

Commission File Number: 001-15749

ALLIANCE DATA SYSTEMS CORPORATION
(Exact Name of Registrant as Specified in its Charter)

Delaware
*(State or Other Jurisdiction of
Incorporation or Organization)*

31-1429215
*(I.R.S. Employer
Identification No.)*

17655 Waterview Parkway
Dallas, Texas 75252
(Address of Principal Executive Office, Including Zip Code)

(972) 348-5100
(Registrant's Telephone Number, Including Area Code)

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

Title of Each Class

Name of Each Exchange on Which Registered

Common Stock, par value \$0.01 per share

New York Stock Exchange

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

None

(Title of Class)

Indicate by check mark whether the registrant: (1) has filed all reports required 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, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer Accelerated filer Non-accelerated filer

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

As of May 1, 2006, 81,212,893 shares of common stock were outstanding.

ALLIANCE DATA SYSTEMS CORPORATION

INDEX

Page
Number

Part I: FINANCIAL INFORMATION

<u>Item 1.</u>	<u>Financial Statements (unaudited)</u>	
	<u>Condensed Consolidated Balance Sheets as of December 31, 2005 and March 31, 2006</u>	3
	<u>Condensed Consolidated Statements of Income for the three months ended March 31, 2005 and 2006</u>	4
	<u>Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2005 and 2006</u>	5
	<u>Notes to Condensed Consolidated Financial Statements</u>	6
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	15
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	25
<u>Item 4.</u>	<u>Controls and Procedures</u>	25

Part II: OTHER INFORMATION

<u>Item 1.</u>	<u>Legal Proceedings</u>	26
<u>Item 1A.</u>	<u>Risk Factors</u>	26
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	26
<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u>	26
<u>Item 4.</u>	<u>Submission of Matters to a Vote of Security Holders</u>	26
<u>Item 5.</u>	<u>Other Information</u>	26
<u>Item 6.</u>	<u>Exhibits</u>	27

SIGNATURES

<u>Sixth Amendment to Credit Agreement</u>	28
<u>Certification of CEO Pursuant to Rule 13a-14(a)</u>	
<u>Certification of CFO Pursuant to Rule 13a-14(a)</u>	
<u>Certification of CEO Pursuant to Rule 13a-14(b)</u>	
<u>Certification of CFO Pursuant to Rule 13a-14(b)</u>	

Table of Contents**PART I****Item 1. Financial Statements****ALLIANCE DATA SYSTEMS CORPORATION****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

	December 31, 2005	March 31, 2006
	(in thousands, except per share amounts)	
ASSETS		
Cash and cash equivalents	\$ 143,213	\$ 256,828
Due from card associations	58,416	13,950
Trade receivables, less allowance for doubtful accounts (\$2,079 and \$1,849 at December 31, 2005 and March 31, 2006, respectively)	203,883	195,814
Seller's interest and credit card receivables, less allowance for doubtful accounts (\$38,415 and \$39,274 at December 31, 2005 and March 31, 2006, respectively)	479,108	428,963
Deferred tax asset, net	70,221	70,221
Other current assets	87,612	102,738
Total current assets	1,042,453	1,068,514
Redemption settlement assets, restricted	260,963	266,394
Property and equipment, net	162,972	169,927
Due from securitizations	271,256	223,662
Intangible assets, net	265,000	252,180
Goodwill	858,470	866,914
Other non-current assets	64,968	60,311
Total assets	\$ 2,926,082	\$ 2,907,902
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accounts payable	\$ 67,384	\$ 72,336
Accrued expenses	198,707	156,325
Merchant settlement obligations	127,038	97,335
Certificates of deposit	342,600	253,100
Credit facilities and other debt, current	235,843	305,775
Other current liabilities	76,999	78,887
Total current liabilities	1,048,571	963,758
Deferred tax liability, net	62,847	59,662
Deferred revenue	610,533	618,786
Certificates of deposit	36,500	25,100

Edgar Filing: ALLIANCE DATA SYSTEMS CORP - Form 10-Q

Long-term and other debt	222,001	257,194
Other liabilities	24,523	11,992
Total liabilities	2,004,975	1,936,492
Stockholders' equity:		
Common stock, \$0.01 par value; authorized 200,000 shares; issued 84,765 shares and 85,449 shares at December 31, 2005 and March 31, 2006, respectively	848	854
Unearned compensation	(14,504)	
Additional paid-in capital	743,545	753,138
Treasury stock, at cost (4,360 shares and 5,030 shares at December 31, 2005 and March 31, 2006, respectively)	(154,952)	(184,587)
Retained earnings	338,081	394,502
Accumulated other comprehensive income	8,089	7,503
Total stockholders' equity	921,107	971,410
Total liabilities and stockholders' equity	\$ 2,926,082	\$ 2,907,902

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

ALLIANCE DATA SYSTEMS CORPORATION
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME

	Three months ended	
	March 31,	
	2005	2006
	(in thousands, except per share amounts)	
Revenues		
Transaction	\$ 142,964	\$ 164,019
Redemption	62,667	78,948
Securitization income and finance charges, net	114,464	160,879
Database marketing fees	44,870	54,289
Other revenue	10,910	19,096
 Total revenue	 375,875	 477,231
Operating expenses		
Cost of operations (exclusive of depreciation and amortization disclosed separately below)	264,157	330,319
General and administrative	24,299	19,966
Depreciation and other amortization	15,329	15,217
Amortization of purchased intangibles	9,841	12,321
 Total operating expenses	 313,626	 377,823
Operating income	62,249	99,408
Interest expense, net	2,761	8,537
 Income before income taxes	 59,488	 90,871
Provision for income taxes	22,306	34,450
 Net income	 \$ 37,182	 \$ 56,421
 Net income per share basic	 \$ 0.45	 \$ 0.70
 Net income per share diluted	 \$ 0.43	 \$ 0.69
 Weighted average shares basic	 82,329	 80,065
 Weighted average shares diluted	 85,713	 81,667

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**ALLIANCE DATA SYSTEMS CORPORATION****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Three months ended March 31,	
	2005	2006
	(in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 37,182	\$ 56,421
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	10,339	12,053
Amortization	14,831	15,485
Deferred income taxes	(2,037)	(3,294)
Provision for doubtful accounts	648	3,557
Non-cash stock compensation	1,444	7,304
Change in operating assets and liabilities, net of acquisitions:		
Change in trade accounts receivable	11,890	20,057
Change in merchant settlement activity	(5,974)	14,763
Change in other assets	6,324	(12,075)
Change in accounts payable and accrued expenses	(5,712)	(32,334)
Change in deferred revenue	6,045	10,935
Change in other liabilities	3,574	(19,664)
Tax benefit of stock option exercises	6,961	
Excess tax benefits from stock-based compensation		(4,412)
Other	(4,856)	1,980
Net cash provided by operating activities	80,659	70,776
CASH FLOWS FROM INVESTING ACTIVITIES:		
Change in redemption settlement assets	(2,401)	(6,156)
Payments for acquired businesses, net of cash acquired	(2,322)	(36,124)
Net decrease in seller's interest and credit card receivables	53,584	56,269
Change in due from securitizations	46,064	52,170
Capital expenditures	(11,905)	(20,397)
Other	319	404
Net cash provided by investing activities	83,339	46,166
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings under debt agreements	163,575	465,323
Repayment of borrowings	(201,575)	(359,000)
Certificate of deposit issuances		20,000
Repayments of certificates of deposits	(59,200)	(120,900)
Payment of capital lease obligations	(1,890)	(2,093)
Excess tax benefits from stock-based compensation		4,412
Proceeds from issuance of common stock	7,527	14,544
Purchase of treasury shares		(25,633)

Edgar Filing: ALLIANCE DATA SYSTEMS CORP - Form 10-Q

Net cash used in financing activities	(91,563)	(3,347)
Effect of exchange rate changes on cash and cash equivalents	(144)	20
Change in cash and cash equivalents	72,291	113,615
Cash and cash equivalents at beginning of period	84,409	143,213
Cash and cash equivalents at end of period	\$ 156,700	\$ 256,828
SUPPLEMENTAL CASH FLOW INFORMATION:		
Interest paid	\$ 2,903	\$ 8,081
Income taxes paid, net of refunds	\$ 18,957	\$ 32,548

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**ALLIANCE DATA SYSTEMS CORPORATION****NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS****1. BASIS OF PRESENTATION**

The unaudited condensed consolidated financial statements included herein have been prepared by Alliance Data Systems Corporation (ADSC or, including its wholly owned subsidiaries, the Company), without audit, 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 accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures are adequate to make the information presented not misleading. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company s Annual Report filed on Form 10-K/A for the year ended December 31, 2005.

The unaudited condensed consolidated financial statements included herein reflect all adjustments (consisting of normal, recurring adjustments) which are, in the opinion of management, necessary to state fairly the results for the interim periods presented. The results of operations for the interim periods presented are not necessarily indicative of the operating results to be expected for any subsequent interim period or for the fiscal year.

The preparation of financial statements in conformity with GAAP 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 date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

For purposes of comparability, certain prior period amounts, including marketing service revenue, have been reclassified to conform to the current year presentation. Such reclassifications have no impact on previously reported net income.

2. SHARES USED IN COMPUTING NET INCOME PER SHARE

The following table sets forth the computation of basic and diluted net income per share for the periods indicated:

	Three months ended March 31,	
	2005	2006
	(in thousands, except per share amounts)	
Numerator		
Net income available to common stockholders	\$ 37,182	\$ 56,421
Denominator		
Weighted average shares, basic	82,329	80,065
Weighted average effect of dilutive securities: Net effect of unvested restricted stock	370	224

Net effect of dilutive stock options	3,014	1,378
Denominator for diluted calculation	85,713	81,667
Basic		
Net income per share	\$ 0.45	\$ 0.70
Diluted		
Net income per share	\$ 0.43	\$ 0.69

Table of Contents

ALLIANCE DATA SYSTEMS CORPORATION

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS (Continued)**

3. ACQUISITIONS