

DELUXE CORP  
Form 10-Q  
May 02, 2013

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, 2013

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: 1-7945

DELUXE CORPORATION  
(Exact name of registrant as specified in its charter)

Minnesota  
(State or other jurisdiction of incorporation or organization) 41-0216800  
(I.R.S. Employer Identification No.)  
3680 Victoria St. N., Shoreview, Minnesota 55126-2966  
(Address of principal executive offices) (Zip Code)

(651) 483-7111  
(Registrant's telephone number, including area code)

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 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  Smaller reporting company

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(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).  
o Yes  No

The number of shares outstanding of registrant's common stock, par value \$1.00 per share, at April 23, 2013 was 50,863,301.

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## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements.

## DELUXE CORPORATION

## CONSOLIDATED BALANCE SHEETS

(in thousands, except share par value)

(Unaudited)

	March 31, 2013	December 31, 2012
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$70,741	\$45,435
Trade accounts receivable (net of allowances for uncollectible accounts of \$3,833 and \$3,912, respectively)	74,873	70,387
Inventories and supplies	23,735	23,291
Deferred income taxes	6,774	7,687
Funds held for customers	41,394	43,140
Other current assets	38,363	29,803
Total current assets	255,880	219,743
Deferred Income Taxes	1,621	1,662
Long-Term Investments (including \$2,111 and \$2,196 of investments at fair value, respectively)	44,415	46,898
Property, Plant And Equipment (net of accumulated depreciation of \$361,384 and \$358,580, respectively)	101,770	104,189
Assets Held For Sale	2,300	970
Intangibles (net of accumulated amortization of \$480,861 and \$472,078, respectively)	146,003	150,717
Goodwill	789,586	789,636
Other Non-Current Assets	100,235	98,625
Total Assets	\$1,441,810	\$1,412,440
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts payable	\$63,210	\$65,107
Accrued liabilities	154,295	155,003
Long-term debt due within one year	172	—
Total current liabilities	217,677	220,110
Long-Term Debt	650,429	652,581
Deferred Income Taxes	74,744	75,147
Other Non-Current Liabilities	35,137	31,667
Commitments And Contingencies (Notes 10 and 11)		
Shareholders' Equity:		
Common shares \$1 par value (authorized: 500,000 shares; outstanding: 2013 – 50,669; 2012 – 50,614)	50,669	50,614
Additional paid-in capital	46,282	47,968
Retained earnings	408,144	375,000
Accumulated other comprehensive loss (Note 5)	(41,272	) (40,647
Total shareholders' equity	463,823	432,935
Total Liabilities And Shareholders' Equity	\$1,441,810	\$1,412,440

See Condensed Notes to Unaudited Consolidated Financial Statements

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DELUXE CORPORATION  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(in thousands, except per share amounts)  
(Unaudited)

	Quarter Ended March 31,	
	2013	2012
Product revenue	\$339,875	\$341,427
Service revenue	47,678	36,554
Total Revenue	387,553	377,981
Cost of products sold	(112,270	) (111,615
Cost of services provided	(21,027	) (15,872
Total Cost Of Revenue	(133,297	) (127,487
Gross Profit	254,256	250,494
Selling, general and administrative expense	(175,152	) (171,831
Net restructuring charges	(1,371	) (638
Operating Income	77,733	78,025
Interest expense	(9,479	) (11,697
Other income	350	39
Income Before Income Taxes	68,604	66,367
Income tax provision	(22,729	) (22,288
Net Income	\$45,875	\$44,079
Comprehensive Income	\$45,250	\$45,610
Basic Earnings Per Share	\$0.90	\$0.86
Diluted Earnings Per Share	0.89	0.86
Cash Dividends Per Share	0.25	0.25

See Condensed Notes to Unaudited Consolidated Financial Statements

DELUXE CORPORATION  
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY  
(in thousands)  
(Unaudited)

	Common shares par value <sup>(1)</sup>	Additional paid-in capital	Retained earnings	Accumulated other comprehensive loss	Total
Balance, December 31, 2012	\$50,614	\$47,968	\$375,000	\$(40,647)	) \$432,935
Net income	—	—	45,875	—	45,875
Cash dividends	—	—	(12,731)	) —	(12,731)
Common shares issued	424	10,600	—	—	11,024
Tax impact of share-based awards	—	473	—	—	473
Common shares repurchased	(309)	) (12,300)	) —	—	(12,609)
Other common shares retired	(60)	) (2,296)	) —	—	(2,356)
Fair value of share-based compensation	—	1,837	—	—	1,837
Other comprehensive loss (Note 5)	—	—	—	(625)	) (625)
Balance, March 31, 2013	\$50,669	\$46,282	\$408,144	\$(41,272)	) \$463,823

<sup>(1)</sup> As the par value of our common shares is \$1.00 per share, the number of shares associated with the transactions presented here is equivalent to the related par value. See Note 12 for share information.

See Condensed Notes to Unaudited Consolidated Financial Statements

DELUXE CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Quarter Ended March 31,	
	2013	2012
Cash Flows From Operating Activities:		
Net income	\$45,875	\$44,079
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	4,556	5,108
Amortization of intangibles	11,343	11,989
Amortization of contract acquisition costs	4,102	4,379
Deferred income taxes	(144	) 2,557
Employee share-based compensation expense	1,919	1,550
Other non-cash items, net	2,016	2,514
Changes in assets and liabilities, net of effect of acquisitions:		
Trade accounts receivable	(5,605	) 532
Inventories and supplies	(948	) (1,043
Other current assets	(4,180	) (5,679
Non-current assets	(3,520	) 1,020
Accounts payable	(1,800	) (3,829
Contract acquisition payments	(3,177	) (9,357
Other accrued and non-current liabilities	1,031	(1,824
Net Cash Provided By Operating Activities	51,468	51,996
Cash Flows From Investing Activities:		
Purchases of capital assets	(8,304	) (8,996
Payments for acquisitions	(1,360	) (417
Loans to distributors	(365	) (123
Other	192	448
Net Cash Used By Investing Activities	(9,837	) (9,088
Cash Flows From Financing Activities:		
Payments for debt issue costs	(138	) (1,038
Change in book overdrafts	55	(2,628
Proceeds from issuing shares under employee plans	8,987	2,661
Excess tax benefit from share-based employee awards	915	362
Payments for common shares repurchased	(12,609	) —
Cash dividends paid to shareholders	(12,731	) (12,760
Net Cash Used By Financing Activities	(15,521	) (13,403
Effect Of Exchange Rate Change On Cash	(804	) 523
Net Change In Cash And Cash Equivalents	25,306	30,028
Cash And Cash Equivalents, Beginning Of Year	45,435	28,687
Cash And Cash Equivalents, End Of Period	\$70,741	\$58,715

See Condensed Notes to Unaudited Consolidated Financial Statements

DELUXE CORPORATION  
 CONDENSED NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (dollars and shares in thousands, except per share amounts)

Note 1: Consolidated financial statements

The consolidated balance sheet as of March 31, 2013, the consolidated statements of comprehensive income for the quarters ended March 31, 2013 and 2012, the consolidated statement of shareholders' equity for the quarter ended March 31, 2013, and the consolidated statements of cash flows for the quarters ended March 31, 2013 and 2012 are unaudited. The consolidated balance sheet as of December 31, 2012 was derived from audited consolidated financial statements, but does not include all disclosures required by generally accepted accounting principles (GAAP) in the United States of America. In the opinion of management, all adjustments necessary for a fair statement of the consolidated financial statements are included. Adjustments consist only of normal recurring items, except for any discussed in the notes below. Interim results are not necessarily indicative of results for a full year. The consolidated financial statements and notes are presented in accordance with instructions for Form 10-Q, and do not contain certain information included in our annual consolidated financial statements and notes. The consolidated financial statements and notes appearing in this report should be read in conjunction with the consolidated audited financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2012 (the "2012 Form 10-K").

Note 2: New accounting pronouncements

On January 1, 2013, we adopted Accounting Standards Update (ASU) No. 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. This standard requires that companies present information about reclassification adjustments from accumulated other comprehensive income in a single note or on the face of the financial statements, including the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source and the line item on the statement of comprehensive income affected by the reclassification adjustment. The disclosures required by this new standard are presented in Note 5: Other comprehensive income.

ASU No. 2012-02, Testing Indefinite-Lived Intangible Assets for Impairment, became effective for us on January 1, 2013. Under this new guidance, companies have the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount. If the qualitative assessment indicates that it is more likely than not that the asset is impaired, then a quantitative assessment must be completed. We complete our annual impairment analysis of our indefinite-lived trade name during the third quarter of the year. At that time, we will determine whether we will complete a qualitative assessment of the asset.

Note 3: Supplemental balance sheet information

Inventories and supplies – Inventories and supplies were comprised of the following:

	March 31, 2013	December 31, 2012
Raw materials	\$4,735	\$4,818
Semi-finished goods	8,350	8,390
Finished goods	7,471	7,005
Supplies, primarily production	3,179	3,078



Inventories and supplies	\$23,735	\$23,291
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Available-for-sale securities – Available-for-sale securities included within cash and cash equivalents, funds held for customers and other current assets were comprised of the following:

	March 31, 2013			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Canadian and provincial government securities	\$10,183	\$—	\$(99)	) \$10,084
Canadian guaranteed investment certificate	5,406	—	—	5,406
Available-for-sale securities (funds held for customers) <sup>(1)</sup>	15,589	—	(99)	) 15,490
Money market securities (cash equivalents)	36,101	—	—	36,101
Canadian money market fund (other current assets)	2,115	—	—	2,115
Total available-for-sale securities	\$53,805	\$—	\$(99)	) \$53,706

<sup>(1)</sup> Funds held for customers, as reported on the consolidated balance sheet as of March 31, 2013, also included cash of \$25,904.

	December 31, 2012			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Canadian and provincial government securities	\$10,371	\$—	\$(115)	) \$10,256
Canadian guaranteed investment certificate	5,544	—	—	5,544
Available-for-sale securities (funds held for customers) <sup>(1)</sup>	15,915	—	(115)	) 15,800
Money market securities (cash equivalents)	9,350	—	—	9,350
Canadian money market fund (other current assets)	2,162	—	—	2,162
Total available-for-sale securities	\$27,427	\$—	\$(115)	) \$27,312

<sup>(1)</sup> Funds held for customers, as reported on the consolidated balance sheet as of December 31, 2012, also included cash of \$27,340.

Expected maturities of available-for-sale securities as of March 31, 2013 were as follows:

Due in one year or less	Fair value
Due in two to five years	\$44,116
Due in six to ten years	3,721
Due in more than ten years	5,506
Total available-for-sale securities	363
	\$53,706

Further information regarding the fair value of available-for-sale securities can be found in Note 7: Fair value measurements.

Assets held for sale – Assets held for sale consisted of the operations of small business distributors which we purchased during the fourth quarter of 2012 and the first quarter of 2013. The assets purchased consisted primarily of customer lists. We are actively marketing the assets and anticipate selling them within the next several months.

Intangibles – Intangibles were comprised of the following:

	March 31, 2013			December 31, 2012		
	Gross carrying amount	Accumulated amortization	Net carrying amount	Gross carrying amount	Accumulated amortization	Net carrying amount
Indefinite-lived:						
Trade name	\$ 19,100	\$—	\$ 19,100	\$ 19,100	\$—	\$ 19,100
Amortizable intangibles:						
Internal-use software	445,584	(383,764 )	61,820	438,988	(376,111 )	62,877
Trade names	68,561	(31,218 )	37,343	68,561	(30,151 )	38,410
Customer lists/relationships	56,223	(29,791 )	26,432	58,735	(30,287 )	28,448
Distributor contracts	30,900	(30,450 )	450	30,900	(29,999 )	901
Other	6,496	(5,638 )	858	6,511	(5,530 )	981
Amortizable intangibles	607,764	(480,861 )	126,903	603,695	(472,078 )	131,617
Intangibles	\$ 626,864	\$(480,861 )	\$ 146,003	\$ 622,795	\$(472,078 )	\$ 150,717

Total amortization of intangibles was \$11,343 for the quarter ended March 31, 2013 and \$11,989 for the quarter ended March 31, 2012. Based on the intangibles in service as of March 31, 2013, estimated future amortization expense is as follows:

	Estimated amortization expense
Remainder of 2013	\$29,040
2014	28,017
2015	15,534
2016	8,679
2017	6,345

Goodwill – Changes in goodwill during the quarter ended March 31, 2013 were as follows:

	Small Business Services	Financial Services	Direct Checks	Total
Balance, December 31, 2012:				
Goodwill, gross	\$ 633,952	\$ 27,178	\$ 148,506	\$ 809,636
Accumulated impairment charges	(20,000 )	—	—	(20,000 )
Goodwill, net of accumulated impairment charges	613,952	27,178	148,506	789,636
Currency translation adjustment	(50 )	—	—	(50 )
Balance, March 31, 2013:				
Goodwill, gross	633,902	27,178	148,506	809,586
Accumulated impairment charges	(20,000 )	—	—	(20,000 )
Goodwill, net of accumulated impairment charges	\$ 613,902	\$ 27,178	\$ 148,506	\$ 789,586

Other non-current assets – Other non-current assets were comprised of the following:

	March 31, 2013	December 31, 2012
Contract acquisition costs	\$43,070	\$43,036
Loans and notes receivable from distributors	17,810	18,162
Deferred advertising costs	10,544	13,783
Other	28,811	23,644
Other non-current assets	\$100,235	\$98,625

Changes in contract acquisition costs during the quarters ended March 31, 2013 and 2012 were as follows:

	Quarter Ended March 31,	
	2013	2012
Balance, beginning of year	\$43,036	\$55,076
Additions <sup>(1)</sup>	4,269	520
Amortization	(4,102	) (4,379
Other	(133	) (149
Balance, end of period	\$43,070	\$51,068

<sup>(1)</sup> Contract acquisition costs are accrued upon contract execution. Cash payments made for contract acquisition costs were \$3,177 for the quarter ended March 31, 2013 and \$9,357 for the quarter ended March 31, 2012.

Accrued liabilities – Accrued liabilities were comprised of the following:

	March 31, 2013	December 31, 2012
Funds held for customers	\$40,648	\$42,460
Customer rebates	20,867	22,164
Income taxes	18,220	—
Employee profit sharing/cash bonus	14,082	40,670
Wages, including vacation	11,296	7,364
Interest	11,213	8,465
Contract acquisition costs due within one year	4,801	3,820
Restructuring due within one year (Note 8)	2,869	4,507
Other	30,299	25,553
Accrued liabilities	\$154,295	\$155,003

## Note 4: Earnings per share

The following table reflects the calculation of basic and diluted earnings per share. During each period, certain stock options, as noted below, were excluded from the calculation of diluted earnings per share because their effect would have been antidilutive.

	Quarter Ended March 31,	
	2013	2012
Earnings per share – basic:		
Net income	\$45,875	\$44,079
Income allocated to participating securities	(330	) (288
Income available to common shareholders	\$45,545	\$43,791
Weighted-average shares outstanding	50,707	50,898
Earnings per share – basic	\$0.90	\$0.86
Earnings per share – diluted:		
Net income	\$45,875	\$44,079
Income allocated to participating securities	(328	) (287
Re-measurement of share-based awards classified as liabilities	153	13
Income available to common shareholders	\$45,700	\$43,805
Weighted-average shares outstanding	50,707	50,898
Dilutive impact of potential common shares	465	298
Weighted-average shares and potential common shares outstanding	51,172	51,196
Earnings per share – diluted	\$0.89	\$0.86
Antidilutive options excluded from calculation	412	2,164

## Note 5: Other comprehensive income

Accumulated other comprehensive loss – Changes in the components of accumulated other comprehensive loss were as follows:

	Pension and postretirement benefit plans, net of tax	Loss on derivatives, net of tax <sup>(1)</sup>	Net unrealized loss on marketable securities, net of tax <sup>(2)</sup>	Currency translation adjustment	Accumulated other comprehensive loss
Balance, December 31, 2012	\$(45,303	) \$(1,821	) \$(92	) \$6,569	\$(40,647
Other comprehensive income (loss) before reclassifications	—	—	8	(1,419	) (1,411
Amounts reclassified from accumulated other comprehensive loss	526	260	—	—	786
Net current-period other comprehensive income (loss)	526	260	8	(1,419	) (625
Balance, March 31, 2013	\$(44,777	) \$(1,561	) \$(84	) \$5,150	\$(41,272

<sup>(1)</sup> Relates to interest rate locks executed in 2004. See the caption "Note 6: Derivative financial instruments" in the Notes to Consolidated Financial Statements appearing in the 2012 Form 10-K.

<sup>(2)</sup> Other comprehensive income before reclassifications is net of an income tax benefit of \$3.



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Reclassification adjustments – Information regarding amounts reclassified from accumulated other comprehensive loss to net income was as follows:

Accumulated other comprehensive loss components	Amounts reclassified from accumulated other comprehensive loss		Affected line item in consolidated statements of comprehensive income
	Quarter Ended March 31, 2013	2012	
Amortization of postretirement benefit plan items:			
Prior service credit	\$355	\$764	(1)
Net actuarial loss	(1,110)	) (1,469	) (1)
Total amortization	(755	) (705	) (1)
Tax benefit	229	266	(1)
Amortization of postretirement benefit plan items, net of tax	\$(526	) \$(439	) (1)
Amortization of loss on interest rate locks	\$(412	) \$(447	) Interest expense
Tax benefit	152	169	Income tax provision
Amortization of loss on interest rate locks, net of tax	\$		