WMS INDUSTRIES INC /DE/
Form 10-Q
May 03, 2012
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2012

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: 1-8300

WMS INDUSTRIES INC.

(Exact name of registrant as specified in its Charter)

Delaware	**36-2814522**
(State or other Jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

800 South Northpoint Blvd.

Waukegan, IL 60085

(Address of Principal Executive Offices)

(847) 785-3000

(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 x No ¨

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 (§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 ¨

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. (Check one):

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 55,081,341 shares of common stock, $0.50 par value, were outstanding at April 30, 2012.

Table of Contents

WMS INDUSTRIES INC.

INDEX

		Page
Part I.	**Financial Information**	3
Item 1.	Financial Statements	3
	Condensed Consolidated Statements of Income (unaudited) for the Three and Nine Months Ended March 31, 2012 and 2011	3
	Condensed Consolidated Balance Sheets as of March 31, 2012 (unaudited) and June 30, 2011	4
	Condensed Consolidated Statements of Cash Flows (unaudited) for the Nine Months Ended March 31, 2012 and 2011	5
	Notes to Condensed Consolidated Financial Statements (unaudited)	6
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	26
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	46
Item 4.	Controls and Procedures	46
Part II.	**Other Information**	46
Item 1.	Legal Proceedings	46
Item 1A.	Risk Factors	46
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	48
Item 3.	Defaults Upon Senior Securities	48
Item 4.	Mine Safety Disclosures	48
Item 5.	Other Information	48
Item 6.	Exhibits	49
Signatures		50

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

WMS INDUSTRIES INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

For the Three and Nine Months Ended March 31, 2012 and 2011

(in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2012	2011	2012	2011
REVENUES:				
Product sales	$ 110.6	$ 120.2	$ 295.2	$ 358.6
Gaming operations	65.4	72.5	198.6	221.5
Total revenues	**176.0**	**192.7**	**493.8**	**580.1**
COSTS AND EXPENSES:				
Cost of product sales(1)	53.3	61.8	144.8	182.0
Cost of gaming operations(1)	12.6	13.9	41.3	44.0
Research and development	22.1	27.7	70.2	86.5
Selling and administrative	33.7	36.1	105.2	112.5
Impairment and restructuring	0.0	0.0	9.7	3.8
Depreciation and amortization(1)	23.1	18.4	66.9	50.5
Total costs and expenses	**144.8**	**157.9**	**438.1**	**479.3**
OPERATING INCOME	**31.2**	**34.8**	**55.7**	**100.8**
Interest expense	(0.4)	(0.3)	(1.2)	(0.9)
Interest income and other income and expense, net	2.6	2.7	9.5	6.6
Income before income taxes	33.4	37.2	64.0	106.5
Provision for income taxes	11.3	13.0	22.0	35.8
NET INCOME	**$ 22.1**	**$ 24.2**	**$ 42.0**	**$ 70.7**
Earnings per share:				
Basic	$ 0.40	$ 0.42	$ 0.75	$ 1.22
Diluted	$ 0.40	$ 0.41	$ 0.75	$ 1.19
Weighted-average common shares:				
Basic common stock outstanding	55.2	57.6	55.7	57.9

Diluted common stock and common stock equivalents	55.5	58.9	56.0	59.3

(1) Cost of product sales and cost of gaming operations exclude the following amounts of depreciation and amortization, which are included in the depreciation and amortization line item:

Cost of product sales	$ 1.5	$ 1.2	$ 4.3	$ 3.6
Cost of gaming operations	$ 14.6	$ 10.7	$ 41.8	$ 29.4

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

3

Table of Contents

WMS INDUSTRIES INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in millions of U.S. dollars and millions of shares)

	March 31, 2012 (unaudited)	June 30, 2011
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 74.5	$ 90.7
Restricted cash and cash equivalents	13.1	14.3
Total cash, cash equivalents and restricted cash	87.6	105.0
Accounts and notes receivable, net of allowances of $7.1 and $5.5, respectively	263.0	284.6
Inventories	60.2	67.1
Other current assets	38.3	40.8
Total current assets	449.1	497.5
NON-CURRENT ASSETS:		
Long-term notes receivable, net	96.4	81.6
Gaming operations equipment, net of accumulated depreciation and amortization of $217.7 and $270.5, respectively	107.4	86.8
Property, plant and equipment, net of accumulated depreciation and amortization of $134.6 and $115.7, respectively	200.4	171.5
Intangible assets, net	147.6	153.9
Deferred income tax assets	48.1	43.1
Other assets, net	19.3	11.9
Total non-current assets	619.2	548.8
TOTAL ASSETS	$ 1,068.3	$ 1,046.3
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 57.1	$ 66.2
Accrued compensation and related benefits	8.2	12.3
Other accrued liabilities	63.4	73.9
Total current liabilities	128.7	152.4
NON-CURRENT LIABILITIES:		
Long-term debt	35.0	0.0
Deferred income tax liabilities	26.7	23.9
Other non-current liabilities	13.5	14.1
Total non-current liabilities	75.2	38.0
Commitments, contingencies and indemnifications (see Note 12)	0.0	0.0
STOCKHOLDERS EQUITY:		
Preferred stock (5.0 shares authorized; none issued)	0.0	0.0

Common stock (200.0 shares authorized; 59.7 shares issued)	29.8	29.8
Additional paid-in capital	440.9	437.9
Treasury stock, at cost (4.6 and 2.9 shares, respectively)	(138.1)	(104.9)
Retained earnings	532.8	490.0
Accumulated other comprehensive income (loss)	(1.0)	3.1
Total stockholders equity	864.4	855.9
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 1,068.3	$ 1,046.3

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

WMS INDUSTRIES INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Nine Months Ended March 31, 2012 and 2011

(in millions of U.S. dollars)

(Unaudited)

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 42.0	$ 70.7
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	56.8	50.5
Amortization of intangible and other non-current assets	20.4	13.9
Share-based compensation	11.5	15.2
Other non-cash items	11.9	8.6
Deferred income taxes	(2.9)	9.5
Excess tax benefit from exercise of stock options	(0.2)	(6.8)
Change in operating assets and liabilities	(32.9)	(60.9)
Net cash provided by operating activities	106.6	100.7
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to gaming operations equipment	(58.1)	(48.3)
Additions of property, plant and equipment	(47.9)	(42.0)
Payments to acquire or license intangible and other non-current assets	(9.3)	(15.8)
Net cash used in investing activities	(115.3)	(106.1)
CASH FLOWS FROM FINANCING ACTIVITIES		
Purchase of treasury stock	(41.9)	(80.0)
Proceeds from borrowings under revolving credit facility	35.0	0.0
Debt issuance costs	(2.5)	0.0
Cash received from exercise of stock options	2.7	11.5
Excess tax benefit from exercise of stock options	0.2	6.8
Net cash used in financing activities	(6.5)	(61.7)
Effect of exchange rates on cash and cash equivalents	(1.0)	0.8
DECREASE IN CASH AND CASH EQUIVALENTS	(16.2)	(66.3)
CASH AND CASH EQUIVALENTS, beginning of period	90.7	166.7
CASH AND CASH EQUIVALENTS, end of period	$ 74.5	$ 100.4

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

1. BASIS OF PRESENTATION AND BUSINESS OVERVIEW

The accompanying unaudited interim Condensed Consolidated Financial Statements of WMS Industries Inc. (WMS , we , us or the Company have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) for quarterly reports on Form 10-Q and do not include all of the information and note disclosures required by U.S. generally accepted accounting principles (U.S. GAAP) for complete financial statements. References to U.S. GAAP within this report cite topics within the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). Certain information and note disclosures normally included in annual financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to those rules and regulations. The accompanying Condensed Consolidated Financial Statements should therefore be read in conjunction with our Consolidated Financial Statements and Notes thereto for the fiscal year ended June 30, 2011, included in our Annual Report on Form 10-K filed with the SEC on August 29, 2011. The accompanying unaudited interim Condensed Consolidated Financial Statements have been prepared in accordance with U.S. GAAP and reflect all adjustments of a normal, recurring nature that are, in the opinion of management, necessary for a fair presentation of results for these interim periods.

Sales of our gaming machines are generally strongest in the spring and slowest in the summer months, while gaming operations revenues are generally strongest in the spring and summer. Typically, our total revenues are lowest in the September quarter and build in each subsequent quarter with the June quarter generating our highest total quarterly revenues. In addition, quarterly revenues and net income may increase when we receive a larger number of approvals for new games from regulators than in other quarters, when a game or platform that achieves significant player appeal is introduced, if a significant number of new casinos open or existing casinos expand or if gaming is permitted in a significant new jurisdiction. Operating results for the three and nine months ended March 31, 2012, are not necessarily indicative of the results that may be expected for the fiscal year ended June 30, 2012. For further information refer to our Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2011.

We are engaged in one business segment: to serve the legalized gaming industry by designing, manufacturing and distributing games, video and mechanical reel-spinning gaming machines and video lottery terminals (VLTs) to authorized customers in legal gaming jurisdictions worldwide. We have production facilities in the United States with development and distribution offices located in the United States, Argentina, Australia, Canada, China, India, Mexico, South Africa and Spain, and an online gaming support office in the United Kingdom and through July 2011 when we sold our subsidiary, Systems in Progress GmbH (SiP), Austria. In fiscal year 2009, we integrated the manufacturing of our Orion Financement Company B.V. (Orion Gaming) products into our Spain and United States facilities, and in fiscal 2011 we closed and sold Orion Gaming s manufacturing facility in the Netherlands and determined that we would wind down the manufacturing of the Orion Gaming product lines over fiscal 2012. We will continue to provide support for spare parts related to Orion Gaming product lines for several years. Orion Gaming and SiP were immaterial to our Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Income and Condensed Consolidated Statements of Cash Flows.

We market our gaming machines in two principal ways. First, product sales include the sale to casinos and other gaming machine operators of new and used gaming machines and VLTs, conversion kits (including game, hardware or operating system conversions) and parts. Second, through gaming operations we license our game content and intellectual property to third parties for distribution; we earn revenues from operating an online gaming site, offering a social game on *Facebook®* and selling select WMS games that have been ported to operate on mobile devices; we earn revenues from networked gaming, which is a system that links groups of networked-enabled gaming machines to a server in the casino data center, and we lease gaming machines and VLTs to casinos and other licensed gaming machine operators under operating leases where the lease payments are based upon (1) a percentage of the net win, which is the earnings generated by casino patrons playing the gaming machine, (2) fixed daily fees or (3) a percentage of the amount wagered (coin-in) or a combination of a fixed daily fee and a percentage of the coin-in. We categorize our lease arrangements into five groups: wide-area progressive (WAP) participation gaming machines; local-area progressive (LAP) participation gaming machines; stand-alone participation gaming machines; casino-owned daily fee games; and gaming machine, VLT and other leases. We refer to WAP, LAP and stand-alone participation gaming machines as participation games and when combined with casino-owned daily fee games, royalties we receive under license agreements with third parties to utilize our game content and intellectual property, gaming machine, VLT and other lease revenues, online social and mobile gaming revenues and networked gaming revenues, we refer to this business as our gaming operations.

Data for product sales and gaming operations is only maintained on a consolidated basis as presented in our Condensed Consolidated Financial Statements, with no additional separate data maintained for product sales and gaming operations (other than the revenues and costs of revenues information included in our Condensed Consolidated Statements of Income and gaming operations equipment and related accumulated depreciation included in our Condensed Consolidated Balance Sheets).

Table of Contents

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

Reclassifications

We reclassified $3.8 million of selling and administrative expense incurred in the nine months ended March 31, 2011, to a separate line item as impairment and restructuring charges in our Condensed Consolidated Statements of Income to conform to the current year s presentation. This reclassification did not affect the reported amounts of total costs and expenses, operating income, pre-tax income or net income in our Condensed Consolidated Statements of Income.

2. PRINCIPAL ACCOUNTING POLICIES

Principal Accounting Policies

For a complete description of our principal accounting policies see Note 2. Principal Accounting Policies, to our Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2011. Shown below are certain of our principal accounting policies.

Revenue Recognition

We evaluate the recognition of revenue based on the criteria set forth in the following accounting guidance: FASB ASC Topic 605, *Revenue Recognition* (Topic 605), FASB Topic 985, *Software* (Topic 985), Accounting Standards Update (ASU) No. 2009-13, *Multiple-Delivera Revenue Arrangements* (ASU No. 2009-13) and ASU No. 2009-14 *Certain Revenue Arrangements That Include Software Elements* (ASU No. 2009-14).

ASU No. 2009-13 replaced and significantly changed the previous separation criteria for multiple-deliverable revenue arrangements, by eliminating the criteria for objective and reliable evidence of fair value for each deliverable. ASU No 2009-13 also eliminated the use of the residual method of allocation of consideration among deliverables and requires, instead, that arrangement consideration be allocated, at the inception of the arrangement, to all deliverables based on their relative selling price (the relative selling price method). When applying the relative selling price method, a hierarchy is used for estimating the selling price based first on vendor specific objective evidence (VSOE), then third-party evidence (TPE) and finally management s estimated selling price (ESP). The establishment of VSOE requires judgment as to whether there is a sufficient quantity of items sold on a stand-alone basis and whether the prices demonstrate an appropriate level of concentration to conclude that VSOE exists. In determining ESP, management considers a variety of information including historic pricing and discounting practices, competitive market activity, internal costs, and the pricing and discounting practices of products sold in bundled arrangements. At the inception of a multiple element arrangement, fees under the arrangement are allocated to the non-software deliverables and to the software deliverables as a group in accordance with the relative selling price method.

ASU No 2009-14 amended the scope of software revenue recognition to exclude all tangible products containing both software and non-software components that function together to deliver the product s essential functionality. Effective July 1, 2009, with the adoption of ASU No. 2009-14, we no longer applied software revenue recognition guidance from Topic 985 to our gaming machine sales as the software and non-software components of the gaming machines function together to deliver the product s essential functionality.

General

Our revenue recognition policy for both product sales and gaming operations is to record revenue when all the following criteria are met:

Ø Persuasive evidence of an agreement exists;

Ø The price to the customer is fixed or determinable;

Ø Delivery has occurred, title has been transferred and any acceptance terms have been fulfilled;

Ø No significant contractual obligations remain; and

Ø Collectability is reasonably assured.

We recognize revenue when all of the criteria listed above are met and do not recognize revenue if all of the criteria are not met. We defer revenue for any undelivered units of accounting. Deliverables are divided into separate units of accounting if:

Ø Each item has value to the customer on a stand-alone basis; and

Ø Delivery of any undelivered item is considered probable and substantially in our control.

7

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

Considerable judgment is required to determine whether an arrangement consists of multiple deliverables, whether the delivered item has value to the customer on a stand-alone basis and to determine the relative selling price used to allocate the arrangement fee to each deliverable. The fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is allocated to the delivered element and is recognized as revenue. Such determination affects the amount and timing of revenue recognition. We evaluate the primary use and functionality of each deliverable in determining whether a delivered item has stand-alone value and qualifies as a separate unit of accounting.

Considerable judgment is also necessary to determine whether certain of our products are within the scope of software revenue recognition and whether the software and non-software elements of these products function together to deliver the essential functionality. Our determination dictates whether general revenue recognition guidance or software revenue recognition guidance applies and could impact the timing of revenue recognition. Topic 985 primarily impacts our networked gaming revenues because networked gaming revenues are derived from computer software applications and systems to be sold or leased. We began to recognize networked gaming revenues in the June 2011 quarter and they were an immaterial portion of our revenue in fiscal 2011 and we expect networked gaming revenues will also be an immaterial portion of our revenues in fiscal 2012. As we continue with the initial commercialization of networked gaming software applications in fiscal 2012, when we offer such applications through multiple deliverable arrangements, the application of Topic 985 requires us to obtain VSOE for undelivered networked gaming software applications in a multiple deliverable arrangement before revenue can be recognized on the subsequent delivery of a software application that is part of the multiple deliverable arrangements. This may delay the recognition of revenue and increase deferred revenues and deferred costs. Revenue for networked gaming is recognized under software revenue recognition guidance in accordance with the terms of the contract.

Product Sales

Revenues are reported net of incentive rebates, discounts, sales taxes and other taxes of a similar nature. In our product sales business, the largest portion of our revenues is sold on credit terms of 30 to 120 days. We also grant extended credit terms for product sales revenues for periods up to one year and beyond, and in some cases for terms up to three years, with interest recognized for terms greater than twelve months at market rates and in some instances such longer-term obligations may be secured by the related gaming machines. For products sold under arrangements with extended payment terms, judgment for revenue recognition is based on the revenue recognition policy stated above as well as the probability of collection and historic collection experience. We annually evaluate sales contracts with extended payment terms in excess of one year to determine if there is sufficient history to prove assurance of collectability and that pricing is fixed or determinable under the original sales contract terms. In concluding that our historical payment history is based on sufficiently similar arrangements, we consider the nature of our customers, our historic collection experience with the specific customer, the terms of the arrangement and the nature of the product being sold. In our evaluation as to whether such arrangement is probable of collection and contains prices that are fixed or determinable, we routinely analyze our domestic and foreign collection history on such arrangements, if we have not allowed customer concessions on refinancing and we evaluate the risk of technological obsolescence of the underlying gaming machines. As a result of our investigation, we have concluded that our extended payment term arrangements with original periods of 36 months or less qualify for revenue recognition at the time of sale because of our history of collecting all amounts due under such arrangements, the lack of concessions given to collect amounts owed under such arrangements, including any refinancing arrangements, and the low risk of technological obsolescence, as our product life significantly exceeds the payment terms. Our product sales contracts do not include specific performance, cancellation, termination or refund type provisions.

Our services for initial gaming machine installation, as well as standard warranty and technical support, are not separately priced components of our sales arrangements and are included in our revenues when the associated product sales revenue is recognized. Arrangements may also include spare parts sales or sales of game content conversion kits, which enable customers to replace game content without purchasing a new gaming machine, or hardware or operating system conversion kits, which include a new CPU board and operating system. Product sales arrangements do not include maintenance and product support fees beyond a standard warranty period. The recognition of revenue from the sale of gaming machines occurs when delivery occurs, title and risk of loss have passed to the customer and all other criteria described above have been satisfied. Labor costs for gaming machine installs are included in selling and administrative expenses and are incidental to the arrangement. We accrue for the cost of installing gaming machines sold to our customers at the time of sale, based on the percent of such gaming machines that we expect to install for our customers. We provide a reserve for warranty costs and our warranty expense has not been material.

Gaming Operations

We earn gaming operations revenues from leasing gaming machines, VLTs and other leased equipment, earn royalties from third parties under license agreements to use our game content and intellectual property and, beginning in fiscal 2011, earn revenues from our online casino operations and networked gaming operations, although the revenue earned in fiscal 2011 and anticipated to be earned in fiscal 2012 from such new operations is immaterial to our Consolidated Financial Statements. We capitalize the costs to install gaming operations equipment. Labor costs associated with performing routine maintenance on participation gaming machines is expensed as incurred and included in selling and administrative expenses.

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

For WAP leasing agreements, revenues are recognized for each gaming machine based upon a percentage of coin-in, which is the amount of coins, currency and credits wagered on the gaming machine, or a combination of a fixed daily fee and a percentage of coin-in. WAP systems entail a configuration of numerous electronically linked gaming machines located in multiple casino properties within a single gaming jurisdiction, which are connected to our central WAP computer system via a network of communications equipment. WAP system gaming machines differ from non-linked gaming machines in that they build a progressive jackpot with every wager until a player hits the top award winning combination. We pay WAP progressive jackpots won by casino patrons. Participating casinos pay a percentage of the coin-in from WAP gaming machines directly to us for services related to the design, assembly, installation, operation, maintenance and marketing of our WAP systems and to administer the progressive jackpot funding. Revenues are recognized as earned when collectability is reasonably assured.

A LAP system electronically links gaming machines within a single casino to a site controller which builds a series of small progressive jackpots within that specific casino based on every wager made on the LAP system; whereas a WAP jackpot system links gaming machines in multiple casinos within a single gaming jurisdiction to a progressive jackpot. Each casino pays LAP progressive jackpots won by patrons of its casino.

We also offer participation gaming machines on a non-linked basis, which we call stand-alone games. Stand-alone and LAP progressive participation lease payments are based on either a pre-determined percentage of the daily net win of each gaming machine or a fixed daily rental fee, or for several specific products, a percentage of the coin-in.

VLTs may be operated as stand-alone units or may interface with central monitoring systems operated by government agencies. Our leased VLTs typically are located in places where casino-style gaming is not the only attraction, such as racetracks, bars and restaurants, and are usually operated by the lottery organization of the jurisdiction. Our lease revenues are based on a fixed percentage of daily net win of the VLTs or a fixed daily lease rate. We exclude our leased VLTs that utilize for-sale game themes from our installed base of participation gaming machines. In all cases, the daily fee entitles the customer to full use of the gaming machine and includes maintenance, licensing of the game content software and connection to a linked progressive system, where applicable. In certain markets, we also charge a daily system connection fee for the customer to connect to a central determination system and/or back-office system that determines the outcome of gaming machines. We do not consider these arrangements to have multiple revenue-generating activities as the services offered are a comprehensive solution in exchange for a daily fee and all of the products and services are delivered contemporaneously; therefore, revenue is recognized under general revenue recognition guidance as the products and services provide the customer with the right to use the gaming machines and software that is essential to the functionality of the gaming machine.

Some customers prefer to lease our standard for-sale gaming machines rather than to purchase them. In these cases, we lease the game and the gaming machine, either for a fixed daily fee or as a percentage of the net win of the gaming machine. We recognize the revenue from these operating leases over the term of the lease. We do not include leased for-sale units in our installed base of participation gaming machines.

Under agreements with licensees who are generally located in geographic areas or operate in markets where we are not active, we license our games, artwork and other intellectual property. License royalties are recorded as earned when the licensee purchases or places the game or other intellectual property, and collectability is reasonably assured. We also earn revenues from operating an online casino for residents of the United Kingdom, offering a social game on *Facebook*, selling select WMS games that have been ported to operate on mobile devices and earn revenues from networked gaming, all of which we include in our other gaming operations revenues. Currently the revenues earned from all of these arrangements are not material to our Consolidated Financial Statements.

Accounts and Notes Receivable, Allowance for Doubtful Accounts and Bad Debt Expense and Credit Quality of Notes Receivable

Accounts and Notes Receivable

Revenues from gaming operations are predominantly operating lease payments that are due monthly. For product sales, we sell gaming machines and VLTs typically with payment terms of 30 to 120 days; however in certain circumstances, we offer extended payment terms

typically for up to one year and beyond and in some cases for terms up to three years. We classify a product sale receivable as a note receivable, if at the time of sale, there are any installment payment terms regardless of whether or not a formal executed note agreement exists, or if the payment terms are beyond 12 months.

Customers consider numerous factors in determining whether to issue a sales order to us including, among others, expected earnings performance of the gaming machines (which we believe is the most significant decision factor), selling price, the value provided for any trade-in of used gaming machines, parts and conversion kit support and payment terms.

We have historically provided extended payment terms to our customers for periods from 120 days through 36 months, with interest payable at prevailing rates for terms greater than 12 months. We file Uniform Commercial Code (UCC) liens on almost all domestic trade accounts and notes receivable with terms greater than 90 days, which secures our interest in the gaming machines underlying the trade accounts and notes receivable until the receivable balance for the gaming machines is fully paid, although the value of the gaming machines, if repossessed, may be less than the receivable balance outstanding. Our recent international expansion

Table of Contents

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

has required us to provide, in certain jurisdictions, a greater amount of extended payment financing terms of 18 to 36 months. In addition, as a result of the financial market crisis, which began in 2008 and led to reduced consumer discretionary spending and a weakened global economic environment, beginning in the March 2009 quarter we began and have continued to provide a greater amount of extended payment terms to select customers. This expanded extended payment term program is expected to continue until the global economy and consumer discretionary spending improves and customer demand for extended payment terms abates. Typically, these sales result in a higher selling price and, if financed over periods longer than 12 months, incur interest at rates in excess of our borrowing rate, both of which provide added profitability to the sale.

We believe our competitors have also expanded their use of extended payment terms. In aggregate, we believe that by expanding our use of extended payment terms, we have provided a competitive response to our customers and that our revenues have been favorably impacted. We are unable to estimate the impact of this program on our revenues. If we ceased providing an expanded amount of extended payment terms, we believe we would not be competitive for some customers in the market place and that our revenues and profits would likely decrease.

The following summarizes the components of current and long-term accounts and notes receivable, net ($ in millions):

	March 31, 2012	June 30, 2011
Current, net:		
Accounts receivable	$ 76.3	$ 105.3
Notes receivable	193.8	184.8
Allowance for doubtful accounts	(7.1)	(5.5)
Current accounts and notes receivable, net	$ 263.0	$ 284.6
Long-term, net:		
Notes receivable	$ 96.4	$ 81.6
Allowance for doubtful accounts	0.0	0.0
Long-term notes receivable, net	$ 96.4	$ 81.6
Total accounts and notes receivable, net	$ 359.4	$ 366.2

As of March 31, 2012, $193.8 million or 66.8% of the notes receivable installments are due within the next 12 months.

Accounts and notes receivable, net from international customers in Argentina, Mexico, Peru and Canada at March 31, 2012, were approximately: $61.8 million, $46.4 million, $26.4 million and $23.0 million, respectively while accounts and notes receivable from international customers in these same countries at June 30, 2011, were approximately: $55.9 million, $59.6 million, $24.5 million and $8.5 million, respectively.

The expansion of our use of extended payment terms since 2009 has increased our current and long-term receivable balances and reduced our cash provided by operating activities. Total receivables, net decreased by $6.8 million from $366.2 million at June 30, 2011, to $359.4 million at March 31, 2012. The decrease primarily reflects the reduction of total revenue by 13.4% or $27.2 million, to $176.0 million for three months

ended March 31, 2012 compared to $203.2 million for three months ended June 30, 2011 partially offset by a higher amount of extended payment terms given to customers.

The fair value of notes receivable, which equals book value, is estimated by discounting expected future cash flows using current interest rates at which similar notes receivable terms would be made to customers with similar credit ratings and remaining maturities.

Allowance for Doubtful Accounts and Bad Debt Expense

We carry our accounts and notes receivable at face amounts less an allowance for doubtful accounts. On a routine basis, but at least quarterly, we evaluate our accounts and notes receivable individually and collectively, and establish the allowance for doubtful accounts based on a combination of specific customer circumstances, economic and credit conditions and our history of write-offs and collections. We consider a variety of factors to evaluate credit risk in recording the allowance for doubtful accounts or as an indicator of an impaired loan including the accounts and notes receivable aging and trends thereof for customer balances, past experience with customers who pay outside of payment terms, the probability of collection, the legal environment and regulatory landscape, the customer s solvency and news related to individual customers, especially if the news calls into question the customer s ability to fully pay balances owed.

The gaming industry is a highly regulated industry requiring most customers to obtain and maintain a gaming operator s license and demonstrate to the applicable regulatory authority that they have the financial resources to operate a gaming establishment. Many of our customers, including new casinos that have opened in recent years, are owned by existing customers who operate multiple properties that have established a favorable payment history with us. Historic collection experience and the aging of customer balances are the primary indicators management utilizes to monitor the credit quality of our receivables. We do not segregate accounts and notes receivable by other credit quality indicators and do not use any other statistics or internal rating system to segregate our

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

customer balances into subgroups with similar risk characteristics. Our aging categories are determined based on contractually agreed payment terms, which are typically the original payment terms. Invoices and expected payments are classified as past due if the payment is not received within the contractually agreed upon terms. Partial payments of account balances are also infrequent and are applied based upon the facts and circumstances related to the payment. Generally, payments are applied based upon customer direction provided with the remittance or as a result of a review of the account balance, dialogue with our customer and the aging of the remaining balance outstanding continues based on its original contractual terms.

Past due accounts receivable are monitored closely to expedite payments and to record necessary allowances. Accounts and notes receivables are evaluated individually for impairment (with specific reserves established) when collectability becomes uncertain due to events and circumstances that cause an adverse change in a customer s cash flows or financial condition, such as changes to industry and regional economic conditions. Accounts placed on specific reserve are evaluated for probability of collection, which is used to determine the amount of the specific reserve. Our bad debt expense is most significantly impacted by bankruptcy filings by our casino customers and pre-bankruptcy reported exposures of individual casino customers. Due to our successful collection experience and our continuing operating relationship with casino customers and their businesses, it is infrequent that we repossess gaming machines from a customer in partial settlement of outstanding accounts or notes receivable balances. In those unusual instances where repossession occurs to mitigate our exposure on the related receivable, the repossessed gaming machines are subsequently resold in the used gaming machine market; however, we may not fully recover the receivable from this re-sale. Uncollectible accounts or notes receivables are written off only when all reasonable collection efforts have been exhausted and we determine that there is minimal chance of any kind of recovery.

For customers in the United States, at the time a customer files for bankruptcy, we typically have a security interest in the gaming machines for that portion of the total accounts and notes receivable, but our accounts and notes receivable related to all other revenue sources are typically unsecured claims. In our gaming operations business, because we own the gaming machines and lease them to the casino operator, in a bankruptcy the customer has to either accept or reject the lease and, if rejected, our gaming machines are returned to us. Due to the significance of our gaming machines to the on-going operations of our casino customers, in a bankruptcy filing we may be designated as a key vendor, which can enhance our position above other creditors in the bankruptcy. For international customers, depending on the country and our historic collection experience with the customer, we may have pledge agreements, bills of exchange or personal guarantees or other forms of agreement to enhance our ability to collect the receivables.

During the trailing twelve months ended March 31, 2012, our bad debt expense totaled $7.5 million representing 1.1% of revenues which was higher than the $4.4 million of bad debt expense for the prior twelve month period, which represented 0.6% of revenues in the prior trailing twelve-month period. The higher bad debt expense in the trailing twelve-months ended March 31, 2012, was primarily due to increasing the dollar amount of bad debt reserves by $4.3 million following government enforcement action beginning in the September 2011 quarter at certain casinos in Mexico and an increase of $1.4 million in the June 2011 quarter related to government action to close casinos in Venezuela. Our bad debt expense for the three months ended March 31, 2012, was $0.5 million, or 0.3% of revenues, compared to $1.3 million, or 0.7% of revenues, for the three months ended March 31, 2011. Our bad debt expense for the nine months ended March 31, 2012, was $6.7 million, or 1.4% of revenues, compared to $3.1 million, or 0.5% of revenues, for the nine months ended March 31, 2011. The higher bad debt expense in the nine months ended March 31, 2012, was primarily due to increasing the dollar amount of bad debt reserves by $4.3 million following government enforcement action beginning in the September 2011 quarter at certain casinos in Mexico. Our total bad debt reserve was $7.1 million at March 31, 2012, compared to $5.5 million at June 30, 2011.

Credit Quality of Notes Receivable

For notes receivable, interest income is recognized ratably over the life of the note receivable and any related fees or costs to establish the notes are charged to expense as incurred, as they are considered insignificant. Actual or imputed interest, if any, is determined based on current market rates at the time the note originated and is recorded in Interest income and other income and expense, net, ratably over the payment period. The interest rates on outstanding notes receivable ranged from 5.25% to 10.0% at March 31, 2012. Our policy is to generally recognize interest on

notes receivables until the note receivable is deemed non-performing. A note receivable is considered non-performing if payments have not been received within 180 days of the agreed upon terms. The amount of our non-performing notes is immaterial.

The majority of our domestic customers are not rated by the credit rating agencies but for those customers who do have credit ratings, the Standard and Poor s credit ratings ranged from BBB+ to D at March 31, 2012. Where possible we seek payment deposits, collateral, pledge agreements, personal guarantees or foreign bank bills of exchange or letters of credit on international trade accounts and notes receivable. However, most of our international trade accounts and notes receivable are not collateralized. Currently we have not sold our accounts or notes receivable to third parties, so we do not have any off-balance sheet liabilities for factored receivables.

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

The following summarizes the components of total notes receivable, net at March 31, 2012:

	March 31, 2012	Balances that are over 90 days past due
Notes receivable:		
Domestic	$ 110.7	$ 1.2
International	179.5	2.9
Notes receivable subtotal	290.2	4.1
Allowance for doubtful accounts	(4.8)	(1.0)
Total notes receivable, net	$ 285.4	$ 3.1

At March 31, 2012, 1.1% of our total notes receivable, net was past due over 90 days.

The following tables detail our evaluation of notes receivable for impairment at March 31, 2012 and June 30, 2011, respectively.

	March 31, 2012	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment
Notes receivable:			
Domestic	$ 110.7	$ 10.6	$ 100.1
International	179.5	36.6	142.9
Total notes receivable	$ 290.2	$ 47.2	$ 243.0

	June 30, 2011	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment
Notes receivable:			
Domestic	$ 87.7	$ 12.8	$ 74.9
International	178.7	39.8	138.9
Total notes receivable	$ 266.4	$ 52.6	$ 213.8

The following table reconciles the current and non-current allowance for doubtful notes receivable from June 30, 2011 to March 31, 2012:

	Total	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment
Beginning balance at June 30, 2011	$ 2.6	$ 2.6	$ 0.0
Charge-offs	(3.1)	(3.1)	0.0
Recoveries	0.0	0.0	0.0
Provision, primarily amounts recorded for Mexican customers notes receivable	5.3	5.3	0.0
Ending Balance at March 31, 2012	$ 4.8	$ 4.8	$ 0.0

Modifications to original financing terms are an exception to our cash collection process and are a function of collection activities with the customer. If a customer requests a modification of financing terms during the collection process, we evaluate the

12

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

proposed modification in relation to the recovery of our gaming machines, seek additional security and recognize any additional interest income ratably over the remaining new financing term. Additionally, we often take the opportunity to simplify the forward payments by consolidating several notes (each typically representing an individual purchase transaction) into one note. In those instances, the aging of any outstanding receivable balance would be adjusted to reflect the new payment terms. Any such modifications generally do not include a concession as they generally result only in a delay of payments from the original terms that are typically insignificant. As a result of the financial crisis that began in 2008, such modifications have increased, but in general, the modification of original financing terms have not been significant to our total accounts and notes receivable balance.

The following summarizes the notes receivable that had modification of financing terms:

	Nine Months Ended March 31, 2012			
	# of Customers	# of Notes	Pre-Modification Investment	Post-Modification Investment
Financing term modifications:				
Domestic			$	$
International(a)	13	46	41.1	41.1
Total financing term modifications	13	46	$ 41.1	$ 41.1

(a) Detailed modifications included:

- Ø One international customer with one note for $14.8 million for which original terms were extended by five months;
- Ø One international customer in which 11 notes were consolidated into three notes aggregating $8.0 million, with an average 14 month extension of terms;
- Ø One international customer in which 10 notes were consolidated into one note aggregating $6.4 million, with an average 10 month extension of terms; and
- Ø The remaining 10 international customers with 24 notes were consolidated into 12 notes aggregating $11.9 million, with an average of 11 month extension of terms.

Cost of Product Sales, Cost of Gaming Operations and Selling and Administrative Expenses

Cost of product sales consists primarily of raw materials, labor and manufacturing overhead. The cost of product sales also includes licensing and royalty charges, inbound and outbound freight charges, purchasing and receiving costs, inspection costs and internal transfer costs.

Cost of gaming operations consists primarily of wide-area progressive jackpot expenses, licensing and royalty charges, telephone costs, gaming operations taxes and fees and parts costs.

Selling and administrative expenses consist primarily of sales, marketing, distribution, installation and corporate support functions such as administration, information technology, legal, regulatory compliance, human resources and finance. The costs of distribution were $5.6 million and $4.9 million for the three months ended March 31, 2012 and 2011, respectively, and $17.6 million and $18.0 million for the nine months ended March 31, 2012 and 2011, respectively.

Fair Value Measurements

We apply the provisions of FASB ASC 820, *Fair Value Measurements* (Topic 820) to our financial assets and financial liabilities. Topic 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Topic 820 also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs when measuring fair value.

Topic 820 describes three levels of inputs that may be used to measure fair value:

Level 1	Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 Inputs to the valuation method include:

- Ø Quoted prices for similar assets or liabilities in active markets;
- Ø Quoted prices for identical or similar assets or liabilities in inactive markets;
- Ø Inputs other than quoted prices that are observable for the asset or liability;
- Ø Inputs that are derived principally from or corroborated by observable market data by correlation or other means;

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

- Ø If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

At March 31, 2012, our investments in various money market funds totaling approximately $1.0 million were subject to fair value measurement in accordance with Topic 820. These money market investments are included in our cash and cash equivalents and restricted cash and cash equivalents on the accompanying Condensed Consolidated Balance Sheets and are considered Level 1 securities. In addition, the carrying amounts reflected in the accompanying Condensed Consolidated Balance Sheets for cash equivalents, total accounts and notes receivable, net, accounts payable and long-term debt approximate their respective fair values at March 31, 2012 and June 30, 2011, respectively.

Goodwill and Intangible Assets

We perform impairment tests of goodwill at our reporting unit level, which is at the consolidated level. Such impairment tests for goodwill include comparing our market capitalization based on outstanding shares to our book value as of June 30, 2011, which resulted in an excess of market value over book value of over $0.9 billion or substantially in excess of book value.

We review the carrying value of our other intangible assets individually when events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. An impairment loss would be recognized when the present value of estimated directly related future cash flows expected to result from the use of the other intangible asset and its eventual disposition is less than its carrying value.

Gaming Operations Equipment

As our gaming operations equipment can be relocated from one customer to another customer, we review the carrying value of gaming operations equipment for impairment by type of equipment (for base gaming machines each of: Legacy, *Bluebird*® mechanical reel, *Bluebird* video, *Bluebird* slant, *Bluebird2* mechanical reel, *Bluebird2* video, *Bluebird2* widescreen, *Bluebird xD* mechanical reel and *Bluebird xD* video; for top boxes by form factor; for signage by form factor; and other equipment by category) when events or changes in circumstances indicate that the carrying value of any of these asset groups may not be recoverable. An impairment loss would be recognized when the present value of estimated directly related future cash flows expected to result from the use of the gaming operations equipment and its eventual disposition is less than its carrying value.

Property, Plant and Equipment

We review the carrying value of property, plant and equipment by office location and functional category, when events or changes in circumstances indicate that the carrying value of any of these asset groups may not be recoverable. An impairment loss would be recognized when the present value of estimated directly related future cash flows expected to result from the use of the property, plant and equipment and its eventual disposition is less than its carrying value.

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

Recently Adopted Accounting Standards

In April 2010, the FASB issued ASU No. 2010-16, *Accruals for Casino Jackpot Liabilities,* (ASU No. 2010-16), which clarifies when a casino entity is required to accrue a jackpot liability. Under ASU No. 2016-16, effective July 1, 2011, we changed our accounting to not record any expense for the base jackpot liability for our progressive jackpots on our WAP gaming machines until the progressive jackpot liability is won by the casino patron. In adopting this accounting standard effective July 1, 2011, we credited retained earnings with $0.8 million, net of related deferred income tax for deferred jackpot liability expense recorded in other current liabilities in our Consolidated Balance Sheets at June 30, 2011. We believe adoption of ASU No. 2010-16 was immaterial to our Consolidated Financial Statements, but could provide more volatility to our consolidated financial results than the previous accounting method.

In May 2011, the FASB issued ASU No. 2011-04, *Fair Value Measurements Disclosures* (ASU No. 2011-04) which will require supplemental disclosures related to purchases, sales, issuances and settlements of fair value instruments within the Level 3 reconciliation. We adopted ASU No. 2011-04 as of January 1, 2012 and the adoption had no material impact on our Consolidated Financial Statements.

Recently Issued Accounting Standards Not Yet Adopted

In June 2011, the FASB issued ASU No. 2011-05, *Presentation of Comprehensive Income* (ASU No. 2011-05) to require other comprehensive income, including reclassification adjustments, to be presented with net income in one continuous statement or in a separate statement consecutively following net income. ASU No. 2011-05 is effective prospectively beginning July 1, 2012 and the adoption is not expected to have a material impact on our Consolidated Financial Statements.

In September 2011, the FASB issued ASU No. 2011-08, *Intangibles Goodwill and Other (Topic 350) Testing for Impairment (* ASU No. 2011-08) to reduce complexity and costs by allowing an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment. ASU No. 2011-08 is effective prospectively beginning July 1, 2012 and the adoption is not expected to have a material impact on our Consolidated Financial Statements.

In December 2011, the FASB issued ASU No. 2011-11, *Disclosures about Offsetting Assets and Liabilities* (ASU No. 2011-11) to require new disclosures about offsetting assets and liabilities to help enable users of financial statements evaluate certain significant quantitative differences in balance sheets prepared under U.S. GAAP and IFRS. ASU No. 2011-11 is effective retrospectively beginning July 1, 2013 and the adoption is not expected to have a material impact on our Consolidated Financial Statements.

In December 2011, the FASB issued update ASC No. 2011-12, *Comprehensive Income: Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05* (ASU No. 2011-12) which will require us to defer only those changes in ASU No. 2011-05 that relate to the presentation of reclassification adjustments, and the paragraphs in this update supersede certain pending paragraphs in ASU No. 2011-05. ASU No. 2011-12 is effective prospectively beginning July 1, 2012 and the adoption is not expected to have a material impact on our Consolidated Financial Statements.

We do not believe there is additional accounting guidance not yet effective that is relevant to the readers of our Consolidated Financial Statements. Several new Exposure Drafts and proposals are under development which may have a significant impact on our Consolidated Financial Statements once enacted.

3. IMPAIRMENT AND RESTRUCTURING

Given the continuing lower levels of capital spending by casinos on replacing gaming machines over the last three years and with no leading indicators suggesting that demand will increase in the near-term, we conducted a thorough review of our product plans and business strategies at the end of fiscal 2011 and beginning of fiscal 2012. We still believe our long-term vision and business strategy is intact but, as a result of this review, we refined our product plans and restructured our organization. Specifically, we have streamlined our product management and product development functions, simplified our product plans and further prioritized on-time commercialization of new game themes, products and portal applications.

Some of the product, operational and other decisions made in this review led to impairment and restructuring charges of $18.4 million, or $0.20 per diluted share, recorded in the June 2011 quarter and $22.2 million, or $0.24 per diluted share, for fiscal 2011. In addition, we implemented a broader restructuring in the September 2011 quarter and recorded a $9.7 million pre-tax charge, or $0.12 per diluted share. These restructuring actions are expected to better direct resources and focus on near-term revenue opportunities and reduce our overall organizational staffing by approximately 10% to a level that better correlates with the current industry operating environment, while maintaining our ability to create great games that engage current players and attract new players.

Table of Contents

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

The decisions made as part of the strategy review led to additional impairment and restructuring charges, which we recorded in the September 2011 quarter, consisting of $5.9 million of separation-related charges and $3.8 million of costs related to the decision to close two facilities. The nine-month period ended March 31, 2011, includes charges recorded in the September 2010 quarter consisting of $3.8 million of pre-tax impairment and restructuring charges, or $0.04 per diluted share, that previously had been included in selling and administrative expense, which includes $2.4 million, or $0.03 per diluted share, of asset impairment charges related to closing WMS main facility in the Netherlands and $1.4 million, or $0.01 per diluted share, of pre-tax separation-related charges. We sold the Netherlands facility in June 2011. The components of the charges recorded in the nine months ended March 31, 2012 and 2011 are:

	Nine Months Ended March 31, 2012		Nine Months Ended March 31, 2011	
DESCRIPTION OF CHARGES	**Pre-tax amounts**	**Per diluted share**	**Pre-tax amounts**	**Per diluted share**
IMPAIRMENT AND RESTRUCTURING CHARGES				
Non-cash Charges				
Impairment of property, plant and equipment	$ 0.6	$ 0.01	$ 2.4	$ 0.03
Cash Charges				
Restructuring charges	9.1	0.11	1.4	0.01
Total Impairment and Restructuring Charges	**$ 9.7**	**$ 0.12**	**$ 3.8**	**$ 0.04**

We paid all of the restructuring charges from the quarter ended September 30, 2010 by June 30, 2011.

At June 30, 2011, $1.9 million of the $3.8 million of the separation-related charges recorded in the June 2011 quarter were unpaid. During the nine months ended March 31, 2012, $1.5 million of these separation-related charges were paid and $0.4 million remain unpaid at March 31, 2012. We expect all of these amounts to be paid by June 30, 2012.

Of the $9.1 million of cash-based impairment and restructuring charges recorded in the September 2011 quarter, $5.7 million of separation-related charges and $0.6 million of costs relating to closing two facilities were paid by March 31, 2012. At March 31, 2012, in addition to the $0.6 million of non-cash charges, $0.2 million of separation-related charges and $2.6 million costs related to closing two facilities were unpaid. We expect to pay the $2.6 million of restructuring charges related to costs related to closing two facilities ratably through July 2015, and $0.2 million of separation-related charges will be paid by September 2012.

4. EARNINGS PER SHARE

Earnings per share is calculated using the weighted average number of common and common stock equivalents outstanding. Restricted stock is considered participating securities and included in our calculation of earnings per share. Basic and diluted earnings per share are calculated as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2012	2011	2012	2011
Net income Basic and Diluted earnings	$ 22.1	$ 24.2	$ 42.0	$ 70.7
Basic weighted average common shares outstanding	55.2	57.6	55.7	57.9
Dilutive effect of stock options	0.2	0.9	0.2	1.0
Dilutive effect of restricted common stock and warrants	0.1	0.4	0.1	0.4
Diluted weighted average common stock and common stock equivalents	55.5	58.9	56.0	59.3
Basic earnings per share of common stock	$ 0.40	$ 0.42	$ 0.75	$ 1.22
Diluted earnings per share of common stock and common stock equivalents	$ 0.40	$ 0.41	$ 0.75	$ 1.19
Common stock equivalents excluded from the calculation of diluted earnings per share because their impact would render them anti-dilutive	5.6	0.8	5.6	2.1

Table of Contents

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

In fiscal 2004, our Board of Directors, as part of the inducement to Hasbro Inc. and Hasbro International, Inc. (collectively, Hasbro) to extend their license agreement with us, approved a grant of warrants (the 2003 Warrants) to purchase 375,000 shares of our common stock valued at $3.9 million using the Black-Scholes pricing model and certain assumptions at the date of issuance of the 2003 Warrants. The warrants exercise price is $23.36 per share of our common stock, subject to adjustment and is currently anti-dilutive at March 31, 2012. The warrants are non-cancelable and are now fully vested. See Note 12. Stockholders Equity - Warrants to our Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2011.

Also, included in our anti-dilutive common stock equivalents for the three months and nine months ended March 31, 2012 and 2011, are warrants to purchase 500,000 shares of our common stock that were issued to Hasbro in 2009 in connection with an amendment and extension of our agreement with them. These warrants were excluded from the calculation because the vesting criteria are contingent upon future events, which were not met at March 31, 2012. See Note 12. Stockholders Equity -Warrants to our Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2011.

5. INVENTORIES

Inventories consisted of the following:

	March 31, 2012	June 30, 2011
Raw materials and work-in-process	$ 37.2	$ 40.5
Finished goods	23.0	26.6
Total inventories	$ 60.2	$ 67.1

Cost elements included in work-in-process and finished goods include raw materials, direct labor and overhead expenses. We recorded raw material and finished goods inventory write-downs totaling approximately $1.1 million and $2.2 million for three months ended March 31, 2012 and 2011, respectively, and $4.6 million and $3.3 million for the nine months ended March 31, 2012 and 2011, respectively. These charges are classified in cost of product sales in our Condensed Consolidated Statements of Income.

6. INTANGIBLE ASSETS

General

Intangible assets recorded on our accompanying Condensed Consolidated Balance Sheets consisted of the following:

	March 31, 2012	June 30, 2011
Goodwill	$ 19.1	$ 20.3

Finite lived intangible assets, net	135.1	136.4
Less: royalty advances and licensed or acquired technologies, short-term	(6.6)	(2.8)
Total long-term intangible assets, net	$ 147.6	$ 153.9

Certain of our intangible assets including goodwill are denominated in foreign currency and, as such, include the effects of foreign currency translation.

Goodwill

The changes in the carrying amount of goodwill for the nine months ended March 31, 2012 include:

Goodwill balance at June 30, 2011	$ 20.3
Foreign currency translation adjustment	(1.2)
Goodwill balance at March 31, 2012	$ 19.1

17

Table of Contents

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

Other Intangible Assets

Other intangible assets consisted of the following:

		March 31, 2012			June 30, 2011		
	Useful Life (Years)	Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
Finite lived intangible assets:							
Royalty advances for licensed brands, talent, music and other	1 - 15	$ 118.5	$ (92.8)	$ 25.7	$ 104.2	$ (83.1)	$ 21.1
Developed, licensed or acquired technologies	1 - 15	116.6	(23.4)	93.2	117.2	(18.1)	99.1
Patents, trademarks and other	4 - 17	34.3	(18.1)	16.2	34.8	(18.6)	16.2
Total		$ 269.4	$ (134.3)	$ 135.1	$ 256.2	$ (119.8)	$ 136.4

The following table summarizes additions to other intangible assets during the nine months ended March 31, 2012:

	Total Additions
Finite lived intangible assets:	
Royalty advances for licensed brands, talent, music and other	$ 14.3
Developed, licensed or acquired technologies	2.9
Patents, trademarks and other	2.5
Total	$ 19.7

Amortization expense for our finite-lived intangible assets was $6.1 million and $3.7 million for the three months ended March 31, 2012 and 2011, respectively, and $16.9 million and $13.4 million for the nine months ended March 31, 2012 and 2011, respectively.

The actual amortization expense for our finite-lived intangible assets for the past three years, including $14.4 million recorded as impairment charges in fiscal 2011, and estimated aggregate amortization expense for other intangible assets for each of the next five years and thereafter is as follows:

Actual			Estimated						
2009	2010	2011	Remaining 2012	2013	2014	2015	2016	2017	Thereafter
$14.2	21.1	38.3	6.7	23.3	22.4	18.7	15.8	14.5	33.7

The estimated aggregate future intangible asset amortization at March 31, 2012, does not reflect the significant commitments we have for future payments for intangible assets. If we determine that we may not realize the value of any of the finite lived intangible net assets or commitments, we would record an immediate charge in our Consolidated Statements of Income up to the full amount of these net assets or commitments in the period in which such determination is made. See Note 12. Commitments, Contingencies and Indemnifications to our Condensed Consolidated Financial Statements and Notes thereto in this report.

7. INCOME TAXES

We, or one of our subsidiaries, files income tax returns in the U.S. Federal, various state, local and foreign jurisdictions. Our provision for income taxes for interim periods is based on an estimate of the effective annual income tax rate adjusted for specific items in any particular interim period. The provision differs from income taxes currently payable because certain items of income and expense are recognized in different periods for financial statement purposes than for tax return purposes. The estimated effective income tax rate was approximately 33.8% and 34.9% for the three months ended March 31, 2012 and 2011, respectively, and 34.4% and 33.6% for the nine months ended March 31, 2012 and 2011, respectively. The effective tax rate for the three and nine months ended March 31, 2012 was favorably impacted by a reduction in uncertain tax liabilities for U.S. Federal tax purposes for fiscal 2008 due to the lapse of the statute of limitations and lower net income and a higher domestic manufacturing deduction. The effective tax rate for the three months and nine months ended March 31, 2011, was favorably impacted by 5.5% and 3.0%, respectively or $0.01 and $0.02, respectively per diluted share as a result of the retroactive reinstatement of the U.S. Federal Research and Development tax credit for the period January 1, 2010 through December 31, 2010.

Table of Contents

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

Under the assumption that the U.S. Federal Research and Development tax credit legislation, which expired December 31, 2011, is not continued, we expect our effective tax rate will be between 36% and 37% for the remainder of our fiscal 2012.

At March 31, 2012, the total unrecognized tax benefits, including accrued interest and penalties of $0.2 million (net of the U.S. Federal benefit), were $3.8 million, which represent the portion that, if recognized, would reduce the effective income tax rate.

We are no longer subject to any significant U.S. Federal tax examinations by tax authorities for years before fiscal 2009, or state, local or foreign income tax examinations by tax authorities for years before fiscal 2007.

8. REVOLVING CREDIT FACILITY

On October 18, 2011, we entered into an amended and restated revolving credit agreement with a group of eight banks. This agreement provides for borrowings up to $400 million through October 18, 2016, with the ability to expand the facility to $500 million from the existing lenders willing to increase their commitments or from additional lenders with the consent of the administrative agent. The revolving credit facility requires that we maintain certain financial and non-financial covenants and two financial ratios: a leverage ratio and an interest coverage ratio. These financial and non-financial covenants and financial ratios could limit our ability to acquire companies, declare dividends, incur additional debt, make any distribution to holders of any shares of capital stock or purchase or otherwise acquire shares of our common stock. The maximum leverage ratio is 3.0x, and is computed as total net funded indebtedness outstanding at the end of each quarter divided by the trailing twelve-month earnings before interest, taxes, depreciation and amortization, including share-based compensation and non-cash charges, as specifically defined in the revolving credit agreement. The minimum interest coverage ratio is 3.0x and is computed as trailing twelve-month adjusted earnings before interest, taxes, depreciation and amortization and share-based compensation and non-cash charges divided by trailing twelve-months interest charges, as specifically defined in the revolving credit agreement. The amended and restated revolving credit agreement is unsecured but guaranteed by all of our significant domestic subsidiaries. In addition, the amended and restated revolving credit agreement contains certain limitations on, among other items, investments, loans, advances, and guarantees.

At March 31, 2012, based upon the leverage ratio as defined in the amended and restated revolving credit agreement, no limitations existed for restricted payment purposes. At March 31, 2012, $35.0 million was outstanding under the amended and restated revolving credit facility. The effective interest rate on our borrowings at March 31, 2012 was 1.5%.

As of March 31, 2012, we maintained an aggregate cash balance of $13.5 million in non-interest bearing accounts with two of the banks in our $400 million amended and restated revolving credit agreement. We were in compliance with all of the financial and non-financial covenants and financial ratios required by our $400 million amended and restated revolving credit agreement as of March 31, 2012.

Prior to entering into this amended and restated revolving credit agreement in October 2011, we had a $150 million revolving credit agreement.

9. STOCKHOLDERS EQUITY AND EQUITY COMPENSATION PLAN

General

Our authorized common stock consists of 200.0 million shares at $0.50 par value. Additionally, we have 5.0 million shares of $0.50 par value preferred stock authorized. The preferred stock is issuable in series, and the relative rights and preferences and the number of shares in each series are to be established by our Board of Directors.

Common Stock Repurchase Program

On August 2, 2010, our Board of Directors announced it was terminating the existing share repurchase program and replacing it with a new $300 million share repurchase program that expires on August 2, 2013. The timing and actual number of shares repurchased will depend on market conditions. During the nine months ended March 31, 2012, we purchased approximately 3.5% of our common shares outstanding, or 2,094,598 shares, in open market purchases for approximately $43.2 million at an average cost of $20.67 per share of which approximately $1.3 million of common shares was settled and paid in early April 2012. During the nine months ended March 31, 2011, we purchased approximately 2,090,212 shares, in open market purchases for approximately $80.0 million at an average cost of $38.26 per share. At March 31, 2012, we had approximately $155.3 million remaining of our current share repurchase authorization.

Table of Contents

WMS INDUSTRIES INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in millions of U.S. dollars and millions of shares, except per share amounts)

(Unaudited)

Equity Compensation Plan

A summary of information with respect to share-based compensation expense included in our Condensed Consolidated Statements of Income for the three and nine months ended March 31, 2012 and 2011, respectively are as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2012	2011	2012	2011
Selling and administrative	$ 2.6	$ 2.9	$ 7.4	$ 9.8
Research and development	1.2	1.7	3.9	5.3
Cost of product sales	0.1	0.0	0.2	0.1
Share-based compensation expense included in pre-tax income	3.9	4.6	11.5	15.2
Income tax benefit related to share-based compensation	(1.5)	(1.8)	(4.4)	(5.8)
Share-based compensation expense included in net income	$ 2.4	$ 2.8	$ 7.1	$ 9.4