UNISYS CORP
Form 10-Q
August 01, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2018
¨ 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 1-8729

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

Delaware	38-0387840
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
801 Lakeview Drive, Suite 100 Blue Bell, Pennsylvania	19422
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (215) 986-4011

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 ý 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 for such shorter period that the registrant was required to submit and post such files). YES ý NO ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer ý
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨
	Emerging growth company ¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

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

Number of shares of Common Stock outstanding as of June 30, 2018: 51,013,181.

UNISYS CORPORATION
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Part I - FINANCIAL INFORMATION
Item 1. Financial Statements

UNISYS CORPORATION
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)
(Millions, except per share data)

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018	2017		2018	2017	
Revenue						
Services	$586.7	$574.8		$1,155.2	$1,160.1	
Technology	80.7	91.4		220.6	170.6	
	667.4	666.2		1,375.8	1,330.7	
Costs and expenses						
Cost of revenue:						
Services	484.2	510.8	*	955.1	997.2	*
Technology	30.3	36.7	*	66.6	76.2	*
	514.5	547.5	*	1,021.7	1,073.4	*
Selling, general and administrative	92.7	111.4	*	183.6	216.4	*
Research and development	6.2	10.8	*	14.7	22.6	*
	613.4	669.7	*	1,220.0	1,312.4	*
Operating income (loss)	54.0	(3.5)	*	155.8	18.3	*
Interest expense	15.7	14.3		32.3	20.0	
Other income (expense), net	(18.0)	(24.5)	*	(40.6)	(57.4)	*
Income (loss) before income taxes	20.3	(42.3)		82.9	(59.1)	
Provision (benefit) for income taxes	14.3	(3.8)		35.2	9.1	
Consolidated net income (loss)	6.0	(38.5)		47.7	(68.2)	
Net income attributable to noncontrolling interests	2.2	3.5		3.3	6.5	
Net income (loss) attributable to Unisys Corporation	$3.8	$(42.0)		$44.4	$(74.7)	
Earnings (loss) per share attributable to Unisys Corporation						
Basic	$0.07	$(0.83)		$0.87	$(1.48)	
Diluted	$0.07	$(0.83)		$0.74	$(1.48)	

See notes to consolidated financial statements
*Amounts were changed to conform to the current-year presentation. See Note 3.

UNISYS CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)
(Millions)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Consolidated net income (loss)	$6.0	$(38.5)	$47.7	$(68.2)
Other comprehensive income:				
Foreign currency translation	(23.3)	42.7	(28.4)	73.8
Postretirement adjustments, net of tax of $1.9 and $2.9 in 2018 and $(7.1) and $(8.1) in 2017	39.9	(10.4)	78.9	12.0
Total other comprehensive income	16.6	32.3	50.5	85.8
Comprehensive income (loss)	22.6	(6.2)	98.2	17.6
Less comprehensive income attributable to noncontrolling interests	(0.9)	(3.7)	(3.2)	(6.9)
Comprehensive income (loss) attributable to Unisys Corporation	$21.7	$(9.9)	$95.0	$10.7

See notes to consolidated financial statements

UNISYS CORPORATION
CONSOLIDATED BALANCE SHEETS (Unaudited)
(Millions)

	June 30, 2018	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	$584.3	$ 733.9
Accounts receivable, net	484.0	503.3
Contract assets	38.3	—
Inventories:		
Parts and finished equipment	12.5	13.6
Work in process and materials	10.2	12.5
Prepaid expenses and other current assets	117.6	126.2
Total current assets	1,246.9	1,389.5
Properties	855.6	898.8
Less-Accumulated depreciation and amortization	739.9	756.3
Properties, net	115.7	142.5
Outsourcing assets, net	208.8	202.3
Marketable software, net	150.7	138.3
Prepaid postretirement assets	152.5	148.3
Deferred income taxes	106.5	119.9
Goodwill	178.7	180.8
Restricted cash	16.8	30.2
Other long-term assets	194.3	190.6
Total assets	$2,370.9	$ 2,542.4
Liabilities and deficit		
Current liabilities:		
Current maturities of long-term-debt	$10.2	$ 10.8
Accounts payable	219.9	241.8
Deferred revenue	284.6	327.5
Other accrued liabilities	319.1	391.5
Total current liabilities	833.8	971.6
Long-term debt	638.1	633.9
Long-term postretirement liabilities	1,886.8	2,004.4
Long-term deferred revenue	177.3	159.0
Other long-term liabilities	79.0	100.0
Commitments and contingencies		
Deficit:		
Common stock, shares issued:		
2018; 54.2, 2017; 53.4	0.5	0.5
Accumulated deficit	(1,940.1)	(1,963.1)
Treasury stock, shares at cost:		
2018; 3.1, 2017; 2.9	(104.8)	(102.7)
Paid-in capital	4,534.1	4,526.4
Accumulated other comprehensive loss	(3,765.2)	(3,815.8)
Total Unisys stockholders' deficit	(1,275.5)	(1,354.7)
Noncontrolling interests	31.4	28.2

Total deficit	(1,244.1)	(1,326.5)
Total liabilities and deficit	$2,370.9	$ 2,542.4

See notes to consolidated financial statements

UNISYS CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(Millions)

	Six Months Ended June 30,	
	2018	2017
Cash flows from operating activities		
Consolidated net income (loss)	$47.7	$(68.2)
Adjustments to reconcile consolidated net income (loss) to net cash used for operating activities:		
Foreign currency transaction losses	1.5	5.1
Non-cash interest expense	5.2	4.4
Loss on debt extinguishment	—	1.5
Employee stock compensation	7.3	6.2
Depreciation and amortization of properties	21.6	19.8
Depreciation and amortization of outsourcing assets	31.9	26.3
Amortization of marketable software	28.6	31.8
Other non-cash operating activities	(1.6)	2.5
Loss on disposal of capital assets	0.3	4.2
Gain on sale of properties	(7.1)	—
Postretirement contributions	(72.9)	(76.2)*
Postretirement expense	38.5	49.2 *
Decrease (increase) in deferred income taxes, net	8.3	(0.4)
Changes in operating assets and liabilities:		
Receivables, net	(21.2)	(57.4)
Inventories	(0.8)	(2.6)
Accounts payable and other accrued liabilities	(152.8)	(28.3)
Other liabilities	10.8	(7.0)*
Other assets	(7.2)	(1.1)
Net cash used for operating activities	(61.9)	(90.2)
Cash flows from investing activities		
Proceeds from investments	2,028.8	2,502.0
Purchases of investments	(2,034.6)	(2,487.1)
Investment in marketable software	(41.1)	(28.8)
Capital additions of properties	(9.9)	(15.9)
Capital additions of outsourcing assets	(42.4)	(36.9)
Net proceeds from sale of properties	19.7	—
Other	(0.9)	(0.3)
Net cash used for investing activities	(80.4)	(67.0)
Cash flows from financing activities		
Proceeds from issuance of long-term debt	—	445.0
Issuance costs relating to long-term debt	—	(11.7)
Payments of long-term debt	(1.3)	(97.7)
Other	(2.1)	(2.1)
Net cash (used for) provided by financing activities	(3.4)	333.5
Effect of exchange rate changes on cash, cash equivalents and restricted cash	(17.3)	12.8
(Decrease) increase in cash, cash equivalents and restricted cash	(163.0)	189.1
Cash, cash equivalents and restricted cash, beginning of period	764.1	401.1

Cash, cash equivalents and restricted cash, end of period	$601.1	$590.2

See notes to consolidated financial statements

*Amounts were changed to conform to the current-year presentation. See Note 3.

UNISYS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
(Dollars in millions, except share and per share amounts)

Note 1 - Basis of Presentation

The accompanying consolidated financial statements and footnotes of Unisys Corporation have been prepared in accordance with generally accepted accounting principles in the United States of America (GAAP). The financial statements and footnotes are unaudited. In the opinion of management, the financial information furnished herein reflects all adjustments necessary for a fair presentation of the financial position, results of operations, comprehensive income and cash flows for the interim periods specified. These adjustments consist only of normal recurring accruals except as disclosed herein. Because of seasonal and other factors, results for interim periods are not necessarily indicative of the results to be expected for the full year.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions about future events. These estimates and assumptions affect the amounts of assets and liabilities reported, disclosures about contingent assets and liabilities and the reported amounts of revenue and expenses. Such estimates include the valuation of accounts receivable, contract assets, inventories, outsourcing assets, marketable software, goodwill and other long-lived assets, legal contingencies, indemnifications, assumptions used in the calculation for systems integration projects, income taxes and retirement and other post-employment benefits, among others. These estimates and assumptions are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. Management adjusts such estimates and assumptions when facts and circumstances dictate. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods.

The company's accounting policies are set forth in detail in Note 1 of the Notes to Consolidated Financial Statements in the company's Annual Report on Form 10-K for the year ended December 31, 2017 (2017 Form 10-K) filed with the Securities and Exchange Commission. Such Annual Report also contains a discussion of the company's critical accounting policies and estimates. The company believes that these critical accounting policies and estimates affect its more significant estimates and judgments used in the preparation of the company's consolidated financial statements.

As described in Note 3, effective January 1, 2018 the company adopted the requirements of Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606) using the modified retrospective method. The company's updated accounting policy on revenue recognition is described in Note 2 and in "Critical accounting policies and estimates update" in Item 2 of this Form 10-Q.

Note 2 - Summary of Significant Accounting Policies

Revenue recognition

Revenue is recognized at an amount that reflects the consideration to which the company expects to be entitled in exchange for transferring goods and services to a customer. The company determines revenue recognition using the following five steps: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5) recognize revenue when (or as) the company satisfies a performance obligation.

Revenue excludes taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the company from a customer (e.g., sales, use and value-added taxes). Revenue includes payments for shipping and handling activities.

At contract inception, the company assesses the goods and services promised in a contract with a customer and identifies as a performance obligation each promise to transfer to the customer either: (1) a good or service (or a bundle of goods or services) that is distinct or (2) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer. The company recognizes revenue only when it satisfies a performance obligation by transferring a promised good or service to a customer.

The company must apply its judgment to determine the timing of the satisfaction of performance obligations as well as the transaction price and the amounts allocated to performance obligations including estimating variable consideration, adjusting the consideration for the effects of the time value of money and assessing whether an estimate of variable consideration is constrained.

Revenue from hardware sales is recognized upon the transfer of control to a customer, which is defined as an entity's ability to direct the use of and obtain substantially all of the remaining benefits of an asset.
Revenue from software licenses is recognized at the inception of either the initial license term or the inception of an extension or renewal to the license term.
Revenue for operating leases is recognized on a monthly basis over the term of the lease and for sales-type leases at the inception of the lease term.
Revenue from equipment and software maintenance and post-contract support is recognized on a straight-line basis as earned over the terms of the respective contracts. Cost related to such contracts is recognized as incurred.
Revenue and profit under systems integration contracts are recognized over time as the company transfers control of goods or services. The company measures its progress toward satisfaction of its performance obligations using the cost-to-cost method, or when services have been performed, depending on the nature of the project. For contracts accounted for using the cost-to-cost method, revenue and profit recognized in any given accounting period are based on estimates of total projected contract costs. The estimates are continually reevaluated and revised, when necessary, throughout the life of a contract. Any adjustments to revenue and profit resulting from changes in estimates are accounted for in the period of the change in estimate. When estimates indicate that a loss will be incurred on a contract upon completion, a provision for the expected loss is recorded in the period in which the loss becomes evident.
Revenue from time and materials service contracts and outsourcing contracts is recognized as the services are provided using either an objective measure of output or on a straight-line basis over the term of the contract.
The company also enters into multiple-element arrangements, which may include any combination of hardware, software or services. For example, a client may purchase an enterprise server that includes operating system software. In addition, the arrangement may include post-contract support for the software and a contract for post-warranty maintenance for service of the hardware. These arrangements consist of multiple performance obligations, with control over hardware and software transferred in one reporting period and the software support and hardware maintenance services performed across multiple reporting periods. In another example, the company may provide desktop managed services to a client on a long-term multiple-year basis and periodically sell hardware and license software products to the client. The services are provided on a continuous basis across multiple reporting periods and control over the hardware and software products occurs in one reporting period. To the extent that a performance obligation in a multiple-deliverable arrangement is subject to specific guidance, that performance obligation is accounted for in accordance with such specific guidance. An example of such an arrangement may include leased assets which are subject to specific leasing accounting guidance.
In multiple-element arrangements, the company allocates the total transaction price to be earned under the arrangement among the various performance obligations in proportion to their standalone selling prices (relative standalone selling price basis). The standalone selling price for a performance obligation is the price at which the company would sell a promised good or service separately to a customer.
A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. Many of the company's contracts have a single performance obligation as the promise to transfer the individual goods or services is not separately identifiable from other promises in the contracts and, therefore, not distinct. For contracts with multiple performance obligations, the company allocates the contract's transaction price to each performance obligation using its best estimate of the standalone selling price of each distinct good or service in the contract. The primary methods used to estimate standalone selling price are as follows: (1) the expected cost plus margin approach, under which the company forecasts its expected costs of satisfying a performance obligation and then adds an appropriate margin for that distinct good or service and (2) the percent discount off of list price approach.
In the Services segment, substantially all of the company's performance obligations are satisfied over time as work progresses and therefore substantially all of the revenue in this segment is recognized over time. The company generally receives payment for these contracts over time as the performance obligations are satisfied.

In the Technology segment, substantially all of the company’s goods and services are transferred to customers at a single point in time. Revenue on these contracts is recognized when control over the product is transferred to the customer or a software license term begins. The company generally receives payment for these contracts upon signature or within 30 to 60 days.

At June 30, 2018, the company had approximately $1.5 billion of remaining performance obligations of which approximately 50% is estimated to be recognized as revenue by the end of 2019. The company does not disclose the value of unsatisfied performance obligations for (1) contracts with an original expected length of one year or less and (2) contracts for which the company recognizes revenue at the amount to which it has the right to invoice for services performed.

The company discloses disaggregation of its customer revenue by geographic areas and by classes of similar products and services, by segment (see Note 16).

The timing of revenue recognition, billings and cash collections results in billed accounts receivable, unbilled receivables, contract assets and deferred revenue (contract liabilities). The disclosure of contract assets is a new requirement due to the adoption of Topic 606. At December 31, 2017, contract assets were included in accounts receivable, net on the company's Consolidated Balance Sheet. At June 30, 2018, $5.8 million of long-term contract assets were included in other long-term assets on the company's Consolidated Balance Sheet.

Significant changes during the three and six months ended June 30, 2018 in the above contract asset and liability balances were as follows: revenue of $86.3 million and $190.9 million, respectively, was recognized that was included in deferred revenue at December 31, 2017.

The company's incremental direct costs of obtaining a contract consist of sales commissions which are deferred and amortized ratably over the initial contract life. These costs are classified as current or noncurrent based on the timing of when the company expects to recognize the expense. The current and noncurrent portions of deferred commissions are included in prepaid expenses and other current assets and in other long-term assets, respectively, in the company's Consolidated Balance Sheets. At June 30, 2018 and December 31, 2017, the company had $10.9 million and $11.0 million, respectively, of deferred commissions. For the three and six months ended June 30, 2018, $1.7 million and $3.4 million, respectively, of amortization expense related to deferred commissions was recorded in selling, general and administrative expense in the company's Consolidated Statement of Income.

Costs to fulfill a contract, which are incurred upon initiation of certain services contracts and are related to initial customer setup, are included in outsourcing assets, net in the company's Consolidated Balance Sheet. The amount of such cost at June 30, 2018 and December 31, 2017 was $76.1 million and $76.0 million, respectively. These costs are amortized over the initial contract life and reported in Services cost of sales. During the three and six months ended June 30, 2018, $5.5 million and $10.7 million, respectively, was amortized. Recoverability of these costs are subject to various business risks. Quarterly, the company compares the carrying value of these assets with the undiscounted future cash flows expected to be generated by them to determine if there is impairment. If impaired, these assets are reduced to an estimated fair value on a discounted cash flow basis. The company prepares its cash flow estimates based on assumptions that it believes to be reasonable but are also inherently uncertain. Actual cash flows could differ from these estimates.

Note 3 - Accounting Standards

Accounting Pronouncements Adopted

Effective January 1, 2018, the company adopted ASU No. 2017-07 Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost issued by the Financial Accounting Standards Board (FASB) which requires employers to present the service cost component of net periodic benefit cost in the same income statement line item(s) as other employee compensation costs arising from services rendered during the period. The other components of net periodic benefit cost are presented separately from the line items that include service cost and outside the subtotal of operating income. ASU No. 2017-07 allows a practical expedient that permits an entity to use amounts disclosed in its pension and other postretirement benefit plan footnote for the prior comparative periods as the estimation basis for applying the retrospective presentation requirements. The new guidance has been applied on a retrospective basis, using the practical expedient, whereby prior-period financial statements have been adjusted to reflect the adoption of the new guidance, as required by the FASB. For the three and six months June 30, 2017, $21.3 million and $45.8 million, respectively, of net periodic benefit cost, other than service costs, was reclassified from cost of revenue, selling, general and administrative expense and research and development expense to other income (expense), net in the company's consolidated results of operations (see Note 5).

Effective January 1, 2018, the company adopted ASU No. 2014-09 Revenue from Contracts with Customers (Topic 606) issued by the FASB which establishes principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows from a contract with a customer. Topic 606 allows for either "full retrospective" adoption, meaning the standard is applied to all periods presented, or “modified retrospective” adoption, meaning the standard is applied only to the most current period presented in the financial statements. Topic 606 requires the company to recognize revenue for certain transactions, including extended payment term software licenses and short-term software licenses, sooner than the prior rules would allow and requires the company to recognize software license extensions and renewals (the most significant impact upon adoption), later than the prior rules would allow. Topic 606 also requires significantly expanded disclosure requirements. The company has adopted the standard using the modified retrospective method and applied the standard to all contracts that were not completed as of January 1, 2018. The cumulative effect of the adoption was recognized as an increase in the company’s accumulated deficit of $21.4 million on January 1, 2018.

The following table summarizes the effects of adopting ASU No. 2014-09 on the company's consolidated financial statements as of and for the three and six months ended June 30, 2018.

	As Reported	Adjustments	Balances Without Adoption of Topic 606
For the three months ended June 30, 2018			
Statement of Income			
Revenue			
Services	$586.7	$ (5.3)	$581.4
Technology	80.7	(16.2)	64.5
Costs and expenses			
Cost of revenue			
Services	484.2	(3.1)	481.1
Technology	30.3	0.2	30.5
Selling, general and administrative expenses	92.7	0.2	92.9
Operating income	54.0	(18.9)	35.1
Income before income taxes	20.3	(18.9)	1.4
Provision for income taxes	14.3	0.1	14.4
Consolidated net income	6.0	(19.0)	(13.0)
Net income attributable to Unisys Corporation	3.8	(19.0)	(15.2)
For the six months ended June 30, 2018			
Statement of Income			
Revenue			
Services	$1,155.2	$ (2.5)	$1,152.7
Technology	220.6	(93.0)	127.6
Costs and expenses			
Cost of revenue			
Services	955.1	(1.3)	953.8
Technology	66.6	(0.7)	65.9
Selling, general and administrative expenses	183.6	0.4	184.0
Operating income	155.8	(94.0)	61.8
Income before income taxes	82.9	(94.0)	(11.1)
Provision for income taxes	35.2	(9.4)	25.8
Consolidated net income	47.7	(84.6)	(36.9)
Net income attributable to Unisys Corporation	44.4	(84.6)	(40.2)
As of June 30, 2018			
Balance Sheet			
Assets			
Accounts receivable, net current	$484.0	$ 26.6	$510.6
Contract assets			