

NEUSTAR INC  
Form 10-Q  
May 02, 2013  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2013

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-32548

**NeuStar, Inc.**

(Exact name of registrant as specified in its charter)

Edgar Filing: NEUSTAR INC - Form 10-Q

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**52-2141938**  
(I.R.S. Employer  
Identification No.)

**21575 Ridgetop Circle**

**Sterling, Virginia 20166**

(Address of principal executive offices) (zip code)

**(571) 434-5400**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

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

There were 65,797,846 shares of Class A common stock, \$0.001 par value, and 3,082 shares of Class B common stock, \$0.001 par value, outstanding at April 24, 2013.

**Table of Contents**

**NEUSTAR, INC.**

**INDEX**

<b><u>PART I FINANCIAL INFORMATION</u></b>	3
Item 1. <u>Financial Statements</u>	3
<u>Consolidated Balance Sheets as of December 31, 2012 and March 31, 2013 (unaudited)</u>	3
<u>Unaudited Consolidated Statements of Operations for three months ended March 31, 2012 and 2013</u>	5
<u>Unaudited Consolidated Statements of Comprehensive Income for the three months ended March 31, 2012 and 2013</u>	6
<u>Unaudited Consolidated Statements of Cash Flows for the three months ended March 31, 2012 and 2013</u>	7
<u>Notes to Unaudited Consolidated Financial Statements</u>	8
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	24
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	32
Item 4. <u>Controls and Procedures</u>	32
<b><u>PART II OTHER INFORMATION</u></b>	32
Item 1. <u>Legal Proceedings</u>	32
Item 1A. <u>Risk Factors</u>	32
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	33
Item 3. <u>Defaults Upon Senior Securities</u>	33
Item 4. <u>Mine Safety Disclosures</u>	33
Item 5. <u>Other Information</u>	33
Item 6. <u>Exhibits</u>	34
<b><u>Signatures</u></b>	
EX 31.1	
EX 31.2	
EX 32.1	
EX 101 INSTANCE DOCUMENT	
EX 101 SCHEMA DOCUMENT	
EX 101 CALCULATION LINKBASE DOCUMENT	
EX 101 LABELS LINKBASE DOCUMENT	
EX 101 PRESENTATION LINKBASE DOCUMENT	
EX 101 DEFINITION LINBASE DOCUMENT	

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements****NEUSTAR, INC.****CONSOLIDATED BALANCE SHEETS**

(in thousands, except share and per share data)

	December 31, 2012	March 31, 2013 (unaudited)
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 340,255	\$ 376,675
Restricted cash	2,543	2,549
Short-term investments	3,666	1,564
Accounts receivable, net of allowance for doubtful accounts of \$2,161 and \$3,013, respectively	131,805	144,319
Unbilled receivables	6,372	6,612
Notes receivable	2,740	2,619
Prepaid expenses and other current assets	17,707	20,344
Deferred costs	7,379	7,291
Income taxes receivable	6,596	
Deferred tax assets	6,693	8,497
<b>Total current assets</b>	<b>525,756</b>	<b>570,470</b>
Property and equipment, net	118,513	113,723
Goodwill	572,178	572,178
Intangible assets, net	288,487	276,115
Notes receivable, long-term	1,008	406
Deferred costs, long-term	702	600
Other assets, long-term	20,080	26,979
<b>Total assets</b>	<b>\$ 1,526,724</b>	<b>\$ 1,560,471</b>

*See accompanying notes.*

**Table of Contents****NEUSTAR, INC.****CONSOLIDATED BALANCE SHEETS**

(in thousands, except share and per share data)

	December 31, 2012	March 31, 2013 (unaudited)
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 9,269	\$ 2,926
Accrued expenses	85,424	59,767
Income taxes payable		6,167
Deferred revenue	49,070	48,387
Notes payable	8,125	7,971
Capital lease obligations	1,686	1,105
Other liabilities	3,856	2,844
 Total current liabilities	 157,430	 129,167
Deferred revenue, long-term	9,922	10,061
Notes payable, long-term	576,688	614,271
Capital lease obligations, long-term	817	422
Deferred tax liabilities, long-term	114,130	117,487
Other liabilities, long-term	21,129	21,592
 Total liabilities	 880,116	 893,000
Commitments and contingencies		
Stockholders equity:		
Preferred stock, \$0.001 par value; 100,000,000 shares authorized; no shares issued and outstanding as of December 31, 2012 and March 31, 2013		
Class A common stock, par value \$0.001; 200,000,000 shares authorized; 85,958,791 and 86,498,716 shares issued; and 66,171,702 and 66,019,245 outstanding at December 31, 2012 and March 31, 2013, respectively		
	86	87
Class B common stock, par value \$0.001; 100,000,000 shares authorized; 3,082 and 3,082 shares issued and outstanding at December 31, 2012 and March 31, 2013, respectively		
Additional paid-in capital	532,743	550,709
Treasury stock, 19,787,089 and 20,479,471 shares at December 31, 2012 and March 31, 2013, respectively, at cost	(604,042)	(634,879)
Accumulated other comprehensive loss	(767)	(798)
Retained earnings	718,588	752,352
 Total stockholders equity	 646,608	 667,471
 Total liabilities and stockholders equity	 \$ 1,526,724	 \$ 1,560,471

*See accompanying notes.*

**Table of Contents****NEUSTAR, INC.****UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS****(in thousands, except per share data)**

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
Revenue:		
Carrier Services	\$ 124,373	\$ 132,171
Enterprise Services	39,485	44,779
Information Services	35,724	39,466
<b>Total revenue</b>	<b>199,582</b>	<b>216,416</b>
Operating expense:		
Cost of revenue (excluding depreciation and amortization shown separately below)	44,898	49,297
Sales and marketing	38,353	42,260
Research and development	7,724	7,484
General and administrative	20,993	21,882
Depreciation and amortization	22,706	24,665
Restructuring charges	522	2
	<b>135,196</b>	<b>145,590</b>
Income from operations	64,386	70,826
Other (expense) income:		
Interest and other expense	(8,193)	(17,562)
Interest and other income	229	141
Income before income taxes	56,422	53,405
Provision for income taxes	22,460	19,641
Net income	\$ 33,962	\$ 33,764
Net income per share:		
Basic	\$ 0.51	\$ 0.51
Diluted	\$ 0.50	\$ 0.50
Weighted average common shares outstanding:		
Basic	67,205	66,184
Diluted	68,478	67,614

*See accompanying notes.*

**Table of Contents****NEUSTAR, INC.****UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(in thousands)**

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
Net income	\$ 33,962	\$ 33,764
Other comprehensive loss, net of tax:		
Available for sale investments, net of tax:		
Change in net unrealized gains, net of tax of \$10 and \$(43), respectively	20	(65)
Reclassification for gains included in net income, net of tax of \$0 and \$0, respectively		
Net change in unrealized gains on investments, net of tax	20	(65)
Foreign currency translation adjustment, net of tax:		
Change in foreign currency translation adjustment, net of tax of \$(69) and \$(11), respectively	(239)	34
Reclassification adjustment included in net income, net of tax of \$0 and \$0, respectively		
Foreign currency translation adjustment, net of tax	(239)	34
Other comprehensive loss, net of tax	(219)	(31)
Comprehensive income	\$ 33,743	\$ 33,733

*See accompanying notes.*

**Table of Contents****NEUSTAR, INC.****UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Operating activities:</b>		
Net income	\$ 33,962	\$ 33,764
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	22,743	24,665
Stock-based compensation	3,901	8,957
Loss on debt modification and extinguishment		10,886
Amortization of deferred financing costs and original issue discount on debt	984	870
Excess tax benefits from stock option exercises	(6,533)	(3,213)
Deferred income taxes	2,666	1,149
Provision for doubtful accounts	702	1,575
Amortization of investment premium (discount), net	152	84
Changes in operating assets and liabilities:		
Accounts receivable	(19,180)	(14,399)
Unbilled receivables	2,574	(240)
Notes receivable	681	723
Prepaid expenses and other current assets	10,077	(2,359)
Deferred costs	(235)	190
Income taxes receivable	34,604	6,596
Other assets	257	86
Other liabilities	(4,867)	102
Accounts payable and accrued expenses	(30,886)	(26,428)
Income taxes payable		9,379
Deferred revenue	8,426	(544)
<b>Net cash provided by operating activities</b>	<b>60,028</b>	<b>51,843</b>
<b>Investing activities:</b>		
Purchases of property and equipment	(9,647)	(13,417)
Sales and maturities of investments	1,403	2,020
<b>Net cash used in investing activities</b>	<b>(8,244)</b>	<b>(11,397)</b>
<b>Financing activities:</b>		
Increase of restricted cash	(7)	(6)
Proceeds from notes payable, net of discount		624,244
Extinguishment of note payable		(592,500)
Debt issuance costs		(11,410)
Payments under notes payable obligations	(1,500)	(2,031)
Principal repayments on capital lease obligations	(900)	(976)
Proceeds from exercise of common stock options	32,084	6,256
Excess tax benefits from stock-based compensation	6,533	3,213
Repurchase of restricted stock awards	(8,913)	(6,392)
Repurchase of common stock	(23,837)	(24,445)
<b>Net cash provided by (used in) financing activities</b>	<b>3,460</b>	<b>(4,047)</b>
Effect of foreign exchange rates on cash and cash equivalents	(313)	21
<b>Net increase in cash and cash equivalents</b>	<b>54,931</b>	<b>36,420</b>



Edgar Filing: NEUSTAR INC - Form 10-Q

Cash and cash equivalents at beginning of period	122,237	340,255
Cash and cash equivalents at end of period	\$ 177,168	\$ 376,675

*See accompanying notes.*

---

**Table of Contents**

**NEUSTAR, INC.**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

**1. DESCRIPTION OF BUSINESS AND ORGANIZATION**

NeuStar, Inc. (the Company or Neustar) is a trusted provider of real-time information and analysis using proprietary and hard to replicate data sets. The Company's customers use its services for commercial insights that help them promote and protect their businesses. The Company combines proprietary, third party and customer data sets to develop unique algorithms, models, point solutions and complete work flow solutions. Among other things, chief marketing, security, information and operating officers use these real-time insights to identify who or what is at the other end of a transaction, the geographic-context of a transaction and the most appropriate response. The Company provides its services in a trusted and neutral manner. The Company's customers access its databases through standard connections, which the Company believes is the most efficient and cost effective way to exchange operationally essential data in a secured environment that does not favor any particular customer or technology. Today the Company primarily serves customers in the Internet, communications, information services, financial services, retail, and media and advertising verticals.

The Company was founded to meet the technical and operational challenges of the communications industry when the U.S. government mandated local number portability in 1996. The Company provides the authoritative solution that the communications industry relies upon to meet this mandate. Since then, the Company has grown to offer a broad range of innovative services, including database services (telephone number databases, domain names, short-codes and fixed IP addresses), analytics platforms used for Internet security services, caller identification services, web performance monitoring services and real-time information and analytics services.

The Company provides the North American communications industry with real-time information that enables the dynamic routing of virtually all telephone calls and text messages among competing carriers in the United States and Canada. The Company's internet and eCommerce customers use its broad array of domain name systems (DNS) solutions to resolve internet queries in a timely manner and to protect their businesses from malicious attacks. The Company also provides a broad suite of solutions that allows its customers to generate marketing leads, offer more relevant services and improve client conversion rates.

The Company categorizes its services into three reportable segments:

*Carrier Services.* The Company's carrier services include numbering services, order management services and IP services. Through its set of unique databases and system infrastructure in geographically dispersed data centers, the Company manages the increasing complexity in the communications industry and ensures the seamless connection of its carrier customers' numerous networks, while also enhancing the capabilities and performance of their infrastructure. The Company operates the authoritative databases that manage virtually all telephone area codes and numbers, and enables the dynamic routing of calls and text messages among numerous competing carriers in the United States and Canada. All carriers that offer telecommunications services to the public at large in the United States and Canada must access a copy of the Company's unique database to properly route their customers' calls and text messages. The Company also facilitates order management and work-flow processing among carriers, and allows operators to manage and optimize the addressing and routing of IP communications.

*Enterprise Services.* The Company's enterprise services include Internet infrastructure services (IIS) and registry services. Through the Company's global directory platform, the Company provides a suite of DNS services to its enterprise customers. The Company manages a collection of directories that maintain addresses in order to direct, prioritize and manage Internet traffic, and to find and resolve Internet queries and top-level domains. The Company is the authoritative provider of essential registry services and manages directories of similar resources, or addresses, that its customers use for reliable, fair and secure access and connectivity. In addition, enterprise customers rely on the Company's services to monitor and load-test websites to help identify issues and optimize performance. The Company also provides fixed IP geolocation services that help enterprises identify the location of their online consumers for a variety of purposes, including fraud prevention and marketing. Additionally, the Company provides directory services for the 5- and 6-digit number strings used for all U.S. Common Short Codes, which is part of the short messaging service relied upon by the U.S. wireless industry. The Company also operates the user authentication and rights management system, which

## Edgar Filing: NEUSTAR INC - Form 10-Q

supports the UltraViolet™ digital content locker that consumers can use to access to their entertainment content.

*Information Services.* The Company's information services include on-demand solutions that help carriers and enterprises identify, verify, evaluate and locate customers and prospective customers. The Company's authoritative databases and solutions enable its clients to return the caller name associated with the calling phone number and to make informed

---

**Table of Contents**

**NEUSTAR, INC.**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

decisions in real time about consumer-initiated interactions on the Internet, over the telephone and at the point of sale, by correlating consumer identifier information with attributes such as demographics, buying behavior surveys and location. This allows the Company's customers to offer consumers more relevant services and products, and leads to higher client conversion rates. Using the Company's proprietary databases, the Company's online display advertising solution allows marketers to display, in real time, advertisements that will be most relevant to online consumers without the need for online behavioral tracking.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Unaudited Interim Financial Information**

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The results of operations for the three months ended March 31, 2013 are not necessarily indicative of the results that may be expected for the full fiscal year. The consolidated balance sheet as of December 31, 2012 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and notes required by U.S. generally accepted accounting principles for complete financial statements. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 (the 2012 Form 10-K) filed with the Securities and Exchange Commission.

**Use of Estimates**

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting periods. Significant estimates and assumptions are inherent in the analysis and the measurement of deferred tax assets; the identification and quantification of income tax liabilities due to uncertain tax positions; restructuring liabilities; valuation of investments; recoverability of intangible assets, other long-lived assets and goodwill; the determination of the allowance for doubtful accounts; and the classification of note payable. The Company bases its estimates on historical experience and assumptions that it believes are reasonable. Actual results could differ from those estimates.

**Fair Value of Financial Instruments**

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic Financial Instruments requires disclosures of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate that value. Due to their short-term nature, the carrying amounts reported in the accompanying unaudited consolidated financial statements approximate the fair value for cash and cash equivalents, accounts receivable, accounts payable and accrued expenses. The Company determines the fair value of its investments using third-party pricing sources, which primarily use a consensus price or weighted average price for the fair value assessment. The consensus price is determined by using matrix prices from a variety of industry standard pricing services, data providers, large financial institutions and other third party sources and utilizing those matrix prices as inputs into a distribution-curve-based algorithm to determine the estimated market value. Matrix prices are based on quoted prices for securities with similar terms (*i.e.*, coupon rate, maturity, credit rating) (see Note 4). The Company believes the carrying value of its notes receivable approximates fair value as the interest rate approximates a market rate. The Company believes the carrying value of its long-term debt approximates the fair value of the debt as the terms and interest rates approximate market rates (see Note 6).

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

The estimated fair values of the Company's financial instruments are as follows (in thousands):

	December 31, 2012		March 31, 2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	\$ 340,255	\$ 340,255	\$ 376,675	\$ 376,675
Restricted cash (current assets)	2,543	2,543	2,549	2,549
Short-term investments	3,666	3,666	1,564	1,564
Notes receivable (including current portion)	3,748	3,748	3,025	3,025
Marketable securities (other assets, long-term)	4,458	4,458	4,621	4,621
Deferred compensation (other liabilities, long-term)	3,874	3,874	4,042	4,042
2011 Term Facility (including current portion, net of discount)	584,813	584,813		
2013 Term Facility (including current portion, net of discount)			322,242	322,242
Senior Notes (including current portion)			300,000	300,000

**Restricted Cash**

As of December 31, 2012 and March 31, 2013, cash of \$2.5 million and \$2.5 million, respectively, was restricted for deposits on leased facilities.

**Recent Accounting Pronouncements**

In February 2013, the FASB issued ASU 2013-02, Comprehensive Income (Topic 220) Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. This update requires the presentation, either in a single note or parenthetically on the face of the financial statements, of the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source and the income statement line items affected by the reclassification. This ASU is effective prospectively for the Company for annual and interim periods beginning January 1, 2013. The adoption of the amended accounting guidance in the first quarter of 2013 impacted the Company's presentation of other comprehensive income and did not have an impact on the Company's consolidated results of operations.

**3. INVESTMENTS**

As of December 31, 2012 and March 31, 2013, the Company held approximately \$3.7 million and \$1.6 million, respectively, in pre-refunded municipal bonds, secured by an escrow fund of U.S. Treasury securities. These investments are accounted for as available-for-sale securities in the Company's consolidated balance sheet pursuant to the Investments - Debt and Equity Securities Topic of the FASB ASC. During the three months ended March 31, 2012 and 2013, the Company sold approximately \$1.4 million and \$2.0 million, respectively, of available-for-sale securities. The Company recognized minimal gains for the three months ended March 31, 2012 and 2013, respectively. The Company did not record any impairment charges related to these investments during the three months ended March 31, 2012 and 2013. As of December 31, 2012 and March 31, 2013, unrealized gains and losses on the pre-refunded municipal bonds were insignificant. The following table summarizes the Company's investment in these municipal bonds as of December 31, 2012 and March 31, 2013 (in thousands):

Amortized Cost	December 31, 2012		Estimated Fair Value
	Gross Unrealized Gains	Losses	

Edgar Filing: NEUSTAR INC - Form 10-Q

Due within one year	\$ 3,666	\$	\$	\$ 3,666
	<b>Amortized Cost</b>	<b>March 31, 2013 Gross Unrealized Gains      Losses</b>		<b>Estimated Fair Value</b>
Due within one year	\$ 1,563	\$ 1	\$	\$ 1,564

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013****4. FAIR VALUE MEASUREMENTS**

Fair value is the price that would be received in the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Fair Value Measurements and Disclosure Topic of FASB ASC establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value and requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1. Observable inputs, such as quoted prices in active markets;

Level 2. Inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and

Level 3. Unobservable inputs for which there is little or no market data, which require the reporting entity to develop its own assumptions.

The Company evaluates assets and liabilities subject to fair value measurements on a recurring and non-recurring basis to determine the appropriate level at which to classify them for each reporting period. This determination requires the Company to make significant judgments.

The Company determines the fair value of its investments using third-party pricing sources, which primarily use a consensus price or weighted average price for the fair value assessment. The consensus price is determined by using matrix prices from a variety of industry standard pricing services, data providers, large financial institutions and other third party sources and utilizing those multiple prices as inputs into a distribution-curve-based algorithm to determine the estimated market value. Matrix prices are based on quoted prices for securities with similar terms (*i.e.*, coupon rate, maturity, credit rating). The Company corroborates consensus prices provided by third party pricing sources using reported trade activity, benchmark yield curves, binding broker/dealer quotes or other relevant price information.

The following table sets forth, as of December 31, 2012 and March 31, 2013, the Company's financial and non-financial assets and liabilities that are measured at fair value on a recurring basis, by level within the fair value hierarchy (in thousands):

	December 31, 2012			Total
	Level 1	Level 2	Level 3	
Municipal bonds (maturities less than one year)	\$	\$ 3,666	\$	\$ 3,666
Marketable securities <sup>(1)</sup>		4,458		4,458
<b>Total</b>		<b>\$ 4,458</b>		<b>\$ 8,124</b>

  

	March 31, 2013			Total
	Level 1	Level 2	Level 3	
Municipal bonds (maturities less than one year)	\$	\$ 1,564	\$	\$ 1,564
Marketable securities <sup>(1)</sup>		4,621		4,621
<b>Total</b>		<b>\$ 4,621</b>		<b>\$ 6,185</b>

- (1) The NeuStar, Inc. Deferred Compensation Plan (the Plan) provides directors and certain employees with the ability to defer a portion of their compensation. The assets of the Plan are invested in marketable securities held in a Rabbi Trust and reported at market value in other assets.



**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013****5. GOODWILL AND INTANGIBLE ASSETS****Goodwill**

The Company's goodwill by operating segment as of December 31, 2012 and March 31, 2013 is as follows (in thousands):

	December 31, 2012	March 31, 2013
<b>Carrier Services:</b>		
Gross goodwill	\$ 222,355	\$ 222,355
Accumulated impairments	(93,602)	(93,602)
Net goodwill	128,753	128,753
<b>Enterprise Services:</b>		
Gross goodwill	16,198	16,198
Accumulated impairments		
Net goodwill	16,198	16,198
<b>Information Services:</b>		
Gross goodwill	427,227	427,227
Accumulated impairments		
Net goodwill	427,227	427,227
<b>Total:</b>		
Gross goodwill	665,780	665,780
Accumulated impairments	(93,602)	(93,602)
Net goodwill	\$ 572,178	\$ 572,178

**Intangible Assets**

Intangible assets consist of the following (in thousands):

	December 31, 2012	March 31, 2013	Weighted- Average Amortization Period (in years)
Intangible assets:			

Edgar Filing: NEUSTAR INC - Form 10-Q

Customer lists and relationships	\$ 315,098	\$ 315,098	7.9
Accumulated amortization	(69,526)	(78,690)	
Customer lists and relationships, net	245,572	236,408	
Acquired technology	58,859	58,859	4.8
Accumulated amortization	(20,387)	(22,976)	
Acquired technology, net	38,472	35,883	
Trade name	7,630	7,630	3.0
Accumulated amortization	(3,187)	(3,806)	
Trade name, net	4,443	3,824	
Intangible assets, net	\$ 288,487	\$ 276,115	

Amortization expense related to intangible assets, which is included in depreciation and amortization expense, was approximately \$12.6 million and \$12.4 million for the three months ended March 31, 2012 and 2013, respectively. Amortization expense related to

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

intangible assets for the years ended December 31, 2013, 2014, 2015, 2016, 2017 and thereafter is expected to be approximately \$48.9 million, \$47.9 million, \$45.9 million, \$44.1 million, \$35.6 million and \$66.1 million, respectively. Intangible assets as of March 31, 2013 will be fully amortized during the year ended December 31, 2021.

**6. NOTES PAYABLE**

Notes payable consist of the following (in thousands):

	<b>December 31, 2012</b>	<b>March 31, 2013</b>
2011 Term Facility (net of discount)	\$ 584,813	\$
2013 Term Facility (net of discount)		322,242
Senior Notes		300,000
Total	584,813	622,242
Less: current portion, net of discount	(8,125)	(7,971)
Long-term portion	\$ 576,688	\$ 614,271

**Debt Refinancing**

As of December 31, 2012, the Company's outstanding borrowings, net of discount, under its credit facility was \$584.8 million. This credit facility provided for: (1) a \$600 million senior secured term loan facility (2011 Term Facility); (2) a \$100 million senior secured revolving credit facility (2011 Revolving Facility and together with the 2011 Term Facility, the 2011 Credit Facilities). As of December 31, 2012, available borrowings under the 2011 Revolving Facility were \$92.2 million.

On January 22, 2013, the Company entered into a credit facility that provided for a \$325 million senior secured term loan facility (2013 Term Facility) and a \$200 million senior secured revolving credit facility (2013 Revolving Facility, and together with the 2013 Term Facility, the 2013 Credit Facilities). In addition, the Company closed an offering of \$300 million aggregate principal amount of senior notes (Senior Notes). The Company used the proceeds received from the 2013 Term Facility and Senior Notes to repay its outstanding principal borrowings of \$592.5 million under the 2011 Term Facility. The Company used available borrowings under the 2013 Revolving Facility for outstanding letters of credit totaling \$7.8 million that were previously secured by the 2011 Revolving Facility. The 2011 Credit Facilities were terminated in connection with this refinancing event.

Certain investors of the 2011 Credit Facilities reinvested in either or both of the 2013 Credit Facilities and Senior Notes and the change in the present value of future cash flows between the investments were less than 10%. Accordingly, the Company accounted for this refinancing event for these investors as a debt modification. Certain investors of the 2011 Credit Facilities either did not invest in the 2013 Credit Facilities or Senior Notes or the change in the present value of future cash flows between the investments was greater than 10%. Accordingly, the Company accounted for this refinancing event for these investors as a debt extinguishment. In applying debt modification accounting, during the three months ended March 31, 2013, the Company recorded \$25.8 million in loan origination fees and deferred financing costs, of which \$16.9 million related to investors that reinvested in either or both of the 2013 Credit Facilities and Senior Notes. This amount is being amortized into interest expense over the term of the 2013 Credit Facilities and Senior Notes using the effective interest method. In addition, related to this refinancing event, the Company recorded \$10.9 million in interest and other expense, comprised of \$9.4 million in loss on debt extinguishment and \$1.5 million in debt modification expense.

***2013 Credit Facilities***

The 2013 Credit Facilities include: (1) the 2013 Term Facility; (2) the 2013 Revolving Facility, of which (a) \$100 million is available for the issuance of letters of credit and (b) \$25 million is available as a swingline subfacility; and (3) incremental term loan facilities in an amount such that after giving effect to the incurrence of any such incremental loans, either (a) the aggregate amount of incremental loans does not exceed \$400 million or (b) the Consolidated Secured Leverage Ratio on a pro forma basis after giving effect to any such increase would not exceed 2.50 to 1.00. The 2013 Revolving Facility and 2013 Term Facility mature on January 22, 2018. As of March 31, 2013, the Company had not borrowed any amounts under the 2013 Revolving Facility and available borrowings were \$192.2 million, exclusive of outstanding letters of credit totaling \$7.8 million.

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

Principal payments under the 2013 Term Facility are as follows (in thousands):

2013	\$ 8,125
2014	8,125
2015	8,125
2016	8,125
2017	8,125
Thereafter	284,375
<b>Total principal payments</b>	<b>\$ 325,000</b>

Principal payments under the 2013 Term Facility of \$2.0 million are due on the last day of the quarter beginning on March 31, 2013 and ending on December 31, 2017. The remaining 2013 Term Facility principal balance of \$284.4 million is due in full on January 22, 2018, subject to early mandatory prepayments.

The loans outstanding under the 2013 Credit Facilities (Loans) bear interest, at the Company's option, either: (1) at the base rate, which is defined as the highest of (a) the federal funds rate plus 0.50%, (b) the interest rate published by the Wall Street Journal from time to time as the U.S. Prime Rate and (c) the adjusted LIBOR rate for a one-month interest period beginning on such day plus 1.00%; or (2) at the LIBOR rate plus, in each case, an applicable margin. The applicable margin is (1) if the Consolidated Leverage Ratio is less than 2.00:1.00, 0.50% per annum for borrowings based on the base rate and 1.50% per annum for borrowings based on the LIBOR rate, or (2) if the Consolidated Leverage Ratio is 2.00:1.00 or greater, 0.75% per annum for borrowings based on the base rate and 1.75% per annum borrowings based on the LIBOR rate. The accrued interest under the 2013 Term Facility is payable quarterly beginning in March 31, 2013. As of March 31, 2013, accrued interest under the 2013 Credit Facilities was \$0.2 million.

The Company may voluntarily prepay the Loans at any time in minimum amounts of \$1 million or an integral multiple of \$500,000 in excess thereof. The 2013 Credit Facilities provide for mandatory prepayments with the net cash proceeds of certain debt issuances, insurance receipts, and dispositions. The 2013 Term Facility also contains certain events of default, upon the occurrence of which, and so long as such event of default is continuing, the amounts outstanding may, at the option of the required Lenders, accrue interest at an increased rate and payments of such outstanding amounts could be accelerated, or other remedies undertaken pursuant to the 2013 Term Facility, by the required Lenders.

As of March 31, 2013, deferred financing costs and loan origination fees related to the 2013 Credit Facilities was \$10.0 million. Total amortization expense of the deferred financing costs and loan origination fees was \$0.4 million for the three months ended March 31, 2013 and was reported as interest expense in the consolidated statements of operations.

**Senior Notes**

On January 22, 2013, the Company closed an offering of \$300 million aggregate principal amount of 4.50% senior notes due 2023 to qualified institutional buyers pursuant to Rule 144A, and outside of the United States pursuant to Regulation S, under the Securities Act of 1933, as amended, or the Securities Act. The Senior Notes were issued pursuant to an indenture, dated as of January 22, 2013, among the Company, certain of its domestic subsidiaries, or the Subsidiary Guarantors, and The Bank of New York Mellon Trust Company, N.A., as trustee, or the Indenture. The Senior Notes are the general unsecured senior obligations of the Company and are guaranteed on a senior unsecured basis by the Subsidiary Guarantors.

Interest is payable on the Senior Notes semi-annually in arrears at an annual rate of 4.50%, on January 15 and July 15 of each year, beginning on July 15, 2013. The Senior Notes will mature on January 15, 2023. Interest will accrue from January 22, 2013. As of March 31, 2013, accrued

## Edgar Filing: NEUSTAR INC - Form 10-Q

interest under the Senior Notes was \$2.6 million.

At any time and from time to time prior to July 15, 2016, the Company may redeem up to a maximum of 35% of the original aggregate principal amount of the Senior Notes with the proceeds of certain equity offerings, at a redemption price equal to 104.50% of the principal amount thereof, plus accrued and unpaid interest thereon, if any, to the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date); provided that: (1) at least 65% of the original aggregate principal amount of the Senior Notes remains outstanding; and (2) the redemption occurs within 90 days of the completion of such equity offering upon not less than 30 nor more than 60 days prior notice.

Prior to January 15, 2018, the Company may redeem some or all of the Senior Notes by paying a make-whole premium based on U.S. Treasury rates. During the 12-month period commencing on January 15 of the relevant year listed below, the Company may

**Table of Contents**

**NEUSTAR, INC.**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

redeem some or all of the Senior Notes at the prices listed below, plus accrued and unpaid interest, if any, to, but not including, the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date): 2018 at a redemption price of 102.25%; 2019 at a redemption price of 101.50%; 2020 at a redemption price of 100.75%; and 2021 and thereafter at a redemption price of 100.00%. If the Company experiences certain changes of control together with a ratings downgrade, it will be required to offer to purchase all of the Senior Notes then outstanding at a purchase price equal to 101.00% of the principal amount thereof, plus accrued and unpaid interest, if any, to the date of purchase. If the Company sells certain assets and does not repay certain debt or reinvest the proceeds of such sales within certain time periods, it will be required to offer to repurchase the Senior Notes with such proceeds at 100.00% of their principal amount, plus accrued and unpaid interest, if any, to the date of purchase.

The Senior Notes contain customary events of default, including among other things, payment default, failure to provide certain notices and certain provision related to bankruptcy events. The Senior Notes also contain customary negative covenants.

On January 22, 2013, the Company entered into a registration rights agreement relating to the Senior Notes that requires it and the Subsidiary Guarantors to, among other things: (1) file a registration statement with respect to a registered offer to exchange the Senior Notes for new notes guaranteed by the Company's Subsidiary Guarantors, with terms substantially identical in all material respects to those of the Senior Notes (except that the new notes will not be subject to restrictions on transfer or to any increase in annual interest rate); (2) use the Company's reasonable best efforts to cause the applicable registration statement to become effective under the Securities Act; and (3) promptly after the applicable registration statement is declared effective, initiate an exchange offer. In addition, under certain circumstances, the Company and the Subsidiary Guarantors may be required to file a shelf registration statement relating to resales of the Senior Notes.

If (1) the exchange offer is not completed within 300 days after the date of original issuance of the Senior Notes; (2) a shelf registration statement, if required, has not become effective within 300 days after the date of original issuance of the Senior Notes; (3) if the Company receives a request to file a shelf registration pursuant to the Registration Rights Agreement and such shelf registration statement has not become effective by the later of (a) 300 days after the date of original issuance of the Senior Notes and (b) 120 days after delivery of such shelf request or (4) any required registration statement is filed and declared effective but thereafter ceases to be effective in certain circumstances during the applicable period (each such event referred to in clauses (1) through (4) above, a Registration Default), then the Company will be obligated to pay additional interest to each holder of the Senior Notes that are subject to transfer restrictions, with respect to the first 90-day period immediately following the occurrence of a Registration Default, at a rate of 0.25% per annum on the principal amount of the Senior Notes that are subject to transfer restrictions held by such holder. The amount of additional interest will increase by an additional 0.25% per annum with respect to each subsequent 90-day period until the Registration Default ends, up to a maximum increase of 1.00% per annum on the principal amount of the Senior Notes that are subject to transfer restrictions.

As of March 31, 2013, deferred financing costs related to the Senior Notes was \$15.2 million. Total amortization expense of the deferred financing costs was \$0.2 million for the three months ended March 31, 2013 and is reported as interest expense in the consolidated statements of operations.

**7. STOCKHOLDERS EQUITY**

**Stock-Based Compensation**

The Company maintains six compensation plans: the NeuStar, Inc. 1999 Equity Incentive Plan (1999 Plan); the NeuStar, Inc. 2005 Stock Incentive Plan (2005 Plan); the Amended and Restated NeuStar, Inc. 2009 Stock Incentive Plan (2009 Plan); the Targus Information Corporation Amended and Restated 2004 Stock Incentive Plan (TARGUSInfo Plan); the AMACAI Information Corporation 2004 Stock Incentive Plan (AMACAI Plan) (collectively, the Plans), and the Neustar, Inc. Employee Stock Purchase Plan (ESPP). The Company may grant to its directors, employees and consultants awards under the 2009 Plan in the form of incentive stock options, nonqualified stock options, stock appreciation rights, shares of restricted stock, restricted stock units, performance vested restricted stock units (PVRsUs) and other stock-based awards. The aggregate number of shares of Class A common stock with respect to which all awards may be granted under the 2009 Plan is

## Edgar Filing: NEUSTAR INC - Form 10-Q

11,911,646, plus the number of shares underlying awards granted under the 1999 Plan, the 2005 Plan, the TARGUSinfo Plan, and the AMACAI Plan that remain undelivered following any expiration, cancellation or forfeiture of such awards. As of March 31, 2013, a total of 5,286,480 shares were available for grant or award under the 2009 Plan.



**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

On June 20, 2012, at the Company's annual shareholder meeting, stockholders approved the ESPP. As of March 31, 2013, a total of 600,000 shares were available under the ESPP. The first six-month offering period under the ESPP will begin on May 1, 2013.

Stock-based compensation expense recognized for the three months ended March 31, 2012 and 2013 was \$3.9 million and \$9.0 million, respectively. As of March 31, 2013, total unrecognized compensation expense related to non-vested stock options, non-vested restricted stock awards, non-vested restricted stock units and non-vested PVRsUs granted prior to that date was estimated at \$69.6 million, which the Company expects to recognize over a weighted average period of approximately 1.71 years. Total unrecognized compensation expense as of March 31, 2013 is estimated based on outstanding non-vested stock options, non-vested restricted stock awards, non-vested restricted stock units and non-vested PVRsUs. Stock-based compensation expense may increase or decrease in future periods for subsequent grants or forfeitures, and changes in the estimated fair value of non-vested awards granted to consultants.

**Stock Options**

The Company utilizes the Black-Scholes option pricing model to estimate the fair value of stock options granted. No options were granted during the three months ended March 31, 2012 and 2013.

The following table summarizes the Company's stock option activity:

	Shares	Weighted-Average Exercise Price	Aggregate Intrinsic Value (in millions)	Weighted-Average Remaining Contractual Life (in years)
Outstanding at December 31, 2012	3,296,040	\$ 24.81		
Options granted				
Options exercised	(251,988)	24.28		
Options forfeited	(147,508)	28.35		
Outstanding at March 31, 2013	2,896,544	\$ 24.68	\$ 63.3	6.82
Exercisable at March 31, 2013	1,497,514	\$ 23.65	\$ 34.3	6.19

The aggregate intrinsic value of options exercised for the three months ended March 31, 2012 and 2013 was \$14.8 million and \$5.3 million, respectively.

**Restricted Stock Awards**

The following table summarizes the Company's non-vested restricted stock activity for the three months ended March 31, 2013:

Shares	Weighted-Average Grant Date	Aggregate Intrinsic Value
--------	-----------------------------	---------------------------

Edgar Filing: NEUSTAR INC - Form 10-Q

		<b>Fair Value</b>	<b>(in millions)</b>
Outstanding at December 31, 2012	305,390	\$ 24.20	
Restricted stock granted			
Restricted stock vested	(82,812)	24.88	
Restricted stock forfeited	(8,292)	25.21	
<b>Outstanding at March 31, 2013</b>	<b>214,286</b>	<b>\$ 23.90</b>	<b>\$ 10.0</b>

The total aggregate intrinsic value of restricted stock vested during the three months ended March 31, 2013 was \$3.7 million. During the three months ended March 31, 2013, the Company repurchased 30,824 shares of common stock for an aggregate purchase price of \$1.4 million pursuant to the participants' rights under the Company's stock incentive plans to elect to use common stock to satisfy their tax withholding obligations.

---

**Table of Contents**

**NEUSTAR, INC.**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

**Performance Vested Restricted Stock Units**

***2012 Long-Term Incentive Program***

During the three months ended March 31, 2013, the Company awarded 99,210 PVRsUs, of which 49,605 PVRsUs were granted with an aggregate fair value of \$2.2 million. In addition, during the three months ended March 31, 2013, the Company established the performance goals for the period beginning on January 1, 2013 and ending on December 31, 2013. The establishment of the 2013 performance goals resulted in the grant of 606,456 PVRsUs with an aggregate fair value of \$26.7 million, originally awarded during the year ended December 31, 2012.

For executive management, the awarded PVRsUs are subject to five one-year performance periods, the first of which began on January 1, 2012 and ended December 31, 2012 and the last of which begins on January 1, 2016 and ends on December 31, 2016. Each executive is eligible to earn up to 150% of one-fifth of the award with respect to each annual performance period subject to the achievement of the respective performance goals for each one-year performance period. For non-executive management, the PVRsUs awarded are subject to three one-year performance periods, the first of which began on January 1, 2012 and ended December 31, 2012 and the last of which begins on January 1, 2014 and ends on December 31, 2014. Each non-executive is eligible to earn up to 150% of one-third of the award with respect to each annual performance period subject to the achievement of the respective performance goals for each one-year performance period. For both executive and non-executive management, the performance goals for each of the 2012 and 2013 performance periods were and will be based on: (i) Non-NPAC Revenue, (ii) Total Revenue, and (iii) Adjusted Net Income. The performance goals for the future one-year performance periods will consist of financial measures, weights and payouts to be established no later than 90 days after the beginning of each such period.

Subject to each participant's continued service and to certain other terms and conditions, the portion of the award, if any, earned (a) by executive management with respect to the first three performance periods will vest on January 1, 2015 and the portion of the award, if any, earned with respect to the final two performance periods will vest on January 1, 2016 and January 1, 2017, respectively; and (b) by non-executive management with respect to all three performance periods will vest 75% of the earned amount on the first business day of 2015, and the remaining 25% of the earned amount on the first business day of 2016. Compensation expense related to these awards is recognized over the requisite service period based on the Company's estimate of the achievement of the performance target and vesting period.

***2013 Long-Term Incentive Program***

During the three months ended March 31, 2013, the Company awarded 117,020 PVRsUs, of which 39,007 PVRsUs were granted with an aggregate fair value of \$1.7 million.

The awarded PVRsUs are subject to three one-year performance periods, the first of which begins on January 1, 2013 and ends on December 31, 2013 and the last of which begins on January 1, 2015 and ends on December 31, 2015. Each participant is eligible to earn up to 150% of one-third of the award with respect to each annual performance period subject to the achievement of the respective performance goals for each one-year performance period. The performance goal for the performance period from January 1, 2013 through December 31, 2013 will be based on: (i) Non-NPAC Revenue, (ii) Total Revenue, and (iii) Adjusted Net Income. The performance goals for the future one-year performance periods will consist of financial measures, weights and payouts to be established no later than 90 days after the beginning of each such period.

Subject to each participant's continued service and to certain other terms and conditions, the portion of the award, if any, earned will vest on March 1 in the year following the respective annual performance period. Compensation expense related to these awards is recognized over the requisite service period based on the Company's estimate of the achievement of the performance target and vesting period.

***Non-Vested PVRsU Activity***

The fair value of a PVRsU is measured by reference to the closing market price of the Company's common stock on the date of the grant. Compensation expense is recognized on a straight-line basis over the requisite service period based on the number of PVRsUs expected to vest.

## Edgar Filing: NEUSTAR INC - Form 10-Q

As of March 31, 2013, the level of achievement of the performance target awards for PVRsUs granted during 2011, 2012 and 2013 was 134%, 129.5% and 100%, respectively.

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

The following table summarizes the Company's non-vested PVRSU activity for the three months ended March 31, 2013:

	Shares	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value (in millions)
Non-vested December 31, 2012	971,023	\$ 31.72	
Granted	695,068	44.08	
Incremental achieved <sup>(1)</sup>	170,225	36.32	
Vested	(159,346)	22.85	
Forfeited	(23,239)	33.99	
Non-vested March 31, 2013	1,653,731	\$ 38.21	\$ 76.9

(1) Incremental achieved represents the additional awards above the target grant resulting from the achievement of performance goals above the performance targets established at grant date.

The total aggregate intrinsic value of PVRSU's vested during the three months ended March 31, 2013 was approximately \$6.7 million. The Company repurchased 60,075 shares of common stock for an aggregate purchase price of \$2.5 million pursuant to the participants' rights under the Plans to elect to use common stock to satisfy their tax withholding obligations.

**Restricted Stock Units**

The following table summarizes the Company's restricted stock units activity for the three months ended March 31, 2013:

	Shares	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value (in millions)
Outstanding at December 31, 2012	922,550	\$ 33.20	
Granted	27,710	44.37	
Vested	(140,621)	36.37	
Forfeited	(6,491)	37.07	
Outstanding at March 31, 2013	803,148	\$ 33.00	\$ 37.4

During the three months ended March 31, 2013, the Company granted 27,710 restricted stock units to certain employees with an aggregate fair value of \$1.2 million. Restricted stock units granted to executive management will vest annually in five equal installments beginning on January 1, 2013. Restricted stock units granted to non-executive management will vest annually in four equal installments beginning on the first business day in 2013.

## Edgar Filing: NEUSTAR INC - Form 10-Q

The restricted stock units previously issued to non-management directors of the Company's Board of Directors will fully vest on the earlier of the first anniversary of the date of grant or the day preceding the date in the following calendar year on which the Company's annual meeting of stockholders is held. Upon vesting of restricted stock units granted prior to 2011, each director's restricted stock units will automatically be converted into deferred stock units, and will be delivered to the director in shares of the Company's stock six months following the director's termination of board service. Upon vesting of restricted stock units that were granted in 2011 and subsequent periods, each director's restricted stock units will automatically be converted into deferred stock units and will be delivered to the director in shares of the Company's stock six months following the director's termination of board service unless a director elected near-term delivery, in which case the vested restricted stock units will be delivered on August 15 in the year following the initial grant.

### **Share Repurchase Program**

Under the 2010 share repurchase program, during the three months ended March 31, 2013, the Company repurchased 0.6 million shares of its Class A common stock at an average price of \$44.38 per share for a total purchase price of \$24.4 million. As of March 31, 2013, a total of 7.7 million shares at an average price of \$30.67 per share had been repurchased under the 2010 share repurchase program for an aggregate purchase price of \$237.2 million. All repurchased shares are accounted for as treasury shares.

On May 2, 2013, the Company announced that its Board of Directors authorized a \$250 million share repurchase program, commencing in the second quarter of 2013 and continuing to December 31, 2013. This program replaces the 2010 share repurchase program.

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013****8. BASIC AND DILUTED NET INCOME PER COMMON SHARE**

The following table provides a reconciliation of the numerators and denominators used in computing basic and diluted net income per common share (in thousands, except per share data):

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Computation of basic net income per common share:</b>		
Net income	\$ 33,962	\$ 33,764
<b>Weighted average common shares and participating securities outstanding basic</b>	<b>67,205</b>	<b>66,184</b>
Basic net income per common share	\$ 0.51	\$ 0.51
<b>Computation of diluted net income per common share:</b>		
<b>Weighted average common shares and participating securities outstanding basic</b>	<b>67,205</b>	<b>66,184</b>
<b>Effect of dilutive securities:</b>		
Stock-based awards	1,273	1,430
<b>Weighted average common shares outstanding diluted</b>	<b>68,478</b>	<b>67,614</b>
Diluted net income per common share	\$ 0.50	\$ 0.50

Diluted net income per common share reflects the potential dilution of common stock equivalents such as options and warrants, to the extent the impact is dilutive. Stock-based awards to purchase an aggregate of 485,906 and 808 shares were excluded from the calculation of the denominator for diluted net income per common share for the three months ended March 31, 2012 and 2013, respectively, due to their anti-dilutive effects.

**9. ACCUMULATED OTHER COMPREHENSIVE INCOME**

The following table provides a reconciliation of the changes in accumulated other comprehensive income, net of tax, by component (in thousands):

	<b>Unrealized Gains and Losses on Investments</b>	<b>Foreign Currency Translation Adjustment</b>	<b>Total</b>
Balance at December 31, 2012	\$ 142	\$ (909)	\$ (767)

Edgar Filing: NEUSTAR INC - Form 10-Q

Other comprehensive income (loss) before reclassifications	(65)	34	(31)
Amounts reclassified from accumulated other comprehensive income (loss)			
Net current-period other comprehensive income	(65)	34	(31)
Balance at March 31, 2013	\$ 77	\$ (875)	\$ (798)



**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013****10. OTHER (EXPENSE) INCOME**

Other (expense) income consists of the following (in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Interest and other expense:</b>		
Interest expense	\$ 8,613	\$ 6,565
Loss on debt modification and extinguishment		10,886
Gain on asset disposals	(130)	(65)
Foreign currency transaction (gain) loss	(290)	176
<b>Total</b>	<b>\$ 8,193</b>	<b>\$ 17,562</b>
<b>Interest and other income:</b>		
Interest income	\$ 229	\$ 141
<b>Total</b>	<b>\$ 229</b>	<b>\$ 141</b>

**11. INCOME TAXES**

The Company's effective tax rate decreased to 36.8% for the three months ended March 31, 2013 from 39.8% for three months ended March 31, 2012 primarily due to the Company's federal research tax credit and domestic production activities deduction.

On January 2, 2013, the American Taxpayer Relief Act of 2012 (the Act) was enacted into law, which included an extension of the federal research tax credit and other tax credits through December 31, 2013. While Congress approved a retroactive extension of certain business tax provisions that expired at the end of 2011 and 2012, under U.S. GAAP, the financial accounting effects of the Act are to be reported in the first quarter of calendar year 2013, the quarter in which the legislation was enacted. As a result, during the first quarter of 2013, the Company recorded a discrete tax benefit of \$0.8 million for its 2012 federal research tax credit.

As of December 31, 2012 and March 31, 2013, the Company had unrecognized tax benefits of \$4.4 million and \$5.0 million, respectively, of which \$4.1 million and \$4.6 million, respectively, would affect the Company's effective tax rate if recognized.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. During the three months ended March 31, 2012 and 2013, the Company recognized potential interest and penalties of \$51,000 and \$19,000, respectively. As of December 31, 2012 and March 31, 2013, the Company had established reserves of approximately \$194,000 and \$213,000, respectively, for accrued potential interest and penalties related to uncertain tax positions. To the extent interest and penalties are not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision.

The Company files income tax returns in the United States Federal jurisdiction and in many state and foreign jurisdictions. The tax years 2007 through 2011 remain open to examination by the major taxing jurisdictions to which the Company is subject. The IRS has initiated an examination of the Company's 2009 federal income tax return. While the ultimate outcome of the audit is uncertain, management does not currently believe that the outcome will have a material adverse effect on the Company's financial position, results of operations or cash flows.



---

**Table of Contents**

**NEUSTAR, INC.**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

The Company anticipates that total unrecognized tax benefits will decrease by approximately \$121,000 over the next 12 months due to the expiration of certain statutes of limitations and settlement of tax audits.

**12. SEGMENT INFORMATION**

The Company has three operating segments, reflective of the manner in which the chief operating decision maker (CODM) allocates resources and assesses performance: Carrier Services, Enterprise Services, and Information Services. The Company's operating segments are the same as its reportable segments.

The Company's Carrier Services operating segment provides services that ensure the seamless connection of its carrier customers' numerous networks, while also enhancing the capabilities and performance of their customers' infrastructure. The Company enables its carrier customers to use, exchange and share critical resources, such as telephone numbers, to facilitate order management and work flow processing among carriers, and allows operators to manage and optimize the addressing and routing of IP communications.

The Company's Enterprise Services operating segment provides services to its enterprise customers to meet their respective directory-related needs, as well as Internet infrastructure services. The Company is the authoritative provider of essential registry services and manages directories of similar resources, or addresses, that its customers use for reliable, fair and secure access and connectivity. The Company provides a suite of DNS services to its enterprise customers built on a global directory platform. The Company manages a collection of directories that maintain addresses in order to direct, prioritize and manage Internet traffic, and to find and resolve Internet queries and top-level domains. The Company's services monitor and load-test websites to help identify issues and optimize performance. In addition, the Company provides fixed IP geolocation services that help enterprises identify the location of their consumers used in a variety of purposes, including fraud prevention and marketing. Additionally, the Company provides directory services for the 5- and 6-digit number strings used for all U.S. Common Short Codes, which is part of the short messaging service relied upon by the U.S. wireless industry.

The Company's Information Services segment provides a broad portfolio of real-time information and analytics services that enable clients to identify, verify and score their customers and prospective customers, or prospects, to deliver customized responses to a large number of consumer-initiated queries. As an example, the Company provides marketers with the ability to tailor offers made to consumers over the telephone or on the Internet in real time. The Company is one of the largest non-carrier providers of Caller ID services, and provides a comprehensive market analytics platform that enables clients to segment and score customers and prospects for real-time interactive marketing initiatives. Additionally, the Company's business listings identity management service provides local businesses and local search platforms with a single, trusted source of verified business listings for local searches. The Company's online audience solution enables online advertisers to display relevant advertisements to specific audiences, increasing the effectiveness of online advertising and delivering a more useful online experience for consumers using a database and targeting system that protect a consumer's privacy.

The Company reports segment information based on the management approach which relies on the internal performance measures used by the CODM to assess the performance of each operating segment in a given period. In connection with that assessment, the CODM reviews revenues and segment contribution, which excludes certain unallocated costs within the following expense classifications: cost of revenue, sales and marketing, research and development and general and administrative. Depreciation and amortization and restructuring charges are also excluded from segment contribution.

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

Information for the three months ended March 31, 2012 and 2013 regarding the Company's reportable segments was as follows (in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Revenue:</b>		
Carrier Services	\$ 124,373	\$ 132,171
Enterprise Services	39,485	44,779
Information Services	35,724	39,466
<b>Total revenue</b>	<b>\$ 199,582</b>	<b>\$ 216,416</b>
<b>Segment contribution:</b>		
Carrier Services	\$ 108,446	\$ 114,394
Enterprise Services	16,731	20,903
Information Services	18,014	17,768
<b>Total segment contribution</b>	<b>143,191</b>	<b>153,065</b>
<b>Indirect operating expenses:</b>		
Cost of revenue (excluding depreciation and amortization shown separately below)	24,269	25,161
Sales and marketing	5,730	6,835
Research and development	4,860	4,284
General and administrative	20,718	21,292
Depreciation and amortization	22,706	24,665
Restructuring charges	522	2
<b>Income from operations</b>	<b>\$ 64,386</b>	<b>\$ 70,826</b>

Assets are not tracked by segment and the CODM does not evaluate segment performance based on asset utilization.

**Enterprise-Wide Disclosures**

Geographic area revenues and service offering revenues from external customers for the three months ended March 31, 2012 and 2013, and geographic area long-lived assets as of December 31, 2012 and March 31, 2013 are as follows (in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
<b>Revenues by geographical areas:</b>		
North America	\$ 189,348	\$ 205,062
Europe and Middle East	6,293	7,182

Edgar Filing: NEUSTAR INC - Form 10-Q

Other regions	3,941	4,172
Total revenues	\$ 199,582	\$ 216,416

**Table of Contents****NEUSTAR, INC.****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2013**

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2013</b>
Revenues by service offerings:		
Carrier Services:		
Numbering Services	\$ 110,489	\$ 118,140
Order Management Services	10,910	9,802
IP Services	2,974	4,229
<b>Total Carrier Services</b>	<b>124,373</b>	<b>132,171</b>
Enterprise Services:		
Internet Infrastructure Services	21,723	23,797
Registry Services	17,762	20,982
<b>Total Enterprise Services</b>	<b>39,485</b>	<b>44,779</b>
Information Services:		
Identification Services	22,719	22,696
Verification & Analytics Services	8,236	11,361
Local Search & Licensed Data Services	4,769	5,409
<b>Total Information Services</b>	<b>35,724</b>	<b>39,466</b>
<b>Total revenues</b>	<b>\$ 199,582</b>	<b>\$ 216,416</b>

	<b>December 31, 2012</b>	<b>March 31, 2013</b>
Long-lived assets, net		
North America	\$ 406,973	\$ 389,813
Central America	16	13
Europe and Middle East	10	11
Other regions	1	1
<b>Total long-lived assets, net</b>	<b>\$ 407,000</b>	<b>\$ 389,838</b>

---

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
**Forward-Looking Statements**

This quarterly report on Form 10-Q contains forward-looking statements, including, without limitation, statements concerning the conditions in our industry, our operations and economic performance, and our business and growth strategy. In some cases, you can identify forward-looking statements by terminology such as may, will, should, expects, intends, plans, anticipates, believes, estimates, predicts, potential, or the negative of these terms or other comparable terminology. These statements relate to future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ materially from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Many of these risks are beyond our ability to control or predict. These forward-looking statements are based on estimates and assumptions by our management that we believe to be reasonable but are inherently uncertain and subject to a number of risks and uncertainties. These risks and uncertainties include, without limitation, those described in this report, in Part II, Item 1A. Risk Factors and in subsequent filings with the Securities and Exchange Commission. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events or otherwise, except as required by law.

**Overview**

During the first quarter, we continued to experience increased demand for our services. Revenue increased 8% to \$216.4 million as compared to \$199.6 million in the first quarter of 2012. Of this increase, our Carrier Services segment contributed 4%, while our Enterprise Services contributed 2% and Information Services contributed 2%. Within our Carrier Services segment, growth in revenue was driven by a contractual increase of 6.5% in the fixed fee under our contracts to provide number portability services.

In addition to our continued growth in revenue, we improved our financial structure through the refinancing of our 2011 Credit Facilities. Specifically, we issued \$300 million of 4.5% 10-year senior notes and we completed a \$525 million credit facility that included a \$325 million term loan A and a \$200 million revolving credit facility. This refinancing provides us with a lower cost of debt, greater financial flexibility, less restrictive financial covenants and staggered maturities.

During the quarter, we continued to position ourselves to renew our contracts with the North American Portability Management LLC, or NAPM. On April 5, 2013, we submitted our response to the NAPM's Request for Proposal, or the RFP, for the selection of the next local number portability administrator in accordance with the RFP submission requirements and timeline. On April 17, 2013, the NAPM announced on its website that it had extended the deadline for interested parties to respond to its RFP until April 22, 2013. The selection timeline published in the RFP provides for a decision to be made in September 2013; however, the dates provided in the RFP timeline are subject to change. We remain confident in the strength of our response to the NAPM's RFP, and we believe that the high quality of our services provides us the best opportunity to remain the NPAC administrator of local number portability for the communications industry.

**Critical Accounting Policies and Estimates**

The discussion and analysis of our financial condition and results of operations are based on our unaudited consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles, or U.S. GAAP. The preparation of these financial statements in accordance with U.S. GAAP requires us to utilize accounting policies and make certain estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingencies as of the date of the financial statements and the reported amounts of revenue and expense during a fiscal period. The Securities and Exchange Commission, or SEC, considers an accounting policy to be critical if it is important to a company's financial condition and results of operations, and if it requires significant judgment and estimates on the part of management in its application. We have discussed the selection and development of the critical accounting policies with the audit committee of our Board of Directors, and the audit committee has reviewed our related disclosures in this report.

Although we believe that our judgments and estimates are appropriate and reasonable, actual results may differ from those estimates. In addition, while we have used our best estimates based on the facts and circumstances available to us at the time, we reasonably could have used different estimates in the current period. Changes in the accounting estimates we use are reasonably likely to occur from period to period, which may have a material impact on the presentation of our financial condition and results of operations. If actual results or events differ materially from those contemplated by us in making these estimates, our reported financial condition and results of operations could be materially affected. See the information in our filings with the SEC from time to time, including Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2011, for certain matters that may bear on our results of operations.





## **Table of Contents**

The following discussion of selected critical accounting policies supplements the information relating to our critical accounting policies described in Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies and Estimates in our Annual Report on Form 10-K for the year ended December 31, 2012.

### ***Stock-Based Compensation***

We recognize stock-based compensation expense in accordance with the Compensation - Stock Compensation Topic of the FASB ASC which requires the measurement and recognition of compensation expense for stock-based awards granted to employees based on estimated fair values on the date of grant.

See Note 7 to our Unaudited Consolidated Financial Statements in Item 1 of Part I of this report for information regarding our assumptions related to stock-based compensation and the amount of stock-based compensation expense we incurred for the periods covered in this report.

We estimate the fair value of our restricted stock unit awards based on the fair value of our common stock on the date of grant. Our outstanding restricted stock unit awards are subject to service-based vesting conditions and performance-based vesting conditions. We recognize the estimated fair value of service-based awards, net of estimated forfeitures, as stock-based compensation expense over the vesting period on a straight-line basis. Awards with performance-based vesting conditions require the achievement of specific financial targets at the end of the specified performance period and the employee's continued employment over the vesting period. We recognize the estimated fair value of performance-based awards, net of estimated forfeitures, as stock-based compensation expense over the vesting period, which considers each performance period or tranche separately, based upon our determination of whether it is probable that the performance targets will be achieved. At each reporting period, we reassess the probability of achieving the performance targets within the related performance period. Determining whether the performance targets will be achieved involves judgment, and the estimate of stock-based compensation expense may be revised periodically based on changes in the probability of achieving the performance targets. If any performance goals are not met, no compensation cost is ultimately recognized against that goal, and to the extent previously recognized, compensation cost is reversed. As of March 31, 2013, we estimated that the level of achievement of the performance targets for performance vested restricted stock units granted during 2013 was 100%.

**Table of Contents****Consolidated Results of Operations****Three Months Ended March 31, 2012 Compared to Three Months Ended March 31, 2013**

The following table presents an overview of our results of operations for the three months ended March 31, 2012 and 2013:

	Three Months Ended March 31,			
	2012	2013	2012 vs. 2013	
	\$	\$	\$ Change	% Change
(unaudited)				
(dollars in thousands, except per share data)				
<b>Revenue:</b>				
Carrier Services	\$ 124,373	\$ 132,171	\$ 7,798	6.3%
Enterprise Services	39,485	44,779	5,294	13.4%
Information Services	35,724	39,466	3,742	10.5%
<b>Total revenue</b>	<b>199,582</b>	<b>216,416</b>	<b>16,834</b>	<b>8.4%</b>
<b>Operating expense:</b>				
Cost of revenue (excludes depreciation and amortization shown separately below)	44,898	49,297	4,399	9.8%
Sales and marketing	38,353	42,260	3,907	10.2%
Research and development	7,724	7,484	(240)	(3.1)%
General and administrative	20,993	21,882	889	4.2%
Depreciation and amortization	22,706	24,665	1,959	8.6%
Restructuring charges	522	2	(520)	(99.6)%
	135,196	145,590	10,394	7.7%
Income from operations	64,386	70,826	6,440	10.0%
<b>Other (expense) income:</b>				
Interest and other expense	(8,193)	(17,562)	(9,369)	114.4%
Interest and other income	229	141	(88)	(38.4)%
Income before income taxes	56,422	53,405	(3,017)	(5.3)%
Provision for income taxes	22,460	19,641	(2,819)	(12.6)%
Net income	\$ 33,962	\$ 33,764	\$ (198)	(0.6)%
<b>Net income per share:</b>				
Basic	\$ 0.51	\$ 0.51		
Diluted	\$ 0.50	\$ 0.50		
<b>Weighted average common shares outstanding:</b>				
Basic	67,205	66,184		
Diluted	68,478	67,614		

---

**Table of Contents****Revenue**

*Carrier Services.* Revenue from our Carrier Services operating segment increased \$7.8 million due to an increase of \$7.7 million in revenue from Numbering Services, an increase of \$1.3 million in revenue from IP Services, and a decrease of \$1.1 million in revenue from our Order Management Services, or OMS. In particular, the Numbering Services revenue increase was driven by a \$6.7 million increase in the fixed fee established under our contracts to provide NPAC Services.

*Enterprise Services.* Revenue from our Enterprise Services operating segment increased \$5.3 million due to an increase of \$3.2 million in revenue from Registry Services and an increase of \$2.1 million in revenue from Internet Infrastructure Services, or IIS. In particular, the Registry Services revenue increase was driven by continued growth in the number of domain names under management and an increase in transactions in one of our new registries. In addition, IIS revenue increased due to higher demand for our managed domain name systems, or DNS, solutions, to direct and manage Internet traffic.

*Information Services.* Revenue from our Information Services operating segment increased \$3.7 million due to an increase of \$3.1 million in revenue from Verification & Analytics Services and an increase of \$0.6 million in revenue from Local Search & Licensed Data Services. In particular, the Verification & Analytics Services revenue increase was driven by new customers and continued demand for our services that provide customized commercial insights. In addition, Local Search & Licensed Data Services revenue increased due to higher demand for our online local business listing identity management solutions.

**Expense**

*Cost of revenue.* Cost of revenue increased \$4.4 million due to an increase of \$2.6 million in personnel and personnel-related expense and an increase of \$2.4 million in costs related to our information technology and systems. In particular, the increase in personnel and personnel-related expense was due to an increase in stock-based compensation driven by performance-based equity that was granted to a higher number of existing and new employees. In addition, the increase in costs related to our information technology and systems was driven by revenue growth that resulted in increased data processing, telecommunications and maintenance costs.

*Sales and marketing.* Sales and marketing expense increased \$3.9 million due to an increase of \$3.1 million in personnel and personnel-related expense driven by increases in stock-based compensation and salary and benefits. In particular, the increase in stock-based compensation expense was driven by performance-based equity that was granted to a higher number of existing and new employees. The increase in salary and benefits was driven by increased headcount related to the expansion of our sales and marketing teams to support service offerings and the migration of employees to a common benefits plan.

*Research and development.* Research and development expense for the three months ended March 31, 2012 was comparable to the expense for the three months ended March 31, 2013.

*General and administrative.* General and administrative expense increased \$0.9 million due to an increase of \$0.4 million in personnel and personnel-related expense. In particular, stock-based compensation expense increased \$2.0 million driven by performance-based equity that was granted to a higher number of existing and new employees. This increase was partially offset by a decrease of \$1.2 million in severance-related costs.

*Depreciation and amortization.* Depreciation and amortization expense increased \$2.0 million due to an increase of \$2.7 million in depreciation expense related to capitalized software costs. This increase was partially offset by a decrease of \$0.6 million in depreciation expense related to capital leases.

*Restructuring charges.* Restructuring charges for the three months ended March 31, 2012 were comparable to the charges recorded for the three months ended March 31, 2013.

*Interest and other expense.* Interest and other expense increased \$9.4 million due to a \$10.9 million loss on debt modification and extinguishment recorded in connection with the refinancing of our 2011 Credit Facilities. This increase was partially offset by \$2.0 million in lower interest expense driven by the refinancing of our 2011 Credit Facilities.

*Interest and other income.* Interest and other income for the three months ended March 31, 2012 was comparable to the income for the three months ended March 31, 2013.

## Edgar Filing: NEUSTAR INC - Form 10-Q

*Provision for income taxes.* Our effective tax rate decreased to 36.8% for the three months ended March 31, 2013 from 39.8% for the three months ended March 31, 2012 primarily due to our federal research tax credit and domestic production activities deduction. On January 2, 2013, the American Taxpayer Relief Act of 2012, or the Act, was enacted into law, which included an extension of the

**Table of Contents**

federal research tax credit and other tax credits through December 31, 2013. While Congress approved a retroactive extension of certain business tax provisions that expired at the end of 2011 and 2012, under U.S. GAAP, the financial accounting effects of the Act are to be reported in the first quarter of calendar year 2013, the quarter in which the legislation was enacted. As a result, during the first quarter of 2013, we recorded a discrete tax benefit of \$0.8 million for our 2012 federal research tax credit.

**Summary of Operating Segments**

The following table presents a summary of our operating segments revenue, contribution and the reconciliation to income from operations for the three months ended March 31, 2012 and 2013 (in thousands):

	Three Months Ended March 31,			
	2012	2013	2012 vs. 2013	
	\$	\$	\$ Change	% Change
<b>Revenue:</b>				
Carrier Services	\$ 124,373	\$ 132,171	\$ 7,798	6.3%
Enterprise Services	39,485	44,779	5,294	13.4%
Information Services	35,724	39,466	3,742	10.5%
<b>Total revenue</b>	<b>\$ 199,582</b>	<b>\$ 216,416</b>	<b>\$ 16,834</b>	<b>8.4%</b>
<b>Segment contribution:</b>				
Carrier Services	\$ 108,446	\$ 114,394	\$ 5,948	5.5%
Enterprise Services	16,731	20,903	4,172	24.9%
Information Services	18,014	17,768	(246)	(1.4)%
<b>Total segment contribution</b>	<b>143,191</b>	<b>153,065</b>	<b>9,874</b>	<b>6.9%</b>
<b>Indirect operating expenses:</b>				
Cost of revenue (excluding depreciation and amortization shown separately below)	24,269	25,161	892	3.7%
Sales and marketing	5,730	6,835	1,105	19.3%
Research and development	4,860	4,284	(576)	(11.9)%
General and administrative	20,718	21,292	574	2.8%
Depreciation and amortization	22,706	24,665	1,959	8.6%
Restructuring charges	522	2	(520)	(99.6)%
<b>Income from operations</b>	<b>\$ 64,386</b>	<b>\$ 70,826</b>	<b>\$ 6,440</b>	<b>10.0%</b>

Segment contribution is determined based on internal performance measures used by the chief operating decision maker, or CODM, to assess the performance of each operating segment in a given period. In connection with this assessment, the CODM reviews revenue and segment contribution, which excludes certain unallocated costs within the following expense classifications: cost of revenue, sales and marketing, research and development and general and administrative. Depreciation and amortization and restructuring charges are also excluded from the segment contribution.

The following is a discussion of our operating segment results for the three months ended March 31, 2012 and 2013:

*Carrier Services.* Revenue from our Carrier Services operating segment increased \$7.8 million due to an increase of \$7.7 million in revenue from Numbering Services, an increase of \$1.3 million in revenue from IP Services, and a decrease of \$1.1 million in revenue from our OMS. In particular, the Numbering Services revenue increase was driven by a \$6.7 million increase in the fixed fee established under our contracts to provide NPAC Services. Segment operating costs for Carrier Services totaled \$17.8 million, an increase of \$1.9 million. This increase was due to an increase in information technology and systems costs driven by revenue growth that resulted in increased data processing, telecommunications and maintenance costs. Carrier Services segment revenue less its segment operating costs resulted in a segment contribution of \$114.4 million, an increase of \$5.9 million.

## Edgar Filing: NEUSTAR INC - Form 10-Q

*Enterprise Services.* Revenue from our Enterprise Services operating segment increased \$5.3 million due to an increase of \$3.2 million in revenue from Registry Services and an increase of \$2.1 million in revenue from IIS. In particular, the Registry Services revenue increase was driven by continued growth in the number of domain names under management and an increase in transactions in one of our new registries. In addition, IIS revenue increased due to higher demand for our DNS solutions to direct and manage Internet traffic. Segment operating costs for Enterprise Services totaled \$23.9 million, an increase of \$1.1 million. This increase in segment operating costs was due to an increase of \$0.8 million in advertising and external marketing costs. Enterprise Services segment revenue less its segment operating costs resulted in a segment contribution of \$20.9 million, an increase of \$4.2 million.

## **Table of Contents**

*Information Services.* Revenue from our Information Services operating segment increased \$3.7 million due to an increase of \$3.1 million in revenue from Verification & Analytics Services and an increase of \$0.6 million in revenue from Local Search & Licensed Data Services. In particular, the Verification & Analytics Services revenue increase was driven by new customers and continued demand for our services that provide customized commercial insights. In addition, Local Search & Licensed Data Services revenue increased due to higher demand for our online local business listing identity management solutions. Segment operating costs for Information Services totaled \$21.7 million, an increase of \$4.0 million. This increase in segment operating costs was due to an increase of \$2.9 million in personnel and personnel-related expense and an increase of \$0.5 million in information technology and systems costs. Information Services segment revenue less its segment operating costs resulted in a segment contribution of \$17.8 million, a decrease of \$0.2 million.

## **Liquidity and Capital Resources**

Our principal source of liquidity is cash provided by operating activities. Our principal uses of cash have been to fund share repurchases, capital expenditures, and debt service requirements. We anticipate that our principal uses of cash in the future will be for share repurchases, capital expenditures, debt service requirements and acquisitions.

Total cash, cash equivalents and investments were \$378.2 million at March 31, 2013, an increase of \$34.3 million from \$343.9 million at December 31, 2012. This increase in cash, cash equivalents and investments was primarily due to cash provided by operations.

We believe that our existing cash and cash equivalents, short-term investments, and cash from operations will be sufficient to fund our operations for the next twelve months.

## ***Credit Facilities***

On January 22, 2013, we entered into a credit facility that provided for a \$325 million senior secured term loan facility, or 2013 Term Facility, and a \$200 million senior secured revolving credit facility, or the 2013 Revolving Facility, and together with the 2013 Term Facility, the 2013 Credit Facilities. In addition, we closed an offering of \$300 million aggregate principal amount of senior notes, or Senior Notes. We used the proceeds received from the 2013 Term Facility and Senior Notes to repay our outstanding principal borrowings of \$592.5 million under our existing 2011 Term Facility. We used available borrowings under the new 2013 Revolving Facility for outstanding letters of credit totaling \$7.8 million that were previously secured by our 2011 Revolving Facility. Our 2011 Term Facility and 2011 Revolving Facility were terminated in connection with this refinancing event. For further discussion of this debt refinancing, see Note 6 to our Consolidated Financial Statements in Item 1 of Part I of this report.

### ***2013 Credit Facilities***

The 2013 Credit Facilities include: (1) the 2013 Term Facility; (2) the 2013 Revolving Facility, of which (a) \$100 million is available for the issuance of letters of credit and (b) \$25 million is available as a swingline subfacility; and (3) incremental term loan facilities in an amount such that after giving effect to the incurrence of any such incremental loans, either (a) the aggregate amount of incremental loans does not exceed \$400 million or (b) the Consolidated Secured Leverage Ratio on a pro forma basis after giving effect to any such increase would not exceed 2.50 to 1.00. The 2013 Revolving Facility and 2013 Term Facility mature on January 22, 2018. As of March 31, 2013, the Company had not borrowed any amounts under the 2013 Revolving Facility and available borrowings were \$192.2 million, exclusive of outstanding letters of credit totaling \$7.8 million.

Principal payments under the 2013 Term Facility of \$2.0 million are due on the last day of the quarter beginning on March 31, 2013 and ending on December 31, 2017. The remaining 2013 Term Facility principal balance of \$284.4 million is due in full on January 22, 2018, subject to early mandatory prepayments.

The loans outstanding under the 2013 Credit Facilities (Loans) bear interest, at our option, either: (1) at the base rate, which is defined as the highest of (a) the federal funds rate plus 0.50%, (b) the interest rate published by the Wall Street Journal from time to time as the U.S. Prime Rate and (c) the adjusted LIBOR rate for a one-month interest period beginning on such day plus 1.00%; or (2) at the LIBOR rate plus, in each case, an applicable margin. The applicable margin is (1) if the Consolidated Leverage Ratio is less than 2.00:1.00, 0.50% per annum for borrowings based on the base rate and 1.50% per annum for borrowings based on the LIBOR rate, or (2) if the Consolidated Leverage Ratio is 2.00:1.00 or greater, 0.75% per annum for borrowings based on the base rate and 1.75% per annum borrowings based on the LIBOR rate. The accrued interest under the 2013 Term Facility is payable quarterly beginning on March 31, 2013. As of March 31, 2013, accrued interest under the 2013 Credit Facilities was \$0.2 million.





---

**Table of Contents**

The Company may voluntarily prepay the Loans at any time in minimum amounts of \$1 million or an integral multiple of \$500,000 in excess thereof. The 2013 Credit Facilities provide for mandatory prepayments with the net cash proceeds of certain debt issuances, insurance receipts, and dispositions. The 2013 Term Facility also contains certain events of default, upon the occurrence of which, and so long as such event of default is continuing, the amounts outstanding may, at the option of the required Lenders, accrue interest at an increased rate and payments of such outstanding amounts could be accelerated, or other remedies undertaken pursuant to the 2013 Term Facility, by the required Lenders.

As of March 31, 2013, deferred financing costs and loan origination fees related to the 2013 Credit Facilities was \$10.0 million. Total amortization expense of the deferred financing costs and loan origination fees was \$0.4 million for the three months ended March 31, 2013 and was reported as interest expense in the consolidated statements of operations.

*Senior Notes*

On January 22, 2013, we closed an offering of \$300 million aggregate principal amount of 4.50% senior notes due 2023 to qualified institutional buyers pursuant to Rule 144A, and outside of the United States pursuant to Regulation S, under the Securities Act of 1933, as amended, or the Securities Act. The Senior Notes were issued pursuant to an indenture, dated as of January 22, 2013, among us, certain of our domestic subsidiaries, or the Subsidiary Guarantors, and The Bank of New York Mellon Trust Company, N.A., as trustee, or the Indenture. The Senior Notes are the general unsecured senior obligations of us and are guaranteed on a senior unsecured basis by the Subsidiary Guarantors.

Interest is payable on the Senior Notes semi-annually in arrears at an annual rate of 4.50%, on January 15 and July 15 of each year, beginning on July 15, 2013. The Senior Notes will mature on January 15, 2023. Interest accrues from January 22, 2013. As of March 31, 2013, accrued interest under the Senior Notes was \$2.6 million.

At any time and from time to time prior to July 15, 2016, we may redeem up to a maximum of 35% of the original aggregate principal amount of the Senior Notes with the proceeds of certain equity offerings, at a redemption price equal to 104.50% of the principal amount thereof, plus accrued and unpaid interest thereon, if any, to the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date); provided that: (1) at least 65% of the original aggregate principal amount of the Senior Notes remains outstanding; and (2) the redemption occurs within 90 days of the completion of such equity offering upon not less than 30 nor more than 60 days prior notice.

Prior to January 15, 2018, we may redeem some or all of the Senior Notes by paying a make-whole premium based on U.S. Treasury rates. During the 12-month period commencing on January 15 of the relevant year listed below, we may redeem some or all of the Senior Notes at the prices listed below, plus accrued and unpaid interest, if any, to, but not including, the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date): 2018 at a redemption price of 102.25%; 2019 at a redemption price of 101.50%; 2020 at a redemption price of 100.75%; and 2021 and thereafter at a redemption price of 100.00%. If we experience certain changes of control together with a ratings downgrade, we will be required to offer to purchase all of the Senior Notes then outstanding at a purchase price equal to 101.00% of the principal amount thereof, plus accrued and unpaid interest, if any, to, the date of purchase. If we sell certain assets and do not repay certain debt or reinvest the proceeds of such sales within certain time periods, we will be required to offer to repurchase the Senior Notes with such proceeds at 100.00% of their principal amount, plus accrued and unpaid interest, if any, to, the date of purchase.

The Senior Notes contain customary events of default, including among other things, payment default, failure to provide certain notices and certain provision related to bankruptcy events. The Senior Notes also contain customary negative covenants.

On January 22, 2013, we entered into a registration rights agreement relating to the Senior Notes that requires us and the Subsidiary Guarantors to, among other things: (1) file a registration statement with respect to a registered offer to exchange the Senior Notes for new notes guaranteed by our Subsidiary Guarantors, with terms substantially identical in all material respects to those of the Senior Notes (except that the new notes will not be subject to restrictions on transfer or to any increase in annual interest rate); (2) use our reasonable best efforts to cause the applicable registration statement to become effective under the Securities Act; and (3) promptly after the applicable registration statement is declared effective, initiate an exchange offer. In addition, under certain circumstances, we and the Subsidiary Guarantors may be required to file a shelf registration statement relating to resales of the Senior Notes.

If (1) the exchange offer is not completed within 300 days after the date of original issuance of the Senior Notes; (2) a shelf registration statement, if required, has not become effective within 300 days after the date of original issuance of the Senior Notes; (3) if we receive a request to file a shelf registration pursuant to the Registration Rights Agreement and such shelf registration statement has not become effective by the later of (a) 300 days after the date of original issuance of the Senior Notes and (b) 120 days after delivery of such shelf request or (4) any required registration statement is filed and declared effective but thereafter ceases to be



---

## **Table of Contents**

effective in certain circumstances during the applicable period (each such event referred to in clauses (1) through (4) above, a Registration Default ), then we will be obligated to pay additional interest to each holder of the Senior Notes that are subject to transfer restrictions, with respect to the first 90-day period immediately following the occurrence of a Registration Default, at a rate of 0.25% per annum on the principal amount of the Senior Notes that are subject to transfer restrictions held by such holder. The amount of additional interest will increase by an additional 0.25% per annum with respect to each subsequent 90-day period until the Registration Default ends, up to a maximum increase of 1.00% per annum on the principal amount of the Senior Notes that are subject to transfer restrictions.

As of March 31, 2013, deferred financing costs related to the Senior Notes was \$15.2 million. Total amortization expense of the deferred financing costs was \$0.2 million for the three months ended March 31, 2013 and is reported as interest expense in the consolidated statements of operations.

### **Discussion of Cash Flows**

#### *Cash flows from operations*

Net cash provided by operating activities for the three months ended March 31, 2013 was \$51.8 million, as compared to \$60.0 million for the three months ended March 31, 2012. This \$8.2 million decrease in net cash provided by operating activities was the result of an increase in non-cash adjustments of \$20.4 million, partially offset by a decrease in net changes in operating assets and liabilities of \$28.3 million.

Non-cash adjustments increased \$20.4 million driven by a loss on debt modification and extinguishment of \$10.9 million recorded in the first quarter of 2013 related to our debt refinancing, an increase of \$5.1 million in stock-based compensation, and an increase of \$3.3 million in excess tax benefits from stock option exercises.

Net changes in operating assets and liabilities decreased \$28.3 million primarily due to a decrease of \$28.0 million in income taxes receivable, a decrease of \$12.4 million in prepaid expenses and other current assets, and a decrease of \$9.0 million in deferred revenue. These increases in net changes in operating assets and liabilities were partially offset by an increase of \$9.4 million in income taxes payable, an increase of \$5.0 million in other liabilities and an increase of \$4.5 million in accounts payable and accrued expenses.

#### *Cash flows from investing*

Net cash used in investing activities for the three months ended March 31, 2013 was \$11.4 million, as compared to \$8.2 million for three months ended March 31, 2012. This \$3.2 million increase in net cash used in investing activities was due to an increase of \$3.8 million in cash used for purchases of property and equipment, partially offset by an increase of \$0.6 million in cash received from sales and maturities of investments.

#### *Cash flows from financing*

Net cash used in financing activities was \$4.0 million for the three months ended March 31, 2013, as compared to net cash provided by financing activities of \$3.5 million for the three months ended March 31, 2012. This \$7.5 million decrease in net cash provided by financing activities was primarily due to a decrease of \$25.8 million in proceeds from the exercise of stock options, cash used of \$11.4 million for debt issuance costs attributable to our debt refinancing completed in the first quarter of 2012, and a decrease of \$3.3 million in excess tax benefits from stock-based compensation. These decreases were partially offset by a net proceeds of \$31.7 million attributable to our debt refinancing and a decrease of \$2.5 million in cash used for the repurchase of restricted stock awards attributable to participants electing to use stock to satisfy their tax withholdings.

### **Recent Accounting Pronouncements**

See Note 2 to our Unaudited Consolidated Financial Statements in Item 1 of Part 1 of this report for a discussion of the effects of recent accounting pronouncements.

### **Off-Balance Sheet Arrangements**

None.



## **Table of Contents**

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

For quantitative and qualitative disclosures about our market risk, see **Quantitative and Qualitative Disclosures About Market Risk** in Item 7A of Part II of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012. Our exposure to market risk has not changed materially since December 31, 2012.

### **Item 4. Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of March 31, 2013, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective and were operating at the reasonable assurance level.

In addition, there were no changes in our internal control over financial reporting that occurred in the first quarter of 2013 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **PART II OTHER INFORMATION**

### **Item 1. Legal Proceedings**

From time to time, we are subject to claims in legal proceedings arising in the normal course of our business. We do not believe that we are party to any pending legal action that could reasonably be expected to have a material adverse effect on our business or operating results.

### **Item 1A. Risk Factors**

In addition to the other information set forth in this Quarterly Report, you should carefully consider the risks discussed in Part I, Item 1A. **Risk Factors** in our Annual Report on Form 10-K for our fiscal year ended December 31, 2012, filed with the SEC on February 28, 2013. The risks discussed in our Annual Report on Form 10-K could materially affect our business, financial condition and future results. The risks described in our Annual Report on Form 10-K are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business, financial condition or operating results.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table is a summary of our repurchases of common stock during each of the three months in the quarter ended March 31, 2013:

Month	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)(3)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (3)(4)
January 1 through January 31, 2013	385,822	\$ 43.44	270,600	\$ 75,393,794
February 1 through February 28, 2013	57,678	44.46	28,800	74,128,987
March 1 through March 31, 2013	252,718	45.01	251,405	62,813,726
Total	696,218	\$ 44.10	550,805	\$ 62,813,726

- (1) The number of shares purchased includes shares of common stock tendered by employees to us to satisfy the employees' tax withholding obligations arising as a result of vesting of restricted stock grants under our stock incentive plan. We purchased these shares for their fair market value on the vesting date.
- (2) The difference between the total number of shares purchased and the total number of shares purchased as part of publicly announced plans or programs is 145,413 shares, all of which relate to shares surrendered to us by employees to satisfy the employees' tax withholding obligations arising as a result of vesting of restricted stock grants under our incentive stock plans.
- (3) On July 28, 2010, we announced the adoption of a share repurchase program. The program authorizes the repurchase of up to \$300 million of Class A common shares through Rule 10b5-1 programs, open market purchases, privately negotiated transactions or otherwise as market conditions warrant, at prices we deem appropriate. The program will expire in July 2013.
- (4) Does not include amounts paid for commissions.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.

**Table of Contents**

**Item 6. Exhibits**

See exhibits listed under the Exhibit Index below.

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**NeuStar, Inc.**

Date: May 2, 2013

By: /s/ Paul S. Lalljie  
Paul S. Lalljie  
Chief Financial Officer  
(Principal Financial and Accounting Officer and Duly Authorized  
Officer)



**Table of Contents**

EXHIBIT INDEX

Exhibit No.	Description
3.1	Restated Certificate of Incorporation, incorporated herein by reference to Exhibit 3.1 to Amendment No. 7 to NeuStar's Registration Statement on Form S-1, filed June 28, 2005 (File No. 333-123635).
3.2	Amended and Restated Bylaws, incorporated herein by reference to Exhibit 3.2 to our Current Report on Form 8-K, filed June 25, 2012.
10.1.2	Amendment to the contractor services agreement entered into the 7 <sup>th</sup> day of November 1997 by and between Neustar, Inc. and North American Portability Management, LLC.
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation
101.DEF	XBRL Taxonomy Extension Definition
101.LAB	XBRL Taxonomy Extension Label
101.PRE	XBRL Taxonomy Extension Presentation