

VIAD CORP  
Form 10-Q  
November 03, 2006

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q**

(Mark one)

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

For the quarterly period ended **September 30, 2006**

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: 001-11015**

**VIAD CORP**

(Exact name of registrant as specified in its charter)

**Delaware**

**36-1169950**

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

**1850 North Central Avenue, Suite 800  
Phoenix, Arizona**

**85004-4545**

(Address of principal executive offices)

(Zip Code)

**(602) 207-4000**

(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

As of September 30, 2006, 21,628,232 shares of common stock (\$1.50 par value) were outstanding.

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**VIAD CORP**  
**CONSOLIDATED BALANCE SHEETS**  
(Unaudited)

	<b>September 30, 2006</b>	<b>December 31, 2005</b>
	<b>(in thousands, except share data)</b>	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 197,225	\$ 152,601
Accounts receivable, net of allowance for doubtful accounts of \$1,648 and \$1,400, respectively	59,964	56,752
Inventories	39,302	37,853
Deferred income taxes	21,567	28,155
Other current assets	9,235	7,348
<b>Total current assets</b>	<b>327,293</b>	<b>282,709</b>
Property and equipment, net	134,805	143,038
Other investments and assets	26,774	28,504
Deferred income taxes	35,772	40,891
Goodwill	186,535	184,310
Other intangible assets, net	6,071	6,238
<b>Total Assets</b>	<b>\$ 717,250</b>	<b>\$ 685,690</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 45,923	\$ 35,150
Other current liabilities	104,396	131,498
Current portion of long-term debt and capital lease obligations	2,044	3,263
<b>Total current liabilities</b>	<b>152,363</b>	<b>169,911</b>
Long-term debt and capital lease obligations	13,301	14,089
Pension and other postretirement benefits	28,702	28,428
Other deferred items and insurance liabilities	69,540	71,589
Commitments and contingencies (Note 14)		
Minority interest	5,344	4,704
Common stock and other equity:		
Common stock, \$1.50 par value, 200,000,000 shares authorized, 24,934,981 shares issued	37,402	37,402
Additional capital	636,717	653,883
Retained earnings (deficit)	22,731	(40,199)
Unearned employee benefits and other	(14,107)	(17,409)
Accumulated other comprehensive income (loss):		
Unrealized gain on investments	478	456
Unrealized gain on derivative financial instruments	2	38

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Cumulative foreign currency translation adjustments	29,935	23,576
Minimum pension liability adjustment	(5,548)	(5,548)
Common stock in treasury, at cost, 3,306,749 and 2,500,927 shares, respectively	(259,610)	(255,230)
Total common stock and other equity	448,000	396,969
<b>Total Liabilities and Stockholders Equity</b>	<b>\$ 717,250</b>	<b>\$ 685,690</b>

See Notes to Consolidated Financial Statements.

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**VIAD CORP**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(Unaudited)**

	<b>Three months ended</b>		<b>Nine months ended September</b>	
	<b>September 30,</b>		<b>30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
	<b>(in thousands, except per share data)</b>			
<b>Revenues:</b>				
Convention show services	\$ 143,342	\$ 110,671	\$ 500,515	\$ 453,635
Exhibit design and construction	40,348	36,199	128,260	146,954
Travel and recreation services	46,858	44,267	72,952	67,091
<b>Total revenues</b>	<b>230,548</b>	<b>191,137</b>	<b>701,727</b>	<b>667,680</b>
<b>Costs and expenses:</b>				
Costs of services	159,161	134,672	500,891	455,821
Costs of products sold	43,758	40,099	129,698	150,437
Corporate activities and minority interest	4,243	4,103	9,295	9,869
Gains on sale of corporate assets			(3,468)	
Restructuring charges (recoveries)	355	(230)	(215)	(593)
Impairment losses (recoveries)	193	843	(650)	843
Net interest income	(1,614)	(348)	(4,572)	(760)
<b>Total costs and expenses</b>	<b>206,096</b>	<b>179,139</b>	<b>630,979</b>	<b>615,617</b>
<b>Income before income taxes</b>	<b>24,452</b>	<b>11,998</b>	<b>70,748</b>	<b>52,063</b>
Income tax expense	2,429	2,627	16,385	19,181
<b>Income from continuing operations</b>	<b>22,023</b>	<b>9,371</b>	<b>54,363</b>	<b>32,882</b>
Income from discontinued operations	1,496	1,328	11,026	1,160
<b>Net income</b>	<b>\$ 23,519</b>	<b>\$ 10,699</b>	<b>\$ 65,389</b>	<b>\$ 34,042</b>
<b>Diluted income per common share</b>				
Income from continuing operations	\$ 1.03	\$ 0.42	\$ 2.49	\$ 1.48
Income from discontinued operations	0.07	0.06	0.50	0.05
<b>Net income</b>	<b>\$ 1.10</b>	<b>\$ 0.48</b>	<b>\$ 2.99</b>	<b>\$ 1.53</b>
<b>Average outstanding and potentially dilutive common shares</b>	<b>21,424</b>	<b>22,345</b>	<b>21,850</b>	<b>22,211</b>
<b>Basic income per common share</b>				

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Income from continuing operations	\$ 1.04	\$ 0.42	\$ 2.54	\$ 1.50
Income from discontinued operations	0.07	0.06	0.51	0.05
<b>Net income</b>	<b>\$ 1.11</b>	<b>\$ 0.48</b>	<b>\$ 3.05</b>	<b>\$ 1.55</b>
Average outstanding common shares	21,121	22,135	21,456	22,028
Dividends declared per common share	\$ 0.04	\$ 0.04	\$ 0.12	\$ 0.12

See Notes to Consolidated Financial Statements.

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**VIAD CORP**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**(Unaudited)**

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
	(in thousands)			
<b>Net income</b>	\$ 23,519	\$ 10,699	\$ 65,389	\$ 34,042
Other comprehensive income (loss):				
Unrealized gains (losses) on investments:				
Holding gains (losses) arising during the period, net of tax	22	15	22	(21)
Unrealized losses on derivative financial instruments:				
Holding losses arising during the period, net of tax	(59)		(36)	
Unrealized foreign currency translation gains (losses)	(117)	6,661	6,359	3,722
Other comprehensive income (loss)	(154)	6,676	6,345	3,701
Comprehensive income	\$ 23,365	\$ 17,375	\$ 71,734	\$ 37,743

See Notes to Consolidated Financial Statements.

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**VIAD CORP**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

	<b>Nine months ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
	<b>(in thousands)</b>	
<b>Cash flows from operating activities:</b>		
Net income	\$ 65,389	\$ 34,042
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	15,044	16,988
Deferred income taxes	1,477	9,682
Income from discontinued operations	(11,026)	(1,160)
Restructuring recoveries	(215)	(593)
Impairment losses	600	843
Gains on dispositions of property and other assets	(3,478)	(61)
Share-based compensation expense	7,072	5,564
Tax benefits from share-based compensation arrangements	7,446	707
Excess tax benefits from share-based compensation arrangements	(4,340)	
Other non-cash items, net	3,531	3,422
Change in operating assets and liabilities:		
Receivables	(4,509)	(21,814)
Inventories	(1,449)	(739)
Accounts payable	13,843	11,246
Restructuring liability	(1,168)	(2,058)
Other assets and liabilities, net	(12,636)	(21,710)
Net cash provided by operating activities	75,581	34,359
<b>Cash flows from investing activities:</b>		
Capital expenditures	(14,695)	(13,921)
Proceeds from dispositions of property and other assets	13,872	8,661
Net cash used in investing activities	(823)	(5,260)
<b>Cash flows from financing activities:</b>		
Payments on debt and capital lease obligations	(2,941)	(3,870)
Dividends paid on common stock	(2,603)	(2,649)
Common stock purchased for treasury	(34,413)	
Debt issuance costs	(488)	
Excess tax benefits from share-based compensation arrangements	4,340	
Proceeds from exercise of stock options	5,028	5,202
Net cash used in financing activities	(31,077)	(1,317)

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Effect of exchange rate changes on cash and cash equivalents	943	822
Net increase in cash and cash equivalents	44,624	28,604
Cash and cash equivalents, beginning of year	152,601	115,050
<b>Cash and cash equivalents, end of period</b>	<b>\$ 197,225</b>	<b>\$ 143,654</b>

**Supplemental disclosure of cash flow information**

Cash paid during the period for:

Income taxes	\$ 11,359	\$ 19,806
Interest	\$ 879	\$ 1,380
Equipment acquired under capital leases	\$ 815	\$ 183

See Notes to Consolidated Financial Statements.

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**VIAD CORP**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**Note 1. Basis of Preparation and Principles of Consolidation**

The accompanying unaudited consolidated financial statements of Viad Corp ( Viad or the Company ) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

For further information, refer to the consolidated financial statements and related footnotes for the year ended December 31, 2005, included in the Company's Form 10-K (File No. 001-11015), filed with the Securities and Exchange Commission ( SEC ) on March 1, 2006.

The consolidated financial statements include the accounts of Viad and all of its subsidiaries. All significant intercompany account balances and transactions between Viad and its subsidiaries have been eliminated in consolidation. Viad's reporting segments consist of: GES Exposition Services, Inc. ( GES ), Exhibitgroup/Giltspur ( Exhibitgroup ) and Travel and Recreation Services.

**Note 2. Share-Based Compensation**

Viad grants share-based compensation awards pursuant to the Viad Corp Omnibus Incentive Plan (the Omnibus Plan ), which was adopted by Viad's stockholders in 1997. The Omnibus Plan provides for the following types of awards to officers, directors and certain key employees: (a) incentive and non-qualified stock options; (b) restricted stock; (c) performance-based awards; and (d) stock appreciation rights. The number of shares of common stock available for grant under the Omnibus Plan in each calendar year is limited to two percent of the total number of shares of common stock outstanding as of the first day of each year, provided that any shares available for grant in a particular year which are not, in fact, granted in that year will be added to the shares available for grant in any subsequent year. Viad issues shares related to its share-based compensation awards from its Employee Equity Trust and from shares held in treasury. Viad has the authority to repurchase common stock for the purpose of replacing shares issued upon exercise of stock options and in connection with other stock compensation plans. There were no repurchases of common stock under this program during the nine months ended September 30, 2006 or 2005.

In December 2004, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 123 (revised 2004), Share-Based Payment, which requires that compensation cost related to all share-based payment arrangements, including employee stock options, be recognized in the financial statements based on the fair value method of accounting. In addition, SFAS No. 123(R) requires that excess tax benefits related to share-based payment arrangements be classified as cash inflows from financing activities and cash outflows from operating activities. SFAS No. 123(R) is a revision of SFAS No. 123, Accounting for Stock-Based Compensation, and supercedes Accounting Principles Board ( APB ) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations.

As originally permitted by SFAS No. 123, Viad had previously elected to apply the guidance in APB Opinion No. 25, which allowed companies to use the intrinsic value method of accounting to measure the value of share-based payment transactions with employees. Based on this method, Viad had not previously recognized the compensation cost related to employee stock options in the consolidated financial statements as the stock options granted had an exercise price equal to the fair market value of the underlying common stock on the date of grant. Effective January 1, 2006, Viad adopted the provisions of SFAS No. 123(R) using the modified prospective application method. Accordingly, prior period amounts have not been restated. Under the modified prospective application method, the compensation cost related to the unvested portion of all awards (including stock options) granted prior to the adoption of SFAS No. 123(R) and all new awards are recognized in the consolidated financial statements over the requisite service period based on the fair value of the awards.

Total share-based compensation expense recognized in the consolidated financial statements during the three months ended September 30, 2006 and 2005, was \$3.0 million and \$1.7 million, respectively, and \$7.1 million and \$5.6 million, during the nine months ended September 30, 2006 and 2005, respectively. Furthermore, the total tax benefits related to such costs were \$1.2 million and \$675,000 for the three months ended September 30, 2006 and 2005, respectively, and \$2.8 million and \$2.2 million for the nine months ended September 30, 2006 and 2005, respectively. No share-based compensation costs were capitalized during the nine months ended September 30, 2006 or 2005.

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During the three and nine months ended September 30, 2006, the adoption of SFAS No. 123(R) resulted in incremental share-based compensation expense (and a reduction of income before income taxes) of \$264,000 and \$800,000, respectively. As a result of this incremental expense, net income was reduced by \$160,000 and \$560,000, respectively. Diluted and basic income per share were each reduced by \$0.03 per share for the nine months ended September 30, 2006. Also in connection with the adoption of SFAS No. 123(R), Viad presented \$4.3 million of excess tax benefits from share-based compensation arrangements as a cash outflow from operating activities and a cash inflow from financing activities during the nine months ended September 30, 2006.

As noted above, prior to the adoption of SFAS No. 123(R), Viad used the intrinsic value method of accounting prescribed by APB Opinion No. 25. Assuming Viad had recognized compensation cost during the three and nine months ended September 30, 2005 related to all share-based compensation awards (including stock options) in accordance with the fair value method of accounting under SFAS No. 123, net income and diluted and basic income per share would have been as presented below. Compensation cost calculated under SFAS No. 123 is recognized over the vesting period and is net of estimated forfeitures and tax effects. The forfeiture rate assumption is based on the Company's historical average forfeiture rate.

	<b>Three months ended September 30, 2005 (in thousands, except per share data)</b>	<b>Nine months ended</b>
Net income, as reported	\$ 10,699	\$ 34,042
Less: share-based compensation expense determined under fair value based method, net of tax	(420)	(1,151)
Pro forma net income	\$ 10,279	\$ 32,891
Diluted income per share:		
As reported	\$ 0.48	\$ 1.53
Pro forma	\$ 0.46	\$ 1.49
Basic income per share:		
As reported	\$ 0.48	\$ 1.55
Pro forma	\$ 0.47	\$ 1.50

For purposes of applying SFAS No. 123(R) (and SFAS No. 123 where applicable), the fair value of each stock option grant was estimated on the date of grant using the Black-Scholes option pricing model for the nine months ended September 30 with the following assumptions:

	<b>2006</b>	<b>2005</b>
Estimated fair value of stock options granted	\$9.29	\$7.57
Expected dividend yield	0.5%	0.6%
Expected volatility	24.3%	26.3%
Expected life	5 years	5 years
Risk-free interest rate	4.57%	3.89%

The expected dividend yield was based on Viad's expectation of future dividend payouts. The volatility assumption was based on Viad's daily historical stock price volatility during the time period that corresponds to the expected weighted-average life of the option. The expected life (estimated period of time outstanding) of stock options granted was estimated based on historical exercise activity. The risk-free interest rate assumption was based on the interest rate of a U.S. Treasury strip for a five-year term from the date the option was granted.

Stock options granted during the nine months ended September 30, 2006 and 2005 were for contractual terms of seven years at exercise prices based on the fair market value of Viad's common stock on the grant date. Stock options become exercisable, based on a graded vesting schedule, in annual increments of 20 percent beginning one year after grant date and become fully exercisable after five years from the date of grant. Stock options granted since 1998 contain certain forfeiture and non-compete provisions. Share-based compensation expense related to stock option awards is recognized on the straight-line method over the requisite service period, which is approximately five years. As of September 30, 2006, the total unrecognized cost related to non-vested stock option awards was \$2.6 million. Viad expects to recognize such costs in the consolidated financial statements over a weighted-average period of approximately 1.9 years.

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Viad's stock options generally contain contingent cash settlement features upon a change of control of the Company as defined in the Omnibus Plan. Management believes this cash settlement event is not considered probable, and therefore, the outstanding stock options are accounted for as equity awards and not considered liability awards under SFAS No. 123(R) and related guidance. Although not considered probable, the cash settlement contingency is deemed to be outside the control of Viad. Accordingly, Viad's stock options are subject to the provisions of SEC Accounting Series Release No. 268, Presentation in Financial Statements of Redeemable Preferred Stocks and Emerging Issues Task Force Issue No. D-98, Classification and Measurement of Redeemable Securities. This guidance generally specifies that when the redemption of instruments (within its scope) is outside the control of the issuer, certain amounts should be classified outside of permanent equity on the balance sheet. As of September 30, 2006, Viad has not recorded any amounts related to stock options outside of permanent equity as there was no intrinsic value (in-the-money redemption amount) related to Viad's stock options on the date of grant. As noted above, the exercise price of Viad's stock option grants is based on the fair market value of the underlying common stock on the date of grant.

The following table summarizes stock option activity during the nine months ended September 30, 2006:

	<b>Shares</b>	<b>Weighted-Average Exercise Price</b>	<b>Options Exercisable</b>
Options outstanding at January 1, 2006	1,109,770	\$ 23.55	745,732
Granted	21,700	31.92	
Exercised	(179,518)	21.99	
Forfeited	(84,848)	22.53	
Options outstanding at September 30, 2006	867,104	24.18	628,274

The following table summarizes information concerning stock options outstanding and exercisable as of September 30, 2006:

<b>Range of Exercise Prices</b>	<b>Options Outstanding</b>			<b>Options Exercisable</b>	
	<b>Shares</b>	<b>Weighted-Average Remaining Contractual Life</b>	<b>Weighted-Average Exercise Price</b>	<b>Shares</b>	<b>Weighted-Average Exercise Price</b>
\$17.51 to \$23.32	187,178	5.0 years	\$ 19.21	187,178	\$ 19.21
\$23.32 to \$24.05	213,023	3.6 years	23.76	213,023	23.76
\$24.22 to \$26.07	190,579	4.9 years	25.18	135,022	25.57
\$26.31 to \$26.37	164,500	5.4 years	26.31	31,220	26.31
\$26.47 to \$31.92	111,824	4.2 years	28.46	61,831	27.88
\$17.51 to \$31.92	867,104	4.6 years	24.18	628,274	23.33

In addition to the above, Viad had stock options outstanding which were granted to employees of MoneyGram International, Inc. ( MoneyGram ) prior to the spin-off of that company as described in Note 15. As of September 30, 2006, there were 103,594 of such options outstanding and 71,530 exercisable, both with exercise prices ranging from \$17.51 to \$28.15. The weighted-average remaining contractual life of these options outstanding was approximately 4.7 years. During the nine months ended September 30, 2006, a total of 60,191 options were exercised by MoneyGram employees at exercise prices ranging from \$13.24 to \$28.15.

The aggregate intrinsic value related to stock options outstanding as of September 30, 2006 was \$9.7 million. The aggregate intrinsic value is based on the weighted-average exercise price and Viad's closing stock price of \$35.41 as of September 30, 2006. The total intrinsic value of stock option awards exercised during the nine months ended September 30, 2006 and 2005 was \$5.8 million and \$4.2 million, respectively. The fair value of stock options that vested during the nine months ended September 30, 2006 and 2005 was \$2.0 million and \$1.7 million, respectively. During the nine months ended September 30, 2006 and 2005, Viad received cash proceeds from the exercise of stock options of \$5.0 million and \$5.2 million, respectively. The actual tax benefits realized for the tax deductions related to the exercise of stock options and vesting of restricted stock and performance-based awards was \$7.4 million and \$707,000 for the nine months ended September 30, 2006 and 2005, respectively.

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Restricted stock awards of 182,000 and 103,300 shares were granted during the nine months ended September 30, 2006 and 2005, respectively, at weighted-average grant date fair values (based on the fair market value on the date of grant) of \$32.80 and \$26.30, respectively. The fair value of restricted stock that vested during the nine months ended September 30, 2006 and 2005 was \$759,000 and \$873,000, respectively. All restricted stock awards vest three years from the date of grant. Share-based compensation expense related to restricted stock awards is recognized on the straight-line method over the requisite service period, which is approximately three years. As of September 30, 2006, the total unrecognized costs related to non-vested restricted stock awards granted was \$5.8 million. Viad expects to recognize such costs in the consolidated financial statements over a weighted-average period of approximately 1.4 years.

During the nine months ended September 30, 2006 and 2005, Viad also granted performance-based restricted stock ( PBRS ) awards of 58,200 and 81,800 shares, respectively, at weighted-average grant date fair values (based on the fair market value on the date of grant) of \$32.60 and \$26.31, respectively. The fair value of PBRS that vested during the nine months ended September 30, 2006 and 2005 was \$1.2 million and \$558,000, respectively. PBRS vests when certain incentive performance targets established in the year of grant are achieved at target levels. PBRS awards are subject to a graded vesting schedule whereby one third of the earned shares vest after the first year, an additional one third after two years and the balance after three years from the date of grant. Share-based compensation expense related to PBRS awards is recognized based on an accelerated multiple-award approach over the requisite service period, which is approximately three years. As of September 30, 2006, the total unrecognized costs related to non-vested PBRS awards granted was \$1.4 million. Viad expects to recognize such costs in the consolidated financial statements over a weighted-average period of approximately one year.

Certain performance-driven restricted stock ( PDRS ) awards granted in 2002 and 2001 vested during the nine months ended September 30, 2006 and 2005 based on achievement of certain long-term incentive performance targets. The fair value of PDRS that vested during the nine months ended September 30, 2006 and 2005 was \$313,000 and \$1.4 million, respectively.

Future vesting of restricted stock and PBRS is generally subject to continued employment with Viad or its subsidiaries. Holders of restricted stock and PBRS have the right to receive dividends and vote the shares, but may not sell, assign, transfer, pledge or otherwise encumber the stock, except to the extent restrictions have lapsed. The following table summarizes restricted stock, PBRS and PDRS activity during the nine months ended September 30, 2006:

<b>Restricted Stock</b>	<b>PBRS</b>	<b>PDRS</b>
-------------------------	-------------	-------------