lululemon athletica inc.
Form 8-K
June 09, 2015

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

FORM 8-K

CURRENT REPORT
Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934
June 9, 2015
Date of Report (Date of earliest event reported)

lululemon athletica inc.
(Exact name of registrant as specified in its charter)

Delaware	001-33608	20-3842867
(State or other jurisdiction of incorporation)	(Commission File Number)	(IRS Employer Identification No.)

1818 Cornwall Avenue
Vancouver, British Columbia
Canada, V6J 1C7
(Address of principal executive offices, including Zip Code)
Registrant’s telephone number, including area code: (604) 732-6124

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
o Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 2.02. Results of Operations and Financial Condition.

On June 9, 2015, lululemon athletica inc. (the "Company") issued a press release announcing its financial results for the first quarter ended May 3, 2015 and certain other information. A copy of the Company's press release is attached hereto as Exhibit 99.1 and is incorporated herein by reference. As previously announced, the Company has scheduled a conference call for 9:00 a.m. Eastern time on June 9, 2015 to discuss financial results.

Item 9.01. Financial Statements and Exhibits.

(d) Exhibits.

Exhibit No.	Description
99.1	Press release entitled "lululemon athletica inc. Announces First Quarter Fiscal 2015 Results," issued on June 9, 2015.

SIGNATURES

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

lululemon athletica inc.

Dated: June 8, 2015

/s/ STUART HASELDEN
Stuart Haselden
Chief Financial Officer

EXHIBIT INDEX

Exhibit No.	Description
99.1	Press release entitled "lululemon athletica inc. Announces First Quarter Fiscal 2015 Results," issued on June 9, 2015.

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9,283

In thousands	Six Months Ended June 30, 2015		2014	
Operating revenues				
Customer Interaction	$	218,490	$	246,055
Trillium Software		25,028		26,982
Total operating revenues	$	243,518	$	273,037
Operating income				
Customer Interaction	$	6,569	$	11,142
Trillium Software		7,580		6,344
Corporate		(3,077)		(1,920)
Total operating income	$	11,072	$	15,566
Income from operations before income taxes	$	11,072	$	15,566
Interest Expense		2,124		1,437
Interest Income		(47)		(129)
Loss on Sale		9,501		
Other, Net		1,110		1,809
Total income (loss) from operations before income taxes	$	(1,616)	$	12,449

Note M Acquisition and Disposition

On March 16, 2015, we completed the acquisition of 3Q Digital. The results of 3Q Digital s operations have been included in our consolidated financial statements since that date and are reported in the Customer Interaction segment. At the time of the acquisition, (i) each outstanding vested share of 3Q Digital capital stock was converted into the right to receive a portion of the merger consideration (including the right to receive a portion of the earnout consideration, if any), (ii) each outstanding unvested share of 3Q capital stock was cancelled, (iii) outstanding vested stock options were converted into the right to receive a portion of the merger consideration (including the right to receive a portion of the defined earnout consideration, if any) (net of the exercise price of such options) and (iv) unvested stock options were cancelled. The initial purchase price was $30.2 million in cash. In addition, the purchase price

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includes a contingent consideration arrangement that requires us to pay the former owners of 3Q Digital an additional cash payment depending on achievement of certain revenue growth goals. The potential undiscounted amount of all future payments that could be required to be paid under the contingent consideration arrangement is between $0 and $35.0 million in cash in 2017.

The intangible assets include customer relationships, trade names and non-compete agreements.

The following table summarizes the consideration paid and the preliminary amounts of estimated fair value of the assets acquired and liabilities assumed at the acquisition date.

(in thousands)		
Cash consideration per purchase agreement	$	30,245
Estimated fair value of contingent consideration		17,940
Fair value of total consideration transferred	$	48,185

(in thousands)		
Recognized amounts of tangible assets and liabiities:		
Current assets	$	4,135
Property and equipment		164
Other assets		389
Current liabilities		(822)
Other liabilities		
Total tangible assets and liabilities:		3,866
Identifiable intangible assets		4,773
Goodwill (including deferrred tax adjustment of $2,298)		41,844
Total	$	50,483

The fair value of the tangible net assets, identifiable intangible assets and goodwill is $48.2 million. The acquired intangible assets, which are being amortized, are as follows: customer relationships of $4.3 million (amortized over seven years), trade names and trademarks of $0.3 million (amortized over two years) and non-compete agreements of $0.2 million (amortized over three years).

A reconciliation of the beginning and ending accrued balances of the earnout consideration using significant unobservable inputs (Level 3) for the six months ended June 30, 2015 follows:

(in thousands)		**Fair Value**
Contingent consideration at acquisition date	$	17,940
Accretion of interest		861
Accrued earnout liability as of June 30, 2015	$	18,801

The purchase price has been preliminarily allocated based on the estimated fair values of assets described above and are subject to achievement of revenue goals. Future purchase price adjustments are possible in future quarters based upon further evaluation and analysis.

On April 14, 2015, Harte Hanks sold its B2B research business. The B2B research business represented less than 5% of our total 2014 revenues. As a result of the sale, the Company recognized a pre-tax loss of $9.5 million in relation to the disposal or transfer of assets and liabilities to the purchasing organization. The related asset group does not meet the criteria to be classified as a component of an entity. As such, the related loss on sale is included in income from continuing operations before income taxes in the income statement in Other Expenses. The assets included both goodwill and intangible assets (see Note D above). Future expenses are possible in future quarter based upon certain working capital settlement provisions.

Note that in conjunction with the purchase agreement, Harte Hanks may continue to provide services to the B2B research business beyond the duration of the transition services agreement. Such services will conducted under a services agreement that is negotiated at arm s length. The payables and receivables that may result are not anticipated to be material to Harte Hanks.

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Note N Subsequent Event

On July 9, 2015, Harte Hanks announced that Douglas C. Shepard would succeed Robert A. Philpott as its (interim) President and Chief Executive Officer, effective immediately. Mr. Philpott resigned as President and Chief Executive Officer and from the Company s board of directors, effective July 7, 2015. In connection with his resignation, Harte Hanks agreed to provide Mr. Philpott severance benefits as though he had been terminated without Cause under the terms of his Employment Agreement with the Company of July 1, 2013. Related to this transition, we expect to incur a post-tax severance charge of approximately $2.0 million to $2.5 million.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Cautionary Note Regarding Forward-Looking Statements

This report, including this Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A), contains forward-looking statements within the meaning of the federal securities laws. All such statements are qualified by this cautionary note, which is provided pursuant to the safe harbor provisions of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements may also be included in our other public filings, press releases, our website and oral and written presentations by management. Statements other than historical facts are forward-looking and may be identified by words such as may, will, expects, believes, anticipates, plans, estimates, seeks intends, or words of similar meaning. Examples include statements regarding (1) our strategies and initiatives related thereto (2) adjustments to our cost structure and other actions designed to respond to market conditions and improve our performance, and the anticipated effectiveness and expenses associated with these actions, (3) our financial outlook for revenues, earnings per share, operating income, expense related to equity-based compensation, capital resources, and other financial items, (4) expectations for our businesses and for the industries in which we operate, including the impact of economic conditions of the markets we serve on the marketing expenditures and activities of our clients and prospects, (5) competitive factors, (6) acquisition and development plans, (7) expectations for and effects of acquired and disposed businesses, (8) our stock repurchase program, (9) expectations regarding legal proceedings and other contingent liabilities, and (10) other statements regarding future events, conditions, or outcomes.

These forward-looking statements are based on current information, expectations, and estimates and involve risks, uncertainties, assumptions, and other factors that are difficult to predict and that could cause actual results to vary materially from what is expressed in or indicated by the forward-looking statements. In that event, our business, financial condition, results of operations, or liquidity could be materially adversely affected and investors in our securities could lose part or all of their investments. Some of these risks, uncertainties, assumptions, and other factors can be found in our filings with the Securities and Exchange Commission, including the factors discussed under Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2014 and in the Cautionary Note Regarding Forward-Looking Statements in our second quarter 2015 earnings release issued on June 30, 2015. The forward-looking statements included in this report and those included in our other public filings, press releases, our website, and oral and written presentations by management are made only as of the respective dates thereof, and we undertake no obligation to update publicly any forward-looking statement in this report or in other documents, our website, or oral statements for any reason, even if new information becomes available or other events occur in the future.

Overview

The following MD&A section is intended to help the reader understand the results of operations and financial condition of Harte Hanks, Inc. This section is provided as a supplement to, and should be read in conjunction with, our financial statements and the accompanying notes to the financial statements contained elsewhere in this report and our MD&A section, financial statements and accompanying notes to financial statements in our 2014 Form 10-K. Our 2014 Form 10-K contains a discussion of other matters not included herein, such as disclosures regarding critical accounting policies and estimates, and contractual obligations.

Harte Hanks partners with clients to deliver relevant, connected and quality customer interactions. Our approach starts with discovery and learning, which leads to customer journey mapping, creative and content development, analytics and data

management, and ends with execution and support in a variety of digital and traditional channels. We do something powerful: we produce engaging and memorable customer interactions to drive business results for our clients, which is why Harte Hanks is famous for developing better customer relationships and experiences and defining interaction-led marketing.

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Our Customer Interaction services offer a wide variety of integrated, multi-channel, data-driven solutions for top brands around the globe. We help our clients gain insight into their customers behaviors from their data and use that insight to create innovative multi-channel marketing programs to deliver a return on marketing investment. We believe our clients success is determined not only by how good their tools are, but how well we help them use the tools to gain insight and analyze their consumers. This results in a strong and enduring relationship between our clients and their customers. We offer a full complement of capabilities and resources to provide a broad range of marketing services, in media from direct mail to email, including:

- agency and digital services;
- database marketing solutions and business-to-business lead generation;
- direct mail; and
- contact centers.

Revenues from the Customer Interaction segment represented approximately 90% of our total revenues for both the three months and six months ended June 30, 2015 and 2014, respectively.

Trillium Software is a leading enterprise data quality solutions provider. Our data quality specialists help organizations achieve increased business from their data management initiatives and existing business-critical processes by providing enterprise data profiling and data cleansing software and services. Trillium Software offers industry-specific business solutions that help solve data problems experienced by financial services, banking, retail, healthcare, manufacturing, and risk professionals. Our full complement of technologies and services include global data profiling, data cleansing, enrichment, and data linking for e-business, Big Data, customer relationship management, data governance, enterprise resource planning, supply chain management, data warehouse, and other enterprise applications. Revenues from the Trillium Software segment are comprised primarily of perpetual software licenses, annual maintenance, and professional services, and represented approximately 10% of our total revenues for both the three months and six months ended June 30, 2015 and 2014, respectively.

We derive revenues by providing Customer Interaction services and Trillium Software licensing sales and services.

General corporate expense consists primarily of pension and worker s compensation expense related to employees of business operations we no longer own.

We are affected by the general, national and international economic and business conditions in the markets where we and our customers operate. Marketing budgets are often discretionary in nature, and are easier to reduce in the short-term than other expenses in response to weak economic conditions. Our revenues are also affected by the economic fundamentals of each industry that we serve, various market factors, including the demand for services by our clients, and the financial condition of and budgets available to specific clients, among other factors. We remain committed to making the investments necessary to execute our multichannel strategy while also continuing to adjust our cost structure to reduce costs in the parts of the business that are not growing as fast. We believe these actions will improve our profitability in future periods.

Our principal operating expense items are labor, outsourced costs, and mail supply chain management.

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Results of Operations

Operating results were as follows:

In thousands, except per share amounts	Three Months Ended June 30, 2015	2014	% Change	Six Months Ended June 30, 2015	2014	% Change
Revenues	$ 122,345	$ 140,310	-12.8%	$ 243,518	$ 273,037	-10.8%
Operating expenses	114,288	129,323	-11.6%	232,446	257,471	-9.7%
Operating income	$ 8,057	$ 10,987	-26.7%	$ 11,072	$ 15,566	-28.9%
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Income (loss) before taxes	$ (4,430)	$ 9,283	-147.7%	$ (1,616)	$ 12,449	-113.0%
Diluted EPS from operations	$ (0.07)	$ 0.09	-177.8%	$ (0.04)	$ 0.12	-133.3%

2nd Quarter 2015 vs. 2nd Quarter 2014

Revenues

Consolidated revenues decreased $18.0 million, or 12.8%, in the second quarter of 2015 compared to the second quarter of 2014. These results reflect the impact of our automobile and consumer brands, technology, and retail verticals decreasing $4.7 million, or 18.7%, $7.1 million, or 21.0%, and $4.5 million, or 13.4%, respectively. This is primarily due to lost clients, clients reducing their marketing spends, and the sale of our B2B research business. In addition, our select markets vertical decreased by $3.6 million, or 20.1%, over the prior year second quarter due to a large non-recurring contact center project in the second quarter of 2014. Revenue from our healthcare services vertical increased $0.5 million, or 5.1%, principally from contact center support for a new pharmaceutical client. Revenue from our financial services vertical increased $1.4 million, or 6.9%, due to the addition of a new client using our solutions for analytics, database, creative, and mail services.

Revenues from our vertical markets are impacted by, among other things, the economic fundamentals of each industry, various market factors, including the demand for services by our clients, and the financial condition of and budgets available to specific clients.

Operating Expenses

Overall operating expenses were $114.3 million in the second quarter of 2015, compared to $129.3 million in the second quarter of 2014. Labor costs decreased $7.2 million, or 10.3%, compared to the second quarter of 2014 primarily due to reduced management labor from headcount reductions and severance expense in the second quarter of 2014. Production and distribution expenses decreased $6.8 million, or 16.0%, over the prior year quarter primarily due to a decrease in outsourced services and job production expense. General and administrative expense decreased $1.1 million, or 7.7%, compared to the prior year primarily due

professional fees related to rebranding and formation of our strategy which occurred in 2014. Depreciation and intangible asset and software amortization expense remained flat to the first quarter of 2014.

Our largest cost components are labor, outsourced costs and mail supply chain costs. Each of these costs are somewhat variable and tend to fluctuate with revenue and the demand for our services. Mail supply chain rates have increased over the last few years due to demand and supply issues within the transportation industry. Future changes in mail supply chain rates will continue to impact our total production costs and total operating expenses and may have an impact on future demand for our supply chain management.

Postage costs of mailings are borne by our clients and are not directly reflected in our revenues or expenses.

First Half 2015 vs. First Half 2014

Revenues

Consolidated revenues decreased $29.5 million, or 10.8%, in the first half of 2015 compared to the first half of 2014. These results reflect the impact of our automobile and consumer brands, technology, and retail verticals decreasing $9.0 million, or 18.4%, $6.4 million, or 10.2%, and $9.6 million, or 14.3%, respectively compared to

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the first half of 2014. This is primarily due to lost clients, clients reducing their marketing spends, and the sale of our B2B research business. In addition, our select markets vertical decreased $6.0 million, or 19.2%, from the first half of the prior year due to a large non-recurring contact center project in the second quarter of 2014. Revenue from our healthcare services vertical increased $0.3 million, or 1.5%, principally from contact center support for a new pharmaceutical client. Revenue from our financial services vertical increased $1.2 million, or 3.2%, due to the addition of a new client using our solutions for analytics, database, creative, and mail services.

Revenues from our vertical markets are impacted by, among other things, the economic fundamentals of each industry, various market factors, including the demand for services by our clients, and the financial condition of and budgets available to specific clients.

Operating Expenses

Overall operating expenses were $232.4 million in the first half of 2015, compared to $257.5 million in the first half of 2014. Labor costs decreased $13.8 million, or 9.8%, compared to the first half of 2014 primarily due to reduced management labor from headcount reductions and severance expense in the first half od 2014. Production and distribution expenses decreased $11.1 million, or 13.4%, over the prior year quarter primarily due to a decrease in outsourced services and job production expense. General and administrative expense increased $0.3 million, or 1.2%, compared to the prior year primarily due to transaction related legal fees and professional services. Depreciation and intangible asset and software amortization expense remained flat to the first half of 2014.

Our largest cost components are labor, outsourced costs and mail supply chain costs. Each of these costs is somewhat variable and tends to fluctuate with revenues and the demand for our services. Mail supply chain rates have increased over the last few years due to demand and supply issues within the transportation industry. Future changes in mail supply chain rates will continue to impact our total production costs and total operating expenses, and may have an impact on future demand for our supply chain management.

Customer Interaction

Customer Interaction operating results were as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
In thousands	**2015**	**2014**	**% Change**	**2015**	**2014**	**% Change**
Revenues	$ 109,175	$ 127,321	-14.3%	$ 218,490	$ 246,055	-11.2%
Operating expenses	104,133	118,129	-11.8%	211,921	234,913	-9.8%
Operating income	$ 5,042	$ 9,192	-45.1%	$ 6,569	$ 11,142	-41.0%

2nd Quarter 2015 vs. 2nd Quarter 2014

Revenues

Customer Interaction revenues decreased $18.1 million, or 14.3%, in the second quarter of 2015 compared to the second quarter of 2014. These results reflect the impact of our automobile and consumer brands, technology, and retail verticals decreasing $4.2 million, or 19.2%, $7.9 million, or 25.6%, and $4.6 million, or 14.1%, respectively. This is primarily due to lost clients, clients reducing their marketing spends, and the sale of the Aberdeen Group and Market Intelligence. In addition, our select markets vertical decreased by $3.6 million, or 22.1%, over the prior year second quarter due to a large non-recurring contact center project in the second quarter of 2014. Revenue from our healthcare services vertical increased $0.7 million, or 6.9%, principally from contact center support for a new pharmaceutical client. Revenue from our financial services vertical increased $1.5 million, or 9.8%, due to the addition of a new client using our solutions for analytics, database, creative, and mail services.

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Revenues from our vertical markets are impacted by, among other things, the economic fundamentals of each industry, various market factors, including the demand for services by our clients, and the financial condition of and budgets available to specific clients.

Future revenue performance will depend on, among other factors, the overall strength of the national and international economies and how successful we are at maintaining and growing business with existing clients organically and through acquisition, acquiring new clients and meeting client demands. We believe that, in the long-term, an increasing portion of overall marketing and advertising expenditures will be moved from other advertising media to the targeted media space, and that our business will benefit as a result. Targeted media advertising results can be more effectively tracked, enabling measurement of the return on marketing investment.

Operating Expenses

Customer Interaction operating expenses decreased $14.0 million, or 11.8%, in the second quarter of 2015 compared to the second quarter of 2014. Labor costs decreased $6.3 million, or 10.2%, compared to the second quarter of 2014, primarily due to a decrease in management labor from headcount reductions and severance expense in the second quarter of 2014. Production costs decreased $6.6 million, or 15.9%, compared to the second quarter of 2014 primarily due to decreased outsourced production costs. In addition, general and administrative expense decreased $1.0 million, or 9.0%. Depreciation and intangible asset and software amortization expense remained flat.

Customer Interaction s largest cost components are labor, outsourced costs and mail supply chain costs. Each of these costs is somewhat variable and tends to fluctuate with revenues and the demand for our services. Mail supply chain rates have increased over the last few years due to demand and supply issues within the transportation industry. Future changes in mail supply chain rates will continue to impact our total production costs and total operating expenses, and may have an impact on future demand for our supply chain management.

First Half 2015 vs. First Half 2014

Revenues

Customer Interaction revenues decreased $27.6 million, or 11.2%, in the first half of 2015 compared to the first half of 2014. These results reflect the impact of our automobile and consumer brands, technology, and retail verticals decreasing $7.2 million, or 17.2%, $7.1 million, or 12.4%, and $9.8 million, or 14.9%, respectively compared to the first half of 2014. This is primarily due to lost clients, clients reducing their marketing spends, and the sale of our B2B research business. In addition, our select markets vertical decreased $5.7 million, or 20.2%, from the first half of the prior year due to a large non-recurring contact center project in the first half of 2014. Revenue from our healthcare services vertical increased $0.5 million, or 2.5%, principally from contact center support for a new pharmaceutical client. Revenue from our financial services vertical increased $1.6 million, or 5.1%, due to

the addition of a new client using our solutions for analytics, database, creative, and mail services.

Revenues from our vertical markets are impacted by, among other things, the economic fundamentals of each industry, various market factors, including the demand for services by our clients, and the financial condition of and budgets available to specific clients.

Operating Expenses

Customer Interaction operating expenses decreased $23.0 million, or 9.8%, in the first half of 2015 compared to the first half of 2014. Labor costs decreased $12.3 million, or 9.8%, compared to the first half of 2014, primarily due to decreased management labor from headcount reductions. Production and distribution costs decreased $10.8 million, or 13.3%, compared to the first half of 2014 primarily due to decreased outsourced services and job production expense. In addition, depreciation and intangible asset and software amortization expense decreased $0.4 million, or 5.9%. The decreases in operating expenses are offset by an increase in general and administrative expense of $0.5 million, or 2.4%.

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Customer Interaction s largest cost components are labor, outsourced costs and mail supply chain costs. Each of these costs is somewhat variable and tends to fluctuate with revenues and the demand for our services. Mail supply chain rates have increased over the last few years due to demand and supply issues within the transportation industry. Future changes in mail supply chain rates will continue to impact our total production costs and total operating expenses, and may have an impact on future demand for our supply chain management.

Trillium Software

Trillium Software operating results were as follows:

	Three Months Ended June 30,					Six Months Ended June 30,				
In thousands		**2015**		**2014**	**% Change**		**2015**		**2014**	**% Change**
Revenues	$	13,170	$	12,989	1.4%	$	25,028	$	26,982	-7.2%
Operating expenses		8,603		10,240	-16.0%		17,448		20,638	-15.5%
Operating income	$	4,567	$	2,749	66.1%	$	7,580	$	6,344	19.5%

2nd Quarter 2015 vs. 2nd Quarter 2014

Revenues

Trillium Software revenues increased $0.2 million, or 1.4%, in the second quarter of 2015 compared to the second quarter of 2014. These results reflect a non-recurring software license event and is offset by a decline in maintenance and professional service fees.

Operating Expenses

Trillium Software operating expenses decreased $1.6 million, or 16.0%, in the second quarter of 2015 compared to the second quarter of 2014. This is primarily due to decreased management labor from headcount reductions and severance expense in the second quarter of 2014.

Trillium Software s largest cost component is software development, which is comprised primarily of labor.

First Half 2015 vs. First Half 2014

Revenues

Trillium Software revenues decreased $2.0 million, or 7.2%, in the first half of 2015 compared to the first half of 2014. This decrease is primarily a result of decreased software license revenues.

Operating Expenses

Trillium Software, operating expenses decreased $3.2 million, or 15.5%, in the first half of 2015 compared to the first half of 2014. This decrease is primarily due to decreased management labor from headcount reductions and severance expense in the first half of 2014.

Corporate

2nd Quarter 2015 vs 2nd Quarter 2014

General corporate expense increased $0.6 million, or 62.7%, in the second quarter of 2015 compared to the second quarter of 2014. This is primarily due to an increase in pension expense compared to the prior year relating to the adoption of the 2014 generational mortality tables and changes in discount rate.

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First Half 2015 vs. First Half 2014

General corporate expense increased $1.2 million, or 60.3%, in the first half of 2015 compared to the first half of 2014. This is primarily due to an increase in pension expense compared to the prior year relating to the adoption of the 2014 generational mortality tables and changes in discount rate.

Interest Expense

2nd Quarter 2015 vs. 2nd Quarter 2014

Interest expense increased $0.8 million, or 133.4%, in the second quarter of 2015 compared to the second quarter of 2014. This was due to the interest accretion of $0.9 for the earnout liability related to the purchase of 3Q Digital. This was offset slightly by a lower average debt balance in the second quarter of 2015. The lower average debt balance in the second quarter of 2015 is a result of scheduled quarterly principal payments on the 2011 Term Loan Facility. See discussion of our credit facilities in the Liquidity and Capital Resources section below.

First Half 2015 vs. First Half 2014

Interest expense increased $0.8 million, or 58.8%, in the first half of 2015 compared to the first half of 2014. This was due to the interest accretion of $0.9 million for the earnout liability related to the purchase of 3Q Digital. This was offset slightly by a lower average debt balance in the second quarter of 2015. The lower average debt balance in the second quarter of 2015 is a result of scheduled quarterly principal payments on the 2011 Term Loan Facility. See discussion of our credit facilities in the Liquidity and Capital Resources section below.

Other Income and Expense

2nd Quarter 2015 vs. 2nd Quarter 2014

Other expense, net, was $1.5 million in the second quarter of 2015 compared to $1.1 million in the second quarter of 2014. This $0.4 million variance from the prior year quarter is primarily due to a $1.3 million foreign currency transaction loss in the second quarter of 2015 versus a $0.8 million foreign currency transaction loss during the prior year quarter.

First Half 2015 vs. First Half 2014

Other expense, net, was $1.1 million in the first half of 2015 compared to $1.8 million in the first half of 2014. This $0.7 million variance from the prior year quarter is due to a $0.7 million change in net foreign currency transaction losses.

On April 14, 2015, the Company entered into an agreement to sell its B2B research business. The B2B research business represented less than 5% of the Company s total 2014 revenues. As a result of the sale, the Company recognized a pre-tax loss of $9.5 million in relation to the disposal or transfer of assets and liabilities to the purchasing organization. The related asset group does not meet the criteria to be classified as a component of an entity. As such, the related loss on sale is included in income from continuing operations before income taxes in the income statement in Other Expenses in the statements of comprehensive income for both the three months and six month ended June 30, 2015.

Income Taxes

2nd Quarter 2015 vs. 2nd Quarter 2014

Income tax expense decreased $3.9 million in the second quarter of 2015 compared to the second quarter of 2014. Our effective tax rate was 5.7% for the second quarter of 2015, decreasing from 39.3% for the second quarter of 2014. Excluding the tax impact of the loss on sale and discrete items related to state and local enacted tax legislation, our second quarter tax rate would have been 41.0%. The increase in the adjusted effective tax rate relates to the impact of nondeductible interest associated with the 3Q earn out.

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First Half 2015 vs. First Half 2014

Income tax expense was $0.9 million in the first half of 2015 compared to $5.0 million in the first half of 2014. The $4.1 million decrease is primarily a result of the change in operating performance coupled with the tax benefit calculated on the loss on sale. Our negative effective tax rate was 58.3% for the first half of 2015, decreasing from 39.9% for the first half of 2014. Excluding the tax benefit on the loss on sale and the impact of other discrete items, our effective tax rate for the first half of 2015 would have been 39.6%.

Income/Earnings Per Share

2nd Quarter 2015 vs. 2nd Quarter 2014

We recorded net loss of $4.2 million and diluted loss per share of $0.07 in the second quarter of 2015. These results compare to net income of $5.6 million and diluted earnings per share of $0.09 per share in the second quarter of 2014. The decrease in net income is primarily a result of the sale of our B2B research business, a decrease in revenues and the change in other income and expense discussed above.

First Half 2015 vs. First Half 2014

We recorded net loss of $2.6 million and diluted loss per share of $0.04. These results compare to net income of $7.5 million and diluted earnings per share from continuing operations of $0.12 per share in the first half of 2014.

Economic Climate and Impact on our Financial Statements

We cannot predict the impact on our business performance of the economic climate in the U.S. and other economies in which we operate, nor can we predict the impact of the economic climate in the industry in which we operate. Economic downturns and turmoil severely affect the marketing services industry. A deep or enduring economic recession in the U.S. or other markets we or our clients serve could have a material adverse effect on our business, financial position, or operating results.

Liquidity and Capital Resources

Sources and Uses of Cash

As of June 30, 2015, cash and cash equivalents were $31.2 million, decreasing $25.5 million from cash and cash equivalents of $56.7 million at December 31, 2014. This net decrease was a result of net cash provided by operating activities of $27.0 million, net cash used in investing activities of $30.0 million, net cash used in financing activities of $22.5 million and the negative effect of exchange rate changes of $0.1 million.

Operating Activities

Net cash provided by operating activities for the six months ended June 30, 2015 was $27.0 million, compared to $11.8 million for the six months ended June 30, 2014. The $15.2 million year-over-year increase was primarily attributable to changes in working capital.

For the six months ended June 30, 2015, our principal working capital changes, which directly affected net cash provided by operating activities, were as follows:

- A decrease in accounts receivable of $19.6 million attributable to collection of the December 31, 2014 receivables as well as higher revenues in the second quarter of 2014 compared to the second quarter of 2015.

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Investing Activities

Net cash used in investing activities was $30.0 million for the six months ended June 30, 2015, compared to net cash used in investing activities of $4.8 million for the six months ended June 30, 2014. The $25.2 million variance is primarily the result of the acquisition of 3Q Digital using cash of $30.2 million in March of 2015. This is offset by the sale of the B2B research business, generating cash of $5.0 million in April of 2015.

Financing Activities

Net cash used in financing activities was $22.5 million for the six months ended June 30, 2015 compared to $19.4 million for the six months ended June 30, 2014. The $3.1 million increase is primarily due to the scheduled increase in repayments of borrowings.

Foreign Holdings of Cash

Foreign holdings of cash as of June 30, 2015 and 2014 were $14.6 million and $12.8 million, respectively. The Company would need to accrue and pay taxes if repatriated; however, the Company does not intend to repatriate funds subject to tax.

Credit Facilities

On August 16, 2011, we entered into a five-year $122.5 million term loan facility (2011 Term Loan Facility) with Bank of America, N.A., as Administrative Agent. The 2011 Term Loan Facility matures on August 16, 2016. For each borrowing under the 2011 Term Loan Facility, we can generally choose to have the interest rate for that borrowing calculated based on either (i) the LIBOR rate (as defined in the 2011 Term Loan Facility) for the applicable interest period, plus a spread (ranging from 2.00% to 2.75% per annum) based on our total net funded debt-to-EBITDA ratio (as defined in the 2011 Term Loan Facility) then in effect; or (ii) the highest of (a) the Agent s prime rate, (b) the BBA daily floating rate LIBOR, as determined by Agent for such date, plus 1.00%, and (c) the Federal Funds Rate plus 0.50%, plus a spread (ranging from 1.00% to 1.75% per annum) based on our total net funded debt-to-EBITDA ratio then in effect. We may elect to prepay the 2011 Term Loan Facility at any time without incurring any prepayment penalties. At June 30, 2015, we had $73.5 million outstanding under the 2011 Term Loan Facility.

On August 8, 2013, we entered into a three-year $80.0 million revolving credit facility, a $25.0 million letter of credit sub-facility and a $5.0 million swing line loan sub-facility (2013 Revolving Credit Facility) by amending and restating our 2010 Revolving Credit Facility agreements. The 2013 Revolving Credit Facility permits us to request up to a $15.0 million increase in the total amount of the facility, and matures on August 16, 2016. For each borrowing under the 2013 Revolving Credit Facility, we can generally choose to have the interest rate for that borrowing calculated on either (i) the Eurodollar rate for the applicable interest period plus a spread which is determined based on our total net debt-to-EBITDA ratio then in effect, which ranges from 2.25% to 3.00% per annum; or (ii) the highest of (a) the Agent s prime rate, (b) the Federal Funds Rate plus 0.50% per annum, (c) Eurodollar rate plus 1.00% per annum, plus a spread which is determined based on our total debt-to-EBITDA ratio then in effect, which spread ranges

from 1.25% to 2.00% per annum. We are also required to pay a quarterly commitment fee under the 2013 Revolving Credit Facility. The rate of which is applied to the amount equal to the difference of the total commitment amount under the 2013 Revolving Credit Facility less the aggregate amount of outstanding obligations under such facility. The commitment fee rate ranges from 0.50% to 0.55% per annum, depending on our total net debt-to-EBITDA ratio then in effect. In addition, we pay a letter of credit fee with respect to outstanding letters of credit. That fee is calculated by applying a rate equal to the spread applicable to Eurodollar based loans plus a fronting fee of 0.125% per annum to the average daily undrawn amount of the outstanding letters of credit. We may elect to prepay the 2013 Revolving Credit Facility at any time without incurring any prepayment penalties.

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Under all of our credit facilities we are required to maintain an interest coverage ratio of not less than 2.75 to 1 and a total debt-to-EBITDA ratio of not more than 2.25 to 1. The credit facilities also contain customary covenants restricting our and our subsidiaries ability to:

- authorize distributions, dividends, stock redemptions, and repurchases if a payment event of default has occurred and is continuing;
- enter into certain merger or liquidation transactions;
- grant liens;
- enter into certain sale and leaseback transactions;
- have foreign subsidiaries account for more than 25% of the consolidated revenue, or 20% of the assets of Harte Hanks and its subsidiaries, in the aggregate;
- enter into certain transactions with affiliates; and
- allow the total indebtedness of Harte Hanks subsidiaries to exceed $20.0 million.

The credit facilities each also include customary covenants regarding reporting obligations, delivery of notices regarding certain events, maintaining our corporate existence, payment of obligations, maintenance of our properties and insurance thereon at customary levels with financially sound and reputable insurance companies, maintaining books and records, and compliance with applicable laws. The credit facilities each also provide for customary events of default including nonpayment of principal or interest, breach of representations and warranties, violations of covenants, failure to pay certain other indebtedness, bankruptcy and material judgments and liabilities, certain violations of environmental laws or ERISA or the occurrence of a change of control. Our material domestic subsidiaries have guaranteed the performance of Harte Hanks under our credit facilities. As of June 30, 2015, we were in compliance with all of the covenants of our credit facilities.

Outlook

We consider such factors as total cash and cash equivalents, current assets, current liabilities, total debt, revenues, operating income, cash flows from operations, investing activities, and financing activities when assessing our liquidity. Our primary sources of liquidity have been cash and cash equivalents on hand and cash generated from operating activities. Our management of cash is designed to optimize returns on cash balances and to ensure that it is readily available to meet our operating, investing, and financing requirements as they arise.

Capital resources are also available from and provided through our 2013 Revolving Credit Facility, subject to the terms and conditions of that facility. The amount of cash on hand and borrowings available under our 2013 Revolving Credit Facility are influenced by a number of factors, including fluctuations in our operating results, revenue growth, accounts receivable collections, working capital changes, capital expenditures, tax payments, share repurchases, pension plan contributions, acquisitions, and dividends.

As of June 30, 2015, we had $73.8 million of unused borrowing capacity under our 2013 Revolving Credit Facility and a cash balance of $31.2 million. Based on our current operational plans, we believe that our cash on hand, cash provided by operating activities, and availability under the 2013 Revolving Credit Facility will be sufficient to fund operations, anticipated capital expenditures, payments of principal and interest on our borrowings, dividends on our common stock and pension contributions for the next 12 months. Nevertheless, we cannot predict the impact on our business performance of the economic climate in the U.S. and other economies in which we operate. A lasting economic recession in the U.S. and other economies could have a material

adverse effect on our business, financial position or operating results.

Critical Accounting Policies

Our financial statements and accompanying notes are prepared in accordance with U.S. GAAP. Preparing financial statements requires that management make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses.

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These estimates and assumptions are affected by management s application of accounting policies. We consider the following to be our critical accounting policies, as described in detail in our 2014 Form 10-K:

- Revenue recognition;
- Allowance for doubtful accounts;
- Reserve for healthcare, workers compensation, automobile, and general liability insurance;
- Goodwill and other intangible assets;
- Income taxes; and
- Stock-based compensation.
- Accounting for contingent consideration

There have been no material changes to the critical accounting policies described above, and in our 2014 Form 10-K.

As of June 30, 2015, in conjunction with the completion of the acquisition of 3Q Digital, Inc. (as described in Note M in the Notes to Financial Statements), we recognize that the estimates and assumptions around management s application of the earnout liability require that we add accounting for contingent consideration as a critical accounting policy. Management applies ASC 805 Business Combinations, *(Subtopic 30-25) Goodwill Recognition, Contingent Consideration.* We recognized the acquisition-date fair value of the contingent consideration as part of the consideration transferred in the exchange. The fair value of the contingent consideration arrangement was estimated by applying a multiple scenario approach.

As discussed in Note B, *Recent Accounting Pronouncements*, of the Notes to Financial Statements, certain new financial accounting pronouncements have been issued which either have already been reflected in the accompanying consolidated financial statements, or will become effective for our financial statements at various dates in the future. The adoptions of these new accounting pronouncements have not had a material effect on our consolidated financial statements; however, the Company is currently evaluating the impact of the new guidance and method of adoption.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk includes the risk of loss arising from adverse changes in market rates and prices. We face market risks related to interest rate variations and to foreign exchange rate variations. From time to time, we may utilize derivative financial instruments to manage our exposure to such risks.

We are exposed to market risk for changes in interest rates related to our credit facilities. Our earnings are affected by changes in short-term interest rates as a result of our credit facilities, which bear interest at variable rates based on LIBOR rates (effective 30 day LIBOR rate of 0.187% at June 30, 2015). Our five-year 2011 Term Loan Facility has a maturity date of August 16, 2016. At June 30, 2015, our debt balance related to the 2011 Term Loan Facility was $73.5 million. The three-year $80.0 million 2013 Revolving Credit Facility has a maturity date of August 16, 2016. At June 30, 2015, we did not have any debt outstanding under the 2013 Revolving Credit Facility.

Assuming the actual level of borrowings throughout the second quarter of 2015, and assuming a one percentage point change in the average interest rates, we estimate that our net income for the second quarter of 2015 would have changed by approximately $0.1 million. Due to our overall debt level and cash balance at June 30, 2015, anticipated cash flows from operations, and the various financial alternatives available to us should there be an adverse change in interest rates, we do not believe that we currently have significant exposure to market risks associated with changing interest rates. At this time we have not entered into any interest rate swap or other derivative instruments to hedge the effects of adverse fluctuations in interest rates.

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Our earnings are also affected by fluctuations in foreign currency exchange rates as a result of our operations in foreign countries. Our primary exchange rate exposure is to the Euro, British Pound, Australian Dollar and Philippine Peso. We monitor these risks throughout the normal course of business. The majority of the transactions of our U.S. and foreign operations are denominated in the respective local currencies. Changes in exchange rates related to these types of transactions are reflected in the applicable line items making up operating income in our Consolidated Statements of Comprehensive Income. Due to the current level of operations conducted in foreign currencies, we do not believe that the impact of fluctuations in foreign currency exchange rates on these types of transactions is significant to our overall annual earnings. A smaller portion of our transactions are denominated in currencies other than the respective local currencies. For example, intercompany transactions that are expected to be settled in the near-term are denominated in U.S. Dollars. Since the accounting records of our foreign operations are kept in the respective local currency, any transactions denominated in other currencies are accounted for in the respective local currency at the time of the transaction. Any foreign currency gain or loss from these transactions, whether realized or unrealized, results in an adjustment to income, which is recorded in Other, net in our Consolidated Statements of Comprehensive Income. Transactions such as these amounted to $1.3 million in pre-tax currency transaction losses in the second quarter of 2015. At this time we are not entered into any foreign currency forward exchange contracts or other derivative instruments to hedge the effects of adverse fluctuations in foreign currency exchange rates.

We do not enter into derivative instruments for any purpose other than cash flow hedging. We do not speculate using derivative instruments.

Item 4. Controls and Procedures

As of the end of the period covered by this report, an evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer, Chief Financial Officer and Chief Accounting Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, or the Exchange Act). It should be noted that, because of inherent limitations, our disclosure controls and procedures, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the disclosure controls and procedures are met. Based upon that evaluation, the Chief Executive Officer, Chief Financial Officer and Chief Accounting Officer concluded that the design and operation of these disclosure controls and procedures were effective, at the reasonable assurance level, to ensure information required to be disclosed by us in the reports that we file or submit under the Exchange Act is properly recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms.

As of the end of the period covered by this report, an evaluation was carried out under the supervision and with the participation of our management, including our Chief Executive Officer, Chief Financial Officer and Chief Accounting Officer, of our internal control over financial reporting to determine whether any changes occurred during the second quarter of 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Based on that evaluation, there were no changes in our internal control over financial reporting or in other factors that have materially affected or are reasonably likely to materially affect our internal control over financial reporting. We may make changes in our internal control processes from time to time in the future. It should also be noted that, because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements, and controls may become inadequate because of changes in conditions or in the degree of compliance with the policies or procedures.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Information regarding legal proceedings is set forth in Note K to the Notes to Unaudited Condensed Consolidated Financial Statements, *Litigation Contingencies*, in Item 1 of Part I of this Quarterly Report on Form 10-Q, which information is incorporated herein by reference.

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Item 1a. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our 2014 Form 10-K, which could materially affect our business, financial condition or future results. The risks described in our 2014 Form 10-K are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and operating results. In our judgment, there were no material changes in the risk factors as previously disclosed in Part I, Item 1A. Risk Factors of our 2014 Form 10-K. Refer to Part I, Item 2 of this Quarterly Report on Form 10-Q, for a discussion of the economic climate and impact on our financial statements.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table contains information about our purchases of equity securities during the second quarter of 2015:

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plan (2)	Maximum Dollar Amount that May Yet Be Spent Under the Plan
April 1-30, 2015	37,406	$ 7.67		$ 16,057,649
May 1-31, 2015	241,811	$ 6.35	240,000	$ 14,533,140
June 1-30, 2015	130,000	$ 6.30	130,000	$ 13,713,768
Total	409,217	$ 6.46	370,000	

(1) Total number of shares purchased includes shares, if any, (i) purchased as part of our publicly announced stock repurchase programs, and (ii) pursuant to our 2005 Omnibus Incentive Plan and 2013 Omnibus Incentive Plan, (a) withheld to pay withholding taxes and the exercise price in certain cashless exercises of stock options, and (b) withheld to offset withholding taxes upon the vesting of unvested shares.

(2) During the second quarter of 2015, we purchased 370,000 shares of our common stock through our stock repurchase program that was publicly announced in August 2014. Under this program, from which shares can be purchased in the open market, our Board of Directors has authorized us to spend up to $20.0 million to repurchase shares of our outstanding common stock. As of June 30, 2015, we have repurchased 965,079 shares and spent $6.3 million under the 2014 stock repurchase program. Through June 30, 2015, we had repurchased a total of 67,346,389 shares at an average price of $18.21 per share under all current and previous repurchase programs.

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Item 6. Exhibits

Exhibit No.	Description of Exhibit
*31.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
*32.1	Furnished Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
*101	XBRL Instance Document.

*Filed or furnished herewith

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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 hereunto duly authorized.

	HARTE HANKS, INC.
August 7, 2015 Date	/s/ Douglas C. Shepard Douglas C. Shepard President, Chief Executive Officer, and Chief Financial Officer
August 7, 2015 Date	/s/ Carlos M. Alvarado Carlos M. Alvarado Vice President, Finance and Corporate Controller